**ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA.**

**INDEX TO CONSOLIDATED FINANCIAL STATEMENTS**

## REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the shareholders and the Board of Directors of

Global Water Resources, Inc.

**Opinion on the Financial Statements**

We have audited the accompanying consolidated balance sheets of Global Water Resources, Inc. and subsidiaries (the "Company") as of December 31, 2020 and 2019, the related consolidated statements of operations, shareholders' equity, and cash flows for each of the two years in the period ended December 31, 2020, and the related notes (collectively referred to as the "financial statements"). In our opinion, the financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2020 and 2019, and the results of its operations and its cash flows for each of the two years in the period ended December 31, 2020, in conformity with accounting principles generally accepted in the United States of America.

**Basis for Opinion**

These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on the Company's financial statements based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) (PCAOB) and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. As part of our audits, we are required to obtain an understanding of internal control over financial reporting but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion.

Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

/s/ DELOITTE & TOUCHE LLP

Phoenix, Arizona
March 3, 2021

We have served as the Company's auditor since 2003.

# GLOBAL WATER RESOURCES, INC.
## CONSOLIDATED BALANCE SHEETS
## (in thousands, except share and per share amounts)

| | December 31, 2020 | December 31, 2019 |
|---|---|---|
| **ASSETS** | | |
| PROPERTY, PLANT AND EQUIPMENT: | | |
| Property, plant and equipment | 340,193 | 326,303 |
| Less accumulated depreciation | (101,302) | (92,749) |
| Net property, plant and equipment | 238,891 | 233,554 |
| CURRENT ASSETS: | | |
| Cash and cash equivalents | 18,033 | 7,513 |
| Accounts receivable — net | 2,147 | 1,631 |
| Customer payments in-transit | 306 | — |
| Due from affiliates | — | 426 |
| Unbilled revenue | 2,304 | 2,048 |
| Prepaid expenses and other current assets | 665 | 675 |
| Total current assets | 23,455 | 12,293 |
| OTHER ASSETS: | | |
| Goodwill | 4,600 | 4,398 |
| Intangible assets — net | 11,185 | 12,554 |
| Regulatory asset | 2,036 | 1,715 |
| Deposits | 9 | — |
| Restricted cash | 3,272 | 1,582 |
| Other noncurrent assets | — | 17 |
| Total other assets | 21,102 | 20,266 |
| TOTAL ASSETS | 283,448 | 266,113 |
| **LIABILITIES AND SHAREHOLDERS' EQUITY** | | |
| CURRENT LIABILITIES: | | |
| Accounts payable | 531 | 992 |
| Accrued expenses | 8,261 | 7,546 |
| Deferred revenue | 4 | — |
| Customer and meter deposits | 1,558 | 1,445 |
| Long-term debt and capital leases — current portion | 2,035 | 117 |
| Total current liabilities | 12,389 | 10,100 |
| NONCURRENT LIABILITIES: | | |
| Long-term debt and capital leases | 112,659 | 114,664 |
| Deferred revenue - ICFA | 17,843 | 17,372 |
| Regulatory liability | 7,986 | 8,803 |
| Advances in aid of construction | 76,384 | 67,621 |
| Contributions in aid of construction — net | 14,632 | 14,520 |
| Deferred income tax liabilities, net | 3,652 | 4,919 |
| Acquisition liability | 1,773 | 1,773 |
| Other noncurrent liabilities | 3,942 | 1,669 |
| Total noncurrent liabilities | 238,871 | 231,341 |
| Total liabilities | 251,260 | 241,441 |
| Commitments and contingencies (Refer to Note 16) | | |
| SHAREHOLDERS' EQUITY: | | |
| Common stock, $0.01 par value, 60,000,000 shares authorized; 22,690,477 and 21,636,420 shares issued as of December 31, 2020 and December 31, 2019, respectively. | 227 | 216 |
| Treasury stock, 102,711 and 99,039 shares at December 31, 2020 and December 31, 2019, respectively. | (1) | (1) |
| Paid in capital | $ 31,962 | $ 24,457 |
| Retained earnings | — | — |
| Total shareholders' equity | 32,188 | 24,672 |
| TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY | 283,448 | 266,113 |

See accompanying notes to the consolidated financial statements

# GLOBAL WATER RESOURCES, INC.
## CONSOLIDATED STATEMENTS OF OPERATIONS
## (in thousands, except share and per share amounts)

| | Year Ended December 31, | |
|---|---|---|
| | 2020 | 2019 |
| REVENUES: | | |
| Water services | $ 18,072 | $ 16,143 |
| Wastewater and recycled water services | 20,394 | 19,263 |
| Unregulated revenues | 161 | 65 |
| Total revenues | 38,627 | 35,471 |
| OPERATING EXPENSES: | | |
| Operations and maintenance | 9,539 | 7,237 |
| Operations and maintenance - related party | — | 1,678 |
| General and administrative | 12,722 | 11,242 |
| Depreciation and amortization | 9,031 | 8,353 |
| Total operating expenses | 31,292 | 28,510 |
| OPERATING INCOME | 7,335 | 6,961 |
| OTHER INCOME (EXPENSE): | | |
| Interest income | 93 | 203 |
| Interest expense | (5,377) | (5,388) |
| Other | (175) | 1,309 |
| Other - related party | — | 301 |
| Total other expense | (5,459) | (3,575) |
| INCOME BEFORE INCOME TAXES | 1,876 | 3,386 |
| INCOME TAX EXPENSE | (771) | (1,162) |
| NET INCOME | $ 1,105 | $ 2,224 |
| Basic earnings per common share | $ 0.05 | $ 0.10 |
| Diluted earnings per common share | $ 0.05 | $ 0.10 |
| Dividends declared per common share | $ 0.29 | $ 0.29 |
| Weighted average number of common shares used in the determination of: | | |
| Basic | 22,518,636 | 21,516,620 |
| Diluted | 22,574,093 | 21,531,594 |

See accompanying notes to the consolidated financial statements

**GLOBAL WATER RESOURCES, INC.**
**CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY**
**(in thousands, except share and per share amounts)**

| | Common Stock Shares | Common Stock | Treasury Stock Shares | Treasury Stock | Paid-in Capital | Retained Earnings | Total Equity |
|---|---|---|---|---|---|---|---|
| BALANCE - December 31, 2018 | 21,530,470 | $ 215 | (59,174) | $ (1) | $ 27,657 | $ — | $ 27,871 |
| Dividend declared $0.29 per share | — | — | — | — | (3,948) | (2,224) | (6,172) |
| Treasury stock | — | — | (39,865) | — | — | — | — |
| Stock option exercise | 105,950 | 1 | — | — | 412 | — | 413 |
| Stock compensation | — | — | — | — | 336 | — | 336 |
| Net income | — | — | — | — | — | 2,224 | 2,224 |
| BALANCE - December 31, 2019 | 21,636,420 | $ 216 | (99,039) | $ (1) | $ 24,457 | $ — | $ 24,672 |
| Dividend declared $0.29 per share | — | — | — | — | (5,434) | (1,105) | (6,539) |
| Issuance of Common Stock | 1,049,163 | 11 | | | 11,508 | | 11,519 |
| Treasury stock | — | — | (3,672) | — | (1) | — | (1) |
| Stock option exercise | 4,894 | — | — | — | — | — | — |
| Stock compensation | — | — | — | — | 1,432 | — | 1,432 |
| Net income | — | — | — | — | — | 1,105 | 1,105 |
| BALANCE - December 31, 2020 | 22,690,477 | $ 227 | (102,711) | $ (1) | $ 31,962 | $ — | $ 32,188 |

See accompanying notes to the consolidated financial statements

**GLOBAL WATER RESOURCES, INC.**
**CONSOLIDATED STATEMENTS OF CASH FLOWS**
**(in thousands)**

| | Year Ended December 31, 2020 | Year Ended December 31, 2019 |
|---|---|---|
| CASH FLOWS FROM OPERATING ACTIVITIES: | | |
| Net income | 1,105 | $ 2,224 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Deferred compensation | 3,286 | 2,051 |
| Depreciation and amortization | 9,031 | 8,353 |
| Amortization of deferred debt issuance costs and discounts | 134 | 88 |
| Gain on sale of Loop 303 contracts | — | (1,000) |
| Loss on equity investment | — | 79 |
| Other gains | 552 | 5 |
| Provision for doubtful accounts receivable | 140 | 50 |
| Deferred income tax expense | (1,275) | 570 |
| Changes in assets and liabilities | | |
| Accounts receivable | (641) | (193) |
| Other current assets | (121) | (60) |
| Accounts payable and other current liabilities | (176) | (1,584) |
| Other noncurrent assets | (321) | 75 |
| Other noncurrent liabilities | 2,852 | 908 |
| Net cash provided by operating activities | 14,566 | 11,566 |
| CASH FLOWS FROM INVESTING ACTIVITIES: | | |
| Capital expenditures | (9,131) | (11,187) |
| Cash paid for acquisitions, net of cash acquired | (302) | — |
| Cash received from the sale of Loop 303 contracts | — | 1,000 |
| Other cash flows from investing activities | (9) | 131 |
| Net cash used in investing activities | (9,442) | (10,056) |
| CASH FLOWS FROM FINANCING ACTIVITIES: | | |
| Dividends paid | (6,539) | (6,165) |
| Advances in aid of construction | 3,304 | 1,199 |
| Refunds of advances for construction | (992) | (952) |
| Proceeds from stock option exercise | — | 414 |
| Principal payments under capital lease | (109) | (64) |
| Loan borrowings | — | 35 |
| Loan repayments | (22) | (39) |
| Proceeds from sale of stock | 11,738 | — |
| Debt issuance costs paid | (73) | (40) |
| Payments of offering costs for sale of stock | (221) | — |
| Net cash provided by (used in) financing activities | 7,086 | (5,612) |
| INCREASE (DECREASE) IN CASH, CASH EQUIVALENTS, AND RESTRICTED CASH | 12,210 | (4,102) |
| CASH, CASH EQUIVALENTS, AND RESTRICTED CASH — Beginning of period | 9,095 | 13,197 |
| CASH, CASH EQUIVALENTS, AND RESTRICTED CASH – End of period | 21,305 | $ 9,095 |

See accompanying notes to the consolidated financial statements

**Supplemental disclosure of cash flow information:**

| | Year Ended December 31, | |
|---|---|---|
| | 2020 | 2019 |
| Cash and cash equivalents | $ 18,033 | $ 7,513 |
| Restricted Cash | 3,272 | 1,582 |
| Total cash, cash equivalents, and restricted cash | $ 21,305 | $ 9,095 |

**GLOBAL WATER RESOURCES, INC.**
**Notes to the Consolidated Financial Statements**

## 1. DESCRIPTION OF BUSINESS, BASIS OF PRESENTATION, CORPORATE TRANSACTIONS, SIGNIFICANT ACCOUNTING POLICIES, AND RECENT ACCOUNTING PRONOUNCEMENTS

### Description of Business

Global Water Resources, Inc. (the "Company" or "GWRI") is 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. GWRI seeks to deploy an integrated approach, which the Company refers to as "Total Water Management". Total Water Management is a comprehensive approach to water utility management that reduces demand on scarce non-renewable water sources and costly renewable water supplies, in a manner that ensures sustainability and greatly benefits communities both environmentally and economically. This approach employs a series of principles and practices that can be tailored to each community:

- Reuse of recycled water, either directly or to non-potable uses, through aquifer recharge, or direct potable reuse;
- Regional planning;
- Use of advanced technology and data;
- Employing subject matter experts and remaining thought and application leaders;
- Leading outreach and educational initiatives to ensure all stakeholders including customers, development partners, regulators, and utility staff are knowledgeable on the principles and practices of our Total Water Management approach; and
- Establishing partnerships with communities, developers, and industry stakeholders to gain support of our Total Water Management principles and practices.

GWRI currently owns sixteen water and wastewater utilities in strategically targeted communities principally in metropolitan Phoenix. GWRI currently serves more than 66,000 people in approximately 24,000 homes within our 366 square miles of certificated service areas, which are serviced by eleven wholly-owned regulated operating subsidiaries as of December 31, 2020. Approximately 92.8% of the Company's active service connections are customers of its Global Water - Santa Cruz Water Company, Inc. ("Santa Cruz") and Global Water - Palo Verde Utilities Company, Inc. ("Palo Verde") utilities. GWRI has grown significantly since its formation in 2003, with total revenues increasing from $4.9 million in 2004 to $38.6 million in 2020, and total service connections increasing from 8,113 as of December 31, 2004 to 49,158 as of December 31, 2020, with regionally planned service areas large enough to serve approximately two million service connections.

### Basis of Presentation and Principles of Consolidation

The Company's consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP") and include the accounts of GWRI and its subsidiaries. All significant intercompany account balances and transactions have been eliminated in consolidation.

The Company prepares its financial statements in accordance with the rules and regulations of the Securities and Exchange Commission ("SEC"). The preparation of the financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of income and expenses during the reporting period. Actual results could differ from those estimates. The U.S. dollar is the Company's reporting currency and functional currency.

The Company qualifies as an "emerging growth company", as defined in the Jumpstart Our Business Startups Act of 2012 (the "JOBS Act"), under the rules and regulations of the SEC. An emerging growth company may take advantage of specified reduced reporting and other requirements that are otherwise applicable generally to public companies. The Company has elected to take advantage of these provisions for up to five years or such earlier time that the Company is no longer an emerging growth company. The Company has elected to take advantage of some of the reduced disclosure obligations regarding financial statements. Also, as an emerging growth company, the Company 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. The Company has chosen to take advantage of this extended accounting transition provision.

**Corporate Transactions**

*Sale of certain MXA and WMA contracts*

In September 2013, the Company sold its Wastewater Facilities Main Extension Agreements (“MXA”) and Offsite Water Management Agreements (“WMA") for the contemplated Loop 303 service area along with their related rights and obligations to EPCOR Water Arizona Inc. (“EPCOR”) (collectively the “Transfer of Project Agreement”, or “Loop 303 Contracts”). Pursuant to the Transfer of Project Agreement, EPCOR agreed to pay GWRI approximately $4.1 million over a multi-year period. As of December 31, 2020, the Company had received the full $4.1 million of the proceeds having received the final payment of $1.0 million in March 2019. These proceeds were recorded as other income.

*Stipulated Condemnation of the Operations and Assets of Valencia Water Company, Inc.*

On July 14, 2015, the Company closed the stipulated condemnation to transfer the operations and assets of Valencia Water Company, Inc. ("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 $0.1 million 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. The Company received growth premiums of $0.2 million and $0.3 million for the years ended December 31, 2020 and 2019, respectively.

*Private Letter Ruling*

On June 2, 2016, the Company received a Private Letter Ruling from the Internal Revenue Service ("IRS") 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.

Pursuant to Internal Revenue Code §1033, we would have been able to defer the gain on condemnation through the end of 2017, which was subsequently extended through the end of 2020. The Company fully deferred the remaining tax liability during the year ended December 31, 2020.

*Acquisition of Red Rock Utilities*

On October 16, 2018, the Company completed the acquisition of Red Rock Utilities ("Red Rock"), an operator of a water and a wastewater utility with service areas in the Pima and Pinal counties of Arizona, for a purchase price of $5.9 million. The acquisition added over 1,650 connections and approximately 9 square miles of service area. The Company is obligated to pay to the seller a growth premium equal to $750 for each new account established within three specified growth premium areas, commencing in each area on the date of the first meter installation and ending on the earlier of ten years after such first installation date or twenty years from the acquisition date. The three specified growth premium areas are located in Pima County, Arizona where Red Rock has not yet begun operating, and where Red Rock is authorized to provide water utility services only. As of December 31, 2020, no meters have been installed and no accounts have been established in any of the three growth premium areas.

*ACC Tax Docket*

The Company had a regulatory asset of $2.0 million and $1.7 million at December 31, 2020 and December 31, 2019, respectively, and regulatory liabilities of $0.7 million and $0.6 million at December 31, 2020 and 2019, respectively, related to the Federal Tax Cuts and Jobs Act (the "TCJA") signed into law on December 22, 2017. Under Accounting Standards Codification ("ASC") 740, *Income Taxes*, the tax effects of changes in tax laws must be recognized in the period in which the law is enacted. ASC 740 also requires deferred income tax assets and liabilities to be measured at the enacted tax rate expected to apply when temporary differences are to be realized or settled. Thus, at the date of enactment, the Company’s deferred income taxes were re-measured based upon the new tax rate. For the Company’s regulated entities, substantially all of the change in deferred income taxes is recorded as an offset to either a regulatory asset or liability because the impact of changes in the rates are expected to be recovered from or refunded to customers.

On December 20, 2017, the Arizona Corporation Commission (the "ACC") opened a docket to address the utility ratemaking implications of the TCJA. The ACC subsequently approved an order in February 2018 requiring Arizona utilities 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.

On September 20, 2018, the ACC issued Rate Decision No. 76901, which set forth the reductions in revenue for our Santa Cruz, Palo Verde, Greater Tonopah, and Northern Scottsdale utilities due to the lower corporate tax rates under the TCJA. Rate Decision No. 76901 adopted a phase-in approach for the reductions to match the phase-in of our revenue requirement under Rate Decision No. 74364 enacted in February 2014. In 2020, the annual reductions in revenue for our Santa Cruz, Palo Verde, Greater Tonopah, and Northern Scottsdale utilities were approximately $381,000, $596,000, $16,000, and $5,000, respectively. In 2021, the final year of the phase-in, the annual reductions in revenue for our Santa Cruz, Palo Verde, Greater Tonopah, and Northern Scottsdale utilities will be approximately $415,000, $669,000, $16,000, and $5,000, respectively. The ACC also approved a carrying cost of 4.25% on regulatory liabilities resulting from the difference of the fully phased-in rates to be applied in 2021 versus the phased-in rates refunded in the years leading up to 2021 (i.e., 2018 through 2020).

Rate Decision No. 76901, however, did not address the impacts of the TCJA on accumulated deferred income taxes ("ADIT"), including excess ADIT ("EADIT"). Following the ACC's request for a proposal, the Company made its proposal in filings on December 19, 2018 and July 1, 2019. ACC Staff reviewed the Company's filing and requested that the Company defer tariff revisions until such revisions can be considered in the next rate case. ACC Staff also requested that the Company defer consideration of the regulatory assets and regulatory liabilities associated with 2018 EADIT amortization. On July 18, 2019, the Company made a filing proposing these items be deferred to the next rate case. Refer to " — Corporate Transactions — ACC Rate Case" for additional information regarding the Company's next rate case.

On November 27, 2018, February 20, 2019, February 28, 2019, and January 23, 2020, the ACC adopted orders relating to the funding for income taxes on contributions in aid of construction ("CIAC") and advances in aid of construction ("AIAC") (which became taxable for our regulated utilities under the TCJA). Those orders 1) require that under the hybrid sharing method, a contributor will pay a gross-up to the utility consisting of 55% of the income tax expense with the utility covering the remaining 45% of the income tax expense; 2) remove the full gross-up method option for Class A and B utilities and their affiliates (which includes all of our utilities); 3) ensure proper ratemaking treatment of a utility using the self-pay method; 4) clarify that pass-through entities that are owned by a "C" corporation can recover tax expense according to methods allowed; and 5) require Class A and B utilities to self-pay the taxes associated with hook-up fee contributions but permit using a portion of the hook-up fees to fund these taxes. The Company's utilities have adopted the hybrid sharing method for income tax on CIAC and AIAC.

*ACC Rate Case*

On August 28, 2020, 12 of our 16 regulated utilities each filed a rate case application with the ACC for water, wastewater, and recycled water rates, which proposed a collective revenue requirement increase of $4.6 million (relative to expected revenues in 2021, which is the final year of the rate phase-in from the last rate case) based on a 2019 test year. Certain of our utilities, including Santa Cruz and Palo Verde, have also requested that the rate increases be phased in over three years, beginning January 1, 2022. The consolidated rate increase, if approved by the ACC, would result in the estimated average monthly residential bill for Santa Cruz and Palo Verde customers increasing approximately $4.93, $5.72, and $4.12 in the aggregate in each of 2022, 2023, and 2024, respectively.

We also requested the consolidation of water and/or wastewater rates for our Red Rock, Santa Cruz, Palo Verde, Picacho Water, and Picacho Utilities. These utilities are all located in Pinal County; make up approximately 97% of the Company's active service connections; provide or will provide water, wastewater, and recycled water services; and are expected to create economies of scale that are beneficial to all customers if consolidated.

There can be no assurance, however, that the ACC will approve the requested rate increase or any increase or the consolidation of water and wastewater rates described above, and the ACC could take other actions as a result of the rate case. Further, it is possible that the ACC may determine to decrease future rates. There can also be no assurance as to the timing of when an approved rate increase (if any) would go into effect.

*2020 Common Stock Offering*

On January 21, 2020, the Company completed a public offering of 870,000 shares of common stock at a public offering price per share of $12.50, for gross proceeds of $10.9 million. On January 30, 2020, an additional 130,000 shares of common stock were issued at the public offering price of $12.50 per share, for gross proceeds of $1.6 million, resulting in total proceeds from the offering of approximately $12.5 million. The issuance of the additional shares was completed pursuant to the exercise in full of the underwriter's over-allotment option. Net proceeds of approximately $11.5 million were received after deducting underwriting discounts and commissions and offering expenses payable by us, which collectively totaled approximately $1.0 million.

*Immaterial Acquisitions*

During the twelve months ended December 31, 2020, the Company completed four immaterial acquisitions of water utilities, Global Water - Mirabell Water Company ("Mirabell"), Global Water - Francesca Water Company ("Francesca"), Global Water - Tortolita Water Company ("Tortolita"), and Global Water - Lyn Lee Water Company ("Lyn Lee"), which added 262 total service connections.

**Significant Accounting Policies**

*Regulation*

Our regulated utilities and certain other balances are subject to regulation by the ACC and are therefore subject to Accounting Standards Codification Topic 980, *Regulated Operations* (“ASC 980”) (See Note 2 – “Regulatory Decision and Related Accounting and Policy Changes”).

*Property, Plant, and Equipment*

Property, plant, and equipment is stated at cost less accumulated depreciation provided on a straight-line basis (See Note 4 – “Property, Plant, and Equipment”).

Depreciation rates for asset classes of utility property, plant, and equipment are established by the ACC. The cost of additions, including betterments and replacements of units of utility fixed assets are charged to utility property, plant, and equipment. When units of utility property are replaced, renewed, or retired, their cost plus removal or disposal costs, less salvage proceeds, is charged to accumulated depreciation.

For non-utility property, plant, and equipment, depreciation is calculated by the straight-line method over the estimated useful lives of depreciable assets. Cost and accumulated depreciation for non-utility property, plant, and equipment retired or disposed of are removed from the accounts and any resulting gain or loss is included in earnings.

In addition to third party costs, direct personnel costs and indirect construction overhead costs may be capitalized. Interest incurred during the construction period is also capitalized as a component of the cost of the constructed assets, which represents the cost of debt associated with construction activity. Expenditures for maintenance and repairs are charged to expense.

*Revenue Recognition—Water Services*

Water services revenues are recorded when service is rendered or water is delivered to customers. However, in addition to the monthly basic service charge, the determination and billing of water sales to individual customers is based on the reading of their meters, which occurs on a systematic basis throughout the month. At the end of each reporting period, amounts of water delivered to customers since the date of the last meter reading are estimated and the corresponding unbilled revenue is recorded.

Water connection fees are the fees associated with the application process to set up a customer to receive utility service on an existing water meter. These fees are approved by the ACC through the regulatory process and are set based on the costs incurred to establish services including the application process, billing setup, initial meter reading, and service transfer. Because the amounts charged for water connection fees are set by our regulator and not negotiated in conjunction with the pricing of ongoing water service, the connection fees represent the culmination of a separate earnings process and are recognized when the service is provided. For the years ended December 31, 2020 and 2019, the Company recognized $0.2 million and $0.3 million in connection fees, respectively.

Meter installation fees are the fees charged to developers or builders associated with installing new water meters. Certain fees for meters are regulated by the ACC, and are refundable to the end customer over a period of time. Refundable meter installation fees are recorded as a liability upon receipt. These fees are recognized as revenue when the service is rendered, or when a water meter is installed.

*Revenue Recognition—Wastewater and Recycled Water Services*

Wastewater and recycled water services revenues are generally recognized when service is rendered. Wastewater services are billed at a fixed monthly amount per connection, and recycled water services are billed monthly based on volumetric fees.

*Revenue Recognition—Unregulated Revenues*

Unregulated revenues represent those revenues that are not subject to the ratemaking process of the ACC. Unregulated revenues are limited to rental revenue and imputed revenues resulting from certain infrastructure coordination and financing agreement arrangements ("ICFAs").

*Allowance for Doubtful Accounts*

Provisions are made for doubtful accounts due to the inherent uncertainty around the collectability of accounts receivable. The allowance for doubtful accounts is recorded as bad debt expense, and is classified as general and administrative expense. The allowance for doubtful accounts is determined considering the age of the receivable balance, type of customer (e.g., residential or commercial), payment history, as well as specific identification of any known or expected collectability issues (see Note 5 – "Accounts Receivable").

*Infrastructure Coordination and Financing Fees*

ICFAs are agreements with developers and homebuilders whereby GWRI, which owns the operating utilities, provides services to plan, coordinate, and finance the water and wastewater infrastructure that would otherwise be required to be performed or subcontracted by the developer or homebuilder. Services provided within these agreements include coordination of construction services for water and wastewater treatment facilities as well as financing, arranging, and coordinating the provision of utility services.

As these arrangements are with developers and not with the end water or wastewater customer, revenue recognition coincides with the completion of our performance obligations under the agreement with the developer and our ability to provide fitted capacity for water and wastewater service. Payments for ICFAs are usually received in advance and are recorded as deferred revenue until earned. Pursuant to Rate Decision No. 74364, as funding is received 70% of ICFAs are now recorded as a hook-up fee ("HUF") liability until the HUF liability is fully funded, with the remaining amount recorded as revenue once all components of revenue recognition are met (See Note 2 – "Regulatory Decision and Related Accounting and Policy Changes").

*Cash and Cash Equivalents*

Cash and cash equivalents include all highly liquid investments in debt instruments with an original maturity of three months or less.

*Restricted Cash*

Restricted cash represents cash deposited relating to HUF tariffs, asset retirement obligations, and pending legal matters. The following table summarizes the restricted cash balance as of December 31, 2020 and 2019 (in thousands):

| | December 31, 2020 | December 31, 2019 |
|---|---|---|
| HUF funds | $ 2,482 | $ 627 |
| Certificate of deposits | $ 790 | 705 |
| Liability Deposit | $ — | 250 |
| | $ 3,272 | $ 1,582 |

*Customer Payments In-Transit*

Customer payments in-transit represent funds received by our third-party payment processor related to customer payments, a majority of which were paid for with debit cards, credit cards, and checks, to which the Company does not have immediate access but settles within a few days of the payment transaction.

*Income Taxes*

The Company utilizes the asset and liability method of accounting for income taxes. Under the asset and liability method, deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or all of the deferred tax assets will not be realized. The Company's valuation allowance totaled zero as of December 31, 2020 and 2019 (see Note 13 – "Income Taxes").

We evaluate uncertain tax positions using a two-step approach. Recognition (step one) occurs when we conclude that a tax position, based solely on its technical merits, is more-likely-than-not to be sustained upon examination. Measurement (step two) determines the amount of benefit that more-likely-than-not will be realized upon settlement. Derecognition of a tax position that was previously recognized would occur when we subsequently determine that a tax position no longer meets the more-likely-than-not threshold of being sustained. The use of a valuation allowance as a substitute for derecognition of tax positions is prohibited, and to the extent that uncertain tax positions exist, we provide expanded disclosures.

*Basic and Diluted Earnings per Common Share*

Diluted EPS is based upon the weighted average number of common shares, including both outstanding shares and shares potentially issuable in connection with stock options and restricted stock awards granted.

As of December 31, 2020, the Company had 625,913 options outstanding to acquire an equivalent number of shares of GWRI common stock. The 382,771 options outstanding from the 2017 option grant equated to 48,094 common share equivalents, which were included within the calculation of diluted earnings per share for the year ended December 31, 2020. The remaining 243,142 options outstanding from the 2019 option grant were not included within the calculation of diluted earnings per share as to do so would be antidilutive. As of December 31, 2020, there were 128,327 restricted stock awards outstanding. The 128,327 restricted stock awards outstanding equated to 7,363 common share equivalents, which were included within the calculation of diluted earnings per share for the year ended December 31, 2020.

As of December 31, 2019, the Company had 632,500 options outstanding to acquire an equivalent number of shares of GWRI common stock. The 386,896 options outstanding from the 2017 option grant equated to 14,974 common share equivalents, which were included within the calculation of diluted earnings per share for the year ended December 31, 2019. The remaining 245,604 options outstanding from the 2019 option grant were not included within the calculation of diluted earnings per share as to do so would be antidilutive.

*Goodwill*

Goodwill represents the excess purchase price over the fair value of net tangible and identifiable intangible assets acquired through acquisitions. Goodwill is not amortized, it is instead tested for impairment annually, or more often, if circumstances indicate a possible impairment may exist. As required, we evaluate goodwill for impairment annually, and do so as of November 1 of each year, and at an interim date if indications of impairment exist. When testing goodwill for impairment, we may assess qualitative factors, including macroeconomic conditions, industry and market considerations, overall financial performance, and entity specific events to determine whether it is more likely than not that the fair value of an operating and reportable segment is less than its carrying amount. We utilize internally developed discounted future cash flow models, third-party appraisals, or broker valuations to determine the fair value of the reporting unit. Under the discounted cash flow approach, we utilize various assumptions requiring judgment, including projected future cash flows, discount rates, and capitalization rates. Our estimated future cash flows are based on historical data, internal estimates, and external sources. We then compare the estimated fair value to the carrying value. If the carrying value is in excess of the fair value, an impairment charge is recorded to asset impairments within our consolidated statement of operations in the amount by which the reporting unit's carrying value exceeds its fair value, limited to the carrying value of goodwill. Refer to Note 8 — "Goodwill and Intangible Assets" for additional information about goodwill.

*Intangible Assets*

Intangible assets not subject to amortization consist of certain permits expected to be renewable indefinitely, water rights, and certain service areas acquired in transactions which did not meet the definition of business combinations for accounting purposes, and are considered to have indefinite lives. Intangible assets with indefinite lives are not amortized but are tested for impairment annually, or more often if certain circumstances indicate a possible impairment may exist. Amortized intangible assets consist primarily of acquired ICFA contract rights. Refer to Note 2 – "Regulatory Decision and Related Accounting and Policy Changes" for additional information about ICFAs.

*Debt Issuance Costs*

In connection with the issuance of some of our long-term debt, we have incurred legal and other costs that we believe are directly attributable to realizing the proceeds of the debt issued. These costs are netted against long-term debt and amortized as interest expense using the effective interest method over the term of the respective debt. Amortization of debt issuance costs and discounts totaled $0.1 million for both years ended December 31, 2020 and 2019.

*Impairment of Long-Lived Assets*

Management evaluates the carrying value of long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying value of such assets may not be recoverable. If an indicator of possible impairment exists, an undiscounted cash flow analysis would be prepared to determine whether there is an actual impairment. Measurement of the impairment loss is based on the fair value of the asset. Generally, fair value will be determined using appraisals or valuation techniques such as the present value of expected future cash flows.

*Advances and Contributions in Aid of Construction*

The Company has various 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 AIAC are non-interest-bearing and are subject to refund 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 advance 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, utility plant funded by AIAC or CIAC are excluded from rate base. AIAC balances of $0.1 million and $2.9 million were transferred to CIAC for the years ended December 31, 2020 and 2019, respectively.

*Fair Value of Financial Instruments*

The carrying values of cash equivalents, trade receivables, and accounts payable approximate fair value due to the short-term maturities of these instruments. See Note 12 – "Debt" for information as to the fair value of our long-term debt. Our refundable AIAC have a carrying value of $76.4 million and $67.6 million as of December 31, 2020 and 2019, respectively. Portions of these non-interest-bearing instruments are payable annually through 2032 and amounts not paid by the contract expiration dates become nonrefundable. Their relative fair values cannot be accurately estimated because future refund payments depend on several variables, including new customer connections, customer consumption levels, and future rate increases. However, the fair value of these amounts would be less than their carrying value due to the non-interest-bearing feature.

*Segments*

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 ("CODM") in deciding how to allocate resources and in assessing operating performance. In consideration of ASC 280—*Segment Reporting* the Company notes it is not organized around specific products and services, geographic regions, or regulatory environments. The Company currently operates in one geographic region within the State of Arizona, wherein each operating utility operates within the same regulatory environment.

While the Company reports its revenue, disaggregated by service type, on the face of its Statements of Operations, the Company does not manage the business based on any performance measure at the individual revenue stream level. The Company does not have any customers that contribute more than 10% to the Company's revenues or revenue streams. Additionally we note that the CODM uses consolidated financial information to evaluate the Company's performance, which is the same basis on which he communicates the Company's results and performance to the Board of Directors. It is upon this consolidated basis from which he bases all significant decisions regarding the allocation of the Company's resources on a consolidated level. Based on the information described above and in accordance with the applicable literature, management has concluded that the Company is currently organized and operated as one operating and reportable segment.

**Recent Accounting Pronouncements**

*Recently Adopted Accounting Standards*

In August 2018, the Financial Accounting Standards Board ("FASB") issued ASU 2018-13, Disclosure Framework - Changes to the Disclosure Requirements for Fair Value Measurement (Topic 820) ("ASU 2018-13"). ASU 2018-13 changes the fair value disclosure requirements including new, eliminated, and modified disclosure requirements of ASC 820. Specifically, the ASU requires the addition of disclosures for Level 3 fair value measurements with unrealized gains and losses included in other comprehensive income and disclosure of the range and weighted average used to develop significant unobservable inputs for Level 3 measurements. The Company implemented ASU 2018-13 on January 1, 2020. The implementation did not result in material changes to our consolidated financial statements.

*Future Adoption of Accounting Standards*

In February 2016, the FASB issued ASU 2016-02, *Leases (Topic 842)* ("ASU 2016-02", or "ASC 842"). ASU 2016-02 requires lessees to record a right-of-use asset and corresponding lease obligation for lease arrangements with a term of greater than twelve months. ASU 2016-02 requires additional disclosures about leasing arrangements and requires the use of the modified retrospective method, which will require adjustment to all comparative periods presented in the consolidated financial statements. In July 2018, the FASB issued ASU 2018-10, *Codification Improvements to Topic 842* ("ASU 2018-10"). ASU 2018-10 improves various aspects within ASC 842, such as rate implicit in the lease, lessee's reassessment of lease classification, lease term and purchase option, as well as many other aspects of the guidance. In July 2018, the FASB issued ASU 2018-11, *Leases Topic 842, Targeted Improvements* ("ASU 2018-11"). ASU 2018-11 provides entities the option to elect not to recast the comparative periods presented when transitioning to ASC 842 and lessors may elect not to separate lease and non-lease components when certain conditions are met. In November 2019, the FASB issued ASU 2019-10, *Financial Instruments - Credit Losses (Topic 326), Derivatives and Hedging (Topic 815), and Leases (Topic 842)* ("ASU 2019-10"). ASU 2019-10 amends the effective dates for certain major new accounting standards including those related to leases. Due to qualifying as an emerging growth company, the Company is required to adopt all lease related ASUs on January 1, 2021. The Company will adopt this new standard during the first quarter of 2021 using the modified retrospective method and will not apply the standard to the comparative periods presented in the year of adoption. The Company is finalizing its implementation of the accounting and is updating certain of its business processes and internal controls to meet the reporting and disclosure requirements of the new standard. The Company does not expect the implementation to result in material changes to our consolidated financial statements.

In January 2017, the FASB issued ASU 2017-04, *Intangibles - Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment* ("ASU 2017-04"). ASU 2017-04 eliminates Step 2 from the impairment test which requires entities to determine the implied fair value of goodwill to measure if any impairment expense is necessary. Instead, entities will record impairment expenses based on the amount by which a reporting unit's carrying value exceeds its fair value, not to exceed the carrying amount of goodwill. ASU 2019-10 extended the effective date for this ASU. Due to qualifying as an emerging growth company, the Company is required to adopt the ASU on January 1, 2023. The Company is currently assessing the impact that adopting this new accounting standard will have on its consolidated financial statements.

In August 2018, the FASB issued ASU 2018-15, *Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract (Topic 350)* ("ASU 2018-15"). ASU 2018-15 amends ASC 350 to include in its scope implementation costs of a Cloud Computing Arrangement ("CCA") that is a service contract and clarifies that a customer should apply ASC 350-40 to determine which implementation costs should be capitalized in a CCA that is considered a service contract. Due to qualifying as an emerging growth company, the Company is required to adopt the ASU on January 1,

2021. Early adoption is permitted, including adoption in any interim period. The Company is currently assessing the impact that adopting this new standard will have on its consolidated financial statements.

**2. REGULATORY DECISION AND RELATED ACCOUNTING AND POLICY CHANGES**

Our regulated utilities and certain other balances are subject to regulation by the ACC and meet the requirements for regulatory accounting found within ASC 980, *Regulated Operations*.

In accordance with ASC 980, rates charged to utility customers are intended to recover the costs of the provision of service plus a reasonable return in the same period. Changes to the rates are made through formal rate applications with the ACC, which we have done for all of our operating utilities and which are described below.

On July 9, 2012, we filed formal rate applications with the ACC to adjust the revenue requirements for seven utilities representing a collective rate increase of approximately 28% over 2011 revenue levels. In August 2013, the Company entered into a settlement agreement with 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's Commissioners before it could take effect. In February 2014, the rate case proceedings were completed and the ACC issued Rate Decision No. 74364, effectively approving the settlement agreement. The rulings of the decision include, but are not limited to, the following:

- For the Company's utilities, adjusting for the condemnation of the operations and assets of Valencia and sale of Willow Valley Water Co., Inc. ("Willow Valley"), which occurred in 2015 and 2016, respectively, a collective 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, not updated for the TCJA, refer to Note 1 — "Basis of Presentation, Corporate Transactions, Significant Accounting Policies, and Recent Accounting Pronouncements — Corporate Transactions — ACC Tax Docket" for further details):

| | 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 increases 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.

- Full reversal of the imputation of CIAC balances associated with funds previously received under ICFAs, as required in the Company's last rate case. The reversal restored rate base or future rate base and had a significant impact of restoring shareholder equity on the balance sheet.
- The Company has agreed to not enter into any new ICFAs. Existing ICFAs will remain in place, but a portion of future payments to be received under the ICFAs will be considered as hook-up fees, which are accounted for as CIAC once expended on plant.
- A 9.5% return on common equity was adopted.

On September 20, 2018, the ACC issued Rate Decision No. 76901, which set forth the reductions in revenue for our Santa Cruz, Palo Verde, Greater Tonopah, and Northern Scottsdale utilities due to the TCJA. Rate Decision No. 76901 adopted a phase-in approach for the reductions to match the phase-in of our revenue requirements under Rate Decision No. 74364. Refer to Note 1 — "Basis of Presentation, Corporate Transactions, Significant Accounting Policies, and Recent Accounting Pronouncements — Corporate Transactions — ACC Tax Docket" for details regarding Rate Decision No. 76901.

On August 28, 2020, 12 of our 16 regulated utilities each filed a rate case application with the ACC for water, wastewater, and recycled water rates, as well as the consolidation of water and/or wastewater rates for certain utilities. Refer to Note 1 — "Basis of Presentation, Corporate Transactions, Significant Accounting Policies, and Recent Accounting Pronouncements — Corporate Transactions — ACC Rate Case" for additional information.

The following provides additional discussion on accounting and policy changes resulting from Rate Decision No. 74364.

**Infrastructure Coordination and Financing Agreements** – ICFAs are agreements with developers and homebuilders whereby GWRI, the indirect parent of the operating utilities, provides services to plan, coordinate, and finance the water and wastewater infrastructure that would otherwise be required to be performed or subcontracted by the developer or homebuilder.

Under the ICFAs, GWRI has a contractual obligation to ensure physical capacity exists through its regulated utilities for water and wastewater to the landowner/developer when needed. This obligation persists regardless of connection growth. Fees for these services are typically a negotiated amount per equivalent dwelling unit for the specified development or portion of land. Payments are generally due in installments, 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. The agreements are generally recorded against the land and must be assumed in the event of a sale or transfer of the land. The regional planning and coordination of the infrastructure in the various service areas has been an important part of GWRI's business model.

In February 2014, the ACC issued Rate Decision No. 74364, and concluded ICFA funds already received would no longer be deemed CIAC for rate making purposes. ICFA funds already received or which had become due prior to the date of Rate Decision No. 74364 were 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, which the Company accounts for in accordance with the Company's 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. The Company is responsible for assuring the full HUF value is paid from ICFA proceeds, and recorded in its full amount, even if it results in recording less than 30% of the ICFA fee as deferred revenue.

The Company will account for the portion allocated to the HUF as a CIAC contribution. However, in accordance with the ACC directives the CIAC is not deducted from rate base until the HUF funds are expended for utility plant. Such funds will be segregated in a separate bank account and used for plant. A HUF liability will be established and will be amortized as a reduction of depreciation expense over the useful life of the related plant once the HUF funds are utilized for the construction of plant. For facilities required under a HUF or ICFA, the utilities must first use the HUF moneys received, after which, it may use debt or equity financing for the remainder of construction. The Company will record 30% of the funds received, up until the HUF liability is fully funded, as deferred revenue, which is to be recognized as revenue once the obligations specified within the ICFA are met, including construction of sufficient operating capacity to serve the customers for which revenue was deferred.

As of December 31, 2020 and December 31, 2019, ICFA deferred revenue recorded on the consolidated balance sheet totaled $17.8 million and $17.4 million, respectively, which represents deferred revenue recorded for ICFA funds received on contracts that had become due prior to Rate Decision No. 74364.

**Intangible assets / Regulatory liability** – Pursuant to Rate Decision No. 74364, approximately 70% of ICFA funds to be received in the future will be recorded as a HUF, until the HUF is fully funded at the Company's applicable utility subsidiary. The remaining approximate 30% of future ICFA funds will be recorded at the parent company level and will be subject to the Company's ICFA revenue recognition accounting policy. As the Company now expects to experience an economic benefit from the approximately 30% portion of future ICFA funds, 30% of the regulatory liability, or $3.4 million, was reversed in 2014. The remaining 70% of the regulatory liability, or $7.9 million, will continue to be recorded on the balance sheet.

The intangible assets amortize when the corresponding ICFA funds are received in proportion to the amount of total cash expected to be received under the underlying agreements. The recognition of amortization expense will be partially offset by a corresponding reduction of the regulatory liability.

As of December 31, 2020, regulatory liability recorded on the consolidated balance sheet totaled $8.0 million, of which $6.6 million relates to the offset of intangible assets related to ICFA contracts obtained in connection with our Santa Cruz, Palo Verde, and Sonoran acquisitions, and the remaining $1.4 million relates to the TCJA rate reduction mandated by the ACC pursuant to Rate Decision No. 76901.

## 3. REVENUE RECOGNITION

On January 1, 2019, the Company adopted ASC 606, using the modified retrospective approach. The Company identified its sources of revenue streams that fall within the scope of this guidance and applied the five-step model to all qualifying revenue streams to determine when to recognize revenue. The Company concluded that there is not a material change to how revenue was recognized before and after the adoption of ASC 606; therefore, no cumulative retained earnings adjustment was required.

**Regulated Revenue**

The Company's operating revenues are primarily attributable to regulated services based upon tariff rates approved by the ACC. Regulated service revenues consist of amounts billed to customers based on approved fixed monthly fees and consumption fees, as well as unbilled revenues estimated from the last meter reading date to the end of the accounting period utilizing historical customer data recorded as accrued revenue. The measurement of sales to customers is generally based on the reading of their meters, which occurs on a systematic basis throughout the month. At the end of each month, the Company estimates consumption since the date of the last meter reading and a corresponding unbilled revenue is recognized. The unbilled revenue estimate is based upon the number of unbilled days that month and the average daily customer billing rate from the previous month (which fluctuates based upon customer usage). The Company applies the invoice practical expedient and recognizes revenue from contracts with customers in the amount for which the Company has a right to invoice. The Company has the right to invoice for the volume of consumption, service charge, and other authorized charges.

The Company satisfies its performance obligation to provide water, wastewater, and recycled water services over time as the services are rendered. Regulated services may be terminated by the customers at will, and, as a result, no separate financing component is recognized for the Company's collections from customers, which generally require payment within 15 days of billing. The Company applies judgment, based principally on historical payment experience, in estimating its customers' ability to pay.

The Company has elected to apply the sales tax practical expedient, whereby qualifying excise and other taxes collected from customers and remitted to governmental authorities are not included in reported revenues.

**Unregulated Revenue**

Unregulated revenues represent those revenues that are not subject to the ratemaking process of the ACC. Unregulated revenues are limited to rental revenue and imputed revenues resulting from a portion of ICFA funds received. ICFAs are agreements with developers and homebuilders where the Company provides services to plan, coordinate, and finance the water and wastewater infrastructure that would otherwise be required to be performed or subcontracted by the developer or homebuilder. In return, the developers and homebuilders pay the Company an agreed-upon amount per dwelling unit for the specified development or portion of land. In addition, under ICFA agreements, the Company has a contractual obligation to ensure physical capacity exists through its regulated utilities for water and wastewater to the developer when needed. This obligation persists regardless of connection growth.

The Company believes that these services are not distinct in the context of the contract because they are highly interdependent with the Company’s ability to provide fitted capacity for water and wastewater services. The Company concluded that the goods and services provided under ICFA contracts constitute a single performance obligation.

IFCA revenue is recognized at a point in time when the Company has the necessary capacity in place within its infrastructure to provide water/wastewater services to the developer. The Company exercises judgment when estimating the number of equivalent dwelling units that the Company has capacity to serve.

*Disaggregated Revenues*

For the years ended December 31, 2020 and 2019, disaggregated revenues from contracts with customers by major source and customer class are as follows (in thousands):

| | Year Ended December 31, | |
|---|---|---|
| | 2020 | 2019 |
| **REGULATED REVENUE** | | |
| Water Services | | |
| Residential | $ 12,818 | $ 11,519 |
| Irrigation | 3,309 | 3,008 |
| Commercial | 836 | 768 |
| Construction | 540 | 152 |
| Other water revenues | 569 | 696 |
| Total water revenues | 18,072 | 16,143 |
| Wastewater and recycled water services | | |
| Residential | 18,056 | 17,053 |
| Commercial | 933 | 908 |
| Recycled water revenues | 1,181 | 922 |
| Other wastewater revenues | 224 | 380 |
| Total wastewater and recycled water revenues | 20,394 | 19,263 |
| TOTAL REGULATED REVENUE | 38,466 | 35,406 |
| **UNREGULATED REVENUE** | | |
| ICFA revenues | — | — |
| Rental revenues | 160 | 64 |
| Other Miscellaneous revenues | 1 | 1 |
| TOTAL UNREGULATED REVENUE | 161 | 65 |
| **TOTAL REVENUE** | $ 38,627 | $ 35,471 |

*Contract Balances*

Our contract assets and liabilities consist of the following (in thousands):

| | December 31, 2020 | December 31, 2019 |
|---|---|---|
| **CONTRACT ASSETS** | | |
| Accounts receivable | | |
| Water services | $ 1,203 | $ 791 |
| Wastewater and recycled water services | 1,149 | 926 |
| Total contract assets(1) | $ 2,352 | $ 1,717 |
| **CONTRACT LIABILITIES** | | |
| Deferred revenue - ICFA | $ 17,843 | $ 17,372 |
| Refund liability - regulated(2) | 733 | 587 |
| Deferred revenue - other(3) | 4 | — |
| Total contract liabilities | $ 18,580 | $ 17,959 |

(1) The increase in accounts receivable was primarily due to the effects of the ACC calling for a moratorium on disconnections and late fees due to the novel strain of coronavirus ("COVID-19") pandemic, coupled with the increase in customers in 2020 compared to 2019.

(2) The increase in refund liability is due to the phase-in approach approved in Rate Decision No. 76901. Refer to Note 1 —"Basis of Presentation, Corporate Transactions, Significant Accounting Policies, and Recent Accounting Pronouncements — Corporate Transactions — ACC Tax Docket" of the notes to the consolidated financial statements for further details.

(3) The increase in deferred revenue - other is due to a new rental contract entered into during the three months ended March 31, 2020, for which rental payments were collected in advance.

*Remaining Performance Obligations*

Revenue allocated to remaining performance obligations represents contracted revenue that has not yet been recognized, which includes deferred revenue and amounts that will be invoiced and recognized as revenue in future periods. Contracted revenue expected to be recognized in future periods was approximately $17.8 million at December 31, 2020 and approximately $17.4 million at December 31, 2019. Deferred revenue 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. Due to the uncertainty of future events, the Company is unable to estimate when to expect recognition of deferred revenue.

**4. PROPERTY, PLANT AND EQUIPMENT**

Property, plant, and equipment at December 31, 2020 and December 31, 2019 consist of the following (in thousands):

| | December 31, 2020 | December 31, 2019 | Average Depreciation Life (in years) |
|---|---|---|---|
| Mains/lines/sewers | $ 145,910 | $ 138,173 | 49 |
| Plant | 96,654 | 94,615 | 31 |
| Equipment | 37,347 | 35,497 | 14 |
| Meters | 14,548 | 14,057 | 13 |
| Furniture, fixture and leasehold improvements | 1,650 | 623 | 27 |
| Computer and office equipment | 1,108 | 785 | 6 |
| Software | 241 | 241 | 3 |
| Land and land rights | 1,159 | 1,051 | |
| Other | 699 | 700 | |
| Construction work-in-process | 40,877 | 40,561 | |
| Total property, plant and equipment | 340,193 | 326,303 | |
| Less accumulated depreciation | (101,302) | (92,749) | |
| Net property, plant and equipment | $ 238,891 | $ 233,554 | |

**5. ACCOUNTS RECEIVABLE**

Accounts receivable as of December 31, 2020 and December 31, 2019 consist of the following (in thousands):

| | December 31, 2020 | December 31, 2019 |
|---|---|---|
| Billed receivables | $ 2,352 | $ 1,718 |
| Less allowance for doubtful accounts | $ (205) | (87) |
| Accounts receivable – net | $ 2,147 | $ 1,631 |

The following table summarizes the allowance for doubtful accounts activity as of and for the years ended December 31, 2020 and December 31, 2019 (in thousands).

| | Balance at Beginning of Period | Additions Charged to Expense | Charged to Other Accounts | Write-offs | Balance at End of Period |
|---|---|---|---|---|---|
| **Allowance for doubtful accounts:** | | | | | |
| Year Ended December 31, 2020 | $ (87) | $ (169) | $ (7) | $ 58 | $ (205) |
| Year Ended December 31, 2019 | $ (145) | $ (56) | $ (24) | $ 138 | $ (87) |

**6. EQUITY METHOD INVESTMENT**

The Company previously had an investment in a limited partnership, FATHOM Water Management Holdings, LLP, which, through subsidiaries, owned Global Water Management, LLC ("GWM"). This investment was accounted for under the equity method due to the investment being considered more than minor. In December of 2019, GWM ceased to provide substantially all of the billing, customer service, and other support services previously provided to its customers, including the Company's regulated utilities. The carrying value of this investment is zero as of both December 31, 2020 and 2019.

**7. GOODWILL AND INTANGIBLE ASSETS**

**Goodwill**

As of December 31, 2020, the goodwill balance of $4.6 million related to the Turner, Red Rock, Mirabell, Francesca, Tortolita, and Lyn Lee acquisitions. There were no indicators of impairment identified as a result of the Company's review of events and circumstances related to its goodwill subsequent to the acquisitions. Based on our annual impairment testing performed on November 1st, no impairment was recorded.

**Intangible Assets**

As of December 31, 2020 and December 31, 2019 intangible assets consisted of the following (in thousands):

| | December 31, 2020 | | | December 31, 2019 | | |
|---|---|---|---|---|---|---|
| | Gross Amount | Accumulated Amortization | Net Amount | Gross Amount | Accumulated Amortization | Net Amount |
| INDEFINITE LIVED INTANGIBLE ASSETS: | | | | | | |
| CP Water Certificate of Convenience & Necessity service area | 1,532 | | $ 1,532 | $ 1,532 | | $ 1,532 |
| Intangible trademark | 13 | | 13 | 13 | | 13 |
| Franchise contract rights | 129 | | 129 | 129 | | 129 |
| Organizational costs | 67 | | 67 | 67 | | 67 |
| | 1,741 | | 1,741 | 1,741 | | 1,741 |
| DEFINITE LIVED INTANGIBLE ASSETS: | | | | | | |
| Acquired ICFAs | 17,978 | (13,718) | 4,260 | 17,978 | (12,568) | 5,410 |
| Sonoran contract rights | 7,406 | (2,222) | 5,184 | 7,406 | (2,003) | 5,403 |
| | 25,384 | (15,940) | 9,444 | 25,384 | (14,571) | 10,813 |
| Total intangible assets | $ 27,125 | $ (15,940) | $ 11,185 | $ 27,125 | $ (14,571) | $ 12,554 |

A Certificate of Convenience & Necessity ("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. The CP Water CC&N intangible asset was acquired through the acquisition of CP Water Company in 2006. This CC&N permit has no outstanding conditions that would require renewal.

Franchise contract rights and organizational costs were acquired as part of the Red Rock acquisition. Franchise contract rights are agreements with Pima and Pinal counties that allow the Company to place infrastructure in public right-of-way and permits expected to be renewable indefinitely. Organizational costs represent fees paid to federal or state governments for the privilege of incorporation and expenditures incident to organizing the corporation and preparing it to conduct business.

Acquired ICFAs and contract rights related to our 2005 acquisition of Sonoran Utility Services, LLC assets are amortized when cash is received in proportion to the amount of total cash expected to be received under the underlying agreements. Due to the uncertainty of the timing of when cash will be received under ICFA agreements and contract rights, we cannot reliably estimate when the remaining intangible assets' amortization will be recorded. Amortization in the amount of $1.4 million and $0.4 million was recorded for these balances for the years ended December 31, 2020 and 2019, respectively.

**8. TRANSACTIONS WITH RELATED PARTIES**

The Company provides medical benefits to our employees through our participation in a pooled plan sponsored by an affiliate of a shareholder and director of the Company. Medical claims paid to the plan were approximately $0.9 million and $0.3 million for the years ended December 31, 2020 and 2019, respectively.

As GWM was previously owned by the Company, it had historically provided billing, customer service, and other support services for the Company's regulated utilities. In connection with the sale of GWM in 2013, the Company agreed to use GWM's FATHOM platform for all of its regulated utility services for an initial term of 10 years pursuant to a services agreement. The services agreement was amended on November 17, 2016, which extended the term of the contract through December 31, 2026. As part of the amended agreement, the Company reduced the monthly rate per connection from $7.79 per water account/month to $6.24 per water account/month. Additionally, the scope of services was expanded to include a meter replacement program of approximately $11.4 million, wherein the Company replaced a majority of its meter infrastructure.

On September 10, 2019, the services agreement was amended and restated to, among other things, revise the scope of services to reflect upgrades and improvements to the FATHOM platform. Pursuant to the amended and restated agreement, GWM agreed to continue providing billing, customer service, and other support services for the Company's regulated utilities at a monthly rate of $6.43 per managed account.

As previously disclosed, based on the breach of the services agreement and cessation of services by GWM on December 20, 2019, the Company considers the services agreement to be terminated effective on that date.

Pursuant to the services agreement, the Company was entitled to quarterly royalty payments based on a percentage of certain of GWM's recurring revenues for a 10-year period, up to a maximum of $15.0 million, of which $2.3 million was received over the six year period. Accordingly, following the termination of the services agreement on December 20, 2019, the Company no longer received such royalty payments for periods after such date. During 2020, no FATHOM royalties were received and zero service fees were incurred. For the year ended December 31, 2019, the FATHOM royalties received totaled approximately $0.4 million and service fees incurred were $1.7 million.

## 9. ACCRUED EXPENSES

Accrued expenses at December 31, 2020 and December 31, 2019 consist of the following (in thousands):

| | December 31, 2020 | December 31, 2019 |
|---|---|---|
| Deferred compensation | $ 1,399 | $ 2,008 |
| Property taxes | 1,191 | 1,095 |
| Interest | 472 | 475 |
| Dividend payable | 550 | 519 |
| Asset retirement obligation | 697 | 697 |
| Accrued Bonus | 569 | 344 |
| Customer prepayments | 356 | 315 |
| Other accrued liabilities | 3,027 | 2,093 |
| Total accrued expenses | $ 8,261 | $ 7,546 |

## 10. FAIR VALUE

*Fair Value of Financial Instruments*

FASB ASC 820 establishes a fair value hierarchy that distinguishes between assumptions based on market data (observable inputs) and the Company's assumptions (unobservable inputs). The hierarchy consists of three levels, as follows:

- Level 1 - Quoted market prices in active markets for identical assets or liabilities
- Level 2 - Inputs other than Level 1 that are either directly or indirectly observable
- Level 3 - Unobservable inputs developed using the Company's estimates and assumptions, which reflect those that the Company believes market participants would use.

Financial assets and liabilities measured at fair value on a recurring basis as of December 31, 2020 and December 31, 2019 were as follows (in thousands):

| | December 31, 2020 | | | | December 31, 2019 | | | |
|---|---|---|---|---|---|---|---|---|
| | Level 1 | Level 2 | Level 3 | Total | Level 1 | Level 2 | Level 3 | Total |
| Asset/Liability Type: | | | | | | | | |
| HUF Funds - restricted cash(1) | $ — | $ 2,482 | $ — | $ 2,482 | $ — | $ 627 | $ — | $ 627 |
| Demand Deposit(2) | 2,135 | — | — | 2,135 | 2,132 | — | — | 2,132 |
| Certificate of Deposit - Restricted(1) | — | 790 | — | 790 | — | 705 | — | 705 |
| Long-term debt(3) | — | 127,724 | — | 127,724 | — | 121,075 | — | 121,075 |
| Acquisition Liability(4) | — | — | 838 | 838 | — | — | 838 | 838 |
| Total | $ 2,135 | $ 130,996 | $ 838 | $ 133,969 | $ 2,132 | $ 122,407 | $ 838 | $ 125,377 |

(1) HUF Funds - restricted cash and Certificate of Deposit - Restricted are presented on the Restricted cash line item of the Company's consolidated balance sheets. They are valued at amortized cost, which approximates fair value.

(2) Demand Deposit are presented on the Cash and cash equivalents line item of the Company's consolidated balance sheets. They are valued at amortized cost, which approximates fair value.

(3) The fair value of our debt was estimated based on interest rates considered available for instruments of similar terms and remaining maturities.

(4) As part of the Red Rock acquisition, the Company is required to pay to the seller a growth premium equal to $750 for each new account established within three specified growth premium areas, commencing in each area on the date of the first meter installation and ending on the earlier of ten years after such first installation date, or twenty years from the acquisition date. The fair value of the acquisition liability was calculated using a discounted cash flow technique which utilized unobservable inputs developed using the Company's estimates and assumptions. Significant inputs used in the fair value calculation are as follows: year of the first meter installation, total new accounts per year, years to complete full build out, and discount rate.

## 11. DEBT

The outstanding balances and maturity dates for short-term (including the current portion of long-term debt) and long-term debt as of December 31, 2020 and December 31, 2019 are as follows (in thousands):

| | December 31, 2020 | | December 31, 2019 | |
|---|---|---|---|---|
| | Short-term | Long-term | Short-term | Long-term |
| BONDS AND NOTES PAYABLE - | | | | |
| 4.38% Series A 2016, maturing June 2028 | — | 28,750 | $ — | $ 28,750 |
| 4.58% Series B 2016, maturing June 2036 | 1,917 | 84,333 | — | 86,250 |
| 1.20% WIFA Loan, maturing October 2032 | — | — | — | — |
| 4.65% Harquahala Loan, maturing January 2021 | 3 | — | 6 | 3 |
| 4.60% WIFA Loan, maturing March 2037 | — | — | 1 | 15 |
| | 1,920 | 113,083 | 7 | 115,018 |
| OTHER | | | | |
| Capital lease obligations | 115 | 136 | 110 | 251 |
| Debt issuance costs | — | (560) | — | (605) |
| Total debt | $ 2,035 | $ 112,659 | $ 117 | $ 114,664 |

***2016 Senior Secured Notes***

On June 24, 2016, the Company issued two series of senior secured notes with an aggregate 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 previously outstanding long-term tax exempt bonds, which were subject to an early redemption option at 103%, plus accrued interest, as a result of the the Company's initial public offering in the United States. As part of the refinancing of the long-term debt, the Company paid a prepayment penalty of $3.2 million and wrote off the remaining $2.2 million in capitalized loan fees related to the tax exempt bonds, which were recorded as additional interest expense in the second quarter of 2016. The senior secured notes are collateralized by a security interest in the Company's equity interest in its subsidiaries, including all payments representing profits and qualifying distributions. Debt issuance costs as of both December 31, 2020 and December 31, 2019 were $0.6 million.

The senior secured notes require the Company to 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. The debt service ratio increases to 1.25 for any fiscal quarter during the period from and after June 30, 2024. As of December 31, 2020, the Company was in compliance with its financial debt covenants.

***Eagletail Loans***

In May 2017, the Company acquired Eagletail Water Company ("Eagletail"). As part of the acquisition, the Company assumed two unsecured loans held by Eagletail. These loans are payable to the Water Infrastructure Finance Authority of Arizona ("WIFA") and Harquahala Valley Community Benefits Foundation ("Harquahala"). The WIFA loan bears an interest rate of 1.20% over a 20-year term, while the Harquahala loan bears an interest rate of 4.65% over a 15-year term. The Company paid off the WIFA loan in March 2019 and the Harquahala loan in January 2021.

In 2017, the Company entered into a second loan payable to WIFA ("2017 WIFA"), and no borrowings were made until 2018. The 2017 WIFA loan bears an interest rate of 4.60% over a 20-year term. The original loan amount was approximately $175,000, of which approximately $157,000 was forgiven. The Company paid off the 2017 WIFA loan in February 2020.

***Revolving Credit Line***

On April 20, 2018, the Company entered into an agreement with MidFirst Bank, a federally chartered savings association (the "MidFirst Bank Loan Agreement"), for a two-year revolving line of credit up to $8.0 million. The credit facility bore an interest rate equal to the London Interbank Offered Rate (LIBOR) plus 2.25%. In April 2019, the Company signed an amendment to the MidFirst Bank Loan Agreement, which extended the maturity of the line of credit to April 30, 2022 and modified the debt service coverage ratio to match the ratio required by the senior secured notes discussed above; all other terms remained unchanged. In April 2020, the Company terminated the MidFirst Bank Loan Agreement and entered into a loan agreement with Northern Trust Company, an Illinois banking corporation (the "Northern Trust Company Loan Agreement"), for a new two-year revolving line of credit up to $10.0 million with a maturity date of April 30, 2022. This new credit facility, which may be used to refinance existing indebtedness, to acquire assets to use and/or expand the Company's business, and for general corporate purposes, bears an interest rate equal to LIBOR plus 2.00% and has no unused line fee. As of December 31, 2020, we had no outstanding borrowings under this credit line. Unamortized debt issuance costs as of December 31, 2020 and 2019 were $46,000 and $49,000, respectively.

The Northern Trust Company Loan Agreement requires the Company to maintain a debt service coverage ratio of consolidated EBITDA to consolidated debt service of at least 1.10 to 1.00. The Northern Trust Company Loan Agreement also contains 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, 2022, the ratio drops to 1.20. As of December 31, 2020, the Company was in compliance with its financial debt covenant.

At December 31, 2020, the remaining aggregate annual maturities of debt and minimum lease payments under capital lease obligations for the years ended December 31 are as follows (in thousands):

| | Debt | Capital Lease Obligations |
|---|---|---|
| 2021 | $ 1,920 | $ 115 |
| 2022 | 3,833 | 88 |
| 2023 | 3,833 | 47 |
| 2024 | 3,833 | 1 |
| 2025 | 3,833 | — |
| Thereafter | 97,751 | — |
| Subtotal | 115,003 | 251 |
| Less: amount representing interest | — | (11) |
| Total | $ 115,003 | $ 240 |

## 12. INCOME TAXES

The Company utilizes the asset and liability method of accounting for income taxes. Under the asset and liability method, deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or all of the deferred tax assets will not be realized. As of December 31, 2020 and December 31, 2019, the Company did not have any valuation allowances or unrecognized tax benefits.

The income tax benefit from continuing operations for the years ended December 31, 2020 and 2019 is comprised of the following (in thousands):

| | 2020 | | |
|---|---|---|---|
| | Federal | State | Total |
| Current income tax expense | $ 1,710 | $ 270 | $ 1,980 |
| Deferred income tax expense (benefit) | $ (1,086) | $ (123) | $ (1,209) |
| Income tax expense | $ 624 | $ 147 | $ 771 |

| | 2019 | | |
|---|---|---|---|
| | Federal | State | Total |
| Current income tax expense | $ 314 | $ 220 | $ 534 |
| Deferred income tax expense | 670 | (42) | $ 628 |
| Income tax expense | $ 984 | $ 178 | $ 1,162 |

ASC 740, *Income Taxes*, prescribes the method to determine whether a deferred tax asset is realizable and significant weight is given to evidence that it can be objectively verified. As of December 31, 2020 and 2019, the Company recorded no valuation allowance.

The following table summarizes the Company's temporary differences between book and tax accounting that give rise to the deferred tax assets and deferred tax liabilities, as of December 31, 2020 and 2019 (in thousands):

| | December 31, 2020 | December 31, 2019 |
|---|---|---|
| DEFERRED TAX ASSETS: | | |
| Taxable meter deposits | 22 | $ 23 |
| Net operating loss carry forwards | — | 453 |
| Balterra intangible asset acquisition | 224 | 224 |
| Deferred gain on Sale of GWM | — | 1,067 |
| Deferred gain on ICFA funds received | 4,438 | 4,320 |
| Equity investment loss | — | 426 |
| AIAC | 3,706 | 1,264 |
| Other | 1,311 | 1,059 |
| Total deferred tax assets | 9,701 | 8,836 |
| Valuation allowance | — | — |
| Net deferred tax asset | 9,701 | 8,836 |
| DEFERRED TAX LIABILITIES: | | |
| Regulatory liability | (272) | (286) |
| CP Water intangible asset acquisition | (381) | (381) |
| ICFA intangible asset | (705) | (807) |
| Property, plant and equipment | (11,127) | (11,302) |
| Gain on condemnation of Valencia | 8 | (120) |
| Other Liabilities | (877) | (858) |
| Total deferred tax liabilities | (13,354) | (13,754) |
| Net deferred tax liability | $ (3,653) | $ (4,918) |

As of December 31, 2020, we have approximately no remaining net operating loss ("NOL") carry forwards.

The effective tax rates for the years ended December 31, 2020 and 2019 were 41.1% and 34.9%, respectively. The effective tax rate for the year ended December 31, 2020 was greater than the federal statutory rate of 21% primarily due to the impact of the regulatory liability recorded as a result of Rate Decision No. 76901, state income taxes, share based compensation, and IRC Section 4534 interest.

## 13. DEFERRED COMPENSATION AWARDS

### Stock-based compensation

Stock-based compensation related to option awards is measured based on the fair value of the award. The fair value of stock option awards is determined using a Black-Scholes option-pricing model. We recognize compensation expense associated with the options over the vesting period.

*2017 stock option grant*

In August 2017, GWRI's Board of Directors granted stock options to acquire 465,000 shares of GWRI's common stock to employees throughout the Company. The options were granted with an exercise price of $9.40, the market price of the Company's common shares on the NASDAQ Global Market at the close of business on August 10, 2017. The options vest over a four-year period, with 25% having vested in August 2018, 25% having vested in August 2019, 25% having vested in August 2020, and 25% vesting in August 2021. The options have a 10-year life. The Company will expense the $1.1 million fair value of the stock option grant ratably over the four-year vesting period. Stock-based compensation expense of $0.3 million was recorded for both years ended December 31, 2020 and 2019. As of December 31, 2020, 13,904 options have been exercised and 68,325 options have been forfeited with 382,771 outstanding.

*2019 stock option grant*

In August 2019, GWRI's Board of directors granted stock options to acquire 250,000 shares of GWRI's common stock to employees throughout the Company. The options were granted with an exercise price of $11.26, the market price of the Company's common shares on the NASDAQ Global Market at the close of business on August 13, 2019. The options vest over a four-year period, with 25% having vested in August 2020, 25% vesting in August 2021, 25% vesting in August 2022, and 25% vesting in August 2023. The options have a 10-year life. The Company will expense the $0.8 million fair value of the stock option grant ratably over the four-year vesting period. Stock-based compensation expense of $0.2 million and $0.1 million was recorded for the years ended December 31, 2020 and 2019, respectively. As of December 31, 2020, 1,144 options have been exercised and 5,714 options have been forfeited with 243,142 outstanding.

A summary of stock option activity is as follows (*in thousands, except option prices and years):*

| | Number of Options | | Weighted Average Exercise Price | Weighted Average Remaining Contractual Life | | Aggregate Intrinsic Value |
|---|---|---|---|---|---|---|
| **Options Outstanding at December 31, 2018** | 498 | $ | 9.02 | 7.0 | $ | 558.9 |
| **Options Vested at December 31, 2018** | 196 | $ | 8.43 | 4.4 | $ | 335.4 |
| Granted | 250 | $ | 11.26 | | | |
| Exercised | (67) | $ | 7.67 | | | |
| Forfeited | (49) | $ | 8.06 | | | |
| Cancelled | — | | | | | |
| **Options Outstanding at December 31, 2019** | 633 | $ | 10.12 | 8.4 | $ | 1,915.1 |
| **Options Vested at December 31, 2019** | 193 | $ | 9.40 | 9.6 | $ | 725.4 |
| Granted | — | | | | | |
| Exercised | (5) | $ | 9.83 | | | |
| Forfeited | (2) | $ | 10.85 | | | |
| Cancelled | — | | | | | |
| **Options Outstanding at December 31, 2020** | 626 | $ | 10.12 | 7.39 | $ | 2,683.6 |
| **Options Vested at December 31, 2020** | 348 | $ | 9.72 | 6.96 | $ | 1,629.7 |

**Phantom stock compensation**

The following table details total awards granted and the number of units outstanding as of December 31, 2020 along with the amounts paid to holders of phantom stock units ("PSUs") for the years ended December 31, 2020 and 2019 (in thousands, except unit amounts):

| | | | Amounts Paid For the Year Ended December 31, | | | |
|---|---|---|---|---|---|---|
| Grant Date | Units Granted | Units Outstanding | | 2020 | | 2019 |
| Q1 2016 | 34,830 | — | | — | | 29 |
| Q1 2017 | 22,712 | — | | 24 | | 80 |
| Q1 2018 | 30,907 | 2,576 | | 113 | | 109 |
| Q1 2019 | 32,190 | 13,413 | | 118 | | 86 |
| Q1 2020 | 22,481 | 16,861 | | 58 | | — |
| Total | 143,120 | 32,850 | $ | 313 | $ | 304 |

**Stock appreciation rights compensation**

The following table details the recipients of the stock appreciation rights ("SARs") awards, the grant date, units granted, exercise price, outstanding units as of December 31, 2020 and amounts paid during the years ended December 31, 2020 and 2019 (in thousands, except unit and per unit amounts):

| | | | | | Amounts Paid For the Year Ended December 31, | |
|---|---|---|---|---|---|---|
| Recipients | Grant Date | Units Granted | Exercise Price | Units Outstanding | 2020 | 2019 |
| Members of Management [(1)(3)] | Q1 2015 | 299,000 | $ 4.26 | 80,500 | 208 | 481 |
| Key Executives [(2)(4)] | Q2 2015 | 300,000 | $ 5.13 | — | 623 | 705 |
| Members of Management [(1)(5)] | Q3 2017 | 103,000 | $ 9.40 | 54,750 | 37 | 125 |
| Members of Management [(1)(6)] | Q1 2018 | 33,000 | $ 8.99 | 24,750 | — | 27 |
| Total | | 735,000 | | 160,000 | $ 868 | $ 1,338 |

(1) The SARs vest ratably over sixteen quarters from the grant date.
(2) The SARs vest over sixteen quarters, vesting 20% per year for the first three years, with the remainder, 40%, vesting in year four.
(3) The exercise price was determined to be the fair market value of one share of GWRC stock on the grant date of February 11, 2015.
(4) The exercise price was determined to be the fair market value of one share of GWRC stock on the grant date of May 8, 2015.
(5) The exercise price was determined to be the fair market value of one share of GWRI stock on the grant date of August 10, 2017.
(6) The exercise price was determined to be the fair market value of one share of GWRI stock on the grant date of March 12, 2018.

For the years ended December 31, 2020 and 2019, the Company recorded approximately $1.6 million and $1.4 million of compensation expense related to the PSUs and SARs, respectively. Based on GWRI's closing share price on December 31, 2020 (the last trading date of the quarter), deferred compensation expense to be recognized over future periods is estimated for the years ending December 31 as follows (in thousands):

| | PSUs | SARs |
|---|---|---|
| 2021 | 273 | 153 |
| 2022 | 112 | 13 |
| Total | 385 | 166 |

**Restricted stock compensation**

On May 7, 2020, the Company's stockholders approved the Global Water Resources, Inc. 2020 Omnibus Incentive Plan which allows restricted stock awards as a form of compensation. A restricted stock award ("RSA") represents the right to receive a share of the Company's common stock. RSAs vest over two to three years, beginning on the date of the grant. The Company assumes that forfeitures will be minimal and recognizes forfeitures as they occur, which results in a reduction in compensation expense. During the year ended December 31, 2020, 177,490 RSAs were issued. The Company recorded approximately $1.0 million of compensation expense related to the grant and partial vesting of RSAs for the year ended December 31, 2020. No compensation expense was recorded for the year ended December 31, 2019. The following table summarizes the RSA transactions for the year ended December 31, 2020:

| | Number of RSAs | Weighted Average Fair Value |
|---|---|---|
| Granted | 177,490 | $ 11.25 |
| Stock units vested and issued | 49,163 | 11.32 |
| Forfeited | — | — |
| Nonvested RSAs at end of period | 128,327 | $ 11.22 |

**14. SUPPLEMENTAL CASH FLOW INFORMATION**

The following is supplemental cash flow information for the years ended December 31, 2020 and 2019 (in thousands):

| | For the Year Ended December 31, | |
|---|---|---|
| | 2020 | 2019 |
| Supplemental cash flow information: | | |
| Cash paid for interest | $ 5,224 | $ 5,228 |
| Cash paid for taxes | $ 240 | $ 86 |
| Non-cash financing and investing activities: | | |
| Capital expenditures included in accounts payable and accrued liabilities | $ 586 | $ 1,500 |
| Contributions in aid of construction - loan forgiveness | $ — | $ 31 |
| Capital lease additions | $ — | $ 296 |

## 15. COMMITMENTS AND CONTINGENCIES

### Commitments

In September 2018, the Company's corporate office lease agreement was amended to include the rental of additional office space for the period of September 1, 2018 through February 28, 2019. In January 2019, the lease agreement was amended to extend the term of the lease, with a commencement date of March 1, 2019 and termination date of May 31, 2022. As such, the Company's monthly rent expense increased to approximately $15,000. Rent expense arising from the operating leases totaled approximately $0.2 million for both the years ended December 31, 2020 and 2019.

### Contingencies

From time to time, in the ordinary course of business, the Company may be subject to pending or threatened lawsuits in which claims for monetary damages are asserted. Management is not aware of any legal proceeding of which the ultimate resolution could materially affect our financial position, results of operations, or cash flows.