# Katy Prairie Conservancy

Financial Statements
and Independent Auditors' Report
for the years ended December 31, 2019 and 2018

# Katy Prairie Conservancy

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Blazek & Vetterling
CERTIFIED PUBLIC ACCOUNTANTS

# Independent Auditors' Report

To the Board of Directors of
Katy Prairie Conservancy:

We have audited the accompanying financial statements of Katy Prairie Conservancy, which comprise the statements of financial position as of December 31, 2019 and 2018 and the related statements of activities, of functional expenses, and of cash flows for the years then ended, and the related notes to the financial statements.

**Management's Responsibility for the Financial Statements –** Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

**Auditors' Responsibility –** Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform our audits to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

**Opinion –** In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Katy Prairie Conservancy as of December 31, 2019 and 2018 and the changes in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Blazek & Vetterling

June 30, 2020

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## Katy Prairie Conservancy

Statements of Financial Position as of December 31, 2019 and 2018

| | 2019 | 2018 |
|---|---|---|
| ASSETS | | |
| Cash | $ 2,677,696 | $ 2,253,546 |
| Receivables and other assets | 9,751 | 5,489 |
| Contributions receivable *(Note 4)* | 209,785 | 228,934 |
| Property, net *(Note 6)* | 31,112,876 | 31,224,241 |
| Investments *(Note 5)* | 874,709 | 709,494 |
| TOTAL ASSETS | $ 34,884,817 | $ 34,421,704 |
| LIABILITIES AND NET ASSETS | | |
| Liabilities: | | |
| Accounts payable and accrued expenses | $ 101,306 | $ 125,375 |
| Accrued interest expense | 141,421 | 127,579 |
| Note payable *(Note 7)* | 8,081,162 | 8,081,162 |
| Total liabilities | 8,323,889 | 8,334,116 |
| Commitments *(Note 12)* | | |
| Net assets: | | |
| Without donor restrictions *(Note 8)* | 17,377,099 | 16,731,365 |
| With donor restrictions *(Notes 9 and 10)* | 9,183,829 | 9,356,223 |
| Total net assets | 26,560,928 | 26,087,588 |
| TOTAL LIABILITIES AND NET ASSETS | $ 34,884,817 | $ 34,421,704 |

*See accompanying notes to financial statements.*

## Katy Prairie Conservancy

Statement of Activities for the year ended December 31, 2019

| | WITHOUT DONOR RESTRICTIONS | WITH DONOR RESTRICTIONS | TOTAL |
|---|---|---|---|
| REVENUE: | | | |
| Contributed revenue: | | | |
| Contributions | $ 342,171 | $ 602,675 | $ 944,846 |
| Contributed conservation easements | 2,687,705 | | 2,687,705 |
| Special events | 287,014 | | 287,014 |
| Direct donor benefit costs | (30,300) | | (30,300) |
| Pipeline easement revenue | 389,800 | | 389,800 |
| Cattle sales and other ranch income | 378,644 | | 378,644 |
| Lease and other income | 240,634 | | 240,634 |
| Net investment return | 35,526 | 129,724 | 165,250 |
| Total revenue | 4,331,194 | 732,399 | 5,063,593 |
| Net assets released from restrictions: | | | |
| Redesignation of donor restrictions | 326,612 | (326,612) | |
| Program expenditures | 389,882 | (389,882) | |
| Land acquisition | 88,299 | (88,299) | |
| Satisfaction of time restriction | 100,000 | (100,000) | |
| Total | 5,235,987 | (172,394) | 5,063,593 |
| EXPENSES: | | | |
| Program services: | | | |
| Land conservation | 3,392,815 | | 3,392,815 |
| Land stewardship | 432,145 | | 432,145 |
| Ranch programs | 282,659 | | 282,659 |
| Public outreach | 165,795 | | 165,795 |
| Total program services | 4,273,414 | | 4,273,414 |
| Supporting services: | | | |
| Management and general | 218,241 | | 218,241 |
| Fundraising | 98,598 | | 98,598 |
| Total expenses | 4,590,253 | | 4,590,253 |
| CHANGES IN NET ASSETS | 645,734 | (172,394) | 473,340 |
| Net assets, beginning of year | 16,731,365 | 9,356,223 | 26,087,588 |
| Net assets, end of year | $ 17,377,099 | $ 9,183,829 | $ 26,560,928 |

*See accompanying notes to financial statements.*

## Katy Prairie Conservancy

Statement of Activities for the year ended December 31, 2018

| | WITHOUT DONOR RESTRICTIONS | WITH DONOR RESTRICTIONS | TOTAL |
|---|---|---|---|
| REVENUE: | | | |
| Contributed revenue: | | | |
| Contributions | $ 503,920 | $ 2,499,615 | $ 3,003,535 |
| Special events | 162,875 | | 162,875 |
| Direct donor benefit costs | (22,675) | | (22,675) |
| Cattle sales and other ranch income | 384,944 | | 384,944 |
| Lease income | 141,175 | | 141,175 |
| Net investment return | (10,769) | (32,975) | (43,744) |
| Gain on sale of land | 627,589 | | 627,589 |
| Stream mitigation and other income | 259,273 | | 259,273 |
| Total revenue | 2,046,332 | 2,466,640 | 4,512,972 |
| Net assets released from restrictions: | | | |
| Program expenditures | 725,190 | (725,190) | |
| Land acquisition | 956,000 | (956,000) | |
| Total | 3,727,522 | 785,450 | 4,512,972 |
| EXPENSES: | | | |
| Program services: | | | |
| Land conservation | 776,310 | | 776,310 |
| Land stewardship | 585,606 | | 585,606 |
| Ranch programs | 269,825 | | 269,825 |
| Public outreach | 271,061 | | 271,061 |
| Total program services | 1,902,802 | | 1,902,802 |
| Supporting services: | | | |
| Management and general | 223,215 | | 223,215 |
| Fundraising | 85,443 | | 85,443 |
| Total expenses | 2,211,460 | | 2,211,460 |
| CHANGES IN NET ASSETS | 1,516,062 | 785,450 | 2,301,512 |
| Net assets, beginning of year | 15,215,303 | 8,570,773 | 23,786,076 |
| Net assets, end of year | $ 16,731,365 | $ 9,356,223 | $ 26,087,588 |

*See accompanying notes to financial statements.*

## Katy Prairie Conservancy

Statement of Functional Expenses for the year ended December 31, 2019

| | LAND CONSERVATION | LAND STEWARDSHIP | RANCH PROGRAMS | PUBLIC OUTREACH | TOTAL PROGRAM SERVICES | MANAGEMENT AND GENERAL | FUNDRAISING | TOTAL |
|---|---|---|---|---|---|---|---|---|
| Salaries and related expenses | $ 111,725 | $ 176,461 | $ 14,046 | $ 114,234 | $ 416,466 | $ 92,169 | $ 66,911 | $ 575,546 |
| Land easements purchased and donated | 2,690,541 | | | | 2,690,541 | | | 2,690,541 |
| Professional fees | 269,325 | 13,803 | 38,349 | 7,246 | 328,723 | 86,791 | 6,705 | 422,219 |
| Interest | 257,367 | | | | 257,367 | | | 257,367 |
| Depreciation | | 92,262 | 58,802 | | 151,064 | 5,980 | | 157,044 |
| Contracted services | 10,000 | 61,200 | 58,002 | 2,518 | 131,720 | | 1,251 | 132,971 |
| Supplies, materials, and postage | 1,538 | 8,024 | 46,895 | 12,615 | 69,072 | 4,126 | 6,574 | 79,772 |
| Office space | 13,242 | 20,525 | 6,038 | 13,904 | 53,709 | 10,594 | 7,945 | 72,248 |
| Equipment repair and maintenance | 438 | 3,700 | 23,411 | | 27,549 | 10,525 | 3,376 | 41,450 |
| Insurance | 4,473 | 6,934 | 12,289 | 4,697 | 28,393 | 3,579 | 2,684 | 34,656 |
| Property taxes | | 23,015 | 10,875 | | 33,890 | | | 33,890 |
| Travel and meetings | 12,540 | 2,448 | 4,725 | 6,195 | 25,908 | 1,973 | | 27,881 |
| Permits and fees | 10,707 | 2,242 | 7,516 | 542 | 21,007 | 606 | 1,321 | 22,934 |
| Utilities | 2,260 | 10,479 | | 3,469 | 16,208 | 1,808 | 1,357 | 19,373 |
| Contract restoration | 659 | 11,052 | | | 11,711 | | | 11,711 |
| Other | 8,000 | | 1,711 | 375 | 10,086 | 90 | 474 | 10,650 |
| Total expenses | $ 3,392,815 | $ 432,145 | $ 282,659 | $ 165,795 | $ 4,273,414 | $ 218,241 | $ 98,598 | $ 4,590,253 |

*See accompanying notes to financial statements.*

## Katy Prairie Conservancy

Statement of Functional Expenses for the year ended December 31, 2018

| | LAND CONSERVATION | LAND STEWARDSHIP | RANCH PROGRAMS | PUBLIC OUTREACH | TOTAL PROGRAM SERVICES | MANAGEMENT AND GENERAL | FUNDRAISING | TOTAL |
|---|---|---|---|---|---|---|---|---|
| Salaries and related expenses | $ 120,924 | $ 198,593 | $ 6,453 | $ 213,873 | $ 539,843 | $ 98,765 | $ 70,366 | $ 708,974 |
| Professional fees | 326,897 | 3,470 | 27,070 | 3,600 | 361,037 | 89,339 | 1,000 | 451,376 |
| Interest | 259,625 | | 2,304 | | 261,929 | | | 261,929 |
| Depreciation | 2,620 | 102,078 | 60,811 | | 165,509 | | | 165,509 |
| Contracted services | 6,000 | 4,678 | 43,512 | 2,874 | 57,064 | | 1,078 | 58,142 |
| Supplies, materials and postage | 4,431 | 10,657 | 61,387 | 8,319 | 84,794 | 3,721 | 3,963 | 92,478 |
| Office space | 10,146 | 19,886 | | 22,893 | 52,925 | 9,695 | 1,757 | 64,377 |
| Equipment repair and maintenance | 2,567 | 5,610 | 21,942 | | 30,119 | 9,191 | 3,297 | 42,607 |
| Insurance | 5,105 | 10,007 | 5,952 | 11,520 | 32,584 | 4,879 | 884 | 38,347 |
| Property taxes | | 26,962 | 14,344 | 64 | 41,370 | | | 41,370 |
| Travel and meetings | 14,658 | 2,943 | 3,832 | 2,070 | 23,503 | 2,388 | 942 | 26,833 |
| Permits and fees | 15,439 | 619 | 13,037 | 264 | 29,359 | 3,450 | 736 | 33,545 |
| Utilities | 1,869 | 12,633 | 5,352 | 5,240 | 25,094 | 1,787 | 323 | 27,204 |
| Contracted restoration | | 187,470 | | | 187,470 | | | 187,470 |
| Other | 6,029 | | 3,829 | 344 | 10,202 | | 1,097 | 11,299 |
| Total expenses | $ 776,310 | $ 585,606 | $ 269,825 | $ 271,061 | $ 1,902,802 | $ 223,215 | $ 85,443 | $ 2,211,460 |

*See accompanying notes to financial statements.*

## Katy Prairie Conservancy

Statements of Cash Flows for the years ended December 31, 2019 and 2018

| | 2019 | 2018 |
|---|---|---|
| CASH FLOWS FROM OPERATING ACTIVITIES: | | |
| Changes in net assets | $ 473,340 | $ 2,301,512 |
| Adjustments to reconcile changes in net assets to net cash provided by operating activities: | | |
| Contributions restricted for land acquisition | | (1,710,000) |
| Depreciation | 157,044 | 165,509 |
| Gain on sale or disposal of property | (9,587) | (623,278) |
| Change in interest in pooled investments | (129,724) | 32,975 |
| Net realized and unrealized (gain) loss on investments | (32,705) | 11,357 |
| Changes in operating assets and liabilities: | | |
| Receivables and other assets | (4,262) | 16,514 |
| Contributions receivable (other than for land acquisition) | 19,149 | 165,093 |
| Accounts payable and accrued expenses | (24,069) | (32,790) |
| Accrued interest expense | 13,842 | (47,965) |
| Net cash provided by operating activities | 463,028 | 278,927 |
| CASH FLOWS FROM INVESTING ACTIVITIES: | | |
| Purchases of land and improvements | (57,899) | (20,372) |
| Purchases of cattle and equipment | (39,739) | (84,957) |
| Purchases of investments | | (175,753) |
| Proceeds from sale of land | | 1,850,000 |
| Proceeds from sale of cattle and equipment | 61,546 | 56,855 |
| Net change in money market mutual funds held as investments | (2,786) | (683) |
| Net cash provided (used) by investing activities | (38,878) | 1,625,090 |
| CASH FLOWS FROM FINANCING ACTIVITIES: | | |
| Repayment of note payable | | (2,240,315) |
| Proceeds from contributions restricted for land acquisition | | 1,710,000 |
| Net cash used by financing activities | | (530,315) |
| NET CHANGE IN CASH | 424,150 | 1,373,702 |
| Cash, beginning of year | 2,253,546 | 879,844 |
| Cash, end of year | $ 2,677,696 | $ 2,253,546 |

*Supplemental disclosure of cash flow information:*

| | | |
|---|---|---|
| Interest paid | $243,524 | $307,590 |

*See accompanying notes to financial statements.*

**NOTE 1 – ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES**

Organization – Katy Prairie Conservancy (the Conservancy) is a Texas nonprofit corporation established to protect and enhance critical and sustainable portions of the Katy Prairie and coastal prairie ecosystems. The Katy Prairie lies in the Texas coastal plain and encompasses over a thousand square miles; the prairie is bounded by the Brazos River on the west, pine-hardwood forest on the north, and the City of Houston on the east. The ecosystem is comprised of a variety of habitats, including agricultural wetlands, depressional wetlands, riparian corridors, and coastal grasslands. The Conservancy works closely with farmers, ranchers, conservation entities, and experts in various fields to develop management plans that are ecologically responsible and environmentally sound for each of its properties, including developing sustainable grazing techniques that enhance water retention and minimize erosion in the Cypress Creek Watershed. The coastal prairie ecosystem also lies in the Texas coastal plain and includes the Katy Prairie area (Fort Bend, Harris, and Waller counties), as well as six other counties (Austin, Brazoria, Colorado, Jackson, Matagorda, and Wharton). All nine counties are located within the Gulf Coast region and exhibit similar habitats.

Federal income tax status – The Conservancy is exempt from federal income tax under §501(c)(3) of the Internal Revenue Code and is classified as a public charity under §509(a)(1).

Cash is held as demand deposits. Bank deposits exceed the federally insured limit per depositor per institution.

Contributions receivable that are expected to be collected within one year are reported at net realizable value. Amounts expected to be collected in future years are discounted to estimate the present value of future cash flows, if material. Discounts are computed using risk-free interest rates applicable to the years in which the promises are received. Amortization of discounts is included in contributions revenue. An allowance for uncollectible receivables is provided when it is believed balances may not be collected in full. The adequacy of the allowance at the end of each period is determined using a combination of historical loss experience and a donor-by-donor analysis of balances.

Property is reported at cost, if purchased, or at estimated fair value at the date of gift, if donated. The Conservancy's policy is to capitalize property acquisitions over $1,500. Land improvements are depreciated on a straight-line basis over 15 to 25 years. Depreciation of cattle and equipment is provided on an accelerated basis using lives of 5 to 7 years. Certain land is subject to conservation easements or other deed restrictions. Costs related to wetland mitigation and conservation maintenance are expensed as incurred.

Investments are reported at fair value. Net investment return consists of interest and dividends, realized and unrealized gains and losses, net of external and direct internal investment expenses.

Net asset classification – Net assets, revenue, gains, and losses are classified based on the existence or absence of donor-imposed restrictions, as follows:

- *Net assets without donor restrictions* are not subject to donor-imposed restrictions even though their use may be limited in other respects such as by contract or board designation.

- *Net assets with donor restrictions* are subject to donor-imposed restrictions. Restrictions may be temporary in nature, such as those that will be met by the passage of time or use for a purpose specified by the donor, or may be perpetual in nature, where the donor stipulates that resources be maintained in perpetuity. Net assets are released from restrictions when the stipulated time has elapsed, or purpose has been fulfilled, or both. Contributions of long-lived assets and of assets restricted for acquisition of long-lived assets are released when those assets are placed in service unless the donor also has placed a time restriction on the use of the long-lived asset, in which case the release occurs over the term of the time restriction. Donor-restricted endowment earnings are released when those earnings are appropriated in accordance with spending policies and are used for the stipulated purpose. The Conservancy reports land purchased with federal funds which require permanent easements as perpetual net assets.

<u>Revenue recognition</u> – The Conservancy recognizes revenue and other income from a variety of sources including hunting lease contracts, cattle and hay sales, contracts for pipeline easements, and mitigation funding for stream and wetland conservation projects. Conservation projects and hunting lease contracts are recognized over time based upon the completion of a project or for hunting leases as access to the land is provided to the lessee. All other sources of revenue are recognized at a point in time when the sale is completed or easement agreement is executed. There are no contract assets or liabilities related to these transactions.

<u>Contributions</u> are recognized as revenue at fair value when an unconditional commitment is received from a donor. Contributions received with donor stipulations that limit their use are classified as *with donor restrictions*. Conditional contributions are subject to one or more barriers that must be overcome before the Conservancy is entitled to receive or retain funding. Conditional contributions are recognized in the same manner when the conditions have been met. Funding received before conditions are met is reported as refundable contributions. At December 31, 2019, approximately 50% of contributions are from two donors. At December 31, 2018, approximately 75% of contributions are from three donors.

<u>Non-cash contributions</u> – Donated property, conservation easements, materials, and use of facilities are recognized at fair value as contributions when an unconditional commitment is received from the donor. The related expense is recognized as the item is used. Contributions of services are recognized when services received (a) create or enhance nonfinancial assets or (b) require specialized skills, are provided by individuals possessing those skills, and would typically need to be purchased if not provided by donation.

<u>Special events revenue</u> is the total amount paid by sponsors and attendees of an event and includes elements of both contributions and exchange transactions. Special event revenue is recognized when the event occurs. Direct donor benefit costs represent the cost of goods and services provided to attendees of the special events.

<u>Conservation easements</u> represent rights to restrict the use, access, and development of certain properties. In conformity with the practice followed by many land trusts, conservation easements purchased or donated are not recorded as assets in the statement of financial position. The Conservancy believes the conservation easements do not have a future value as the property interest held by the Conservancy provides no affirmative rights beyond the obligation to monitor and enforce the terms of the easements (with the exception of potential proceeds in a condemnation action, which proceeds must be used consistently with the original conservation purpose). Costs incurred in obtaining easements are expensed as incurred. Contributed easements and purchased easements acquired are recognized at the estimated fair value of the easement on the date of donation as conservation contributions and expensed in the statement of activities.

Functional allocation of expenses – Expenses are reported by their functional classification. Program services are the direct conduct or supervision of activities that fulfill the purposes for which the organization exists. Fundraising activities include the solicitation of contributions of money, securities, materials, facilities, other assets, and time. Management and general activities are not directly identifiable with specific program or fundraising activities. Expenses that are attributable to more than one activity are allocated among the activities benefitted. Salaries and related costs and office space have been allocated between program, management and general, and fundraising on the basis of estimated time and effort expended.

Estimates – Management must make estimates and assumptions to prepare financial statements in accordance with generally accepted accounting principles. These estimates and assumptions affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, the amounts of reported revenue and expenses, and the allocation of expenses among various functions. Actual results could vary from the estimates that were used.

## NOTE 2 – ADOPTION OF ACCOUNTING STANDARDS UPDATES

The Conservancy adopted ASU 2014-09, *Revenue from Contracts with Customers (Topic 606)*. The core principle of the new guidance is that the entity should recognize revenue in an amount that reflects the consideration to which it expects to be entitled in exchange for transferred goods or services using a 5-step process to determine when performance obligations are satisfied and revenue is recognized and requires expanded disclosures related to the nature, amount, timing and uncertainty of revenue and cash flows from contracts with customers. The Conservancy adopted the new standard effective January 1, 2018, using the full retrospective method. The timing and amount of revenue recognized previously is consistent with how revenue is recognized under this ASU and therefore, adoption of this ASU had no impact on total beginning net assets or changes in net assets for 2018, but resulted in additional dislosures and changes in presentation.

The Conservancy also adopted ASU 2018-08, *Not-for-Profit Entities (Topic 958): Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made*. The amendments in this ASU clarify and improve current guidance about whether a transfer of assets (or the reduction, settlement, or cancellation of liabilities) is a contribution or an exchange transaction and provide additional guidance on determining whether a contribution is conditional or unconditional. The Conservancy adopted the new standard effective January 1, 2019. Adoption of this ASU had no impact on total net assets or total changes in net assets for 2018.

## NOTE 3 – LIQUIDITY AND AVAILABILITY OF RESOURCES

Financial assets available for general expenditure, that is, without donor or other restrictions limiting their use within one year of December 31 comprise the following:

| | 2019 | 2018 |
|---|---|---|
| Financial assets: | | |
| Cash | $ 2,677,696 | $ 2,253,546 |
| Receivables | 3,635 | |
| Contributions receivable | 209,785 | 228,934 |
| Investments | 874,709 | 709,494 |
| Total financial assets | 3,765,825 | 3,191,974 |
| Less financial assets not available for general expenditure: | | |
| Endowment investments | (674,140) | (544,416) |
| Other donor-restricted assets subject to satisfaction of restriction and passage of time | (953,657) | (379,378) |
| Board-designated for conservation easement – stewardship and defense | (299,881) | (273,756) |
| Total financial assets available for general expenditure | $ 1,838,147 | $ 1,994,424 |

The Conservancy is substantially supported by contributions, program revenues such as hunting and agricultural leases and revenue from the Warren Ranch, and the sale of stream mitigation credits. As part of the Conservancy's liquidity management, it has a policy to structure its financial assets to be available as its general expenditures, liabilities, and other obligations become due. For purposes of analyzing resources available to meet general expenditures over a 12-month period, the Conservancy considers all expenditures related to its ongoing activities to be general expenditures, including planned expenditures for property and debt retirement.

The Conservancy's Board of Directors (the Board) has designated a portion of its resources without donor restrictions for specific purposes as board-designated. A portion of these funds are invested for long-term appreciation and current income, but remain available to be spent at the Board's discretion.

The organization has a goal to maintain available financial assets totaling approximately $300,000 in cash and investments to meet 90 days of normal operating expenses.

## NOTE 4 – CONTRIBUTIONS RECEIVABLE

Contributions receivable at December 31, 2019 are expected to be collected as follows:

| | |
|---|---|
| Within one year | $ 199,785 |
| In one to five years | 10,000 |
| Total contributions receivable | $ 209,785 |

At December 31, 2019, 67% of contributions receivable are from two donors. At December 31, 2018, 87% of contributions receivable are from one donor.

At December 31, 2019, approximately $1,228,000 in conditional government grant awards for land acquisition and conservation have not been recognized as the conditions have not yet been met.

## NOTE 5 – INVESTMENTS AND FAIR VALUE MEASUREMENTS

Investments consist of the following:

| | 2019 | 2018 |
|---|---|---|
| Endowments | $ 674,140 | $ 544,416 |
| Board-designated | 200,569 | 165,078 |
| Total investments | $ 874,709 | $ 709,494 |

*Fair Value*

Generally accepted accounting principles require that certain assets and liabilities be reported at fair value and establish a hierarchy that prioritizes inputs used to measure fair value. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The three levels of the fair value hierarchy are as follows:

- *Level 1* – Inputs are unadjusted quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the reporting date.
- *Level 2* – Inputs are other than quoted prices included in Level 1, which are either directly observable or can be derived from or corroborated by observable market data at the reporting date.
- *Level 3* – Inputs are not observable and are based on the reporting entity's assumptions about the inputs market participants would use in pricing the asset or liability. Inputs are unobservable for the asset and include situations where there is little, if any, market activity for the investment. The types of investments in Level 3 include funds where the fair value for portfolio investments is estimated by the fund management using valuation methodologies that consider a range of factors including, but not limited to, the price at which the investment was acquired, the nature of the investment, local market conditions, trading values on public exchanges for comparable securities, current and projected operating performance, financial condition, and financing transactions subsequent to the acquisition of the investment.

Assets measured at fair value at December 31, 2019 are as follows:

| | LEVEL 1 | LEVEL 2 | LEVEL 3 | TOTAL |
|---|---|---|---|---|
| Investments: | | | | |
| Interest in CNLM investments | | | $ 674,140 | $ 674,140 |
| Large cap exchanged-traded funds | $ 134,813 | | | 134,813 |
| Common stock | 62,287 | | | 62,287 |
| Money market mutual funds | 3,469 | | | 3,469 |
| Total assets measured at fair value | $ 200,569 | $ 0 | $ 674,140 | $ 874,709 |

Assets measured at fair value at December 31, 2018 are as follows:

| | LEVEL 1 | LEVEL 2 | LEVEL 3 | TOTAL |
|---|---|---|---|---|
| Investments: | | | | |
| Interest in CNLM investments | | | $ 544,416 | $ 544,416 |
| Large cap exchanged-traded funds | $ 108,246 | | | 108,246 |
| Common stock | 56,149 | | | 56,149 |
| Money market mutual funds | 683 | | | 683 |
| Total assets measured at fair value | $ 165,078 | $ 0 | $ 544,416 | $ 709,494 |

Valuation methods used for assets measured at fair value are as follows:

- *Interest in the Center for Natural Land Management (CNLM) investments* is based on the percentage of the Conservancy's pooled shares held at CNLM applied to the total net asset value of the fund.
- *Exchange-traded funds* and *common stock* are valued at the closing price reported on the active market on which the individual securities are traded.
- *Mutual funds* are valued at the reported net asset value.

These valuation methods may produce a fair value that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while the Conservancy believes its valuation methods are appropriate, the use of different methods or assumptions could result in a different fair value measurement at the reporting date.

Changes in the fair value of Level 3 assets are as follows:

| | |
|---|---|
| Balance at January 1, 2018 | $ 577,390 |
| Change in interest in pooled investments | (32,974) |
| Balance at December 31, 2018 | 544,416 |
| Change in interest in pooled investments | 129,724 |
| Balance at December 31, 2019 | $ 674,140 |

Investments are exposed to various risks such as interest rate, market, and credit risks. Because of these risks, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such changes could materially affect the amounts reported in the statement of financial position and statement of activities.

## NOTE 6 – PROPERTY

Property consists of the following:

| | 2019 | 2018 |
|---|---|---|
| Land, undivided interest in Warren Ranch | $ 12,461,189 | $ 12,461,189 |
| Land | 17,547,820 | 17,489,921 |
| Land improvements | 1,590,956 | 1,590,956 |
| Construction in progress – land improvements | 135,659 | 135,659 |
| Cattle and equipment | 413,615 | 441,682 |
| Total | 32,149,239 | 32,119,407 |
| Accumulated depreciation | (1,036,363) | (895,166) |
| Property, net | $ 31,112,876 | $ 31,224,241 |

Nearly 20,000 acres of land are protected on the Katy Prairie through fee acquisition, conservation easements, or public ownership. The Conservancy owns approximately 13,400 acres. Approximately 6,000 acres of the Conservancy's land are owned as a 71.23346% undivided interest in a working cattle ranch. In addition, the Conservancy has protected an additional 6,005 acres in Matagorda and Jackson counties, including the 5,332 acre Spread Oaks Ranch, as part of its work to protect coastal prairie.

Grants from federal agencies have funded a portion of the purchase price of various tracts of land. Under the terms of these agreements, the Conservancy must inform the federal agencies before selling the land and must repay the grant if the amount is not reinvested in similar conservation land. The Conservancy's total land purchases with federal funds are reflected as perpetually-restricted net assets totaling $7,176,143 at December 31, 2019 and 2018.

## NOTE 7 – NOTE PAYABLE

The Conservancy has a note payable agreement with a private foundation collateralized by land with annual interest (3%) payments only until June 2029 when the principal becomes due. Repayment covenants require 75% of the future proceeds of land sales and mitigation revenue be used to repay the loan until the $3 million in principal is repaid, at which time 50% of all proceeds must be paid to the private foundation until an additional $2 million in principal is repaid. After $5 million in principal is paid, the Conservancy will still be required to use 25% of all proceeds from mitigation revenue and any land sales until the full amount of the loan is paid. The outstanding balance at December 31, 2019 and 2018 is $8,081,162.

No principal payments are due in the next five years. Interest expense in 2019 and 2018 was $257,367 and $259,625, respectively.

## NOTE 8 – NET ASSETS WITHOUT DONOR RESTRICTIONS

Net assets without donor restrictions consist of the following:

| | 2019 | 2018 |
|---|---|---|
| Undesignated | $ 1,221,647 | $ 490,673 |
| Property, net of notes payable and perpetually-restricted land | 15,855,571 | 15,966,936 |
| Board-designated for conservation easement – stewardship and defense | 299,881 | 273,756 |
| Total net assets without donor restrictions | $ 17,377,099 | $ 16,731,365 |

The conservation easement – stewardship and defense funds were designated to provide a long-term, ongoing source of income to cover the annual cost associated with monitoring and managing the Conservancy's portfolio of conservation easements and to be available to cover extraordinary expenses associated with managing and defending an easement, should its validity be at risk.

## NOTE 9 – NET ASSETS WITH DONOR RESTRICTIONS

Net assets with donor restrictions are restricted as follows:

| | 2019 | 2018 |
|---|---|---|
| Subject to expenditure for specified purpose: | | |
| Land acquisition | $ 685,301 | $ 754,000 |
| Public outreach and education | 257,619 | 14,620 |
| Land restoration | 164,874 | 111,574 |
| Research and planning | 85,752 | 216,391 |
| Easement stewardship | 40,000 | |
| Capacity building | | 326,613 |
| Other | | 12,466 |
| Total subject to expenditure for specified purpose | 1,233,546 | 1,435,664 |
| Subject to passage of time: | | |
| Contributions receivable that are not restricted by donors, but which are unavailable for expenditure until due | 100,000 | 200,000 |
| Endowment subject to spending policy and appropriation: | | |
| Stream mitigation long-term management | 674,140 | 544,416 |
| Land purchased with federal funds which require permanent easement | 7,176,143 | 7,176,143 |
| Total net assets with donor restrictions | $ 9,183,829 | $ 9,356,223 |

## NOTE 10 – ENDOWMENT FUNDS

The Conservancy entered into an agreement with the CNLM to establish an endowment for funding the perpetual management and stewardship of Phase I of its stream mitigation bank. All amounts maintained at CNLM will be invested and held for the benefit of the management of the bank parcel on behalf of the Conservancy. Once the U. S. Army Corps of Engineers closes out the bank, the Conservancy will be responsible for the bank's long-term management and maintenance. At the time of close out, the Conservancy may request disbursements on or within five calendar days after the start of each quarter from CNLM to monitor, maintain, and manage the stream mitigation bank. The Conservancy may withdraw up to 4.5% of the fair market value of the endowment fund each fiscal year. Additional disbursements above 4.5% of the fair market value of the endowment fund may be requested for capital and emergency expenses if approved in advance by the U. S. Army Corps of Engineers. These funds cannot be distributed to any other party without the express permission of the Conservancy. The investments held by the CNLM are in pooled accounts and are invested for the benefit of the Conservancy in the Commonfund at December 31, 2019.

Donor-restricted endowment funds are subject to the Texas Uniform Prudent Management of Institutional Funds Act (TUPMIFA). The Board has interpreted TUPMIFA as allowing the Conservancy to appropriate for expenditure or accumulate as much of a fund as it determines is prudent for the uses, benefits, purposes, and duration for which the endowment fund was established, subject to explicit donor stipulations. Donor-restricted endowment net assets are classified as *net assets with donor restrictions* until appropriated in accordance with spending policies and used for the stipulated purpose, if any. In the absence of explicit donor stipulations otherwise, the Conservancy classifies contributions to an endowment as *net assets with donor restrictions* required to be maintained in perpetuity. Contributions that donors have specified do not have to be maintained in perpetuity and unappropriated investment earnings on donor-restricted endowments are classified as *net assets with donor restrictions* available for distribution. The Board has interpreted TUPMIFA as not precluding the Conservancy from spending below the amount required to be maintained in perpetuity subject to prudent standards. An endowment fund is *underwater* if the fair value of the fund's investments falls below the amount required to be maintained in perpetuity because of declines in the fair value of investments and/or continued appropriation and spending in accordance prudent measures.

Changes in endowment net assets are as follows:

| | WITH DONOR RESTRICTIONS | | |
|---|---|---|---|
| | ACCUMULATED NET INVESTMENT RETURN | REQUIRED TO BE MAINTAINED IN PERPETUITY | TOTAL |
| Endowment net assets, December 31, 2017 | $ 123,822 | $ 453,569 | $ 577,391 |
| Change in interest in pooled investments | (32,975) | | (32,975) |
| Endowment net assets, December 31, 2018 | 90,847 | 453,569 | 544,416 |
| Change in interest in pooled investments | 129,724 | | 129,724 |
| Endowment net assets, December 31, 2019 | $ 220,571 | $ 453,569 | $ 674,140 |

**Investment Policy**

The Conservancy has adopted investment policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of the endowment assets. To satisfy its long-term rate-of-return objectives, the Conservancy relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). The Conservancy targets a diversified asset allocation through the Commonfund that places emphasis on a blend of equity-based and fixed-income investments to achieve its long-term return objectives within prudent risk constraints.

## NOTE 11 – STREAM MITIGATION TRANSACTIONS

The Conservancy has entered into a joint venture partnership to create a 500-acre stream mitigation umbrella bank on the Warren Ranch. The bank will provide stream mitigation credits to be sold to entities whose projects require stream mitigation credits under Section 404 of the Clean Water Act. In connection with the stream mitigation bank, the Conservancy, as a part of the joint venture partnership, is responsible for the long-term stewardship of the stream bank area after the bank is completed and the regulatory agencies have determined that all objectives have been met and have approved the closeout of the bank.

In June 2015, the Conservancy entered into an agreement with its joint venture partner to create a perpetual long-term management fund for the management and long-term stewardship and monitoring activities of the stream bank properties. The Conservancy will manage the fund and the income generated until the bank is closed out (in approximately 8 years).

The Conservancy will use the interest generated from the corpus to maintain and manage the bank in perpetuity. In connection with the Phase I stewardship, the joint venture partner paid approximately $70,000 to the Long Term Management Fund and $364,000 to the perpetually-restricted Stewardship Endowment Fund. The Conservancy was required to fund approximately $5,000 to the Long Term Management Fund and $89,000 to the perpetually-restricted Stewardship Endowment Fund.

Under the agreement there are four remaining phases; each phase requiring a final property analysis record and a Management and Funding Agreement approved before being funded. In addition, under the agreement, the Conservancy would be required to fund approximately 20% of future funding agreements. No amounts related to these phases have been funded by either party as of December 31, 2019.

## NOTE 12 – COMMITMENTS

*Leases*

The Conservancy leases office space under an operating lease. Future minimum commitments under the lease are as follows:

| | |
|---|---|
| 2020 | $ 39,942 |
| 2021 | 41,021 |
| 2022 | 42,101 |
| Total | $ 123,064 |

Lease expense was approximately $66,200 and $64,400 in 2019 and 2018, respectively.

*Easements*

As of December 31, 2019, the Conservancy holds fifteen conservation easements covering approximately 10,866 acres. The Conservancy is committed to monitoring these properties in order to ensure that the conditions of the conservation easements are not violated. In the event that any violation of these easements is deemed to have occurred, the Conservancy is committed to bringing any and all actions necessary to bring remedy.

## NOTE 13 – SUBSEQUENT EVENTS

On March 11, 2020, the Director-General of the World Health Organization declared a pandemic related to the global outbreak of the new coronavirus COVID-19 and on March 13, 2020, a national emergency was declared in the United States. The extent of the impact of COVID-19 on the Conservancy's operational and financial performance will depend on developments such as the duration and spread of the outbreak, impact on donors, employees, and vendors all of which are uncertain and cannot be predicted. Additionally, the Conservancy did not hold its special event in May 2020 and has rescheduled this fundraising event to a later date in 2020. Therefore, while the Conservancy expects this matter to negatively impact its operating results and financial position, the financial impact cannot be reasonably estimated at this time.

Subsequent to December 31, 2019, the Conservancy received a federal payroll protection loan totaling approximately $93,000. This loan was provided during the economic downturn and is expected to be forgiven in 2020.

Management has evaluated subsequent events through June 30, 2020, which is the date that the financial statements were available for issuance. As a result of this evaluation, no other events were identified that are required to be disclosed or would have a material impact on reported net assets or changes in net assets.