



Certified Public Accountants and Consultants

STROUD WATER RESEARCH CENTER, INC.

SINGLE AUDIT REPORT

DECEMBER 31, 2016

CONTENTS

INDEPENDENT AUDITORS' REPORT	1
FINANCIAL STATEMENTS	
STATEMENT OF FINANCIAL POSITION	3
STATEMENT OF ACTIVITIES	4
STATEMENT OF CASH FLOWS	6
NOTES TO FINANCIAL STATEMENTS	7
SUPPLEMENTARY INFORMATION	
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS	24
NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS	25
INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH <i>GOVERNMENT AUDITING STANDARDS</i>	26
INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE FOR EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE REQUIRED BY THE UNIFORM GUIDANCE	28
SCHEDULE OF FINDINGS AND QUESTIONED COSTS	30
SUMMARY STATUS OF PRIOR YEAR AUDIT FINDINGS	32

INDEPENDENT AUDITORS' REPORT

To the Board of Directors
Stroud Water Research Center, Inc.

Report on the Financial Statements

We have audited the accompanying financial statements of Stroud Water Research Center, Inc. (a nonprofit corporation), which comprise the statement of financial position as of December 31, 2016, and the related statements of activities and cash flows for the year 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 the financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting 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 Stroud Water Research Center, Inc. as of December 31, 2016, and the changes in its net assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Report on Summarized Comparative Information

We have previously audited Stroud Water Research Center, Inc.'s 2015 financial statements, and our report dated September 8, 2016, expressed an unmodified opinion on those audited financial statements. In our opinion, the summarized comparative information presented herein as of and for the year ended December 31, 2015, is consistent, in all material respects, with the audited financial statements from which it has been derived.

Other Matters

Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The accompanying schedule of expenditures of federal awards, as required by Title 2 U.S. Code of Federal Regulations (CFR) Part 200, Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards, is presented for purposes of additional analysis and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated, in all material respects, in relation to the financial statements as a whole.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated September 7, 2017, on our consideration of Stroud Water Research Center, Inc.'s internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Stroud Water Research Center, Inc.'s internal control over financial reporting and compliance.

Gunnip & Company LLP

September 7, 2017

FINANCIAL STATEMENTS

STATEMENT OF FINANCIAL POSITION

DECEMBER 31, 2016 AND 2015

	2016	2015
ASSETS		
CURRENT ASSETS		
Cash	\$ 2,471,058	\$ 2,195,202
Accounts and grants receivable	2,042,643	1,522,266
Pledges receivable	73,250	191,865
Prepaid expenses	37,540	16,743
	<u>4,624,491</u>	<u>3,926,076</u>
PROPERTY AND EQUIPMENT		
Land	2,357,839	2,357,839
Buildings and improvements	12,333,742	12,295,883
Equipment	2,823,368	2,686,069
Vehicles	231,275	204,424
	<u>17,746,224</u>	<u>17,544,215</u>
Less accumulated depreciation	5,826,615	5,293,896
	<u>11,919,609</u>	<u>12,250,319</u>
CONSTRUCTION IN PROGRESS	6,631	0
PLEDGES RECEIVABLE	90,622	84,590
INVESTMENTS	20,996,472	20,305,989
BENEFICIAL INTEREST IN PERPETUAL TRUST	<u>9,343,528</u>	<u>9,265,177</u>
Total assets	<u><u>\$ 46,981,353</u></u>	<u><u>\$ 45,832,151</u></u>

See accompanying notes to financial statements.

STROUD WATER RESEARCH CENTER, INC.

	2016	2015
LIABILITIES AND NET ASSETS		
CURRENT LIABILITIES		
Current portion of bonds payable	\$ 245,674	\$ 241,202
Accounts payable and accrued expenses	507,462	635,964
Taxes payable - payroll	6,368	5,671
	<u>759,504</u>	<u>882,837</u>
 BONDS PAYABLE	 5,488,626	 5,734,301
 PENSION BENEFIT OBLIGATION	 <u>2,093,430</u>	 <u>1,540,586</u>
 Total liabilities	 <u>8,341,560</u>	 <u>8,157,724</u>
 NET ASSETS		
Unrestricted		
Board designated	16,277,650	15,343,668
Undesignated	5,605,163	5,529,195
	<u>21,882,813</u>	<u>20,872,863</u>
 Temporarily restricted	 4,424,845	 4,547,780
Permanently restricted	<u>12,332,135</u>	<u>12,253,784</u>
 Total net assets	 <u>38,639,793</u>	 <u>37,674,427</u>
 Total liabilities and net assets	 <u><u>\$ 46,981,353</u></u>	 <u><u>\$ 45,832,151</u></u>

See accompanying notes to financial statements.

STATEMENT OF ACTIVITIES

STROUD WATER RESEARCH CENTER, INC.

FOR THE YEAR ENDED DECEMBER 31, 2016 WITH COMPARATIVE TOTALS FOR 2015

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total 2016	Total 2015
OPERATING REVENUE					
Research programs	\$ 1,878,293	\$ 1,851,872	\$ 0	\$ 3,730,165	\$ 4,408,528
Education/public programs	468,426	79,180	0	547,606	961,809
Watershed restoration programs	1,652,094	174,351	0	1,826,445	1,145,223
Annual fund	535,170	0	0	535,170	567,745
Contributions	140,101	298,138	0	438,239	656,029
Contribution from beneficial interest in perpetual trust	414,503	0	0	414,503	396,401
Other income	82,143	0	0	82,143	100,557
Special event	340,761	0	0	340,761	261,934
Net assets released from restriction	5,511,491	2,403,541	0	7,915,032	8,498,226
	2,526,476	(2,526,476)	0	0	0
Total operating revenue	8,037,967	(122,935)	0	7,915,032	8,498,226
OPERATING EXPENSES					
Program services					
Research	3,573,833	0	0	3,573,833	3,679,278
Education	570,666	0	0	570,666	831,486
Watershed restoration	1,578,627	0	0	1,578,627	1,082,814
Total program services	5,723,126	0	0	5,723,126	5,593,578
Supporting services					
Outreach	349,502	0	0	349,502	324,236
Finance and administrative	648,201	0	0	648,201	624,664
Information services	360,451	0	0	360,451	344,845
Facilities	917,814	0	0	917,814	845,158
Communications and marketing	45,057	0	0	45,057	134,328
Special event	34,382	0	0	34,382	39,990
Total supporting services	2,355,407	0	0	2,355,407	2,313,221
Total operating expenses	8,078,533	0	0	8,078,533	7,906,799
NET INCOME (LOSS) FROM OPERATIONS	(40,566)	(122,935)	0	(163,501)	591,427

See accompanying notes to financial statements.

STATEMENT OF ACTIVITIES (cont'd)

STROUD WATER RESEARCH CENTER, INC.

FOR THE YEAR ENDED DECEMBER 31, 2016 WITH COMPARATIVE TOTALS FOR 2015

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total 2016	Total 2015
OTHER CHANGES					
Pension-related changes other than net periodic pension cost	(643,628)	0	0	(643,628)	(288,979)
Investment income	1,078,402	0	0	1,078,402	728,127
Net realized and unrealized gains (losses) on:					
Beneficial interest in perpetual trust	0	0	78,351	78,351	(507,325)
Investments	615,742	0	0	615,742	(1,279,172)
Total other changes	1,050,516	0	78,351	1,128,867	(1,347,349)
CHANGE IN NET ASSETS	1,009,950	(122,935)	78,351	965,366	(755,922)
NET ASSETS, BEGINNING OF YEAR	20,872,863	4,547,780	12,253,784	37,674,427	38,430,349
NET ASSETS, END OF YEAR	<u>\$ 21,882,813</u>	<u>\$ 4,424,845</u>	<u>\$ 12,332,135</u>	<u>\$ 38,639,793</u>	<u>\$ 37,674,427</u>

See accompanying notes to financial statements.

STATEMENT OF CASH FLOWS

STROUD WATER RESEARCH CENTER, INC.

FOR THE YEARS ENDED DECEMBER 31, 2016 AND 2015

	2016	2015
OPERATING ACTIVITIES		
Change in net assets	\$ 965,366	\$ (755,922)
Adjustments to reconcile change in net assets to net cash flow used by operating activities		
Depreciation	532,103	511,195
Amortization of debt issuance costs	1,597	1,524
Net realized and unrealized (gains) losses	(694,093)	1,786,497
Contributed investments	(234,457)	(923,397)
(Increase) decrease in -		
Accounts and grants receivable	(520,377)	(155,456)
Pledges receivable	(36,282)	(27,992)
Prepaid expenses	(20,797)	47,380
Increase (decrease) in -		
Accounts payable and accrued expenses	(128,502)	(23,518)
Pension benefit obligation	552,844	53,189
Taxes payable - payroll	697	(300)
Net cash flow from operating activities	<u>418,099</u>	<u>513,200</u>
INVESTING ACTIVITIES		
Purchase of property and equipment	(208,024)	(218,725)
Purchase of investment securities	(3,139,358)	(4,137,756)
Proceeds on sale of investment securities	<u>3,299,074</u>	<u>4,994,587</u>
Net cash flow from (used by) investing activities	<u>(48,308)</u>	<u>638,106</u>
FINANCING ACTIVITIES		
Pledge payments received	148,865	554,219
Repayment of bond payable	<u>(242,800)</u>	<u>(238,460)</u>
Net cash flow from (used by) financing activities	<u>(93,935)</u>	<u>315,759</u>
NET CHANGE IN CASH	275,856	1,467,065
CASH, BEGINNING OF YEAR	<u>2,195,202</u>	<u>728,137</u>
CASH, END OF YEAR	<u>\$ 2,471,058</u>	<u>\$ 2,195,202</u>
CASH PAID FOR INTEREST	<u>\$ 252,718</u>	<u>\$ 261,885</u>
SCHEDULE OF NONCASH INVESTING AND FINANCING ACTIVITIES		
Contributed investments	<u>\$ 234,457</u>	<u>\$ 923,397</u>

See accompanying notes to financial statements.

Note 1 Summary of Corporation activities and significant accounting policiesCorporation activities

Stroud Water Research Center, Inc. ("the Corporation") operates as a nonprofit corporation established under Delaware law. The Corporation's purpose is to advance knowledge of stream and river ecosystems through interdisciplinary research; to develop and communicate new ecological ideas; to provide solutions for water resource problems worldwide; and to promote public understanding of freshwater ecology through education programs, watershed restoration, conservation leadership, and professional service.

Use of estimates in the preparation of financial statements

The preparation of financial statements in conformity with U.S. generally accepted accounting principles 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 revenues and expenses during the reporting period. Actual results could differ from those estimates.

Comparative information

The financial statements include certain prior-year summarized comparative information in total but not by net asset class. Such information does not include sufficient detail to constitute a complete presentation in conformity with generally accepted accounting principles. Accordingly, such information should be read in conjunction with the Corporation's financial statements for the year ended December 31, 2015, from which the summarized information was derived.

Basis of presentation

In accordance with Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") 958 – Not-for-Profit Entities, the Corporation reports information regarding its financial position and activities according to three classes of net assets: unrestricted net assets, temporarily restricted net assets and permanently restricted net assets.

Contributions and revenue recognition

Contributions received are recorded as unrestricted, temporarily restricted or permanently restricted support, depending on the existence and/or nature of any donor restrictions. Support that is restricted by the donor is reported as an increase in temporarily or permanently restricted net assets, depending on the nature of the restriction.

Note 1 Summary of significant accounting policies (cont'd)

Contributions and revenue recognition (cont'd)

Contributions, including unconditional promises to give, are recognized in the period received. Conditional promises to give are not recognized until the condition is met. Contributions of assets other than cash are recorded at their estimated fair values. Contributions (pledges) to be received after one year are discounted at appropriate rates commensurate with the risks involved.

Contributions with restrictions met in the same year

Contributions received with donor-imposed restrictions that are met in the same year as received are reported as revenues of the temporarily restricted net asset class, and a reclassification to unrestricted net assets is made to reflect the expiration of such restrictions

Net asset classifications

FASB ASC 958-10 – Not-for-Profit Entities-Disclosure, provides guidance on the net asset classification of donor-restricted endowment funds for a not-for-profit organization that is subject to an enacted version of the Uniform Prudent Management of Institutional Funds Act of 2006 (“UPMIFA”). The accounting standard also requires disclosures about an organization's endowment funds, both donor restricted endowment funds and board designated endowment funds, whether or not the organization is subject to UPMIFA.

The State of Delaware complies with UPMIFA. The Corporation has determined that a portion of its net assets meet the definition of endowment under UPMIFA.

Net assets, revenues, expenses, gains and losses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, net assets and changes therein are classified as follows:

Permanently restricted net assets - resources contributed by donors under the stipulation that the principal of the gift be retained intact in perpetuity and that investment earnings on those gifts, both yields and gains and losses, be used to support operations. The donor may further stipulate that the earnings be applied to a specific operating purpose.

Temporarily restricted net assets - resources contributed by donors subject to use for a stipulated purpose or in a stipulated future time period.

Unrestricted net assets - resources available to support any operating need of the Corporation.

Revenues are reported as increases in unrestricted net assets unless use of the related assets is limited by donor-imposed restrictions. Expenses are reported as decreases in unrestricted net assets. Gains and losses on investments and other assets or liabilities are reported as increases or decreases in unrestricted net assets unless their use is restricted by explicit donor stipulation or law.

Note 1 Summary of significant accounting policies (cont'd)

Net asset classifications (cont'd)

When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of activities as net assets released from restriction.

Release of restriction on net assets for acquisition of property and equipment

Contributions of land, buildings and equipment with donor stipulations concerning the use of such long lived assets are reported as revenues of the unrestricted net asset class. Contributions of cash or other assets to be used to acquire land, buildings and equipment are reported as revenues of the temporarily restricted net asset class. The restrictions are considered to be released at the time of acquisition of such long lived assets.

Endowment investment and spending policies

The Corporation's endowment consists of individual funds established for a variety of purposes. Its endowment includes both donor-restricted funds and funds designated by the Board of Directors to function as endowments. As required by generally accepted accounting principles, net assets associated with endowment funds, including funds designated by the Board of Directors to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions.

The Board of Directors of the Corporation has interpreted the State Prudent Management of Institutional Funds Act ("SPMIFA") as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the Corporation classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund, and (d) changes in the fair value of the beneficial interest in perpetual trust. The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Corporation in a manner consistent with the standard of prudence prescribed by SPMIFA. In accordance with SPMIFA, the Corporation considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds: (1) the duration and preservation of the various funds, (2) the purposes of the donor-restricted endowment funds, (3) general economic conditions, (4) the possible effect of inflation and deflation, (5) the expected total return from income and the appreciation of investments, (6) other resources of the Corporation, and (7) the Corporation's investment policies.

Note 1 Summary of significant accounting policies (cont'd)

Endowment investment and spending policies (cont'd)

The Corporation has adopted investment and spending policies, approved by the Board of Directors, for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment funds while also maintaining the purchasing power of those endowment assets over the long-term. The Corporation's objective is for its spending and investment policies to work together to achieve this objective. The investment guidelines are based upon an investment horizon of greater than ten years. In establishing the risk tolerances for this strategy, the Corporation's ability to withstand short- and intermediate-term variability were considered. The current long-term return objective is to return an average of 8%. Actual returns in any given year may vary from this amount.

To satisfy its long-term rate-of-return objectives, the Corporation 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 Corporation targets a diversified asset allocation that places a greater emphasis on equity-based investments to achieve its long-term return objectives within prudent risk parameters.

The spending policy calculates the amount of money annually distributed from the Corporation's various endowed funds to fund Corporation operations and capital acquisitions. The current spending policy is to distribute an amount equal to 5% of a thirteen quarter weighted average of the value of endowment assets. In addition to this distribution, the Corporation's finance committee has the authority to distribute additional funds as they are deemed necessary. Distributions from the endowment were \$ 2,152,498 in 2016 (\$ 2,249,323 in 2015), which included \$ 1,091,924 in funds authorized by the finance committee.

Investments

Investments are comprised of common stock, mutual funds, alternative investment and cash management funds. Investments are stated at fair market value.

Property and equipment

Property and equipment are stated at cost. Cost is the purchase price at date of acquisition, if purchased, or the fair value at date of donation, if acquired by gift.

Depreciation is computed over the estimated useful lives of property and equipment using the straight-line method. The annual depreciation rates are based on the following ranges of useful lives:

Buildings	20-50 years
Building improvements	5-20 years
Equipment	3-10 years
Vehicles	5 years

Note 1 Summary of significant accounting policies (cont'd)

Property and equipment (cont'd)

Renewals and improvements are capitalized. Normal maintenance and repairs are expensed as incurred and major renewals and improvements are capitalized.

Depreciation expense was \$ 532,103 in 2016 (\$ 511,195 in 2015).

Deferred fees and amortization

Debt issuance costs of \$ 58,670, net of accumulated amortization of \$ 8,549, are reported as a direct deduction from the face amount of the bonds payable to which such costs relate. Amortization of debt issuance costs is reported as a component of interest expense and is computed using the effective interest method, over the terms of the respective notes payable.

Interest expense related to the debt issuance costs for the years ended December 31, 2016 and 2015 was \$ 1,597 and \$ 1,524, respectively.

Beneficial interest in perpetual trust

Under the terms of the perpetual trust held and administered by a third party, the Corporation is the beneficiary of income earned on those trust's assets in perpetuity. The Corporation recognized the fair value of the trust's assets as permanently restricted contribution revenue and an asset (beneficial interest in perpetual trust) when it was notified of the trust's existence.

Changes in the fair value of the trust's assets are recognized as permanently restricted unrealized gains or losses in the period the change occurs. The change in value recognized was an unrealized gain of \$ 78,351 in 2016 (unrealized loss of \$ 507,325 in 2015).

The Corporation records income, in the period it is received from the trust, as an unrestricted contribution. Contributions received from the trust were \$ 414,503 in 2016 (\$ 396,401 in 2015).

Income taxes

The Corporation is exempt from income taxes under the provisions of Section 501(c)(3) of the Internal Revenue Code but can be subject to tax on unrelated trade or business income.

The Corporation complies with FASB ASC 740 – Accounting for Uncertainty in Income Taxes. For the years ended December 31, 2016 and 2015, the Corporation has determined it did not have a material tax liability for uncertain tax positions.

Note 1 Summary of significant accounting policies (cont'd)

Income taxes (cont'd)

The Corporation's policy for penalties and interest assessed by income taxing authorities is to include them in other expenses. For the years ended December 31, 2016 and 2015, the Corporation did not incur any interest and penalties from taxing authorities.

The federal income tax returns of the Corporation for 2013, 2014 and 2015 are subject to examination by the Internal Revenue Service, generally for three years after they were filed.

Advertising costs

Advertising costs are charged to operations when incurred. Total advertising costs were \$ 50 in 2016 (\$ 1,365 in 2015).

Subsequent events

The date to which events occurring after December 31, 2016, the date of the most recent statement of financial position, have been evaluated for possible adjustment to the financial statements or disclosure is August 29, 2017, which is the date on which the financial statements were available to be issued.

Change in accounting principle

During 2016, the Corporation adopted the provisions of Accounting Standards Update 2015-03, *Simplifying the Presentation of Debt Issuance Costs*, which modifies the presentation of debt issuance costs and the related amortization. The change in accounting under this update affected the reporting of debt issuance costs by no longer reporting them as assets. It also modified the reporting of the related amortization by including it as a component of interest expense. This update has been adopted by the Corporation on a retrospective basis. As a result, total assets as well as bonds payable for the year ended December 31, 2015 have been reduced by the effect of the reclassification of debt issuance costs of \$ 58,670, net of accumulated amortization of \$ 6,952.

Note 2 Financial instruments

Concentrations of credit risk

Financial instruments that potentially subject the Corporation to significant concentrations of credit risk are principally cash, receivables and investments.

Cash is maintained in bank deposit accounts with financial institutions that at times exceeds federally insured limits. The Corporation has not experienced any losses in such accounts and does not believe it is exposed to any significant risk.

Note 2 Financial instruments (cont'd)

Concentrations of credit risk (cont'd)

Receivables, which represent unsecured support and revenue, are periodically reviewed by management for collectability. An allowance for doubtful accounts is established if required.

Investments are unsecured and are managed by professional advisors subject to the Corporation's investment policy. The degree and concentration of credit risk vary by type of investment.

Fair value measurement of financial instruments

The Corporation complies with FASB ASC 820 – Fair Value Measurements and Disclosures. FASB ASC 820 defines fair value, establishes a framework for measuring fair value in accordance with generally accepted accounting principles, and expands disclosures about fair value measurements. The definitions, framework and disclosures required by FASB ASC 820 apply to other accounting pronouncements that require or permit fair value measurement. FASB ASC 820 does not require any new fair value measurements of reported balances.

FASB ASC 820 establishes a three-level hierarchy that prioritizes the factors (inputs) used to calculate the fair value of assets and liabilities:

Level 1 - inputs are unadjusted quoted prices, such as a New York Stock Exchange closing price in active markets for identical assets. Level 1 is the highest priority in the hierarchy.

Level 2 - inputs may include quoted prices for similar assets and liabilities in active markets, as well as other significant inputs that are observable at commonly quoted intervals, such as interest rates, foreign exchange rates, and yield curves.

Level 3 - inputs are unobservable. Typically, assumptions determine the inputs since there is little, if any, related market activity. Level 3 is the lowest priority in the hierarchy.

The following methods and assumptions were used to estimate the fair value of each class of financial instruments:

Investments - the carrying amount approximates the fair value of investments. The fair value of Level 1 securities is determined by reference to quoted market prices and other relevant information generated by market transactions. The fair value of Level 2 securities is determined by using a market approach and reflects the fair value of an investment's underlying securities divided by the number of shares that are outstanding within the fund.

Beneficial interest in perpetual trust - the carrying amount approximates the fair value which is determined by reference to quoted market prices and other relevant information generated by market transactions.

Note 2 Financial instruments (cont'd)

Fair value measurement of financial instruments (cont'd)

Fair values of assets measured on a recurring basis at December 31, 2016 are as follows:

	<u>Fair Value Measurement at Reporting Date Using</u>		
	<u>Fair Value</u>	<u>Quoted Prices In Active Markets for Identical Assets (Level 1)</u>	<u>Significant Other Observable Inputs (Level 2)</u>
Cash management fund	\$ 339,003	\$ 339,003	\$ 0
Mutual funds			
Domestic blended equities	1,663,787	1,663,787	
Domestic large cap equities	2,517,887	2,517,887	
Domestic small cap equities	2,860,301	2,860,301	
Fixed income	4,468,541	4,468,541	
International equities			
Developed	1,835,338	1,835,338	
Emerging markets	1,099,123	1,099,123	
Investment in limited partnership	<u>6,212,492</u>	<u> </u>	<u>6,212,492</u>
Total investments	<u>\$ 20,996,472</u>	<u>\$ 14,783,980</u>	<u>\$ 6,212,492</u>
Beneficial interest in perpetual trust	<u>\$ 9,343,528</u>	<u>\$ 0</u>	<u>\$ 9,343,528</u>

[Remainder of page intentionally left blank]

Note 2 Financial instruments (cont'd)

Fair value measurement of financial instruments (cont'd)

Fair values of assets measured on a recurring basis at December 31, 2015 are as follows:

	<u>Fair Value Measurement at Reporting Date Using</u>		
	<u>Fair Value</u>	<u>Quoted Prices In Active Markets for Identical Assets (Level 1)</u>	<u>Significant Other Observable Inputs (Level 2)</u>
Cash management fund	\$ 242,663	\$ 242,663	\$ 0
Mutual funds			
Domestic blended equities	1,595,470	1,595,470	
Domestic large cap equities	2,589,715	2,589,715	
Domestic small cap equities	2,209,716	2,209,716	
Fixed income	4,487,697	4,487,697	
International equities			
Developed	1,700,643	1,700,643	
Emerging markets	1,005,891	1,005,891	
Alternative investment	38,905		38,905
Investment in limited partnership	<u>6,435,289</u>	<u> </u>	<u>6,435,289</u>
Total investments	<u>\$ 20,305,989</u>	<u>\$ 13,831,795</u>	<u>\$ 6,474,194</u>
Beneficial interest in perpetual trust	<u>\$ 9,265,177</u>	<u>\$ 0</u>	<u>\$ 9,265,177</u>

Note 3 Pledges receivable

Pledges receivable consisted of the following at December 31:

	2016	2015
Receivable in less than one year	\$ 73,250	\$ 191,865
Receivable in one to five years	100,000	100,000
Receivable in greater than five years	<u>0</u>	<u>0</u>
Total pledges	173,250	291,865
Less discounts to net present value	9,378	15,410
Less allowance for uncollectible pledges receivable	<u>0</u>	<u>0</u>
	<u>\$ 163,872</u>	<u>\$ 276,455</u>

Note 4 Investments

Investments are stated at fair value and are summarized as follows at December 31:

	2016		
	Cost	Fair Value	Unrealized Appreciation
Cash management fund	\$ 339,003	\$ 339,003	\$ 0
Mutual funds	12,514,346	14,444,977	1,930,631
Investment in limited partnership	<u>5,872,570</u>	<u>6,212,492</u>	<u>339,922</u>
Total investments	<u>\$ 18,725,919</u>	<u>\$ 20,996,472</u>	<u>\$ 2,270,553</u>

	2015		
	Cost	Fair Value	Unrealized Appreciation (Depreciation)
Cash management fund	\$ 242,663	\$ 242,663	\$ 0
Mutual funds	12,440,207	13,589,132	1,148,925
Alternative investment	106,677	38,905	(67,772)
Investment in limited partnership	<u>5,733,298</u>	<u>6,435,289</u>	<u>701,991</u>
Total investments	<u>\$ 18,522,845</u>	<u>\$ 20,305,989</u>	<u>\$ 1,783,144</u>

Investment income consisted of the following for the years ended December 31:

	2016	2015
Interest and dividends	\$ 425,557	\$ 407,226
Partnership income	695,431	364,652
Fees and other expenses	<u>(42,586)</u>	<u>(43,751)</u>
	<u>\$ 1,078,402</u>	<u>\$ 728,127</u>

Note 5 Bonds payable

In 2008, the Corporation entered into an agreement to construct a new building to accommodate the needs of their education, communications, development and business departments which was completed in 2012. A portion of the funding for the project was obtained from tax-exempt bond financing in the amount of \$ 6,500,000 which was approved by the Central and Western Chester County Industrial Development Authority and was advanced by Brown Brothers Harriman & Co ("BBH").

Note 5 Bonds payable (cont'd)

Bonds payable totalled \$ 5,734,300 as of December 31, 2016 (\$ 5,975,503 as of December 31, 2015). The first \$ 3,250,000 of the bond issue bears interest at 4.70% until December 23, 2035. The second \$ 3,250,000 of the bond issue bears interest at 3.65% until December 23, 2035. Payments of interest and principal are due in accordance with the schedule outlined in the bond issue through December 2035.

Components of bonds payable are as follows for December 31, 2016:

	Bonds Payable	Unamortized Loan Costs	Net
Current portion	\$ 247,347	\$ 1,674	\$ 245,673
Long-term portion	<u>5,537,074</u>	<u>48,447</u>	<u>5,488,627</u>
Total	<u>\$ 5,784,421</u>	<u>\$ 50,121</u>	<u>\$ 5,734,300</u>

Components of bonds payable are as follows for December 31, 2015:

	Bonds Payable	Unamortized Loan Costs	Net
Current portion	\$ 242,799	\$ 1,597	\$ 241,202
Long-term portion	<u>5,784,422</u>	<u>50,121</u>	<u>5,734,301</u>
Total	<u>\$ 6,027,221</u>	<u>\$ 51,718</u>	<u>\$ 5,975,503</u>

Components of interest expense on the bonds payable for the year ended December 31, 2016 and 2015 are as follows:

	2016	2015
Interest expense	\$ 252,718	\$ 261,885
Amortization of loan costs	<u>1,597</u>	<u>1,524</u>
Total interest expense	<u>\$ 254,315</u>	<u>\$ 263,409</u>

Scheduled principal payments on the bond payable for each of the next five years, thereafter and in the aggregate are as follows:

2017	\$ 247,347
2018	252,112
2019	257,106
2020	262,338
2021	262,820
Thereafter	<u>4,502,698</u>
	<u>\$ 5,784,421</u>

Note 5 Bond payable (cont'd)

Covenants

The Corporation must maintain the following financial covenants for the bond payable to its bank as follows:

The Corporation's unrestricted investments shall not be less than \$ 8,000,000.

The Corporation shall not incur an operating deficit for any fiscal year, as defined in the bond agreement, in an amount greater than \$ 200,000.

The Corporation met the covenants described above as of December 31, 2016 and 2015.

Note 6 Temporarily restricted net assets

Temporarily restricted net assets are available for the following purposes at December 31:

	2016	2015
Research programs	\$ 2,437,071	\$ 2,200,714
Education/public programs	42,002	48,467
Watershed Restoration	28,911	34,344
Other programs	22,774	22,774
Assistant director's fund	491,379	641,394
New building	<u>1,402,708</u>	<u>1,600,087</u>
	<u>\$ 4,424,845</u>	<u>\$ 4,547,780</u>

Note 7 Permanently restricted net assets

Permanently restricted net assets are restricted to investment in perpetuity, the investment income and gains and losses, however, are expendable for the mission of the Corporation. Permanently restricted net assets consisted of the following at December 31:

	2016	2015
Investments	\$ 2,988,607	\$ 2,988,607
Beneficial interest in perpetual trust	<u>9,343,528</u>	<u>9,265,177</u>
	<u>\$ 12,332,135</u>	<u>\$ 12,253,784</u>

Note 8 Net assets released from restriction

Net assets were released from donor restrictions by incurring expenses satisfying restricted purposes or by occurrence of other events specified by donors are as follows for the years ended December 31:

	2016	2015
Research programs	\$ 1,615,515	\$ 1,594,974
Education/public programs	85,645	68,684
Watershed Restoration	179,784	517,507
Assistant director's fund	150,015	141,477
New building	<u>495,517</u>	<u>500,344</u>
	<u>\$ 2,526,476</u>	<u>\$ 2,822,986</u>

Note 9 Major contributors

Of the \$ 973,409 in contributions received in 2016, none were received from major contributors (approximately 24%, or \$ 298,476 of \$ 1,223,774 was received from two contributors in 2015). Pledges receivable from major contributors was \$ 150,000 as of December 31, 2016 and 2015.

Note 10 Major grantors

Of the \$ 6,104,216 in program grants and contracts received in 2016, approximately 68%, or \$ 4,133,916 of these program grants and contracts were received from three grantors (approximately 80%, or \$ 5,193,617 of \$ 6,515,560 were received from three grantors in 2015). Grants receivable from major grantors was \$ 910,767 and \$ 907,589 as of December 31, 2016 and 2015, respectively.

Note 11 Pension plan

The Corporation complies with FASB ASC 715 - Compensation-Retirement Benefits, for recognition and disclosure of its pension plan activity.

The Corporation has a defined benefit pension plan which covers all full-time employees with a minimum of one year of service. Annual pension benefits beginning at normal retirement age are equal to 1.25% of final average compensation for each year of service.

Note 11 Pension plan (cont'd)

The following tables set forth further information about the Corporation's defined benefit pension plan for the years ended December 31:

Pension plan obligations and funded status:

	2016	2015
Projected benefit obligation	\$ 8,866,467	\$ 7,637,294
Fair value of plan assets	<u>6,773,037</u>	<u>6,096,708</u>
Funded status	<u>\$ (2,093,430)</u>	<u>\$ (1,540,586)</u>
Accumulated benefit obligation	\$ 7,924,234	\$ 7,082,535
Employer contributions	\$ 296,000	\$ 422,000
Participant contributions	\$ 0	\$ 0
Benefits paid	\$ (166,691)	\$ (159,461)

Amounts recognized in the statement of financial position:

	2016	2015
Pension benefit obligation	<u>\$ 2,093,430</u>	<u>\$ 1,540,586</u>

Amounts recognized in the statement of activities:

	2016	2015
Components of net periodic benefit cost		
Service cost	\$ 247,638	\$ 259,910
Interest cost	317,062	292,730
Amortization of net loss	54,895	41,729
Expected return on plan assets	<u>(414,379)</u>	<u>(408,159)</u>
Net periodic benefit cost	205,216	186,210
Changes in plan assets and benefit obligations recognized in other changes in unrestricted net assets		
Net loss	698,523	330,708
Amortization of net loss	<u>(54,895)</u>	<u>(41,729)</u>
Total recognized in net periodic benefit costs and other changes in unrestricted net assets	<u>\$ 848,844</u>	<u>\$ 475,189</u>

Note 11 Pension plan (cont'd)

The estimated net loss and prior service cost for the defined benefit pension plan that will be amortized from other changes in unrestricted net assets into the net periodic benefit over the next year are \$ 85,485 and \$ 54,895, respectively.

The following assumptions were used in accounting for the pension plan:

Weighted average assumptions used to determine the pension benefit obligation at December 31:

	2016	2015
Discount rate	4.15%	4.25%
Rate of compensation increase	3.00%	2.00%
Expected return on plan assets	6.10%	7.00%

Weighted average assumptions used to determine the net periodic benefit cost during the year ended December 31:

	2016	2015
Discount rate	4.25%	4.00%
Rate of compensation increase	2.00%	2.00%
Expected return on plan assets	7.00%	7.00%

The expected rate of return on pension plan assets is determined by those assets' historical long-term investment performance, current asset allocation, and estimates of future long-term returns by asset class.

The percentage of the fair value of total pension plan assets held as of December 31, 2016 by asset category is as follows:

Cash and alternatives	5.3%
Equities	59.2%
Fixed income securities	35.5%
Other	0.0%
	<u>100.0%</u>

The Corporation expects to contribute approximately \$ 305,000 to the pension plan in the year ended December 31, 2017. No plan assets are expected to be returned to the Corporation during the year ended December 31, 2017. Future benefit payments, which reflect expected service as appropriate, are expected to be paid as follows:

2017	\$ 337,098
2018	\$ 332,913
2019	\$ 432,627
2020	\$ 426,565
2021	\$ 426,064
2022 – 2025	\$ 2,273,380

Note 12 Commitments - copier leases

The Corporation leases copiers under various operating leases. Future minimum rental payments under these operating leases by year and in the aggregate for each of the next five years ending December 31 are as follows:

2017	\$ 13,342
2018	4,875
2019	2,783
2020	2,551
2021	<u>0</u>
	<u>\$ 23,551</u>

Rent expense was \$ 13,780 in 2016 (\$ 9,137 in 2015).

Note 13 Endowment assets

Endowment net asset composition by type of fund as of December 31, 2016 is as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Endowment funds				
Donor-restricted	\$ 0	\$ 1,894,087	\$ 12,332,135	\$ 14,226,222
Board-designated	<u>16,277,650</u>	<u>0</u>	<u>0</u>	<u>16,277,650</u>
	<u>\$ 16,277,650</u>	<u>\$ 1,894,087</u>	<u>\$ 12,332,135</u>	<u>\$ 30,503,872</u>

Changes in endowment net assets for the year ended December 31, 2016 were as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Endowment net assets, January 01, 2016	\$ 15,343,668	\$ 2,250,169	\$ 12,253,784	\$ 29,847,621
Investment return:				
Investment income, net of fees	1,078,402	0	0	1,078,402
Net realized/unrealized gains	<u>615,742</u>	<u>0</u>	<u>78,351</u>	<u>694,093</u>
Total investment return	<u>1,694,144</u>	<u>0</u>	<u>78,351</u>	<u>1,772,495</u>
Contributions transferred into endowment	738,114	298,138	0	1,036,254
Appropriation of assets for expenditure	(2,152,498)	(654,220)	0	(2,806,718)
Other changes:				
Transfers to board- designated endowment	<u>654,220</u>	<u>0</u>	<u>0</u>	<u>654,220</u>
Endowment net assets, December 31, 2016	<u>\$ 16,277,650</u>	<u>\$ 1,894,087</u>	<u>\$ 12,332,135</u>	<u>\$ 30,503,872</u>

Note 13 Endowment assets (cont'd)

Endowment net asset composition by type of fund as of December 31, 2015 is as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Endowment funds				
Donor-restricted	\$ 0	\$ 2,250,169	\$ 12,253,784	\$ 14,503,953
Board-designated	<u>15,343,668</u>	<u>0</u>	<u>0</u>	<u>15,343,668</u>
	<u>\$ 15,343,668</u>	<u>\$ 2,250,169</u>	<u>\$ 12,253,784</u>	<u>\$ 29,847,621</u>

Changes in endowment net assets for the year ended December 31, 2015 were as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Endowment net assets, January 01, 2015	\$ 16,813,113	\$ 2,519,557	\$ 12,761,109	\$ 32,093,779
Investment return:				
Investment income, net of fees	728,127	0	0	728,127
Net realized/unrealized losses	<u>(1,279,172)</u>	<u>0</u>	<u>(507,325)</u>	<u>(1,786,497)</u>
Total investment return	(551,045)	0	(507,325)	(1,058,370)
Contributions transferred into endowment	697,790	363,745	0	1,061,535
Appropriation of assets for expenditure	(2,249,323)	(633,133)	0	(2,882,456)
Other changes:				
Transfers to board- designated endowment	<u>633,133</u>	<u>0</u>	<u>0</u>	<u>633,133</u>
Endowment net assets, December 31, 2015	<u>\$ 15,343,668</u>	<u>\$ 2,250,169</u>	<u>\$ 12,253,784</u>	<u>\$ 29,847,621</u>

SUPPLEMENTARY INFORMATION

**SCHEDULE OF EXPENDITURES OF
FEDERAL AWARDS**

STROUD WATER RESEARCH CENTER, INC.

FOR THE YEAR ENDED DECEMBER 31, 2016

Federal Grantor/Pass-through Grantor/Program Title	Federal CFDA Number	Award Number	Pass-through Entity Identification Number	Pass-through to subrecipient	Expenditures
Research and Development Cluster:					
National Science Foundation (NSF):					
Direct programs:					
Collaborative Research: Coupled Geochemical and Geobiological Characterization of Dissolved Organic Matter Oxidation to Carbon Dioxide	47.050	EAR-1452039			\$ 106,270
Collaborative Research: Integration of Physiological, Life-history, and Macro-ecological Approaches for Understanding Thermal Limitation in Aquatic Insects	47.074	IOS - 1455906			71,238
Improving Infrastructure for Data Access, Storage and Recovery, and Network Communication at Stroud Water Research Center	47.074	DBI - 1522479			4,259
REU/RET Site: Collaborative Research: Introducing Critical Zone Observatory Science to Students and Teachers	47.050	EAR-1263222			91,536
Integrated Data Management System for Critical Zone Observatories	47.050	EAR-1332257		\$ 221,283	287,379
Collaborative Research: SI2-SSI: The Community-Driven BIG CZ Software System for Integration and Analysis of Bio- and Geoscience Data in the Critical Zone	47.070	ACI-1339834		170,526	181,038
LTERB: Trajectory for the Recovery of Stream Ecosystem Structure and Function During Reforestation	47.074	DEB-1052716			41,447
Collaborative Research: Teaching Environmental Sustainability - Model My Watershed	47.076	DRL-1418133		142,136	221,849
Collaborative Research: Sediment stabilization by animals in stream ecosystems: consequences for erosion, ecosystem process, and biodiversity	47.074	DEB-1557032			26,993
Pass-through program:					
Carnegie Mellon University					
Education and human resources	47.076	DRL-1623969	1122371-358367		16,360
Pass-through program:					
Kansas State University- subaward					
CNH: Coupled Climate, Cultivation, and Culture in the Great Plains: Understanding Water Supply and Water Quality in a Fragile Landscape	47.050	ICER-1313815	S14141	2,389	36,654
Pass-through program:					
The Concord Consortium					
Supporting Collaborative Inquiry, Engineering, and Career Exploration with Water: Water SCIENCE	47.076	DRL-1433761	268.03.01		79,383
Total National Science Foundation				<u>536,334</u>	<u>1,164,406</u>
U.S. Department of the Interior:					
Direct program:					
National Park Service Conservation, Protection, Outreach, and Education	15.954	P13AC01266			8,450
Pass-through program:					
National Fish and Wildlife Foundation (NFWF):					
Leveraging Agricultural Best Management Practices and Forested Buffers for Middle Schuylkill (PA)	15.663/10.069	0403.14.044742	FA.A064/FC.R204		13,711
Reducing Flood Impacts and Restoring Habitat in the Brandywine River Watershed (PA)	15.153	43759	FC.A062		1,050,298
Total U.S. Department of the Interior				<u>0</u>	<u>1,072,459</u>
U.S. Environmental Protection Agency:					
Pass-through program:					
National Fish and Wildlife Foundation (NFWF):					
	66.466/10.069				
Whole Farm Conservation Including Forested Buffers (PA)	10.678/10.683	0602.14.045131	FC.R237/FC.R204/ FC.R194/FA.A063	35,000	94,561
Delivering the National Fish and Wildlife Foundation Regional Conservation Partnership Program in Lancaster County (PA)	66.466/10.932	0602.15.049681	FC.R237/FC.R249		82,689
Pass-through program:					
Potomac Conservancy					
Chesapeake Riparian Forest Buffer Initiative (MD,VA, PA)	66.466/10.683	0602.13.040457	FC.R142/FC.A060/F A.A060		123,926
Total U.S. Environmental Protection Agency				<u>35,000</u>	<u>301,176</u>
U.S. Department of Agriculture:					
Direct programs:					
National Resources Conservation Service					
Improving stream water quality and reducing runoff by improving soil health through multi-species permanent cover cropping	10.912	69-2D37-15-784			35,836
Regional Conservation Partnership Program	10.932	68-2D37-15-760			16,763
Environmental Education Grants	66.951	NE-83675001			13,577
Pass-through program:					
National Fish and Wildlife Foundation (NFWF):					
Leveraging Farm Bill Funds for Water Quality in the Brandywine-Christina Cluster (PA)	99-UNKNOWN	0403.15.049038	TR.A191		76,170
Leveraging USDA Funds for Water Quality in Middle Schuylkill Cluster (PA)	99-UNKNOWN	0403.15.049017	TR.A191		21,562
Western PA Business Plan for Restoration of Healthy Forests and Freshwater Habitat (PA)	99-UNKNOWN	0404.16.054726	TR.A276		5,269
Pass-through program:					
University of Delaware - subaward					
Large runoff flux and transformation of particulate nitrogen following large, large storms: A critical but unexplored component of N cycling	10.310	2015-67020-23585	40356		55,575
Total U.S. Department of Agriculture				<u>0</u>	<u>224,752</u>
Total Research and Development Cluster Expenditures				<u>\$ 571,334</u>	<u>\$ 2,762,793</u>
Total Expenditures of Federal Awards				<u>\$ 571,334</u>	<u>\$ 2,762,793</u>

See Notes to Schedule of Federal Expenditures

NOTES TO SCHEDULE OF EXPENDITURES
OF FEDERAL AWARDS

STROUD WATER RESEARCH CENTER, INC.

FOR THE YEAR ENDED DECEMBER 31, 2016

Note A Basis of presentation

The accompanying schedule of expenditures of federal awards includes the federal award activity of Stroud Water Research Center, Inc. under programs of the federal government for the year ended December 31, 2016. The information in this schedule is presented in accordance with the requirements of Title 2 U.S. Code of Federal Regulations Part 200, Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards (Uniform Guidance). Because the schedule presents only a selected portion of the operations of Stroud Water Research Center, Inc., it is not intended to and does not present the financial position, change in net assets or cash flows of Stroud Water Research Center, Inc.

Note B Summary of significant accounting principles

Expenditures reported on the schedule are reported on the accrual basis of accounting. Such expenditures are recognized following, as applicable, either the cost principles in OMB Circular A-122, *Cost Principles for Non-Profit Organizations*, or the cost principles contained in Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards*, wherein certain types of expenditures are not allowable or are limited as to reimbursement. Stroud Water Research Center, Inc. has elected not to use the 10-percent de minimis indirect cost rate allowed under the Uniform Guidance.

INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

To the Board of Directors
Stroud Water Research Center, Inc.

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in the *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of Stroud Water Research Center, Inc., which comprise the statement of financial position as of December 31, 2016, and the related statements of operations, and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated September 7, 2017.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered Stroud Water Research Center, Inc.'s internal control over financial reporting to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Stroud Water Research Center, Inc.'s internal control. Accordingly, we do not express an opinion on the effectiveness of the Stroud Water Research Center, Inc.'s internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Stroud Water Research Center, Inc.'s financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the organization's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the organization's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Gunnip & Company LLP

Wilmington, Delaware
September 7, 2017

INDEPENDENT AUDITORS' REPORT ON COMPLIANCE FOR EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE REQUIRED BY THE UNIFORM GUIDANCE

To the Board of Directors
Stroud Water Research Center, Inc.

Report on Compliance for Each Major Federal Program

We have audited Stroud Water Research Center, Inc.'s compliance with the types of compliance requirements described in the *OMB Compliance Supplement* that could have a direct and material effect on each of Stroud Water Research Center, Inc.'s major federal programs for the year ended December 31, 2016. Stroud Water Research Center, Inc.'s major federal program is identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with the requirements of federal statutes, regulations, and the terms and conditions of its federal awards applicable to its federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of Stroud Water Research Center, Inc.'s major federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; the audit requirements of Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Those standards and Uniform Guidance require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about Stroud Water Research Center, Inc.'s compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for each major federal program. However, our audit does not provide a legal determination of Stroud Water Research Center, Inc.'s compliance.

Opinion on Each Major Federal Program

In our opinion, Stroud Water Research Center, Inc. complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended December 31, 2016.

Report on Internal Control over Compliance

Management of Stroud Water Research Center, Inc. is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered Stroud Water Research Center, Inc.'s internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with the Uniform Guidance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of Stroud Water Research Center, Inc.'s internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. *A material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. *A significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of the Uniform Guidance. Accordingly, this report is not suitable for any other purpose.

Gunnip & Company LLP

Wilmington, Delaware
September 7, 2017

**SCHEDULE OF FINDINGS AND
QUESTIONED COSTS**

STROUD WATER RESEARCH CENTER, INC.

FOR THE YEAR ENDED DECEMBER 31, 2016

Section I - Summary of Audit Results

Financial Statements

Type of auditor's report issued:

unmodified opinion

Internal control over financial reporting:

Significant deficiencies in internal control over
financial reporting?

_____ yes X no

Material weaknesses?

_____ yes X no

Noncompliance material to financial statements
noted?

_____ yes X no

Federal Awards

Internal Control over major programs:

Significant deficiencies in internal control over
major programs?

_____ yes X no

Material weaknesses?

_____ yes X no

Type of auditors' report issued on compliance
for major programs:

unmodified opinion

Any audit findings disclosed that are required
to be reported in accordance with
2 CFR 200.516(a)?

_____ yes X no

Major Programs:

CFDA Number(s)
10.069, 10.310, 10.678
10.678, 10.683, 10.912
10.932, 15.153, 15.663
15.954, 47.050, 47.070
47.074, 47.076, 66.466
66.951

Name of Federal Program or Cluster
Research and Development Cluster

Dollar threshold used to distinguish between
Type A and Type B programs:

\$ 750,000

Auditee qualified as low-risk auditee?

 X yes _____ no

**SCHEDULE OF FINDINGS AND
QUESTIONED COSTS (cont'd)**

STROUD WATER RESEARCH CENTER, INC.

FOR THE YEAR ENDED DECEMBER 31, 2016

Section II - Financial Statement Findings

NONE REPORTED

Section III - Federal Award Findings and Questioned Costs

NONE REPORTED

**SCHEDULE OF FINDINGS AND
QUESTIONED COSTS (cont'd)**

STROUD WATER RESEARCH CENTER, INC.

FOR THE YEAR ENDED DECEMBER 31, 2015

Section IV - Federal Award Findings and Questioned Costs

NONE REPORTED