Valencia Water Company

Financial Statements as of and for the
Years Ended December 31, 2014 and 2013, and
Independent Auditors' Report

Deloitte.

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INDEPENDENT AUDITORS' REPORT

To the Board of Directors of
Valencia Water Company
Valencia, California

We have audited the accompanying financial statements of Valencia Water Company (the "Company"), which comprise the balance sheets as of December 31, 2014 and 2013, and the related statements of income, changes in stockholder's equity, and 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 the audit 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 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 Company'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 Company'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 the Company as of December 31, 2014 and 2013, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Deloitte & Touche LLP

March 18, 2015

VALENCIA WATER COMPANY

BALANCE SHEETS
AS OF DECEMBER 31, 2014 AND 2013
(In thousands)

	2014	2013
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 10,489	$ 9,571
Metered and other receivables—net of allowances for doubtful accounts of $41 in 2014 and $41 in 2013 (Note 7)	2,475	2,236
Materials and supplies	391	392
Income taxes receivable (Note 5)	55	-
Deferred tax assets (Note 5)	422	813
Total current assets	13,832	13,012
UTILITY AND GENERAL PLANT ASSETS:		
Land and buildings	3,669	3,649
Wells	11,044	10,948
Pumping equipment	9,739	9,522
Transmission and distribution system	137,431	134,876
General plant	6,077	6,137
Construction in progress	3,081	3,866
Total utility and general plant assets	171,041	168,998
Accumulated depreciation and amortization	(64,001)	(59,610)
Utility and general plant assets—net	107,040	109,388
OTHER ASSETS	1,252	1,491
TOTAL	$ 122,124	$ 123,891

(Continued)

VALENCIA WATER COMPANY

BALANCE SHEETS
AS OF DECEMBER 31, 2014 AND 2013
(In thousands)

LIABILITIES AND STOCKHOLDER'S EQUITY	2014	2013
CURRENT LIABILITIES:		
Accounts payable and accrued liabilities (Notes 7 and 9)	$ 2,623	$ 2,473
Income taxes payable (Note 5)	-	239
Advances for construction—current portion (Note 8)	698	699
Total current liabilities	3,321	3,411
LONG-TERM LIABILITIES:		
Secured notes payable (Notes 4 and 8)	24,000	24,000
Advances for construction—less current portion (Note 8)	9,598	10,296
Deferred revenue	318	229
Net deferred tax liabilities (Note 5)	5,460	4,999
Deposits held for construction (Note 7)	1,951	3,402
Total long-term liabilities	41,327	42,926
Total liabilities	44,648	46,337
CONTRIBUTIONS IN AID OF CONSTRUCTION	52,605	52,581
COMMITMENTS AND CONTINGENCIES (Note 9)		
STOCKHOLDER'S EQUITY:		
Common stock, $100 par value—authorized, 50,000 shares; issued, 15,365 shares (Note 6)	1,537	1,537
Paid-in capital	6,207	6,207
Retained earnings	17,127	17,229
Total stockholder's equity	24,871	24,973
TOTAL	$ 122,124	$ 123,891

See notes to financial statements. (Concluded)

VALENCIA WATER COMPANY

STATEMENTS OF INCOME
FOR THE YEARS ENDED DECEMBER 31, 2014 AND 2013
(In thousands)

	2014	2013
OPERATING REVENUES (Note 7)	$ 26,131	$ 26,819
OPERATING EXPENSES:		
Purchased water (Note 7)	6,705	7,952
Purchased power	2,480	1,797
Operations and maintenance (Note 9)	5,190	4,581
General and administrative (Note 7)	4,915	4,754
Property taxes	147	378
Depreciation and amortization	2,750	2,710
Total operating expenses	22,187	22,172
OPERATING INCOME	3,944	4,647
OTHER (EXPENSE) INCOME:		
Interest expense	(1,161)	(1,161)
Interest income	10	7
Other (Note 2)	94	(211)
Total Other expense—net	(1,057)	(1,365)
INCOME BEFORE INCOME TAXES	2,887	3,282
INCOME TAXES (Note 5)	2,190	1,340
NET INCOME	$ 697	$ 1,942

See notes to financial statements.

VALENCIA WATER COMPANY

STATEMENTS OF CHANGES IN STOCKHOLDER'S EQUITY
FOR THE YEARS ENDED DECEMBER 31, 2014 AND 2013
(In thousands)

	Common Stock	Paid-In Capital	Retained Earnings	Total Stockholder's Equity
BALANCE—January 1, 2013	$ 1,537	$ 6,207	$ 16,086	$ 23,830
Net income	-	-	1,942	1,942
Dividends (Note 6)—common stock	-	-	(799)	(799)
BALANCE—December 31, 2013	1,537	6,207	17,229	24,973
Net income	-	-	697	697
Dividends (Note 6)—common stock	-	-	(799)	(799)
BALANCE—December 31, 2014	$ 1,537	$ 6,207	$ 17,127	$ 24,871

See notes to financial statements.

VALENCIA WATER COMPANY

STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2014 AND 2013
(In thousands)

	2014	2013
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$ 697	$ 1,942
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	2,750	2,710
Deferred income taxes	852	138
Changes in assets and liabilities:		
(Increase) decrease in metered and other receivables	(239)	263
Increase in income tax receivable	(55)	-
Decrease (increase) in materials and supplies	1	(35)
Decrease (increase) in other assets	239	(603)
Increase in accounts payable and accrued liabilities	99	425
Decrease in income taxes payable	(239)	(274)
Increase (decrease) in deferred revenue	89	(23)
Net cash provided by operating activities	4,194	4,543
CASH FLOWS FROM INVESTING ACTIVITY—Acquisition of utility and general plant assets	(2,255)	(2,377)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Refunds of advances for construction	(699)	(700)
Deposits for construction received	1,313	1,301
(Decrease) increase in contributions in aid of construction	(836)	182
Dividends paid	(799)	(799)
Net cash used in financing activities	(1,021)	(16)
NET INCREASE IN CASH AND CASH EQUIVALENTS	918	2,150
CASH AND CASH EQUIVALENTS—Beginning of year	9,571	7,421
CASH AND CASH EQUIVALENTS—End of year	$ 10,489	$ 9,571

(Continued)

VALENCIA WATER COMPANY

STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2014 AND 2013
(In thousands)

	2014	2013
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:		
Interest paid	$ 1,109	$ 1,109
Income taxes paid	$ 1,623	$ 1,471
SUPPLEMENTAL DISCLOSURES OF NONCASH INVESTING AND FINANCING ACTIVITIES:		
Amortization of contributions in aid of construction and related reduction to net utility and general plant assets	$ 1,904	$ 1,895
Transfers of deposits for construction to contributions in aid of construction	$ 2,764	$ 196
Liabilities accrued for the purchase of utility and general plant assets	$ 108	$ 57

See notes to financial statements. (Concluded)

1. ORGANIZATION AND DESCRIPTION OF THE REPORTING ENTITY

Valencia Water Company (the “Company”) was incorporated on April 7, 1954, in the state of California and was granted a certificate of public convenience and necessity by the California Public Utilities Commission (the “Commission”) in Decision No. 69744 dated October 5, 1965. The Company provides potable water service to an area encompassing a portion of the incorporated City of Santa Clarita and within the surrounding unincorporated communities of Castaic, Newhall, Saugus, Stevenson Ranch, and Valencia in northern Los Angeles County.

On December 21, 2012, Castaic Lake Water Agency (“Castaic”) acquired all of the Company’s common stock from The Newhall Land and Farming Company, a California limited partnership (“Newhall Land”), by an action in eminent domain. Certain officers of Castaic are on the Company’s board of directors (the “Board of Directors”). Castaic is a public water wholesaler that provides water from the California State Water Project to the Company and other water retailers in the Santa Clarita Valley.

In addition to the water purchased by the Company from Castaic, the Company’s water supply consists of local ground water and recycled water to serve nonpotable landscape irrigation services. Generally, the potable water represents 99% of total revenues. The mix of groundwater, purchased water, and recycled water was 73%, 25%, and 2%, respectively, in 2014 and 43%, 56%, and 1%, respectively, in 2013.

2. REGULATORY MATTERS

Prior to February 27, 2014, the Company was regulated by the Commission, who set rates sufficient to allow the Company to recover its reasonable cost of operations and maintenance and to provide the Company the opportunity to realize its authorized rate of return on its investment. However, on February 27, 2014, the Commission concluded that due to Castaic’s acquisition of all of the Company’s common stock, the Company can no longer be regulated by the Commission. As a result, the Company discontinued its application of the provisions of accounting principles generally accepted in the United States of America for accounting for regulated utilities. Under these provisions, a regulated utility defers certain costs and credits on the balance sheet as regulatory assets and liabilities when it is probable that those costs and credits will be recognized in the ratemaking process in a period different from the period in which they would have been reflected in income by an unregulated company.

The financial statement impact of the Company discontinuing the accounting for regulated utilities was to write off all regulatory assets and liabilities recorded as of February 27, 2014, which resulted in other income of $45,000 and income tax expense of $818,000. The regulatory assets and liabilities previously recorded primarily related to deferred rate case costs, the rate impact resulting from bonus tax depreciation, and regulatory assets created to reflect the impact of future recoverable revenues associated with income taxes payable when flow-through items were recognized as taxable income for ratemaking purposes.

As part of the Company’s discontinuation of accounting for regulated utilities as of February 27, 2014, the Company identified an immaterial error in its prior-year financial statements as the Company had unrecognized regulatory assets of $927,000 as of December 31, 2013. As of February 27, 2014, the unrecognized regulatory assets were $709,000, which would have further reduced income before income taxes described above for the Company's discontinuation of accounting for regulated utilities had these regulatory assets been appropriately recognized. Based upon an evaluation of all relevant quantitative and qualitative factors, the Company believes this uncorrected error is not material to its results of operations for the periods presented.

As the Company is no longer subject to regulation by the Commission, any future rate changes by the Company will not be subject to the Commission's jurisdiction. Any future rate changes by the Company will be subject to the Board of Directors' approval. The Company anticipates implementing a rate increase during 2015.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation—The financial statements of the Company are presented in conformity with accounting principles generally accepted in the United States of America.

Management Estimates—The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make certain estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, and expenses; disclosure of contingent assets or liabilities as of the date of the financial statements; and reported amounts of changes in stockholder's equity during the reporting period. Actual results could differ from those estimates. Significant accounting estimates reflected in the Company's financial statements include depreciation, fair value measurements used for disclosures, valuation allowances to deferred tax assets, accounts receivable, and unbilled revenues.

Revenue Recognition—Water utility revenues include amounts billed monthly to customers and unbilled revenue of $1,801,000 and $1,585,000 in 2014 and 2013, respectively, based on estimated usage from the last meter-reading date to December 31 at current rates. Water utility revenues are recognized as water is delivered to the customer.

Cash and Cash Equivalents—Included in cash and cash equivalents are short-term investments that have original maturity dates of six months or less. The carrying amount approximates fair value due to the short-term nature of these investments. The Company has its cash and cash equivalents on deposit with banks, which are insured by the Federal Deposit Insurance Corporation up to $250,000 per financial institution. At various times during the years ended December 31, 2014 and 2013, the Company maintained balances in excess of insured amounts.

Utility and General Plant Assets—The cost of additions, renewals, and betterments to utility and general plant assets is capitalized in the appropriate plant accounts. Costs include labor, material, and other direct and certain indirect charges. The cost of utility and general plant assets retired or otherwise disposed of, including removal costs, is charged to accumulated depreciation. Depreciation is recorded primarily on the straight-line basis over the assets' useful lives (40 years for buildings, 30 years for wells, 20 years for pumping equipment, 20–40 years for transmission and distribution system, and 7–20 years for general plant) and was equivalent to approximately 3% of depreciable utility and general plant assets for the years ended December 31, 2014 and 2013.

Expenditures that materially increase utility and general plant lives are capitalized, while costs of maintenance and repairs are charged to expense as incurred.

Other Assets—Included in other assets are loan costs of $555,000 that have been capitalized and are amortized over the life of the related loan. As of December 31, 2014 and 2013, accumulated amortization was $208,000 and $162,000, respectively. Other assets also include prepaid expenses related primarily to property and liability insurance policies. Prior to February 27, 2014, the Company recognized deferred rate case costs to be amortized over the ratemaking years to which the costs related. After February 27, 2014, the Company stopped recognizing deferred rate case costs due to the discontinuation of accounting for regulated utilities. As such, the related regulatory asset of $334,000 was written off as of February 27, 2014.

Accounts Payable and Accrued Liabilities—Prior to February 27, 2014, accounts payable and accrued liabilities included a regulatory liability related to the rate impact resulting from bonus tax depreciation. After February 27, 2014, the Company stopped recognizing regulatory assets and liabilities due to the discontinuation of accounting for regulated utilities. As such, the regulatory liability of $379,000 was written off as of February 27, 2014.

Advances for Construction—Advances for construction represent cash received from developers by the Company for extensions of the Company's distribution system. Advance contracts are generally refundable to the depositor at a rate of 2.5% each year over a 40-year period and do not bear interest. The Company expects to repay approximately $698,000 in advances in each year from 2015 through 2019, with the remaining $6,806,000 in advances due in years thereafter.

Contributions in Aid of Construction—Contributions in aid of construction are nonrefundable contributions received by the Company in cash, services, or property, primarily from developers for the purpose of constructing utility plant assets. Depreciation applicable to such utility plant assets is charged directly to the contributions in aid of construction account rather than to depreciation expense in the statements of income. The charges continue until the cost applicable to such utility plant assets has been fully depreciated or the asset is retired. Although the contribution remains on the Company's financial statements until the asset is fully depreciated, the Company has no future obligations to these developers for the contribution other than general maintenance of these utility plant assets. Accordingly, contributions in aid of construction have not been classified as a liability or as equity in the accompanying financial statements.

Deposits Held for Construction—Deposits held for construction represent cash received by the Company for extensions of the Company's distribution system. Deposits are based on the estimated cost to construct the extension of the Company's distribution system. When construction of these assets is complete, they become part of the Company's distribution system and are accounted for as advances for construction or contributions in aid of construction.

Impairment of Assets—The Company reviews its investment in long-lived assets whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. If, after review, an asset is determined to be impaired, an impairment loss in the amount by which the carrying amount of the asset exceeds its fair value is recorded. There were no impairment losses recorded during the years ended December 31, 2014 and 2013. Additionally, the Company considered the impairment of its long-lived assets as a result of discontinuing the accounting for regulated utilities as of February 27, 2014, and concluded that this was not an indication that the carrying amount of any of its assets may not be recoverable.

Income Taxes—The Company uses the asset and liability method of accounting for income taxes. This method requires the recognition of tax consequences of temporary differences between tax bases and financial reporting bases of other assets and liabilities. Prior to February 27, 2014, regulatory assets and liabilities were created to reflect the impact of future recoverable revenues (or refundable revenues) associated with income taxes payable (or refundable) when flow-through items were recognized as taxable income (or expense) for ratemaking purposes, which affected the Company's effective tax rate (see Note 5). After February 27, 2014, the Company stopped recognizing flow-through items as taxable income (or expense) for ratemaking purposes due to the discontinuation of accounting for regulated utilities. As such, the related regulatory tax asset of $1,152,000 was written off as of February 27, 2014.

The Company files income tax returns in the US federal jurisdiction and in the state of California. The Company is no longer subject to US federal and state tax examinations by tax authorities for years before 2011 and 2010, respectively.

Fair Value Measurements—The accounting guidance for fair value measurements and disclosures emphasizes that fair value is a market-based measurement, not an entity-specific measurement. Therefore, a fair value measurement should be determined based on the assumptions that market participants would use in pricing the asset or liability. As a basis for considering market participant assumptions in fair value measurements, the guidance establishes a fair value hierarchy that distinguishes between market participant assumptions based on market data obtained from sources independent of the reporting entity and the reporting entity's own assumptions about market participant assumptions. Financial assets and liabilities carried at fair value will be classified and disclosed in one of the following three categories:

Level 1—Quoted prices for identical instruments that are highly liquid, observable, and actively traded in over-the-counter markets. The Company had no assets or liabilities included in Level 1 as of December 31, 2014 and 2013.

Level 2—Quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-derived valuations whose inputs are observable and can be corroborated by market data. Level 2 financial liabilities include the secured note payable and advances for construction as of December 31, 2014 and 2013 (see Note 8).

Level 3—Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. Level 3 assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation. The Company had no assets or liabilities included in Level 3 as of December 31, 2014 and 2013.

In instances where the determination of the fair value measurement is based on inputs from different levels of the fair value hierarchy, the level in the fair value hierarchy within which the entire fair value measurement falls is based on the lowest-level input that is significant to the fair value measurement in its entirety. The Company's assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment and considers factors specific to the asset or liability.

The Company calculates the fair value of financial instruments and includes this additional information in the notes to financial statements (see Note 8).

4. SECURED NOTES PAYABLE

On June 1, 2010, the Company entered into a $12,000,000 senior secured note with Modern Woodmen of America ("Modern Woodmen"). On September 15, 2010, the Company entered into an additional $12,000,000 senior secured note with Modern Woodmen (collectively, the "Senior Secured Notes"). The Senior Secured Notes are secured by all of the Company's assets. Interest is payable semiannually on

April 15 and October 15 at a fixed rate of 4.62% per annum. The Senior Secured Notes contain various financial covenants with which the Company was in compliance as of December 31, 2014 and 2013. There are no principal payments due until the Senior Secured Notes mature on September 15, 2022.

5. INCOME TAXES

The provision for income taxes for the years ended December 31, 2014 and 2013, is as follows (in thousands):

	2014	2013
Current:		
Federal	$ 1,087	$ 926
State	251	276
Total current	1,338	1,202
Deferred:		
Federal	979	159
State	(127)	(21)
Total deferred	852	138
Total provision for income taxes	$ 2,190	$ 1,340

The income tax provision recorded at the effective tax rate approximates the amount that would have been recorded at the statutory tax rate. The 2014 income tax provision includes $818,000 due to the Company's discontinuation of accounting for regulated utilities as of February 27, 2014.

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and liabilities as of December 31, 2014 and 2013, are as follows (in thousands):

	2014	2013
Deferred tax assets:		
Advances for construction	$ 1,290	$ 1,826
Contributions in aid of construction liability	20,648	20,479
Fixed assets	-	295
Regulatory asset	-	1,153
Settlement proceeds	536	445
Other	116	-
Total deferred tax assets (including $422 and $813 in current assets at December 31, 2014 and 2013, respectively)	22,590	24,198
Deferred tax liabilities:		
Excess tax depreciation	(9,931)	(10,447)
Contributions in aid of construction fixed assets	(17,562)	(17,552)
Investment tax credit	(134)	(243)
Other	-	(142)
Total deferred tax liabilities	(27,627)	(28,384)
Net deferred tax liabilities	$ (5,037)	$ (4,186)

No valuation allowance was provided against the deferred tax assets as of December 31, 2014 and 2013. In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. Based on management's assessment, management has concluded that it is more likely than not that the results of future operations will generate sufficient taxable income to realize the deferred tax assets.

At December 31, 2014 and 2013, the Company does not have unrecognized tax benefits that, if recognized, would affect the annual effective tax rate. The Company recognizes interest accrued related to unrecognized tax benefits as income tax expense. During the years ended December 31, 2014 and 2013, the Company recognized (reversed) approximately $0 and $58,000, respectively, in interest expense related to income taxes.

6. STOCKHOLDER'S EQUITY

The Board of Directors authorized and the Company declared dividends in 2014 and 2013 of $799,000 on its common stock, of which $799,000 was paid in 2014 and 2013.

7. RELATED-PARTY TRANSACTIONS

Human resources services are provided by Castaic, and the associated expense is included within general and administrative expenses. Water quality testing expense provided by Castaic is included within operations and maintenance expenses.

During the normal course of business, the Company has additional transactions with Castaic, as listed below (in thousands):

	2014
Purchased water	$ 6,705
Water quality testing	42
Human resources services expense	36
Accounts receivable	47
Accounts payable	592
Deposits held for construction	81

	2013
Purchased water	$ 7,952
Water quality testing	59
Human resources services expense	30
Accounts receivable	75
Accounts payable	593
Deposits held for construction	424

8. DISCLOSURES ABOUT FAIR VALUE OF FINANCIAL INSTRUMENTS

The estimated fair values of certain of the Company's financial instruments as of December 31, 2014 and 2013, are as follows (in thousands):

	2014		2013	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Secured notes payable	$ 24,000	$ 26,018	$ 24,000	$ 25,254
Advances for construction	10,296	5,517	10,995	5,811

The following methods and assumptions were used to estimate the fair value of each class of financial instruments for which it is practicable to estimate that value:

Secured Notes Payable—The Company estimates fair value by using a discounted cash flow analysis based on current borrowing rates for similar types of borrowing arrangements and credit risk (3.37% and 3.89% as of December 31, 2014 and 2013, respectively).

Advances for Construction—Generally, advances are refundable to the developer at the rate of 2.5% per year over 40 years without interest. The fair value is estimated as the discounted value of the future cash flows to be paid on the advances based on current borrowing rates for similar types of borrowing arrangements and credit risk (8.50% and 8.25% as of December 31, 2014 and 2013, respectively).

Other Financial Instruments—The carrying values of cash and cash equivalents, metered and other receivables, and accounts payable and accrued liabilities approximate fair values due to their short-term nature.

9. COMMITMENTS AND CONTINGENCIES

Commitments—The Company leases vehicles under operating leases expiring in 2015 through 2018. Rent expenses under these leases were $152,000 and $134,000 for the years ended December 31, 2014 and 2013, respectively, and are included within operations and maintenance expenses. Future minimum payments due under these leases as of December 31, 2014, are as follows (in thousands):

Years Ending December 31	
2015	$ 157
2016	131
2017	99
2018	22

Litigation—The Company is involved in litigation and various claims, including those arising from its ordinary conduct of business. Management is of the opinion that the ultimate liability from this litigation and/or various claims will not materially affect the Company's financial statements. The Company believes it has adequate insurance to protect itself against any future material property and casualty losses.

On January 4, 2013, Santa Clarita Organization for Planning and the Environment (SCOPE) and Friends of the River (together, "Complainants") filed a complaint (C.13-01-005, the "SCOPE CPUC Complaint") before the Commission alleging that the Company and Castaic violated various provisions of the Public Utilities Code in connection with Castaic's December 21, 2012, acquisition of all of the

Company's common stock by an action in eminent domain, which was effectuated under the authority of the Los Angeles County Superior Court (the "Transaction"). The Administrative Law Judge consolidated the SCOPE CPUC Complaint with the Company's pending rate-setting proceedings (A.13-01-003 and A.13-01-004) and a related Commission investigation (I.13-04-003), and made the Commission's Office of Ratepayer Advocates, Newhall Land, and the Newhall County Water District parties to the proceeding. The Company and Castaic have each filed substantive pleadings in response to the SCOPE CPUC Complaint, including, but not limited to, (a) separate answers to the complaint, which generally deny the complaint's factual basis; (b) separate motions to dismiss the complaint, which detail the legal arguments against an assertion of Commission jurisdiction to grant the relief requested by Complainants; and (c) separate briefings on jurisdictional issues. The other parties also have filed briefs on jurisdictional issues. On February 27, 2014, the Commission adopted a final decision on the subject of the Commission's jurisdiction to regulate the Transaction and the Company. The decision found that the Commission had no authority to consider the legality of the Transaction itself, but that as a result of the Transaction, the Company was no longer a "private corporation" subject to the Commission's jurisdiction. Accordingly, the decision (1) dismissed the Company's applications for changes in its rates and its cost of capital, (2) dismissed the SCOPE CPUC Complaint, (3) closed the Commission's investigation, and (4) canceled the Company's certificate of public convenience and necessity. Going forward, the Commission will neither set nor enforce the Company's rates and rules of operation. On March 7, 2014, Newhall Land filed an application for rehearing of the decision by the Commission, asserting that the Commission's determination that it lacks jurisdiction over the Company was legally erroneous and that the Commission had failed to follow required procedures in resolving the case. If rehearing is denied or produces an unsatisfactory result, Newhall Land may seek judicial review by petition for writ of review in the California Courts of Appeal or the California Supreme Court. On December 5, 2014, with the Commission not having acted on its application for rehearing, Newhall Land filed a request to hold its application in abeyance pending a final judgment in the related civil case, described more fully below. The Company is not presently in a position to predict whether the effects of the Commission's decision will be sustained or whether it will have a material financial impact.

In addition to the SCOPE CPUC Complaint, on February 8, 2013, SCOPE filed an action in Los Angeles County Superior Court alleging various violations of the Code of Civil Procedure (including a claim of illegal expenditure by Castaic), the California Environmental Quality Act (CEQA) Public Resources Code § 21000 et seq., and the Government Code (including a claim for conflict of interest) in connection with the aforementioned Transaction (Case No. BS141673, the "SCOPE Superior Court Case"). In addition to the Company and its Board of Directors, Newhall Land, Castaic and its board of directors, Stevenson Ranch Venture LLC, and the Company's general manager were named as defendants in the SCOPE Superior Court Case. The Company and its codefendants successfully argued that the CEQA cause of action in the SCOPE Superior Court Case should be dismissed. Additionally, the Company's codefendants filed a motion for judgment on the pleadings regarding SCOPE's conflict of interest claims against Castaic and the Company's general manager (as an individual). On March 20, 2014, the Superior Court granted that motion, resulting in (1) a final judgment in favor of the Company's general manager and (2) an interlocutory judgment in favor of Castaic since Castaic remains a party to the remaining causes of action. SCOPE appealed the judgment in favor of the general manager (but not Castaic) and filed its opening brief on appeal on December 8, 2014. The Company's general manager will file his own brief within 15 days after receiving notice from the court of appeal. Castaic has prepared the administrative record that forms the basis of the evidence in the remainder of the litigation. The court set a trial date of February 24, 2015, and SCOPE filed its opening brief on December 26, 2014. The Company filed its opposition brief, jointly with Castaic and Newhall Land, on January 26, 2015. SCOPE filed its reply brief on February 10, 2015. On February 24, 2015, the parties appeared before the court for oral argument, after which the court took the matter under submission. On March 10, 2015, the court issued a written decision denying all of SCOPE's remaining claims. The court also issued a minute order directing Castaic to prepare a proposed judgment. Once final judgment is entered, a party will have 60 days to appeal the court's judgment. The Company believes that the SCOPE Superior Court Case is without merit and that an unfavorable outcome is unlikely should there be an appeal. If the final decision on appeal in the SCOPE Superior Court Case is unfavorable to the Company, the Company believes the financial impact to it will be immaterial.

10. SUBSEQUENT EVENTS

The Company has evaluated subsequent events through March 18, 2015, the date financial statements were available to be issued.

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