PURE CYCLE CORP
Form 10-Q
January 08, 2010

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
Form 10-Q

(Mark One)

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

For the quarterly period ended: November 30, 2009

or

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

For the transition period from __________ to __________

Commission file number 0-8814

PURE CYCLE CORPORATION

(Exact name of registrant as specified in its charter)

Colorado	**84-0705083**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)
500 E. 8th Ave, Suite 201, Denver, CO	**80203**
(Address of principal executive offices)	(Zip Code)

(303) 292 3456

(Registrant s telephone number, including area code)

8451 Delaware Street, Thornton, CO 80260

(Former name, former address and former fiscal year, if changed since last report)

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

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

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

Large accelerated filer o	Accelerated filer þ	Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller Reporting Company o

Indicate by check mark whether the registrant is a shell company filer (as defined in rule 12b-2 of the Exchange Act). Yes o No þ

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of January 7, 2010:

Common stock, 1/3 of $.01 par value	20,206,566
(Class)	(Number of Shares)

PURE CYCLE CORPORATION
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PURE CYCLE CORPORATION
BALANCE SHEETS

	November 30, 2009 (unaudited)	August 31, 2009
ASSETS:		
Current assets:		
Cash and cash equivalents	$ 408,283	$ 705,083
Marketable securities	3,010,473	3,002,208
Trade accounts receivable	66,385	63,394
Prepaid expenses	138,912	154,928
Current portion of construction proceeds receivable	64,783	64,783
Total current assets	3,688,836	3,990,396
Investments in water and water systems, net	103,068,708	103,159,632
Construction proceeds receivable, less current portion	400,843	414,494
Notes receviable related parties:		
Rangeview Metropolitan District, including accrued interest	510,797	507,795
Well Enhancement and Recovery Systems, LLC	1,998	2,171
Property and equipment, net	14,484	16,593
Total assets	$ 107,685,666	$ 108,091,081
LIABILITIES:		
Current liabilities:		
Accounts payable	$ 13,907	$ 22,216
Accrued liabilities	51,018	60,080
Deferred revenues	55,800	55,800
Total current liabilities	120,725	138,096
Deferred revenues, less current portion	1,432,157	1,446,108
Participating Interests in Export Water Supply	1,216,005	1,216,360
Tap Participation Fee payable to HP A&M, net of $54.7 million and $55.6 million discount	58,405,329	57,521,329
Total liabilities	61,174,216	60,321,893
Commitments and Contingencies		
SHAREHOLDERS EQUITY:		
Preferred stock:		
Series B par value $.001 per share, 25 million shares authorized; 432,513 shares issued and outstanding (liquidation preference of $432,513)	433	433

Common stock:		
Par value 1/3 of $.01 per share, 40 million shares authorized; 20,206,566 shares outstanding	67,360	67,360
Additional paid-in capital	92,276,568	92,253,916
Accumulated comprehensive income	2,283	3,986
Accumulated deficit	(45,835,194)	(44,556,507)
Total shareholders equity	46,511,450	47,769,188
Total liabilities and shareholders equity	$ 107,685,666	$ 108,091,081

See Accompanying Notes to Financial Statements

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PURE CYCLE CORPORATION
STATEMENTS OF OPERATIONS
(unaudited)

	Three months ended November 30, 2009	2008
Revenues:		
Metered water usage	$ 28,878	$ 33,147
Wastewater treatment fees	16,744	16,744
Recognition of deferred revenues:		
Special facility funding	10,377	10,377
Water tap fees	3,574	3,574
Total revenues	59,573	63,842
Expenses:		
Water service operations	(14,761)	(18,871)
Wastewater service operations	(5,629)	(5,493)
Depletion and depreciation	(22,104)	(22,139)
Total cost of revenues	(42,494)	(46,503)
Gross margin	17,079	17,339
General and administrative expenses	(357,410)	(531,305)
Depreciation	(74,729)	(72,612)
Operating loss	(415,060)	(586,578)
Other income (expense):		
Interest income	20,651	35,282
Land use payment		5,000
Share of losses of Well Enhancement and Recovery Systems, LLC	(278)	(2,759)
Interest imputed on the Tap Participation Fee payable to HP A&M	(884,000)	(1,163,000)
Net loss	$ (1,278,687)	$ (1,712,055)
Net loss per common share basic and diluted	$ (0.06)	$ (0.08)
Weighted average common shares outstanding basic and diluted	20,206,566	20,206,566

See Accompanying Notes to Financial Statements

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PURE CYCLE CORPORATION
STATEMENTS OF CASH FLOWS
(unaudited)

	Three months ended November 30, 2009	2008
Cash flows from operating activities:		
Net loss	$ (1,278,687)	$ (1,712,055)
Adjustments to reconcile net loss to net cash used for operating activities:		
Imputed interest on Tap Participation Fee payable to HP A&M	884,000	1,163,000
Depreciation, depletion and other non-cash items	97,498	95,357
Stock-based compensation expense included with general and administrative expenses	22,652	79,202
Share of losses of Well Enhancement and Recovery Systems, LLC	278	2,759
Interest added to construction proceeds receivable	(6,898)	(7,691)
Interest added to notes receivable related parties:		
Rangeview Metropolitan District	(3,002)	(3,907)
Well Enhancement and Recovery Systems, LLC	(105)	(40)
Changes in operating assets and liabilities:		
Trade accounts receivable	(2,991)	24,792
Interest receivable and prepaid expenses	16,016	(55,651)
Accounts payable and accrued liabilities	(17,371)	3,702
Deferred revenues	(13,951)	(13,950)
Net cash used by operating activities	(302,561)	(424,482)
Cash flows from investing activities:		
Investments in water and water systems	(3,801)	(21,065)
Purchase of marketable securities	(9,968)	
Purchase of property and equipment		(12,703)
Issuance of note to Well Enhancement and Recovery Systems LLC		(7,000)
Net cash used by investing activities	(13,769)	(40,768)
Cash flows from financing activities:		
Arapahoe County construction proceeds	20,549	20,549
Payments to contingent liability holders	(1,019)	(931)
Net cash provided by financing activities	19,530	19,618
Net change in cash and cash equivalents	(296,800)	(445,632)
Cash and cash equivalents beginning of year	705,083	5,238,973
Cash and cash equivalents end of year	$ 408,283	$ 4,793,341

See Accompanying Notes to Financial Statements

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PURE CYCLE CORPORATION
NOTES TO FINANCIAL STATEMENTS
NOVEMBER 30, 2009

NOTE 1 PRESENTATION OF INTERIM INFORMATION

The November 30, 2009 balance sheet, the statements of operations for the three months ended November 30, 2009 and 2008, and the statements of cash flows for the three months ended November 30, 2009 and 2008, respectively, have been prepared by Pure Cycle Corporation (the Company) and have not been audited. In the opinion of management, all adjustments, consisting only of normal recurring adjustments necessary to present fairly the financial position, results of operations and cash flows at November 30, 2009, and for all periods presented have been made appropriately.

Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) have been condensed or omitted. It is suggested that these financial statements be read in conjunction with the financial statements and notes thereto included in the Company s 2009 Annual Report on Form 10-K filed with the Securities and Exchange Commission on November 13, 2008. The results of operations for interim periods presented are not necessarily indicative of the operating results for the full year.

The August 31, 2009 balance sheet was taken directly from the Company s audited financial statements.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash and Cash Equivalents

Cash and cash equivalents include all highly liquid debt instruments with original maturities of three months or less. The Company s cash equivalents are comprised entirely of money market funds maintained at a high quality financial institution.

Marketable Securities

At November 30, 2009 and August 31, 2009, the Company s marketable securities were comprised entirely of certificates of deposit maintained at various financial institutions, each of which have invested balances below federally insured limits and pay interest at stated rates through maturity. None of the Company s certificates of deposit had unrealized losses at November 30, 2009 or August 31, 2009. The certificates mature at various dates through February 2011; however, these securities represent temporary investments and it is management s intent to hold these securities available for current operations and not hold them until maturity, therefore they are classified as available-for-sale securities and are recorded at fair value. The Company has no investments in equity instruments.

The Company s marketable securities are recorded as available-for-sale and therefore any unrecognized changes in the fair value of these marketable securities is included as a component of accumulated comprehensive income (loss).

There were no gross realized gains or losses recorded during the three months ended November 30, 2009 or 2008.

Tap Participation Fee payable to HP A&M

Pursuant to the Asset Purchase Agreement (the Arkansas River Agreement) dated August 31, 2006, the Company granted High Plains A&M, LLC (HP A&M) the right to receive ten percent (10%) of the Company s gross proceeds, or the equivalent thereof, from the sale of the next 40,000 water taps sold by the Company from and after the date of the Arkansas River Agreement (the Tap Participation Fee). The 40,000 figure was reduced to 39,470 at the August 31, 2006 closing date because HP A&M sold certain assets and properties not related to the FLCC shares which were subject to the Arkansas River Agreement and were available for credit against the Tap Participation Fee. The 39,470 figure was reduced to 38,965 during the fiscal year ended August 31, 2007, when the Company sold 509 Lower Arkansas Water Management Association (LAWMA) shares for approximately $849,700 (as described in Note 4 to the Company s 2009 Annual Report on Form 10-K). Pursuant to the Arkansas River Agreement, 100% of the proceeds from the sale of the LAWMA shares were required to be paid to HP A&M, which resulted in a credit to the Tap Participation Fee equivalent to the sale of 505 water taps. The 38,965 figure was reduced to 38,937 taps as a result of the sale of non-irrigated land during the fiscal year ended August 31, 2009 (as described in Note 4 to the Company s 2009 Annual Report on Form 10-K).

PURE CYCLE CORPORATION
NOTES TO FINANCIAL STATEMENTS
NOVEMBER 30, 2009

The Tap Participation Fee is due and payable once the Company has sold a water tap and received the consideration due for such water tap. The Company did not sell any water taps during the three months ended November 30, 2009 or 2008.

The Tap Participation Fee was initially valued at approximately $45.6 million at the acquisition date using a discounted cash flow analysis of the projected future payments to HP A&M. The $58.4 million balance at November 30, 2009, includes approximately $13.7 million of imputed interest, recorded using the effective interest method. The Company estimates the value of the Tap Participation Fee by projecting new home development in the Company s targeted service area over an estimated development period. This was done by utilizing third party historical and projected housing and population growth data for the Denver, Colorado metropolitan area applied to an estimated development pattern supported by historical development patterns of certain master planned communities in the Denver, Colorado metropolitan area. This development pattern was then applied to estimated future water tap fees calculated using historical water tap fees. Based on the weak new home construction market in the Denver metropolitan area, the Company updated its estimated discounted cash flow analysis as of February 28, 2009. There have been no significant changes in the assumptions since February 28, 2009, therefore, no change in the Tap Participation Fee was determined necessary after that date.

Actual new home development in the Company s service area and actual future tap fees inevitably will vary significantly from the Company s estimates which could have a material impact on the Company s financial statements as well as its results of operations. An important component in the Company s estimate of the value of the Tap Participation Fee, which is based on historical trends, is that the Company reasonably expects water tap fees to continue to increase in the coming years. Tap fees are a market based pricing metric which in part demonstrates the increasing costs to acquire and develop new water supplies. It is thus a market metric which in part demonstrates the increasing value of the Company s water assets. The Company continues to assess the value of the Tap Participation Fee liability and updates its valuation analysis whenever events or circumstances indicate the assumptions used to estimate the value of the liability have changed materially. The difference between the net present value and the estimated realizable value will be imputed as interest expense using the effective interest method over the estimated development period utilized in the valuation of the Tap Participation Fee.

The Company imputes interest expense on the unpaid Tap Participation Fee using the effective interest method over the estimated development period utilized in the valuation of the liability. The Company imputed interest of approximately $884,000 and $1.2 million during the three months ended November 30, 2009 and 2008, respectively.

After August 31, 2011, under circumstances defined in the Arkansas River Agreement, the Tap Participation Fee can increase to 20% of the Company s water tap fees and the number of water taps subject to the Tap Participation Fee would be correspondingly reduced by half. Payment of the Tap Participation Fee may be accelerated in the event of a merger, reorganization, sale of substantially all assets, or similar transactions and in the event of bankruptcy and insolvency events.

Revenue Recognition

The Company s revenue recognition policies have not changed since August 31, 2009, and therefore are more fully described in Note 2 to the financial statements contained in the Company s 2009 Annual Report on Form 10-K.

The Company recognized approximately $3,600 of water tap fee revenues during each of the three month periods ended November 30, 2009 and 2008, related to the Water Service Agreement (the County Agreement) with Arapahoe County (the County) entered into in August 2005. The Company began recognizing the water tap fees as revenue ratably over the estimated service period upon completion of the Wholesale Facilities (defined in the Company s 2009 Annual Report on Form 10-K) in its fiscal 2006. The water tap fees to be recognized over this period are net of the royalty payments to the State of Colorado Board of Land Commissioners (the Land Board) and amounts paid to third parties pursuant to the Comprehensive Amendment Agreement No. 1 (the CAA) as further described in Note 6 below.

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The Company recognized approximately $10,400 of Special Facilities (defined in the Company s 2009 Annual Report on Form 10-K) funding as revenue during each of the three month periods ended November 30, 2009 and 2008. This is the ratable portion of the Special Facilities funding proceeds received from the County pursuant to the County Agreement as more fully described in Note 4 to the Company s financial statements contained in the Company s 2009 Annual Report on Form 10-K.

As of November 30, 2009, the Company has deferred recognition of approximately $1.5 million of water tap and construction fee revenue from the County, which will be recognized as revenue ratably over the estimated useful accounting life of the assets constructed with the construction proceeds as described above.

Royalty and other obligations

Revenues from the sale of Export Water (which is defined in the Company s 2009 Annual Report on form 10-K) are shown net of royalties payable to the Land Board. Revenues from the sale of water on the Lowry Range Property are shown net of the royalties to the Land Board and the fees retained by the Rangeview Metropolitan District (the District).

Water and Wastewater Systems

If costs meet the Company s capitalization criteria, costs to construct water and wastewater systems are capitalized as incurred, including interest, and depreciated over their estimated useful lives. The Company capitalizes design and construction costs related to construction activities and it capitalizes certain legal, engineering and permitting costs relating to the adjudication and improvement of its water assets.

Depletion and Depreciation of Water Assets

The Company depletes its water assets that are being utilized on the basis of units produced divided by the total volume of water adjudicated in the water decrees. Water systems are depreciated on a straight line basis over their estimated useful lives of up to thirty years.

Share-based Compensation

The Company maintains a stock option plan for the benefit of its employees and directors. The Company records share-based compensation costs which are measured at the grant date based on the fair value of the award and are recognized as expense over the applicable vesting period of the stock award using the straight-line method. The Company has adopted the alternative transition method for calculating the tax effects of share-based compensation which allows for a simplified method of calculating the tax effects of employee share-based compensation. Because the Company has a full valuation allowance on its deferred tax assets, the granting and exercise of stock options has no impact on the income tax provisions.

The Company recognized approximately $22,700 and $79,200 of share-based compensation expenses during the three months ended November 30, 2009 and 2008, respectively.

Income taxes

The Company follows a more-likely-than-not threshold for the recognition and de-recognition of tax positions, including any potential interest and penalties relating to tax positions taken by the Company. The Company does not have any significant unrecognized tax benefits or liabilities.

The Company files income tax returns with the Internal Revenue Service and the State of Colorado. The tax years that remain subject to examination are fiscal 2006 through fiscal 2009. The Company does not believe there will be any material changes in its unrecognized tax positions over the next twelve months.

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The Company s policy is to recognize interest and penalties accrued on any unrecognized tax benefits as a component of income tax expense. At November 30, 2009, the Company did not have any accrued interest or penalties associated with any unrecognized tax benefits, nor was any interest expense recognized during the three months ended November 30, 2009 or 2008.

Recently Issued Accounting Pronouncements

The Company continually assesses new accounting pronouncements to determine their applicability to the Company. Where it is determined that a new accounting pronouncement affects the Company s financial reporting, the Company undertakes a study to determine the consequence of the change to its financial statements and assures that there are proper controls in place to ascertain that the Company s financials properly reflect the change. New pronouncements assessed by the Company recently are discussed below:

In December 2007, the Financial Accounting Standards Board (FASB) issued new accounting and reporting standards for ownership interests in subsidiaries held by parties other than the parent, changes in a parent s ownership of a noncontrolling interest, calculation and disclosure of the consolidated net income attributable to the parent and the noncontrolling interest, changes in a parent s ownership interest while the parent retains its controlling financial interest and fair value measurement of any retained noncontrolling equity investment. The Company adopted the new standards effective September 1, 2009, which did not have a material effect on the Company s financial position, results of operations or cash flows.

In October 2008, the FASB issued new accounting and reporting standards to clarify the application of fair value in inactive markets and allow for the use of management s internal assumptions about future cash flows with appropriately risk-adjusted discount rates when relevant observable market data does not exist. The new guidance has an immediate effective date, including prior periods for which financial statements have not been issued. The objectives of fair value accounting have not changed and the determination of fair value continues to be the determination of the price that would be received in an orderly transaction that is not a forced liquidation or distressed sale at the measurement date. The adoption of the new standards did not have a material effect on the Company s financial position, results of operations or cash flows.

In June 2009, the FASB issued the Accounting Standards Codification (the Codification) to become the single official source of authoritative, nongovernmental GAAP. The Codification did not change GAAP but reorganized the literature. The Company adopted the Codification standards effective September 1, 2009, which did not have a material effect on the Company s financial position, results of operations or cash flows.

In June 2009, the FASB issued new accounting and reporting standards to improve financial reporting by enterprises involved with variable interest entities and to address (1) the effects on certain provisions of FASB Interpretation No. 46 (revised December 2003), *Consolidation of Variable Interest Entities*, (Interpretation 46(R)) as a result of the elimination of the qualifying special-purpose entity concept and (2) constituent concerns about the application of certain key provisions of Interpretation 46(R), including those in which the accounting and disclosures under Interpretation 46(R) do not always provide timely and useful information about an enterprise s involvement in a variable interest entity. The new guidance is effective as of the beginning of each reporting entity s first annual reporting period that begins after November 15, 2009 (September 1, 2010 for the Company), for interim periods within that first annual reporting period, and for interim and annual reporting periods thereafter. The Company is evaluating the impact the adoption of this guidance will have on its financial statements.

NOTE 2 FAIR VALUE MEASUREMENTS

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date in the principal or most advantageous market. The Company uses a fair value hierarchy that has three levels of inputs, both observable and unobservable, with use of the lowest possible level of input to determine fair value.

Level 1 Valuations for assets and liabilities traded in active exchange markets, such as the New York Stock Exchange. The Company had none of these instruments at November 30, 2009.

Level 2 Valuations are obtained from readily available pricing sources via independent providers for market transactions involving similar assets or liabilities. The Company s principal market for these securities is the secondary institutional markets and valuations are based on observable market data in those markets. The Company had one Level 2 asset at November 30, 2009.

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Level 3 Valuations for assets and liabilities that are derived from other valuation methodologies, including discounted cash flow models and similar techniques, and not based on market exchange, dealer, or broker traded transactions. Level 3 valuations incorporate certain assumptions and projections in determining the fair value assigned to such assets or liabilities. The Company had one Level 3 liability at November 30, 2009, the Tap Participation Fee liability, which is described in greater detail in Note 1 above.

The Company maintains policies and procedures to value instruments using the best and most relevant data available. The Company applied the new accounting guidance issued by the FASB for all non-financial assets and liabilities measured at fair value on a non-recurring basis at September 1, 2009. The Company s non-financial assets measured at fair value on a non-recurring basis consists entirely of its investments in water and water systems and other long-lived assets. Since the Company performed its annual impairment analyses of its long-lived assets as of August 31, 2009, (with no indicators of impairment) and since no impairment trigger event occurred during the first quarter of fiscal 2010, the adoption of the new FASB standard for non-financial assets and liabilities measured at fair value on a non-recurring basis did not have an impact on the Company s financial position, results of operations or cash flows.

Level 2 Asset Marketable Securities Measured on a Recurring Basis

The Company s marketable securities are the Company s only financial assets measured on a recurring basis. The fair values of the marketable securities are based on the values reported by the financial institutions where the funds are held. These securities include only federally insured certificates of deposit.

Level 3 Liability Tap Participation Fee Payable to HP A&M

The Company s Tap Participation Fee liability is the Company s only financial liability measured on a non-recurring basis. As further described in Note 1 above, the Tap Participation Fee liability is valued by projecting new home development in the Company s targeted service area over an estimated development period.

The following table provides information on the assets and liabilities measured at fair value as of November 30, 2009.

			Fair Value Measurement Using:			
	Carrying Value	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Unrealized Gains and Losses
Marketable securities	$ 3,010,473	$ 3,010,473	$	$ 3,010,473	$	$ 2,283
Tap Participation Fee liability	$ 58,405,329	$ 58,405,329	$	$	$ 58,405,329	$

Although not required, the Company deems the following table, which presents the changes in the Tap Participation Fee for the three months ended November 30, 2009, to be helpful to the users of its financial statements.

PURE CYCLE CORPORATION
NOTES TO FINANCIAL STATEMENTS
NOVEMBER 30, 2009

	Fair Value Measurement at November 30 using Significant Unobservable Inputs (Level 3)		
	Gross Estimated Tap Participation Fee Liability	Tap Participation Fee Reported Liability	Discount - to be imputed as interest expense in future periods
Balance at August 31, 2009	$ 113,147,688	$ 57,521,329	$ 55,626,359
Total gains and losses (realized and unrealized):			
Imputed interest recorded as Other Expense		884,000	(884,000)
Increase in estimated value (to be realized in future periods)			
Purchases, sales, issuances, payments, and settlements			
Transfers in and/or out of Level 3			
Balance at November 30, 2009	$ 113,147,688	$ 58,405,329	$ 54,742,359

The methodologies for estimating the fair value of financial assets and liabilities that are measured at fair value are discussed above. The methodologies for other financial assets and liabilities are discussed below.

Cash and Cash Equivalents: The Company s cash and cash equivalents are reported using the values as reported by the financial institution where the funds are held. These securities primarily include balances in the Company s operating and savings accounts. The carrying amount of cash and cash equivalents approximate fair value.

Accounts Receivable and Accounts Payable: The carrying amounts of accounts receivable and accounts payable approximate fair value due to the relatively short period to maturity for these instruments.

Notes Receivable and Construction Proceeds Receivable: The carrying amounts of the Company s notes receivable and construction proceeds receivable approximate fair value as they bear interest at rates which are comparable to current market rates.

Off-Balance Sheet Instruments: The Company s off-balance sheet instruments consist entirely of the contingent portion of the CAA (described further in Note 6 below). Because repayment of this portion of the CAA is contingent on the sale of Export Water, the Company has determined that the contingent portion of the CAA does not have a determinable fair value.

NOTE 3 INVESTMENTS IN WATER AND WATER SYSTEMS

The Company s investments in water and water systems consist of the following:

	November 30, 2009 (unaudited)		August 31, 2009	
	Costs	Accumulated Depreciation and Depletion	Costs	Accumulated Depreciation and Depletion
Arkansas River Valley assets	$ 81,241,428	$ (893,797)	$ 81,241,428	$ (823,660)
Rangeview water supply	14,271,786	(5,632)	14,271,786	(5,544)
Rangeview water system	167,720	(53,276)	167,720	(51,978)

Paradise water supply	5,536,420		5,532,619	
Fairgrounds water and water system	2,899,863	(292,334)	2,899,863	(270,317)
Sky Ranch water supply	100,000		100,000	
LAWMA Shares	77,940		77,940	
Water supply other	23,713	(5,123)	23,713	(3,938)
Totals	104,318,870	(1,250,162)	104,315,069	(1,155,437)
Net investments in water and water systems	$ 103,068,708		$ 103,159,632	

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PURE CYCLE CORPORATION
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The Company s water rights and current water and wastewater service agreements are more fully described in Note 4 to the financial statements contained in the Company s 2009 Annual Report on Form 10-K. There have been no significant changes to the Company s water rights or water and wastewater service agreements during the three months ended November 30, 2009.

Depletion and Depreciation

The Company recorded approximately $100 and $120 of depletion charges during the three months ended November 30, 2009 and 2008, respectively. This related entirely to the use of the Rangeview Water Supply. No depletion is taken against the Arkansas River water, the Paradise Water Supply or Sky Ranch Water Supply because these assets have not been placed into service as of November 30, 2009.

The Company recorded approximately $96,700 and $94,600 of depreciation expense during the three months ended November 30, 2009 and 2008, respectively.

NOTE 4 HP A&M PROMISSORY NOTES

Certain of the properties the Company acquired from HP A&M are subject to outstanding promissory notes with principal and accrued interest totaling approximately $12.0 million at November 30, 2009 and August 31, 2009. Additional information regarding these promissory notes, the circumstances under which the Company would be required to make payments pursuant to these notes and the accounting treatment of these notes is more fully described in Note 8 to the financial statements contained in the Company s 2009 Annual Report on Form 10-K.

NOTE 5 INVESTMENT IN, AND NOTE RECEIVABLE FROM, WELL ENHANCEMENT LLC

Effective January 30, 2007, the Company entered into an Operating Agreement with Energy Technologies, Inc. and Hydro Resources Holdings, Inc. (collectively the Company, Energy Technologies, Inc. and Hydro Resources Holdings, Inc. are referred to as the LLC Owners) to form Well Enhancement LLC. Well Enhancement LLC was established to develop a proprietary new deep water well enhancement tool and process which the LLC Owners believe will increase the efficiency of deep water wells in the Denver metropolitan area. Each of the LLC Owners holds a 1/3 interest in Well Enhancement LLC. The President of the Company acts as the manager of Well Enhancement LLC.

The Company uses the equity method to account for its investment in Well Enhancement LLC. As of November 30, 2009, as a result of the recognition of the Company s 1/3 share of the losses of Well Enhancement LLC, the Company s *Investment in Well Enhancement and Recovery Systems, LLC* account on its balance sheet has been reduced to zero. However, once the investment account was reduced to zero, the Company began recording its share of Well Enhancement LLC s losses against the note receivable from Well Enhancement LLC described below. The investment account and the receivable account on the Company s balance sheet include $87,000 of capital contributions made to date, the $7,000 loan with accrued interest of $460 and the Company s 1/3 share of the approximately $277,000 of net losses of Well Enhancement LLC from inception through November 30, 2009.

For the three months ended November 30, 2009 and 2008, the Company recorded approximately $280 and $2,800, respectively, of its share of Well Enhancement LLC s losses. The net losses are primarily a result of research and development costs and professional fees associated with the design and patent application process of the well enhancement tool. During the three months ended November 30, 2008, as a result of the recognition of the Company s 1/3rd share of the losses of Well Enhancement LLC, the Company s *Investment in Well Enhancement and Recovery Systems, LLC* account on its balance sheet had been reduced to zero. Because of this, the Company ceased recognizing its share of Well Enhancement LLC s losses until the Company made an additional contribution to Well Enhancement LLC. Therefore, the Company did not recognize approximately $3,200 of Well Enhancement LLC s losses for the three months ended November 30, 2008.

PURE CYCLE CORPORATION
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As of November 30, 2009, Well Enhancement LLC s assets and liabilities consisted of the following approximate amounts:

Well Enhancement LLC Assets and Liabilities

Cash	$	4,200
Accrued professional fees	$	1,800
Notes payable related parties, including accrued interest	$	21,600

On October 27, 2008, the Company loaned Well Enhancement LLC $7,000 for use in its operations. The note receivable from Well Enhancement LLC carries simple interest at six percent (6%) per annum, and matures on October 27, 2011, with no payments due until maturity.

NOTE 6 PARTICIPATING INTERESTS IN EXPORT WATER

The Company acquired its Rangeview Water Supply through various amended agreements entered into in the early 1990 s. The acquisition was consummated with the signing of the CAA in 1996. Upon entering into the CAA, the Company recorded an initial liability of approximately $11.1 million, which represents the cash the Company received and used to purchase its Export Water. In return, the Company agreed to remit a total of $31.8 million of proceeds received from the sale of Export Water to the participating interest holders. The oblig