
HERRON MAINTENANCE COMPANY

AUDITED FINANCIAL STATEMENTS

For the Fiscal Year Ended September 30, 2002

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To the Board of Directors and Members
Herron Maintenance Company
Herron Island, Washington

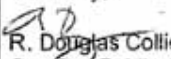
INDEPENDENT AUDITOR'S REPORT

We have audited the accompanying Balance Sheet of **Herron Maintenance Company** as of September 30, 2002 and the related Statements of Revenues, Expenses and Changes in Members' Equity, and Cash Flows for the year then ended. These financial statements are the responsibility of the Association's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards. 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 includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion the financial statements referred to above present fairly, in all material respects, the financial position of Herron Maintenance Company as of September 30, 2002, and the results of its activities and its cash flows for the years then ended in conformity with generally accepted accounting principles. This report is intended solely for the information and use of (the specified parties) and is not intended to be and should not be used by anyone other than these specified parties.

Sincerely,


R. Douglas Collier
Certified Public Accountant
November 11, 2002

HERRON MAINTENANCE COMPANY

(A Homeowners' Association)

BALANCE SHEET

September 30, 2002

ASSETS

Cash and Cash Equivalents		\$	39,845
Accounts Receivable	\$	108,268	
Less Allowance for Uncollectible Accounts		-	
Total Accounts Receivable			108,268
Restricted Funds (Vanguard)			
Docks/Dolphins Reserves	76,536		
Dry Dock Reserves	78,408		
Legal and Insurance Reserves	12,358		
Road Reserves	7,838		
Water Reserves	58,245		
Total Restricted Funds			233,385
Taxes receivable			0
Certificate of Deposit			1,017
Prepaid Expenses			7,257
Property & Equipment			
Ferry	729,711		
Ferry Major Repair & Dry Dock	48,650		
Ferry Steering System	19,435		
Ferry Dock & Repairs	1,232,386		
Ferry Dock Dolphins	37,838		
Equipment & Office Improvements	45,652		
Small Boat Dock	30,459		
Major Road Repairs	40,245		
Less Accumulated Depreciation	(786,717)		
Total Property & Equipment			1,397,659
Land			16,930
TOTAL ASSETS		\$	1,804,361

LIABILITIES & MEMBERS' EQUITY

Accounts Payable	\$	6,000
Payroll & Pension Liability		3,319
Members' Equity		1,795,042
TOTAL LIABILITIES & MEMBERS' EQUITY	\$	1,804,361

See accompanying Independent Auditor's Report.
The accompanying notes are an integral part of the financial statements.

HERRON MAINTENANCE COMPANY

(A Homeowners' Association)

STATEMENT OF REVENUES & EXPENSES AND CHANGES IN MEMBERS' EQUITY

For the Fiscal Year Ended September 30, 2002

REVENUES			
Annual Assessments	\$	300,127	
Ferry Fees		109,048	
Interest Income		18,093	
Miscellaneous		14,615	
TOTAL REVENUES			\$ 441,883
EXPENSES			
Administrative			
Accounting & Payroll Service	\$	5,205	
Amortization & Depreciation		9,259	
Bad Debt		37,361	
Insurance		25,436	
Legal & Collection Fees		9,296	
Miscellaneous		4,294	
Office, Printing & Postage		8,255	
Salaries, Payroll Taxes, & Benefits		40,313	
State & County Taxes		2,457	
Telephone		1,163	
Total Administrative Expenses			143,039
Ferry Docks			
Depreciation		34,594	
Repairs & Maintenance		17,085	
Parts & Supplies		1,454	
Utilities		966	
Total Ferry Docks Expenses			54,119
Ferry			
Depreciation		44,410	
Equipment		1,132	
Fuel		16,504	
Insurance		42,427	
Major Repairs & Dry Dock		476	
Routine Maintenance		8,990	
Salaries, Payroll Taxes & Benefits		162,264	
Taxes- Personal Property & Excise		2,933	
Utilities, Supplies & Other		9,450	
Total Ferry Expenses			288,586
Park Expenses			8,255
Road Expenses			14,036
Water Expenses			
Salaries & Payroll Taxes		4,337	
Repairs, Supplies, Utilities & Other		8,921	
Total Water Expenses			13,258
TOTAL EXPENSES			<u>521,283</u>
Excess/(Deficiency) of Revenues over Expenses			(79,410)
Members' Equity on September 30, 2001			<u>1,874,452</u>
Members' Equity on September 30, 2002			<u>\$ 1,795,042</u>

See accompanying Independent Auditor's Report.
The accompanying notes are an integral part of the financial statements.

HERRON MAINTENANCE COMPANY

(A Homeowners' Association)

STATEMENT OF CASH FLOWS

For the Fiscal Year Ended September 30, 2002

Cash Flows from Operating Activities

Deficiency of Revenue over Expenses \$ (79,410)

Adjustments to reconcile Deficiency of Revenue over Expenses to Cash Flows from Operating Activities:

Amortization & Depreciation	89,024
Decrease in Accounts Receivable	21,287
Decrease in Allowance for Collectibles	(3,044)
Decrease in Federal Taxes Receivable	3,000
Increase in Prepaid Insurance	(7,257)
Increase in Accounts Payable	2,016
Increase in Pension Payable	484

Net Cash used by Operating Activities \$ 26,100

Cash Flows from Investing Activities

Investment in Reserve Accounts (28,152)

Net Cash used by Investing Activities (28,152)

Net Decrease in Cash \$ (2,052)

CASH ON SEPTEMBER 30, 2001 41,897

CASH ON SEPTEMBER 30, 2002 \$ 39,845

See accompanying Independent Auditor's Report.
The accompanying notes are an integral part of the financial statements.

HERRON MAINTENANCE COMPANY
NOTES TO THE FINANCIAL STATEMENTS
For the Fiscal Year Ended September 30, 2002

**NOTE A - NATURE OF ORGANIZATION AND SUMMARY OF SIGNIFICANT
ACCOUNTING POLICIES**

Nature of Organization

Herron Maintenance Company (HMC) was incorporated on May 1, 1958, in the state of Washington. HMC is responsible for the operation and maintenance of the common property on Herron Island and the wharf of the corporation located at Herron, including the specific purpose of maintaining and operating the private ferry between the wharf at Herron and Herron Island. All island lot owners are members of HMC. There are approximately 376 members.

Accrual Basis

HMC's financial statements present financial position and results of operations on the accrual basis of accounting. Accrual accounting is the method of recording transactions, by which revenues and expenses are reflected in the accounts in the period in which they are considered to have been earned and incurred, respectively, whether or not such transactions have been finally settled by the receipt or payment of cash or its equivalent.

Cash and Cash Equivalents

The Association considers cash on deposit, cash on hand, money market funds (if any) to be cash equivalents.

Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires the board of directors to make estimates and assumptions that may 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.

Member Assessments

HMC members are subject to annual assessments to provide funds for HMC's operating expenses, future capital acquisitions, and major repairs and replacements. Accounts receivable at the balance sheet date represents fees due from lot owners. HMC's policy is to retain legal counsel and place liens on the properties of lot owners whose assessments are 30 days or more delinquent. Any excess assessments at year-end are retained by HMC for use in the succeeding year.

HERRON MAINTENANCE COMPANY

NOTES TO THE FINANCIAL STATEMENTS

For the Fiscal Year Ended September 30, 2002

Income Taxes

Homeowners' associations may be taxed either as homeowners' associations or as regular corporations. HMC has elected to be taxed as homeowners' association. Under that election, the association is taxed on its nonexempt function income, such as interest earnings, at a flat rate of 30%. Exempt function income, which consists primarily of member assessments, is not taxable.

Property and Equipment

Property, plant, and equipment are stated at cost. All assets purchased for over \$500 are capitalized and depreciated over their useful life. Capitalized common property is depreciated over its estimated useful life using the straight-line method of depreciation. At acquisition, the estimated useful life of the ferry and ferry docks were 20 years and 40 years respectively. The estimated useful lives of capitalized equipment are five to seven years.

Assets acquired when the organization was first formed were not capitalized. This is a departure from generally accepted accounting principles. Its effect on HMC's financial position has not been determined, but it is considered immaterial due to the age of the assets.

Land

Property not capitalized includes, but is not limited to, land parcels acquired through foreclosure. At September 30, 2002 a total of twenty-one such parcels have been acquired.

A total of four lots have been deeded in lieu of paying the outstanding assessments to the organization. The value of these lots as of the balance sheet date was \$16,930. The organization plans to retain one lot. The other three lots are to be sold in the near future to recover their costs. Three of these lots are recorded at their assessed value of \$3,800, and the balance of the outstanding assessment was allocated to bad debt expense. The remaining lot is recorded at a cost (delinquent amount) of \$13,130.

NOTE B - ASSESSMENTS RECEIVABLE

Assessments receivable consists of general assessments which are used to maintain operations of HMC property and the ferry dock assessment, which was used to build the new ferry dock.

HERRON MAINTENANCE COMPANY
NOTES TO THE FINANCIAL STATEMENTS
For the Fiscal Year Ended September 30, 2002

NOTE C - FUTURE MAJOR REPAIRS AND REPLACEMENTS

HMC's governing documents do not require the accumulation of funds to finance estimated future major repairs and replacements. The corporation has not conducted a study to determine the remaining useful lives of the components of common property and estimates of the costs of major repairs and replacements that may be required in the future. Herron Maintenance currently sets aside funds for dry dock, docks and dolphins, legal and insurance, water system, roads, and a few other planned and unplanned expenses. If these funds are drained the corporation plans to borrow, increase maintenance assessments, or delay repairs and replacements until funds are available. The effect on future assessments has not been determined.

NOTE D - INSURANCE

HMC is an accrual basis corporation. Insurance is reported on cash basis. In prior years HMC has used the pure accrual method for reporting insurance by use of a prepaid insurance asset account. The Board of Directors has determined that they would like to see the insurance when paid for ease in budgeting for future periods. The amounts have been determined to be immaterial when looking at the financial statement in its entirety.