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# HERRON MAINTENANCE COMPANY

## AUDITED FINANCIAL STATEMENTS

*For the Fiscal Year Ended September 30, 2003*

### CONTENTS

Independent Auditors' Report.....	1
Balance Sheet .....	2
Statement of Revenue, Expenses and Changes in Members' Equity.....	3
Statement of Cash Flows .....	4
Notes to the Financial Statements .....	5-7

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

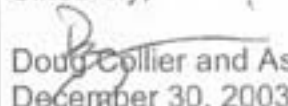
## INDEPENDENT AUDITORS' REPORT

We have audited the accompanying Balance Sheet of **Herron Maintenance Company** as of September 30, 2003 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 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 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, 2003, 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,

  
Doug Collier and Associates, P.S.  
December 30, 2003

# HERRON MAINTENANCE COMPANY

(A Homeowners' Association)

## BALANCE SHEET

September 30, 2003

### ASSETS

Cash and Cash Equivalents \$ 41,517

Accounts Receivable 69,687

Total Accounts Receivable

Restricted Funds (Vanguard)

Docks/Dolphins Reserves 77,344

Dry Dock Reserves 11,069

Legal and Insurance Reserves 25,038

Road Reserves 7,921

Water Reserves 58,860

Total Restricted Funds 180,232

Certificate of Deposit 1,034

Prepaid Expenses 963

Property & Equipment

Ferry 729,711

Ferry Major Repair & Dry Dock 48,650

Ferry Steering System 19,435

Ferry Dock & Repairs 1,232,388

Ferry Dock Dolphins 37,838

Equipment & Office Improvements 45,652

Small Boat Dock 30,459

Major Road Repairs 40,245

Less Accumulated Depreciation (875,572)

Total Property & Equipment 1,308,804

Land 16,930

**TOTAL ASSETS \$ 1,619,167**

### LIABILITIES & MEMBERS' EQUITY

Accounts Payable \$ 9,189

Members' Equity 1,609,978

**TOTAL LIABILITIES & MEMBERS' EQUITY \$ 1,619,167**

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, 2003

### REVENUES

Annual Assessments	\$	331,592	
Ferry Fees		111,725	
Interest Income		10,922	
Miscellaneous		11,230	
<b>TOTAL REVENUES</b>			\$ 465,469

### EXPENSES

Administrative			
Accounting & Payroll Service	\$	5,391	
Amortization & Depreciation		9,095	
Bad Debt		56,284	
Insurance		18,282	
Legal & Collection Fees		9,186	
Miscellaneous		4,091	
Office, Printing & Postage		6,837	
Salaries, Payroll Taxes, & Benefits		47,097	
State & County Taxes		1,973	
Telephone		1,730	
<b>Total Administrative Expenses</b>			159,966
Ferry Docks			
Depreciation		34,594	
Repairs & Maintenance		629	
Parts & Supplies		2,214	
Utilities		1,054	
<b>Total Ferry Docks Expenses</b>			38,491
Ferry			
Depreciation		44,405	
Equipment		2,427	
Fuel		22,024	
Insurance		42,114	
Major Repairs & Dry Dock		117,822	
Routine Maintenance		5,962	
Salaries, Payroll Taxes & Benefits		173,713	
Taxes- Personal Property & Excise		2,706	
Utilities, Supplies & Other		9,486	
<b>Total Ferry Expenses</b>			420,659
Park Expenses			6,982
Road Expenses			6,661
Water Expenses			
Salaries & Payroll Taxes		4,545	
Repairs, Supplies, Utilities & Other		14,632	
<b>Total Water Expenses</b>			19,177
<b>TOTAL EXPENSES</b>			<u>651,936</u>
<b>Deficiency of Revenues over Expenses</b>			(186,467)
<b>Members' Equity on September 30, 2002</b>			<u>1,796,445</u>
<b>Members' Equity on September 30, 2003</b>			<u>\$ 1,609,978</u>

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, 2003

### Cash Flows from Operating Activities

Deficiency of Revenue over Expenses \$ (186,467)

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

Amortization & Depreciation	88,856
Decrease in Accounts Receivable	38,591
Decrease in Prepaid Insurance	6,672
Increase in Accounts Payable	900

Net Cash used by Operating Activities \$ (51,448)

Net Decrease in Cash (51,448)

CASH AND CASH EQUIVALENTS ON SEPTEMBER 30, 2002 274,231

CASH AND CASH EQUIVALENTS ON SEPTEMBER 30, 2003 \$ 222,783

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, 2003*

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**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 369 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, 2003*

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**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, 2003 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, 2003*

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**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.