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# HERRON MAINTENANCE COMPANY

## AUDITED FINANCIAL STATEMENTS

*For the Fiscal Year Ended September 30, 2003*

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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
<b>TOTAL ASSETS</b>		<b>\$</b>	<b>1,619,167</b>
<b>LIABILITIES &amp; MEMBERS' EQUITY</b>			
Accounts Payable		\$	9,189
Members' Equity			1,609,978
<b>TOTAL LIABILITIES &amp; MEMBERS' EQUITY</b>		<b>\$</b>	<b>1,619,167</b>

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>	<b>\$ 465,469</b>
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>	<b>159,966</b>
Ferry Docks	
Depreciation	34,594
Repairs & Maintenance	629
Parts & Supplies	2,214
Utilities	1,054
<b>Total Ferry Docks Expenses</b>	<b>38,491</b>
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>	<b>420,659</b>
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>	<b>19,177</b>
<b>TOTAL EXPENSES</b>	<b>651,936</b>
Deficiency of Revenues over Expenses	(186,467)
Members' Equity on September 30, 2002	1,796,445
Members' Equity on September 30, 2003	<b>\$ 1,609,978</b>

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.