

# FREDRICKZINKELLIOTT

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## INDEPENDENT AUDITOR'S REPORT


To the Board of Directors  
Colorado's Timber Ridge Homeowners Association  
Pagosa Springs, Colorado

We have audited the accompanying balance sheets of Colorado's Timber Ridge Homeowners Association as of December 31, 2000, 2001, 2002, 2003, 2004 and August 21, 2005, and the related statements of revenues, expenses, and changes in members' equity and cash flows for the periods from inception to August 21, 2005. These financial statements are the responsibility of the Declarant acting as 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 Colorado's Timber Ridge Homeowners Association as of December 31, 2000, 2001, 2002, 2003, 2004 and August 21, 2005, and the results of its operations and its cash flows for the periods from inception to August 21, 2005 in conformity with accounting principles generally accepted in the United States of America.

Colorado's Timber Ridge Homeowners Association has not estimated the remaining lives and replacements costs of the common property and, therefore, has not presented the required supplementary information about future major repairs and replacements that accounting principles generally accepted in the United States of America has determined is required to supplement, although not required to be a part of, the basic financial statements.

  
FredrickZinkElliott, PC

March 15, 2006

**COLORADO'S TIMBER RIDGE  
HOMEOWNERS ASSOCIATION**

**BALANCE SHEETS**

December 31, 2000, 2001, 2002, 2003, 2004 and  
August 21, 2005

	<u>December 31, 2000</u>	<u>December 31, 2001</u>	<u>December 31, 2002</u>	<u>December 31, 2003</u>	<u>December 31, 2004</u>	<u>August 21, 2005</u>
<b>ASSETS</b>						
Current Assets						
Cash	\$ 8,751	\$ 13,628	\$ 23,455	\$ 12,525	\$ 13,289	\$ 48,521
Assessments receivable-members	74	250	1,375	8,125	16,375	9,375
Assessments receivable-developer	11,546	20,788	26,462	38,437	46,905	41,311
Accounts receivable - developer	-	5,153	9,893	21,158	30,488	31,339
Prepaid expenses	345	561	1,367	1,388	1,337	2,595
Total current assets	<u>20,716</u>	<u>40,380</u>	<u>62,552</u>	<u>81,633</u>	<u>108,394</u>	<u>133,141</u>
Other assets						
Mailboxes	-	-	-	5,607	5,607	5,607
Accumulated depreciation	-	-	-	(280)	(840)	(1,400)
Total other assets	<u>-</u>	<u>-</u>	<u>-</u>	<u>5,327</u>	<u>4,767</u>	<u>4,207</u>
Total assets	<u>\$ 20,716</u>	<u>\$ 40,380</u>	<u>\$ 62,552</u>	<u>\$ 86,960</u>	<u>\$ 113,161</u>	<u>\$ 137,348</u>
<b>LIABILITIES AND MEMBER'S EQUITY</b>						
Current Liabilities						
Accounts payable	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 441
Prepaid assessments	-	-	250	-	1,021	-
Total current liabilities	<u>-</u>	<u>-</u>	<u>250</u>	<u>-</u>	<u>1,021</u>	<u>441</u>
Members' equity						
Undesignated	20,716	40,380	62,302	86,960	112,140	136,907
Total members' equity	<u>20,716</u>	<u>40,380</u>	<u>62,302</u>	<u>86,960</u>	<u>112,140</u>	<u>136,907</u>
Total liabilities and members' equity	<u>\$ 20,716</u>	<u>\$ 40,380</u>	<u>\$ 62,552</u>	<u>\$ 86,960</u>	<u>\$ 113,161</u>	<u>\$ 137,348</u>

The accompanying notes are an integral part of these financial statements.

**COLORADO'S TIMBER RIDGE**  
**HOMEOWNERS ASSOCIATION**

**STATEMENTS OF REVENUES AND EXPENSES AND CHANGES IN MEMBERS' EQUITY**

For the Period from Inception to December 31, 2000,  
The Years Ended December 31, 2001, 2002, 2003 and 2004, and  
The Period January 1 to August 21, 2005

	Inception to December 31, 2000	Year Ended December 31, 2001	Year Ended December 31, 2002	Year Ended December 31, 2003	Year Ended December 31, 2004	January 1, to August 21, 2005
<b>Revenues</b>						
Assessments	\$ 23,978	\$ 32,045	\$ 40,449	\$ 50,975	\$ 50,475	\$ 50,750
Other income	207	695	1,051	3,123	1,009	750
Total revenues	<u>24,185</u>	<u>32,740</u>	<u>41,500</u>	<u>54,098</u>	<u>51,484</u>	<u>51,500</u>
<b>Expenses</b>						
Operating expenses						
Grounds maintenance	-	350	3,673	4,575	4,149	-
Snow plowing	1,875	8,365	1,140	5,043	11,450	10,962
Other repairs, maintenance	180	345	1,160	924	225	-
Professional fees	350	3,142	5,365	5,683	5,539	4,085
Insurance	441	874	1,850	2,900	3,102	1,986
Office and other expense	623	-	709	969	957	615
Depreciation	-	-	-	280	560	560
Total operating expenses	<u>3,469</u>	<u>13,076</u>	<u>13,897</u>	<u>20,374</u>	<u>25,982</u>	<u>18,208</u>
Other expenses and losses						
Annual picnic	-	-	5,397	8,450	-	-
Contributions	-	-	150	100	76	-
Loss on write-offs	-	-	134	516	246	8,525
Total other	<u>-</u>	<u>-</u>	<u>5,681</u>	<u>9,066</u>	<u>322</u>	<u>8,525</u>
Total expenses	<u>3,469</u>	<u>13,076</u>	<u>19,578</u>	<u>29,440</u>	<u>26,304</u>	<u>26,733</u>
Excess of revenues over expenses	20,716	19,664	21,922	24,658	25,180	24,767
Members' equity beginning of period	-	20,716	40,380	62,302	86,960	112,140
Members' equity end of period	<u>\$ 20,716</u>	<u>\$ 40,380</u>	<u>\$ 62,302</u>	<u>\$ 86,960</u>	<u>\$ 112,140</u>	<u>\$ 136,907</u>

The accompanying notes are an integral part of these financial statements.

**COLORADO'S TIMBER RIDGE**  
**HOMEOWNERS ASSOCIATION**

**STATEMENTS OF CASH FLOWS**

For the Period from Inception to December 31, 2000,  
The Years Ended December 31, 2001, 2002, 2003 and 2004, and  
The Period January 1 to August 21, 2005

	Inception to December 31, 2000	Year Ended December 31, 2001	Year Ended December 31, 2002	Year Ended December 31, 2003	Year Ended December 31, 2004	January 1, to August 21, 2005
<b>Cash flows from operating activities</b>						
Cash received from developer and members	\$ 12,565	\$ 18,169	\$ 30,211	\$ 23,858	\$ 26,457	\$ 63,243
Cash paid to suppliers	(3,814)	(13,292)	(20,384)	(29,181)	(25,693)	(28,011)
Net cash provided (used) by operating activities	<u>8,751</u>	<u>4,877</u>	<u>9,827</u>	<u>(5,323)</u>	<u>764</u>	<u>35,232</u>
<b>Cash flows from investing activities</b>						
Purchase of depreciable assets	-	-	-	(5,607)	-	-
Net cash used by investing activities	<u>-</u>	<u>-</u>	<u>-</u>	<u>(5,607)</u>	<u>-</u>	<u>-</u>
<b>Cash flows from financing activities</b>						
	-	-	-	-	-	-
Net increase (decrease) in cash	8,751	4,877	9,827	(10,930)	764	35,232
Cash Beginning of Period	-	8,751	13,628	23,455	12,525	13,289
Cash End of Period	<u>\$ 8,751</u>	<u>\$ 13,628</u>	<u>\$ 23,455</u>	<u>\$ 12,525</u>	<u>\$ 13,289</u>	<u>\$ 48,521</u>
<b>Reconciliation of excess revenues over expenses to net cash provided (used) by operating activities</b>						
Excess of revenues over expenses	\$ 20,716	\$ 19,664	\$ 21,922	\$ 24,658	\$ 25,180	\$ 24,767
<b>Adjustments to reconcile excess of revenues over expenses to net cash provided (used) by operating activities</b>						
Decrease (increase) in						
Assessments receivable-members	(74)	(176)	(1,125)	(6,750)	(8,250)	7,000
Assessments receivable-developer	(11,546)	(9,242)	(5,674)	(11,975)	(8,468)	5,594
Accounts receivable-developer	-	(5,153)	(4,740)	(11,265)	(9,330)	(851)
Prepaid expenses	(345)	(216)	(806)	(21)	51	(1,258)
Increase (decrease) in						
Accounts payable	-	-	-	-	-	441
Prepaid assessments	-	-	250	(250)	1,021	(1,021)
Depreciation	-	-	-	280	560	560
Total adjustments	<u>(11,965)</u>	<u>(14,787)</u>	<u>(12,095)</u>	<u>(29,981)</u>	<u>(24,416)</u>	<u>10,465</u>
Net cash provided (used) by operating activities	<u>\$ 8,751</u>	<u>\$ 4,877</u>	<u>\$ 9,827</u>	<u>\$ (5,323)</u>	<u>\$ 764</u>	<u>\$ 35,232</u>

The accompanying notes are an integral part of these financial statements.

# **COLORADO'S TIMBER RIDGE** **HOMEOWNERS ASSOCIATION**

## **NOTES TO FINANCIAL STATEMENTS**

Inception to August 21, 2005

### **NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

#### **Nature of organization**

Colorado's Timber Ridge Homeowners Association was incorporated as a non-profit corporation in the State of Colorado on September 27, 1999 for the purposes of operating and maintaining the roads and other common property of Colorado's Timber Ridge Homeowners Association. Colorado's Timber Ridge Homeowners Association consists of 203 lots located in Archuleta County, Colorado. The Association began operations in January 2000. In accordance with the Association's bylaws, the declarant control period was deemed to have ended August 21, 2005.

#### **Basis of presentation**

The Association's financial statements are presented on the accrual basis of accounting. The accounting policies followed conform to the industry audit and accounting guide titled *Common Interest Realty Associations* issued by the American Institute of Certified Public Accountants.

#### **Assessments receivable - members**

Association members are subject to annual assessments to provide funds for the Association's operating expenses and major repairs and replacements. Any excess assessments at year end are retained by the Association for use in the succeeding year. The first member assessments were levied in 2000. Assessments receivable-members at the balance sheet date represent fees due from lot owners. The Association's stated policy is to retain legal counsel and place liens on the lots of members whose assessments are delinquent. Accordingly, no amounts would typically be considered uncollectible. However, since analysis of assessments receivable was not performed until 2005, it was determined at that time that the likelihood of collecting certain balances was remote (primarily on properties that had changed ownership and had not been liened). Balances from 2003 or earlier were recognized as losses in 2005 and an allowance for uncollectible accounts was established. (Note 2)

Special assessments may be levied, upon approval by the members, to defray costs of construction, reconstruction, repair or replacement of improvements, or to make up shortfalls in a current budget.

#### **Assessments and accounts receivable - developer**

The developer is liable for assessments on unsold lots from the date of the first sale within each particular phase. The first developer assessments were calculated based on the initial sale date of September 9, 1999, but have been recognized as assessment income in 2000, the first year of Association operations. Assessments receivable-developer at the balance sheet date represent assessments prorated using a daily rate determined by dividing the annual assessment amount by 365 days. Balances due are considered fully collectible.

Accounts receivable-developer represent costs paid by developer from member assessments that have been deemed non-Association costs and charged back to the developer. Balances due are considered fully collectible.

#### **Income taxes**

The Association is classified as a nonexempt membership organization for both federal and state income tax purposes. It does not qualify as an exempt organization. The Association is subject to specific rulings and regulations applicable to nonexempt membership organizations. In general, the Association is required to separate its taxable income and deductions into membership transactions, nonmembership transactions, and capital transactions.

# **COLORADO'S TIMBER RIDGE** **HOMEOWNERS ASSOCIATION**

## NOTES TO FINANCIAL STATEMENTS - Continued Inception to August 21, 2005

### **NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – Continued**

#### Income taxes - continued

For federal tax purposes, the Association is taxed on all net income from nonmembership activities reduced only by losses from nonmembership activities for which a profit motive exists. Nonmembership income may not be offset by membership losses, and any excess membership deductions may only be carried forward to offset membership income of future tax periods. Any net membership income not applied to the subsequent tax year is subject to taxation. The Association files Form 1120H, which has graduated effective tax rates of 15% to 39% that are applied to net taxable income.

For state income tax purposes, the Association also is taxed on all net income from nonmembership activities reduced only by losses from nonmembership activities for which a profit motive exists. Nonmembership income may not be offset by membership losses. Any net membership income is not subject to taxation. The tax rate that is applied to net taxable income is 5%.

#### Cash

For purposes of the statement of cash flows, cash is defined as cash held in a demand deposit account at a federally insured financial institution.

#### Property and equipment

Real property and common areas acquired from the developer and related improvements to such property are not recorded in the Association's financial statements because those properties are owned by the individual unit owners in common and not by the Association. Fixtures and equipment are capitalized at cost and depreciated using the straight-line method over their expected useful lives.

#### Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

### **NOTE 2 - ASSESSMENTS RECEIVABLE**

Assessments due from the developer were not levied on a timely basis, but were charged back during 2005 on the basis described in Note 1. At August 21, 2005, assessments receivable from the developer included assessments totaling \$41,311.

Assessments due from members were not consistently accrued throughout the years. As of August 21, 2005, balances due were recalculated using available information to account for any past year assessments not accrued or collected. An allowance for doubtful accounts was established in 2005 for delinquent accounts considered unlikely to be collected. Assessments receivable due from members are aged as follows.

<u>Year ended</u>	<u>Total Due</u>	<u>Allowance</u>	<u>Net Receivable</u>
2001	\$ 250	\$ (250)	\$ -
2002	875	(875)	-
2003	7,000	(7,000)	-
2004	500	-	500
2005	8,875	-	8,875
	<u>\$ 17,500</u>	<u>\$ (8,125)</u>	<u>\$ 9,375</u>

# **COLORADO'S TIMBER RIDGE** **HOMEOWNERS ASSOCIATION**

## **NOTES TO FINANCIAL STATEMENTS - Continued** Inception to August 21, 2005

### **NOTE 3 - CAPITALIZATION OF THE ASSOCIATION**

In accordance with the bylaws of the Association adopted in 1999, a working capital fund was to have been established and maintained in a separate bank account. That separate fund was not established, but in the process of accruing assessments due from the developer as described in Notes 1 and 2, the assessments that should have been placed in the working capital fund have been recovered by the Association.

The bylaws also call for a reserve fund for the replacement of improvements to the common elements. Such a fund is to be based on the age, remaining life and the quantity and replacement cost of major common element improvements. As of August 21, 2005, no analysis of future needs had been completed and no such fund had been established.

### **NOTE 4 - RELATED PARTY TRANSACTIONS**

The developer, Colorado Timber Ridge Ranch, LLP is considered a related party by virtue of control during the period under audit. A variety of transactions occurred between the Association and the developer in the normal course of business. These transactions are purported to be equivalent to arm's length transactions.

The newly elected Board of Directors, upon receiving the records of the Association, reviewed cash disbursements since inception and identified certain costs they believed should be borne in part or in full by the developer. The total of such costs through August 21, 2005 was \$31,339. The developer has agreed to reimburse the Association.

### **NOTE 5 - CONTINGENCIES**

The Association is not in compliance with certain requirements set out in the Declarations of Protective Covenants, Conditions and Restrictions (CC&Rs) and its bylaws. Among those with bearing on financial matters are the requirement for an annual budget and establishment of a working capital fund and a replacement reserve as described in Note 3. The effects, if any, of these matters of noncompliance on the accompanying financial statements has not been determined.

As described in Note 4, the developer has agreed to reimburse the Association for certain questioned costs. In addition, the developer has agreed to arbitration with regard to other costs questioned by the newly seated Association board of directors. To be resolved are the cost of acquiring and installing mailboxes and the costs associated with picnics paid for by the Association in 2002 and 2003. The effects, if any, of the resolution of these matters on the accompanying financial statements has not been determined.