

**Qualchan Hills Homeowners
Association**

Financial Statements
Six Months Ended December 31, 2012

TABLE OF CONTENTS

REPORT OF CERTIFIED PUBLIC ACCOUNTANTS ON THE FINANCIAL STATEMENTS	1
FINANCIAL STATEMENTS	
Balance Sheet - Cash Basis	2
Statement of Revenues, Expenses, and Changes in Members' Equity - Cash Basis.....	3
Notes to Financial Statements.....	4-6
INDEPENDENT AUDITORS' REPORT ON THE SUPPLEMENTARY INFORMATION.....	7
SUPPLEMENTARY INFORMATION	
Future Major Repairs and Replacements (Unaudited).....	8



Langenhorst & Self-Merritt CPAs, P.S.
Business and Financial Consultants

To the Board of Directors
Qualchan Hills Homeowners Association
Spokane, Washington

Independent Auditors' Report

We have audited the accompanying financial statements of Qualchan Hills Homeowners Association (a Washington homeowners association corporation), which comprise the balance sheet – cash basis as of December 31, 2012, and the related statement of revenues, expenses, and changes in members' equity – cash basis for the six month period then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with the cash basis of accounting described in Note 1; this includes determining that the cash basis of accounting is an acceptable basis for the preparation of the financial statements in the circumstances. Management is also responsible for the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

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 from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Qualchan Hills Homeowners Association as of December 31, 2012, and the results of its operations for the six month period then ended, in accordance with the basis of accounting as described in Note 1.

Basis of Accounting

We draw attention to Note 1 of the financial statements, which describes the basis of accounting. The financial statements are prepared on the cash basis of accounting, which is a basis of accounting other than accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to that matter.

W. S. Langenhorst C.P.A.

Spokane, WA

December 4, 2013

QUALCHAN HILLS HOMEOWNERS ASSOCIATION

Balance Sheet – Cash Basis December 31, 2012

ASSETS	<u>2012</u>	MEMBERS' EQUITY	<u>2012</u>
Cash - unrestricted (Note 4)	<u>\$ 42,710</u>	Members' equity	<u>\$ 42,710</u>

QUALCHAN HILLS HOMEOWNERS ASSOCIATION

Statement of Revenues, Expenses, and Changes in Members' Equity – Cash Basis Six Months Ended December 31, 2012

	<u>2012</u>
RECEIPTS	
Members' assessments	
Operating dues, gross	\$ 14,728
Private streets	2,851
Late fees and interest	53
Utilities	26,149
Endowment and grant income (Note 5)	5,000
Other	490
	<hr/>
TOTAL RECEIPTS	49,271
	<hr/>
EXPENDITURES	
Insurance	756
Landscaping	10,506
Maintenance	2,353
Management fees	3,861
Marketing	169
Miscellaneous	95
Office expense	540
Other administrative expenses	1,270
Professional fees	1,899
Real estate taxes and licenses	561
Utilities	26,499
	<hr/>
TOTAL EXPENDITURES	48,509
	<hr/>
NET RECEIPTS OVER EXPENDITURES	762
MEMBERS' EQUITY - Beginning of period	41,948
	<hr/>
MEMBERS' EQUITY - End of period	\$ 42,710
	<hr/> <hr/>

QUALCHAN HILLS HOMEOWNERS ASSOCIATION

Notes to Financial Statements Six Months Ended December 31, 2012

NOTE 1. SIGNIFICANT ACCOUNTING POLICIES

Organization's activities:

The Qualchan Hills Homeowners Association (the Association) was incorporated as a homeowners association on November 18, 1991, in the state of Washington. The Association is responsible for the operation and maintenance of the common property within the development. The development consists of 96 residential units located on approximately 300 acres in Spokane, Washington.

Basis of Accounting:

The accompanying financial statements have been prepared on the cash receipts and disbursements basis of accounting, which is a comprehensive basis of accounting other than generally accepted accounting principles. Under that basis, the only asset recognized is cash, and no liabilities are recognized. All transactions are recognized as either cash receipts or disbursements, and noncash transactions are not recognized. The cash basis differs from generally accepted accounting principles primarily because (a) the effects of outstanding dues and obligations for assessments unpaid at the date of the financial statements are not included in the balance sheet and (b) accounts payable are not calculated or recorded in the balance sheet.

Member assessments:

Association members are subject to monthly assessments to provide funds for the Association's operating expenses. As of December 31, 2012, no funds had been established and no dues assessed for future capital acquisitions and major repairs and replacements. The Association's policy is to retain legal counsel and place liens on the properties of homeowners whose assessments are thirty days or more delinquent. Any excess assessments at year-end are retained by the Association for use in the succeeding year.

Cash and cash equivalents:

Cash and cash equivalents include all unrestricted cash accounts and short-term liquid investments having an original maturity of three months or less.

Use of estimates:

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

QUALCHAN HILLS HOMEOWNERS ASSOCIATION

Notes to Financial Statements Six Months Ended December 31, 2012

NOTE 1. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Subsequent events:

In preparing the financial statements, the Association has evaluated events and transactions for potential recognition or disclosure through the date of the accountants' report on the financial statements, which is also the issuance date of the financial statements.

Reporting period:

The Association's financial reporting period is on a calendar year basis. The Association elected to report on only the last six months of operations for calendar 2012 due to a change in management company effective July 1, 2012 and expected difficulties in obtaining detailed records prior to that time.

NOTE 2. INCOME TAXES

Homeowners associations may be taxed either as homeowners associations or as regular corporations. For the year ended December 31, 2012, the Association was taxed as a homeowners association and filed Form 1120-H in accordance with Internal Revenue Service (IRS) Code section 528. Under that section, the Association excludes from taxation exempt function income, which generally consists of revenue from uniform assessments to owners.

Pursuant to FASB ASC 740-10-50-15, as of December 4, 2013, the tax years that remain subject to examination by the IRS include the tax years ended December 31, 2012, 2011, and 2010.

NOTE 3. FUTURE MAJOR REPAIRS AND REPLACEMENTS

In prior periods, the Association had funded actual major repair and replacement expenditures from excess operating fund assessments as expenditures were incurred. Subsequent to December 31, 2012, the Association adopted a program to begin accumulating funds for estimated future major repairs and replacements in a reserve fund restricted for such expenditures. The Association levied no additional special assessments for the six month period ended December 31, 2012.

In accordance with state of Washington RCW 64.34.380, the Association's board of directors initiated a reserve study in August 2012 to estimate the remaining useful lives and the replacement costs of the components of the development's common property. The study was conducted by a reserve study professional that inspected the property.

QUALCHAN HILLS HOMEOWNERS ASSOCIATION

Notes to Financial Statements Six Months Ended December 31, 2012

NOTE 3. FUTURE MAJOR REPAIRS AND REPLACEMENTS (CONTINUED)

The Association plans to fund such major repairs and replacements over the estimated useful lives of the components based on the study's estimates of current replacement costs, considering that there were previously no amounts accumulated in a replacement fund. Actual expenditures, however, may vary from the estimated amounts and the variations may be material. Amounts accumulated in such a replacement fund may not be adequate to meet future needs. If additional funds are needed, however, the Association has the right, subject to member approval, to increase regular assessments or levy special assessments, or it may delay major repairs and replacements until funds are available.

NOTE 4. CONCENTRATION OF CREDIT RISK

The Association's cash and cash equivalents consist principally of money funds invested with one financial institution. Generally, cash and cash equivalents are available on demand and are subject to minimal market risk. Although possible, the Association does not expect that the amounts on deposit will exceed the insured limit of \$250,000 established by the United States Federal Deposit Insurance Corporation, which may potentially subject the Association to credit risk.

NOTE 5. CONTRIBUTIONS

During the six month period ended December 31, 2012, the Association received a contribution of \$5,000 from a homeowner to be used to assist the Association for the costs of maintenance for a parcel of land donated several years ago by the homeowner that is now used as a park.

NOTE 6. CONTINGENCY

During September 2012, a homeowner filed suit against the Association alleging that the Association had engaged in timber trespass on the homeowner's property and that there was ongoing trespass with regards to drainage being directed over and across the homeowner's property, resulting in wrongful timber removal and vegetation removal. The Association turned the matter over to its insurance carrier and a settlement was reached during November 2013 resulting in the Association's insurance carrier, not the Association itself, paying an unspecified amount to the homeowner.



Langenhorst & Self-Merritt CPAs, P.S.
Business and Financial Consultants

To the Board of Directors
Qualchan Hills Homeowners Association
Spokane, Washington

Independent Auditors' Report on Supplementary Information

We have audited the financial statements of Qualchan Hills Homeowners Association as of and for the six month period ended December 31, 2012, and our report thereon dated December 4, 2013, which expressed an unmodified opinion on those financial statements, appears on page 1. Our audit was conducted for the purpose of forming an opinion on the basic financial statements as a whole.

Accounting principles generally accepted in the United States of America require that the information about future major repairs and replacements of common property on page 8 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Financial Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have not audited, reviewed, or compiled the required supplementary information, and, accordingly, we do not assume any responsibility for it.

W.S. Langenhorst C.P.A.

Spokane, WA
December 4, 2013

QUALCHAN HILLS HOMEOWNERS ASSOCIATION

Future Major Repairs and Replacements (Unaudited) Six Months Ended December 31, 2012

The Association's board of directors conducted a study in August 2012 to estimate the remaining useful lives and the replacement costs of the components of common property. The estimates were obtained from licensed contractors who inspected the property. Replacement costs were based on the estimated costs to repair or replace the common property components at the date of the study. Estimated current replacement costs have not been revised since that date and do not take into account the effects of inflation between the date of the study and the date that the components will require repair or replacement.

The following information is based on the study and presents significant information about the components of common property.

<u>Components</u>	<u>Estimated Remaining Useful Lives (Years)</u>	<u>Estimated Current Replacement Cost</u>
Overlay Keyes Ct and Kip Ln	7	\$ 100,905
Overlay Winder and Pender Ln	10	62,211
Repair sidewalk at Keyes Ct	1	112
Repair dip in Winder Ln	9	1,687
Repair Kip Ln sidewalk and fence	2	450
Repair sidewalks at street entries	7	1,674
Repair drain at Pender Ln	1	1,000
Backfill gravel along Pender Ln	2	250
Replace 5% of sidewalks	15	6,138
Re-roof gazebo	20	1,170
Re-roof monuments	21	1,000
Replace park sign	15	600
Seal Kip Ln and Keyes Ct	2	8,072
Seal Winder Ln and Pender Ln	2	4,977
		<u>\$ 190,246</u>