

# Cheatham & Lansford

Certified Public Accountants  
Granbury - Stephenville

## INDEPENDENT AUDITORS' REPORT

To the Board of Directors  
Pecan Plantation Owners' Association, Inc.

We have audited the consolidated balance sheet of Pecan Plantation Owners' Association, Inc. (the "Association") as of October 31, 1999, and the related consolidated statements of revenues, expenses, and changes in fund balance and cash flows for the year then ended. These consolidated 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. The financial statements of Pecan Plantation Owners' Association, Inc. as of October 31, 1998, were audited by other auditors whose report dated December 19, 1998, on those statements included an explanatory paragraph that described a valuation determination of contributed assets as discussed in Note 1 to the financial statements.

Except as discussed in the following paragraph, we conducted our audits 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 misstatements. 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 audits provide a reasonable basis for our opinion.

As indicated in Note 1 to the consolidated financial statements, several years ago certain land and improvements were transferred to the Association by the developer. In order to provide a basis for accountability, the Association's Board of Directors existing at that time appointed an appraisal committee to review and value the acquired assets. The valuation process resulted in an assigned value of approximately \$5,048,000. Due to the nature of this valuation determination, we were unable to satisfy ourselves by application of other auditing procedures as to the assigned value referred to above.

In our opinion, except for the effects of such adjustments, if any, as might have been determined to be necessary to record independently determined fair values of contributed property and any related changes in depreciation expense and accumulated depreciation of the assets described in the preceding paragraph, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Pecan Plantation Owners' Association, Inc. as of October 31, 1999, and the results of operations and its cash flows for the year then ended in conformity with generally accepted accounting principles.

The Association has not estimated the remaining lives and replacement costs of the common property and, therefore, has not presented supplementary information that the American Institute of Certified Public Accountants has determined is required to supplement, although not required to be a part of, the basic financial statements.

Granbury, Texas  
December 16, 1999

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PECAN PLANTATION OWNERS' ASSOCIATION, INC.  
CONSOLIDATED BALANCE SHEETS  
As of October 31,

	Operating Fund	Replacement Fund	Totals	
			1999	1998
<b>ASSETS</b>				
Cash, including interest-bearing deposits	\$301,790	\$246,750	\$548,540	\$398,316
Temporary investments	44,171	309,128	353,299	349,473
Accounts receivable:				
Members, less allowance for doubtful accounts of \$45,000 in 1999 and \$34,161 in 1998	319,206	37,650	356,856	387,527
Other	22,868		22,868	20,977
Inventories	116,389		116,389	132,090
Prepaid expenses:				
Insurance	23,625		23,625	50,858
Other	13,989		13,989	13,722
Other Assets	75,501		75,501	77,250
Property, Plant and Equipment Purchased at cost:				
Land	82,849		82,849	72,669
Buildings and improvements	999,880		999,880	878,237
Equipment and other	2,605,785		2,605,785	2,449,754
Construction in progress		865,240	865,240	38,790
Contributed, at assigned value	5,048,148		5,048,148	5,048,148
	8,736,662	865,240	9,601,902	8,487,598
Less accumulated depreciation	(6,515,053)		(6,515,053)	(6,299,608)
	2,221,609	865,240	3,086,849	2,187,990
Real estate held for sale	90,338		90,338	81,034
<b>TOTAL ASSETS</b>	<b>\$3,229,486</b>	<b>\$1,458,768</b>	<b>\$4,688,254</b>	<b>\$3,699,237</b>
<b>LIABILITIES AND FUND BALANCES</b>				
Accounts payable	\$182,814	\$98,497	\$281,311	\$182,754
Accrued liabilities:				
Payroll	44,991		44,991	109,110
Other	108,249	92,538	200,787	71,093
Deferred revenue-members assessments	268,640	953,762	1,222,402	710,199
Note payable		294,000	294,000	9,254
Rental deposits	10,000		10,000	9,500
Deferred employee benefits	75,501		75,501	77,250
FUND BALANCES	2,539,291	19,971	2,559,262	2,530,077
<b>TOTAL LIABILITIES AND FUND BALANCES</b>	<b>\$3,229,486</b>	<b>\$1,458,768</b>	<b>\$4,688,254</b>	<b>\$3,699,237</b>

See Accompanying Notes to Consolidated Financial Statements

PECAN PLANTATION OWNERS' ASSOCIATION, INC.  
CONSOLIDATED STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN FUND BALANCES  
Year Ended October 31,

	Operating Fund	Replacement Fund	Totals	
			1999	1998
<b>Revenues:</b>				
Members' Assessments	\$1,853,341	\$	\$1,853,341	\$1,808,076
Food and beverage	664,183		664,183	633,692
Inn & reception	136,912		136,912	152,862
Golf & tennis	516,404		516,404	506,667
Marina	462,398		462,398	421,582
Roads, grounds and recreation	233,160		233,160	258,162
Member Services & administration	279,385	13,012	292,397	191,110
Security	71,226		71,226	75,300
Contributed assets	1,750		1,750	13,188
	<u>4,218,759</u>	<u>13,012</u>	<u>4,231,771</u>	<u>4,060,639</u>
<b>Expenses:</b>				
Food and beverage	713,150		713,150	718,253
Inn & reception	178,270		178,270	148,789
Golf & tennis	716,613		716,613	672,382
Marina	437,297		437,297	398,074
Roads, grounds and recreation	327,159		327,159	362,063
Member Services & administration	1,166,403		1,166,403	1,087,779
Security	404,560		404,560	354,156
	<u>3,943,452</u>	<u>0</u>	<u>3,943,452</u>	<u>3,741,496</u>
Excess revenues over expenses before depreciation	275,307	13,012	288,319	319,143
Less depreciation expense	<u>259,134</u>		<u>259,134</u>	<u>388,092</u>
Excess of revenues over (expenses)	16,173	13,012	29,185	(68,949)
Beginning Fund Balances	2,525,760	4,317	2,530,077	2,599,026
Transfer between funds	(2,642)	2,642		
Ending Fund Balances	<u>\$2,539,291</u>	<u>\$19,971</u>	<u>\$2,559,262</u>	<u>\$2,530,077</u>

See Accompanying Notes to Consolidated Financial Statements

PECAN PLANTATION OWNERS' ASSOCIATION, INC.  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
Year Ended October 31,

	Operating Fund	Replacement Fund	Totals	
			1999	1998
<b>Cash Flows Form Operating Activities</b>				
Excess (deficiency) of revenues over expenses	\$16,173	\$13,012	\$29,185	(\$68,949)
Adjustments to reconcile excess (deficiency) of revenues over expenses to net cash provided by operating activities:				
Depreciation	259,134		259,134	388,092
Bad debt expense	1,532		1,532	6,995
Gain on sale of equipment and real estate	(11,726)		(11,726)	(40,642)
Decrease (increase) in accounts receivable, before bad debt expense	55,591	(37,650)	17,941	(33,839)
Decrease (increase) in inventories	15,701		15,701	(10,454)
(Increase) decrease in prepaid expenses	26,966		26,966	(14,708)
(Increase) decrease in real estate held for sale	(9,304)		(9,304)	16,641
(Decrease) increase in deferred revenues	(33,689)	545,892	512,203	566,640
Increase (decrease) in accounts payable	60	98,497	98,557	(47,591)
Increase in rental deposits	500		500	1,496
(Decrease) increase in accrued liabilities	(26,963)	92,538	65,575	7,999
Total adjustments	277,802	699,277	977,079	840,629
<b>Net cash provided by (used in) operating activities</b>	<b>293,975</b>	<b>712,289</b>	<b>1,006,264</b>	<b>771,680</b>
<b>Investing Activities</b>				
Capital expenditures	(331,710)	(826,450)	(1,158,160)	(227,910)
Proceeds from sale of real estate and other assets	13,696		13,696	17,766
<b>Net cash provided by (used in) investing activities</b>	<b>(318,014)</b>	<b>(826,450)</b>	<b>(1,144,464)</b>	<b>(210,144)</b>
<b>Financing activities</b>				
Proceeds from loans		294,000	294,000	
Designated capital contributions	(1,750)		(1,750)	(13,188)
Transfer between funds	(2,642)	2,642		
<b>Net cash provided by (used in) financing activities</b>	<b>(4,392)</b>	<b>296,642</b>	<b>292,250</b>	<b>(13,188)</b>
<b>Net increase (decrease) in cash and cash equivalents</b>	<b>(28,431)</b>	<b>182,481</b>	<b>154,050</b>	<b>548,348</b>
Cash and cash equivalents at beginning of year	374,392	373,397	747,789	199,441
<b>Cash and cash equivalents at end of year</b>	<b>\$345,961</b>	<b>\$555,878</b>	<b>\$901,839</b>	<b>\$747,789</b>

See Accompanying Notes to Consolidated Financial Statements

PECAN PLANTATION OWNERS' ASSOCIATION, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
October 31, 1999 and 1998

NOTE 1 -- HISTORY OF ASSOCIATION

Pecan Plantations Owners' Association, Inc. (the "Association") commenced operations in August 1978. The Association is responsible for the operation and maintenance of the common property within the development which consists of approximately 1,500 residential units located in north central Texas. The Association's charter provides for a membership association without stock or paid-in capital. Each lot owner in the development is a member and pays monthly assessments for the maintenance of the common facilities.

Republic Land Company had subdivided and developed a residential area and common facilities consisting of streets, club house, golf course, tennis courts, recreation parks, airstrip and other improvements. On August 1, 1978, Republic Land Company transferred the common facilities to the Association. The acquisition of the property transferred to the Association was valued by an appraisal committee appointed by the Board of Directors existing at August 1, 1978. The committee determined that the donated assets should be recorded at the original cost to Republic Land Company for improvements and at \$2,500 per acre for land. The assigned values (which have no tax basis) are as follows:

Land	\$ 1,196,000
Golf course, equipment and sprinkler system	756,472
Roads, bridges and culverts	702,355
Club house, including furnishings	1,842,663
Other recreational facilities	370,333
Other improvements	<u>180,325</u>
	<u>\$ 5,048,148</u>

Effective March 1, 1979, Pecan Plantation Country Club, Inc. (the "Country Club") was formed to transact the business related to the operations of the Country Club and all recreational facilities. The Country Club is a wholly-owned subsidiary of the Association.

NOTE 2 -- SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation

The accompanying consolidated financial statements reflect the accounts of the Association and its wholly-owned subsidiary. All significant inter-company accounts and transactions have been eliminated. Certain amounts previously reported have been reclassified to conform to the current format.

PECAN PLANTATION OWNERS' ASSOCIATION, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
October 31, 1999 and 1998

NOTE 2 -- SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Fund Accounting

The Association's governing documents provide certain guidelines for governing its financial activities. To ensure observance of limitations and restrictions on the use of financial resources, the Association maintains its accounts using fund accounting. Financial resources are classified for accounting and reporting purposes in the following funds established according to their nature and purpose:

Operating Fund - This fund is used to account for financial resources available for the general operations of the Association.

Replacement Fund - This fund is used to accumulate financial resources designated for future repairs and replacements.

Member Assessments

Association members are subject to monthly assessments to provide funds for the Association's operating expenses, future capital acquisitions, and major repairs and replacements. Accounts receivable at the balance sheet date include fees due from unit owners. The Association's policy is to retain legal counsel and place liens on the properties of homeowners whose assessments are delinquent.

Interest Income

Interest income is allocated to the operating and replacement funds in proportion to the interest-bearing deposits of each fund.

Land, Buildings and Equipment

Depreciation is calculated by the straight-line method at rates which approximate the property's estimated useful life. Different depreciation methods are used for tax purposes.

Inventories

Inventories consist of food, beverages, gas, golf accessories and equipment and are stated at the lower of cost (determined by the first-in, first-out method) or market.

Income Taxes

The Association and Country Club file separate federal income tax returns. Homeowners' associations may be taxed either as homeowners' associations or as regular corporations. For the years ending October 31, 1999 and 1998, the Association elected to be taxed as a homeowners' association. Under that election, the Association is taxed on its nonexempt function income, such as income from

PECAN PLANTATION OWNERS' ASSOCIATION, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
October 31, 1999 and 1998

NOTE 2 -- SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

interest earnings, at a flat rate of 30%. Exempt function income, which consists primarily of member assessments, is not taxable.

The Country Club is taxed as a regular corporation. Deferred income taxes are recorded, when applicable, for differences in timing of the recognition of income and expense for financial and tax purposes when appropriate. The Country Club has incurred net operating losses for the years ending October 31, 1999 and 1998.

Statement of Cash Flows

For purposes of the statement of cash flows, the Association considers cash (including interest bearing deposits) and temporary investments to be cash equivalents.

Supplemental information - Cash paid during the year ended October 31, 1999 for interest was approximately \$623 (\$1,248 in 1998). No payments were made for income taxes in 1999 and 1998.

Temporary Investments

The Association considers all highly liquid investments with a maturity of six months or less when purchased, to be temporary investments. In the opinion of management, market value of these temporary investments approximates cost.

Estimates

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

NOTE 3 -- SIGNIFICANT CONCENTRATIONS OF CREDIT RISK

The Association is considered to have concentrated its credit risk with respect to accounts and notes receivable because substantially all of the balances are receivable from individuals located within the same geographic region.

The Association has interest bearing deposits in various commercial banks. At October 31, 1999, the Association's deposits exceeded federal depository insurance coverage by approximately \$203,000.

PECAN PLANTATION OWNERS' ASSOCIATION, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
October 31, 1999 and 1998

**NOTE 4 - NOTE PAYABLE**

The financial statements include a fixed rate 7.00% note payable of \$294,000 as of October 31, 1999. The proceeds of this note are being used for the construction of the bridge at the front gate. The note is secured by the assignment of a special bridge assessment. The note does not call for scheduled payments but requires all collected bridge assessments be applied against the note monthly until paid in full. The note has a maturity date of March 3, 2010 at which time any unpaid principal and interest is due and payable.

**NOTE 5 - FEDERAL INCOME TAXES**

The Association has recorded no income tax expense for 1999 and 1998, respectively.

The country club had incurred net operating losses since it began filing separate income tax returns in 1994. No tax benefit has been reported in the financial statements regarding net operating losses of the country club because the Association believes that there is at least a 50% chance that the carry forward will expire unused.

**NOTE 6 -- EMPLOYEE BENEFITS**

The Association provides certain health care and life insurance benefits for all full-time employees (approximately 55). The Association and participants pay monthly costs and expenses to the plan for administration and claims. These costs were approximately \$111,000 and \$97,000 in 1999 and 1998, respectively, and are included in the various departmental expenses.

The Association participates in a multi-employer non-qualified deferred compensation plan which provides benefits to certain employees. As of October 31, 1999 (most recent measurement date), the value of the plan's assets, which are subject to the general creditors of the Association, was approximately \$75,500. The Association also established a non-matching 401(k) plan for its employees in 1999.

**NOTE 7 -- LITIGATION**

At October 31, 1998, there are pending actions incident to normal operations of the Association. In the opinion of Management, the Association's potential liability in these matters will not have a material impact on the financial statements.

**NOTE 8 -- FUTURE MAJOR REPAIRS AND REPLACEMENTS**

The Association's management is currently conducting a study to estimate the remaining useful lives and the replacement costs of the common property components. The Association's governing documents do not specifically provide for the accumulation of funds to finance estimated future major repairs and replacements. When funds are required for major repairs and replacements, the Association plans to borrow, increase maintenance assessments, or delay repairs and replacements until funds are available. The effect on future assessments has not been determined.