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CERTIFIED PUBLIC ACCOUNTANTS

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## REPORT OF INDEPENDENT AUDITORS

Board of Directors  
Pecan Plantation Owners' Association, Inc.

We have audited the consolidated balance sheets of Pecan Plantation Owners' Association, Inc. (the "Association") as of October 31, 1998 and 1997, and the related consolidated statements of revenues, expenses, and changes in fund balances and cash flows for the years 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 audits.

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 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 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 at October 31, 1998 and 1997, and the consolidated results of its operations and its cash flows for the years 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.

*George, Morgan & Sneed, P.C.*

December 19, 1998

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

	Operating Fund	Replacement Fund	Totals	
			1998	1997
<b>ASSETS</b>				
Current Assets				
Cash, including interest-bearing deposits	\$224,333	\$173,983	\$398,316	\$199,441
Temporary investments	150,059	199,414	349,473	-
Accounts receivable:				
Members, less allowance for doubtful accounts of \$34,161 in 1998 and \$40,000 in 1997	387,527		387,527	339,605
Other	20,977		20,977	29,221
Inventories	132,090		132,090	121,636
Prepaid expenses:				
Insurance	50,858		50,858	37,243
Other	13,722		13,722	12,629
Total Current Assets	<u>979,566</u>	<u>373,397</u>	<u>1,352,963</u>	<u>739,775</u>
Other Assets (Note 6)	77,250		77,250	75,580
Property, Plant and Equipment (Note 1)				
Purchased, at cost:				
Land	72,669		72,669	72,669
Buildings and improvements	878,237		878,237	831,064
Equipment and other	2,449,754		2,449,754	2,294,619
Construction in progress		38,790	38,790	-
Contributed, at assigned value	5,048,148		5,048,148	5,048,148
	8,448,808	38,790	8,487,598	8,246,500
Less accumulated depreciation	<u>(6,299,608)</u>		<u>(6,299,608)</u>	<u>(5,930,812)</u>
	2,149,200	38,790	2,187,990	2,315,688
Real estate held for sale	81,034		81,034	97,675
TOTAL ASSETS	<u>\$3,287,050</u>	<u>\$412,187</u>	<u>\$3,699,237</u>	<u>\$3,228,718</u>
<b>LIABILITIES AND FUND BALANCES</b>				
Current Liabilities				
Accounts payable	\$182,754		\$182,754	\$230,345
Accrued liabilities				
Payroll	109,110		109,110	90,747
Property taxes	29,569		29,569	27,822
Other	41,524		41,524	53,635
Deferred revenues, members' assessments	302,329	407,870	710,199	143,559
Note Payable	9,254		9,254	-
Rental deposits	9,500		9,500	8,004
Total Current Liabilities	<u>684,040</u>	<u>407,870</u>	<u>1,091,910</u>	<u>554,112</u>
Deferred employee benefits (Note 6)	77,250		77,250	75,580
FUND BALANCES	<u>2,525,760</u>	<u>4,317</u>	<u>2,530,077</u>	<u>2,599,026</u>
TOTAL LIABILITIES AND FUND BALANCES	<u>\$3,287,050</u>	<u>\$412,187</u>	<u>\$3,699,237</u>	<u>\$3,228,718</u>

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	
			1998	1997
<b>Revenues:</b>				
Members' assessments	\$1,808,076		\$1,808,076	\$1,786,505
Food and beverage	633,692		633,692	661,921
Inn	152,862		152,862	168,057
Golf	504,880		504,880	453,585
Marina & Tennis	423,369		423,369	376,476
Roads and grounds/recreation	258,162		258,162	207,056
Member Services & administration	186,793	4,317	191,110	145,394
Security	75,300		75,300	81,316
Contributed assets	13,188		13,188	28,659
	<u>4,056,322</u>	<u>4,317</u>	<u>4,060,639</u>	<u>3,908,969</u>
<b>Expenses:</b>				
Food and beverage	718,253		718,253	764,550
Inn	148,789		148,789	220,384
Golf	618,932		618,932	581,854
Marina & Tennis	451,524		451,524	365,230
Roads and grounds/recreation	362,063		362,063	205,241
Member Services & administration	1,087,779		1,087,779	1,244,035
Security	354,156		354,156	328,040
	<u>3,741,496</u>	<u>-</u>	<u>3,741,496</u>	<u>3,709,334</u>
 Excess revenues over expenses before depreciation	 <u>314,826</u>	 <u>4,317</u>	 <u>319,143</u>	 <u>199,635</u>
 Less depreciation expense (Note 1)				
Purchased assets	218,054		218,054	235,362
Contributed assets	170,038		170,038	192,600
	<u>388,092</u>	<u>-</u>	<u>388,092</u>	<u>427,962</u>
 Excess of Revenues Over (Expenses)	 <u>(73,266)</u>	 <u>4,317</u>	 <u>(68,949)</u>	 <u>(228,327)</u>
 Beginning Fund Balance	 <u>2,599,026</u>	 <u>-</u>	 <u>2,599,026</u>	 <u>2,827,353</u>
 Ending Fund Balance	 <u>\$2,525,760</u>	 <u>\$4,317</u>	 <u>\$2,530,077</u>	 <u>\$2,599,026</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	
			1998	1997
Cash Flows From Operating Activities				
Excess (deficiency) of revenues over expenses	(\$73,266)	\$4,317	(\$68,949)	(\$228,327)
Adjustments to reconcile excess (deficiency) of revenues over expenses to net cash provided by operating activities:				
Depreciation	388,092		388,092	427,962
Bad debt expense	6,995		6,995	15,177
Gain on sale of equipment and real estate	(40,642)		(40,642)	(25,333)
Increase in accounts receivable, before bad debt expense	(33,839)		(33,839)	(9,108)
Decrease in long-term receivable-members			-	379
Decrease (Increase) in inventories	(10,454)		(10,454)	(2,188)
(Increase) decrease in prepaid expenses	(14,708)		(14,708)	1,382
(Increase) decrease in real estate held for sale	16,641		16,641	(3,808)
(Decrease) increase in deferred revenues	158,770	407,870	566,640	(9,085)
Increase (decrease) in accounts payable	(47,591)		(47,591)	54,413
Increase in rental deposits	1,496		1,496	4,504
(Decrease) increase in accrued liabilities	7,999		7,999	35,930
Total adjustments	432,759	407,870	840,629	490,225
Net cash provided by (used in) operating activities	359,493	412,187	771,680	261,898
Investing Activities				
Capital expenditures	(189,120)	(38,790)	(227,910)	(292,858)
Proceeds from sale of real estate	17,266		17,266	38,528
Proceeds from sale of assets	500		500	340
Net cash provided by (used in) investing activities	(171,354)	(38,790)	(210,144)	(253,990)
Financing Activities				
Designated Capital contributions	(13,188)	-	(13,188)	(28,659)
Net cash provided by (used in) financing activities	(13,188)	-	(13,188)	(28,659)
Net increase (decrease) in cash and cash equivalents	174,951	373,397	548,348	(20,751)
Cash and cash equivalents at beginning of year	199,441	-	199,441	220,192
Cash and cash equivalents at end of year	\$374,392	\$373,397	747,789	\$199,441

See Accompanying Notes to Consolidated Financial Statements

PECAN PLANTATION OWNERS' ASSOCIATION, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
October 31, 1998 and 1997

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 1,473 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		180,325
		<u>5,048,148</u>

The Association recorded depreciation expense of \$170,038 and \$192,600 in relation to these assets for years ended October 31, 1998 and 1997 respectively. Accumulated depreciation at October 31, 1998 amounted to \$3,852,148 for these contributed assets.

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 intercompany 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, 1998 and 1997

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 and tennis 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, 1998 and 1997, 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 interest earnings, at a flat rate of 30%. Exempt function income, which consists primarily of member assessments, is not taxable.

PECAN PLANTATION OWNERS' ASSOCIATION, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
October 31, 1998 and 1997

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

Income Taxes - continued

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, 1998 and 1997.

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, 1998 for interest was approximately \$1,248 (\$350 in 1997). No payments were made for income taxes in 1998 and 1997.

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.

NOTE 4 -- FEDERAL INCOME TAXES

The Association has recorded no income tax expense for 1998 and 1997, respectively.

The country club has 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 there is at least a 50% chance that the carry forward will expire unused.

PECAN PLANTATION OWNERS' ASSOCIATION, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
October 31, 1998 and 1997

**NOTE 5 -- 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 \$97,000 and \$105,000 in 1998 and 1997, respectively, and are included in the various departmental expenses.

The Association participates in a non-qualified deferred compensation plan which provides benefits to certain employees. Employees can elect to contribute up to \$1,200 per year to the plan which is matched 100% by the Association. As of October 31, 1998 (most recent measurement date), the value of the plan's assets, which are subject to the general creditors of the Association, was approximately \$77,250.

**NOTE 6 -- 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 7 -- 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.