

ORCAS HIGHLANDS ASSOCIATION
INDEPENDENT AUDITOR'S REPORT
AND
AUDITED FINANCIAL STATEMENTS
FOR THE
YEAR ENDED JUNE 30, 2022
AND
UNAUDITED SUPPLEMENTARY INFORMATION

ORCAS HIGHLANDS ASSOCIATION

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Joseph H. Vandal, CPA, PS

Member of American Institute of CPAs, Washington Society of CPAs
A Professional Service Corporation

INDEPENDENT AUDITOR'S REPORT

To the Board of Directors and Members
Orcas Highlands Association

We have audited the accompanying financial statements of Orcas Highlands Association, which comprise the balance sheet as of December 31, 2022, and the related statements of revenues, expenses, and changes in fund balance and cash flows for the year then ended, and the related notes to the financial statements.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Orcas Highlands Association as of December 31, 2022, and the results of its operations and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Basis for Opinion

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Our responsibility under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of our report. We are required to be independent of Orcas Highlands Association and to meet our other ethical responsibilities in accordance with the relevant ethical requirements relating to our audit. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Responsibilities of Management for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes 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.

In preparing the financial statements, management is required to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about Orcas Highlands Association's ability to continue as a going concern within one year after the date that the financial statements are available to be issued.

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance but is not absolute assurance and therefore is not a guarantee that an audit conducted in accordance with generally accepted auditing standards will always detect a material misstatement when it exists. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. Misstatements are considered material if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgment made by a reasonable user based on the financial statements.

INDEPENDENT AUDITOR'S REPORT--Continued

Auditor's Responsibilities for the Audit of the Financial Statements - Continued

In performing an audit in accordance with generally accepted auditing standards, we:

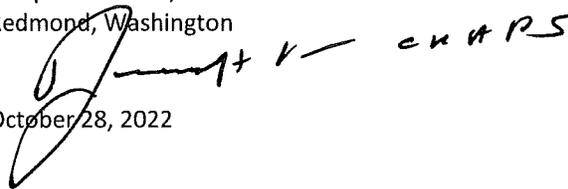
- Exercise professional judgment and maintain professional skepticism throughout the audit.
- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements.
- Obtain an understanding of internal control relevant to the audit 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 Orcas Highlands Association's internal control. Accordingly, no such opinion is expressed.
- Evaluate the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluate the overall presentation of the financial statements.
- Conclude whether, in our judgment, there are conditions or events, considered in the aggregate, that raise substantial doubt about Orcas Highlands Association's ability to continue as a going concern for a reasonable period of time.

We are required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit, significant audit findings, and certain internal control related matters that we identified during the audit.

Disclaimer of Opinion on Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the information on future major repairs and replacements on common property on page 11 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 basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Joseph H. Vandal, CPA PS
Redmond, Washington


October 28, 2022

ORCAS HIGHLANDS ASSOCIATION
BALANCE SHEET
June 30, 2022

| | <u>OPERATING FUND</u> | <u>REPLACEMENT RESERVE FUND</u> | <u>TOTAL</u> |
|---|---------------------------|---|-----------------------|
| <u>ASSETS</u> | | | |
| Cash-Checking | \$ 31,509 | \$ 73,890 | \$ 105,399 |
| Assessments Receivable | 11,218 | - | 11,218 |
| Allowance for Doubtful Accounts | (8,797) | - | (8,797) |
| Prepaid Income Tax | - | 4,039 | 4,039 |
| Capital Improvements | 110,837 | - | 110,837 |
| Accumulated Depreciation | <u>(110,837)</u> | <u>-</u> | <u>(110,837)</u> |
| Total Assets | <u>\$ 33,930</u> | <u>\$ 77,929</u> | <u>\$ 111,859</u> |
| <u>LIABILITIES AND FUND BALANCE</u> | | | |
| Loan Payable | \$ - | \$ 20,783 | \$ 20,783 |
| Prepaid Assessments | <u>3,166</u> | <u>-</u> | <u>3,166</u> |
| Total Liabilities | 3,166 | 20,783 | 23,949 |
| Fund Balance | <u>30,764</u> | <u>57,146</u> | <u>87,910</u> |
| Total Liabilities & Fund Balance | <u>\$ 33,930</u> | <u>\$ 77,929</u> | <u>\$ 111,859</u> |

ORCAS HIGHLANDS ASSOCIATION
STATEMENT OF REVENUES, EXPENSES AND CHANGE IN FUND BALANCE
For the Year Ended June 30, 2022

| | <u>OPERATING FUND</u> | <u>REPLACEMENT RESERVE FUND</u> | <u>TOTAL</u> |
|---------------------------------------|---------------------------|---|------------------|
| REVENUES | | | |
| Assessments | | | |
| Regular | \$ 25,946 | \$ - | \$ 25,946 |
| Roads | - | 28,920 | 28,920 |
| Fiber Assessments | - | 10,667 | 10,667 |
| Wildfire Mitigation Assessments | - | 16,750 | 16,750 |
| Other | 10,250 | - | 10,250 |
| Interest | - | 14 | 14 |
| TOTAL REVENUE | <u>36,196</u> | <u>56,351</u> | <u>92,547</u> |
| EXPENSES | | | |
| Bookkeeping | 7,285 | - | 7,285 |
| Administration | 3,128 | - | 3,128 |
| Professional Services | 2,800 | - | 2,800 |
| Licenses and Permits | 20 | - | 20 |
| State Taxes | 320 | - | 320 |
| Insurance | 4,454 | - | 4,454 |
| Wildfire Mitigation | 3,167 | - | 3,167 |
| Road Maintenance | 15,043 | - | 15,043 |
| Water System | 28,413 | - | 28,413 |
| Bad Debt | 8,111 | - | 8,111 |
| Reserve Study | - | 2,135 | 2,135 |
| TOTAL EXPENSES | <u>72,741</u> | <u>2,135</u> | <u>74,876</u> |
| REVENUES OVER/(UNDER) EXPENSES | (36,545) | 54,216 | 17,671 |
| BEGINNING FUND BALANCE | 34,609 | 35,630 | 70,239 |
| Transfer to (from) | <u>32,700</u> | <u>(32,700)</u> | <u>-</u> |
| ENDING BALANCE | <u>\$ 30,764</u> | <u>\$ 57,146</u> | <u>\$ 87,910</u> |

ORCAS HIGHLANDS ASSOCIATION
STATEMENT OF CASH FLOWS
For the Year Ended June 30, 2022

| | <u>OPERATING FUND</u> | <u>REPLACEMENT RESERVE FUND</u> | <u>TOTAL</u> |
|---|---------------------------|---|-------------------|
| <u>CASH FLOWS FROM OPERATING</u> | | | |
| <u>ACTIVITIES</u> | | | |
| REVENUE OVER/(UNDER) EXPENSES | \$ (36,545) | \$ 54,216 | \$ 17,671 |
| Adjustments to reconcile excess of expenses over revenues to net cash provided by activities: | | | |
| (Increase) Decrease in: | | | |
| Assessments Receivable | (2,194) | - | (2,194) |
| Prepaid Insurance | 4,204 | - | 4,204 |
| Increase (Decrease) in: | | | |
| Accounts Payable | (4,211) | - | (4,211) |
| Loan Payable | - | (8,485) | (8,485) |
| Prepaid Assessments | 1,506 | - | 1,506 |
| <u>NET CASH PROVIDED BY OPERATING ACTIVITIES</u> | <u>(37,240)</u> | <u>45,731</u> | <u>8,491</u> |
| <u>CASH FLOWS FROM</u> | | | |
| <u>FINANCING ACTIVITIES</u> | | | |
| Interfund transfers | <u>32,700</u> | <u>(32,700)</u> | <u>-</u> |
| NET INCREASE (DECREASE) IN CASH & EQUIVALENTS | (4,540) | 13,031 | 8,491 |
| CASH & EQUIVALENTS AT BEGINNING OF THE PERIOD | <u>36,049</u> | <u>60,859</u> | <u>96,908</u> |
| CASH & EQUIVALENTS AT END OF THE PERIOD | <u>\$ 31,509</u> | <u>\$ 73,890</u> | <u>\$ 105,399</u> |

ORCAS HIGHLANDS ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
June 30, 2022

NOTE A – NATURE OF ORGANIZATION

Orcas Highlands Association is a statutory homeowner association in the State of Washington organized in 1972 and incorporated in 1980. The Association is responsible for the operation and maintenance of the common property of Orcas Highlands Association. Orcas Highlands Association consists of 120 residential tax parcels located on Orcas Island, Washington.

NOTE B – DATE OF MANAGEMENT’S REVIEW

In preparing the financial statements, the Association has evaluated events and transactions for potential recognition or disclosure through October 28, 2022, the date that the financial statements were available to be issued.

NOTE C-SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

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 the financial resources available for the general operations of the Association.

Replacement Fund-This fund is used to accumulate financial resources designated for future major repairs and replacements, insurance proceeds (if any), insurance repairs (if any), and litigation costs (if any) relating to the afore mentioned proceeds.

Cash and Cash Equivalents

The Association considers cash on deposit, cash on hand, money market funds (if any) and certificates of deposit (if any) and any other highly-liquid securities to be cash and or cash equivalents. Any penalties for early withdrawal would not have a material effect on the financial statements.

ORCAS HIGHLANDS ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
June 30, 2022

NOTE C-SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES-CONTINUED

Member Assessments

Association members are subject to quarterly assessments to provide funds for the Association's operating expenses, future capital acquisitions, and major repairs and replacements. Assessments receivable at the balance sheet date represent 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. Any excess assessments at year end are retained by the Association for use in the succeeding year. If assessments are inadequate, the Board of Directors, subject to the limitations of their authority described in the Association's governing documents, may have to increase regular assessments or pass special assessments. At June 30, 2022, the Association had assessments delinquent 90 days or more of approximately \$8,797.

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 individual unit owners in common and not by the Association. The Association capitalizes personal property at cost and depreciates it using the straight-line method.

Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that 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.

NOTE D-COMMITMENTS

The Association has various contracts for services including but not limited to management, maintenance, and landscaping.

NOTE E-SPECIAL ASSESSMEN

The Association collected an additional \$60 per month for a special assessment in the amount of to pay for fiber installation.

ORCAS HIGHLANDS ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
June 30, 2022

NOTE F-INCOME TAXES

Condominium Associations may be taxed either as homeowners' Associations or as regular corporations. In 2021, the Association elected to be taxed as a homeowners' Association. Under that election, the Association is taxed on its nonexempt function income, such as net interest earnings, at a flat rate of 30%. Exempt function income, which consists primarily of member assessments, is not taxable.

As of June 30, 2022, the tax years that remain subject to examination by taxing authorities begin with 2018.

NOTE G-FUTURE MAJOR REPAIRS AND REPLACEMENTS

The Association's governing documents require funds to be accumulated for future major repairs and replacements. Accumulated funds (assets less liabilities as reported on the balance sheet), which in aggregate are approximately \$57,146 at June 30, 2022, are held in separate accounts and are generally not available for operating purposes. Cash balances shown on the balance sheet that are part of these funds are held in separate bank accounts.

The Association performed a self-study in 2020 to estimate the remaining useful lives and the replacement costs of the common property components. The Association is partially funding for such major repairs and replacements over the estimated lives of the components based on the study's estimates of current replacement costs, considering amounts previously accumulated in the replacement fund. Actual expenditures, however, may vary from the estimated amounts and the variations may be material. Therefore, amounts accumulated in the replacement fund may not be adequate to meet future needs. If additional funds are needed, however, the Association has the right, subject to the limitations of the authority described in the Association's governing documents, to increase regular assessments or levy special assessments, or it may delay major repairs and replacements until funds are available.

NOTE H-LOAN PAYABLE

The Association took out a loan in the amount of \$42,910 to pay for fiber installation. At June 30, 2022 the balance of loan was approximately \$20,783.

**ORCAS HIGHLANDS ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
June 30, 2022**

NOTE G-ACCOUNTS RECEIVABLE

Accounts receivable consisted of the following at June 30, 2022:

| | <u>Operating Fund</u> |
|------------------------------------|---------------------------|
| Assessments | \$ 11,218 |
| Allowance for Doubtful Accounts | <u>(8,797)</u> |
| | <u>\$ 2,421</u> |

Bad debt expense for the year ended June 30, 2022, was \$8,111.

SUPPLEMENTARY INFORMATION

ORCAS HIGHLANDS ASSOCIATION
UNAUDITED SUPPLEMENTARY INFORMATION ON
FUTURE MAJOR REPAIRS AND REPLACEMENTS
June 30, 2022

The Association conducted a self-study in 2020 to estimate the remaining useful lives and the replacement costs of the components of common 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 on page 11 is based on the study and present significant information about the components of common property.

THE SUPPLEMENTARY INFORMATION ON FUTURE MAJOR REPAIRS AND REPLACEMENTS THAT HAS
NOT BEEN AUDITED APPEARS ON PAGE 11

UNAUDITED SUPPLEMENTARY INFORMATION

Orcas Highlands Association

Reserve Study

Reserve Study
Executive Summary

Orcas Highlands Association
Orcas Island, Washington
Level of Service: Reserve Study – FULL

120 Lots
July 1, 2020 through June 30, 2021

| | |
|--|-------------|
| Starting Road Fund Reserve Balance..... | \$17,786.50 |
| Starting Reserve Fund..... | \$9977 |
| Fully Funded Reserve Balance..... | \$34,240 |
| Percent Funded..... | 81% |
| Recommended 2020 Quarterly "Fully Funding" Reserve Contribution..... | \$21,600 |
| Recommended 2020 "Special Assessment" for Reserve..... | \$0 |
| Most recent Reserve Contribution Rate per Quarter per Lot..... | \$45 |

Risk of a Special Assessment.....Low

Economic Assumptions

Annual Inflation Rate including rate of petroleum.....4.00%

Comments:

This reserve study was prepared by the Board of Directors for the Orcas Highlands Association. The unique construction costs and remote location of the Association property limits the number of contractors available to maintain the roadway system and would be difficult for an outside consultant to estimate costs of repair. Additionally, the cost of a credentialed Reserve Specialist to develop a study would be in excess of 5% of the annual budget and create an undue hardship on the Association.

The Road Fund Reserve funds are needed for the paving of the Association's road system. The roadway paving and subgrade is estimated to have a viable life span of 8 – 10 years. Some lightly used sections historically last much longer, wear and deterioration is not uniform and repaving applications varies by section. We are basing the reserve funding on being able to repave in 7 – 8 years with funds left over for beginning to rebuild for the next 8-year cycle.

The Reserve Fund is to provide moneys for rebuilding the mailbox structure. The structure has an estimated life span of 20 years and will need reroofing at that time. It may be decided to replace the structure with a modular system in the future as the volume of mail is on the decline. The current balance in the reserve account will accommodate future needs and does not require additional funding.