

**THE RANCHES HOME
OWNERS' ASSOCIATION**

Independent Auditors' Report
and
Financial Statements

December 31, 2006

**THE RANCHES HOME
OWNERS' ASSOCIATION**
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Independent Auditors' Report

To the Board of Directors and Members
The Ranches Home Owners' Association

We have audited the balance sheet of The Ranches Home Owners' Association as of December 31, 2006 and the related statements of revenues, expenses, and changes in fund balance and cash flows for the period then ended. These 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.

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 The Ranches Home Owners' Association as of December 31, 2006, and the results of its operations and its cash flows for the period then ended in conformity with accounting principles generally accepted in the United States of America.

The supplementary information on future major repairs and replacements on page 8 is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

MANTYLA McREYNOLDS
Salt Lake City, Utah
February 28, 2006

**THE RANCHES HOME
OWNERS' ASSOCIATION
BALANCE SHEET
December 31, 2006**

	Operating Fund	Replacement Fund	Total
ASSETS			
Current Assets			
Cash, including interest-bearing deposits	\$ 12,750	\$ 206,589	\$ 219,339
Assessments receivable, net of allowance for doubtful accounts of \$35,123 - Note B	106,966	-	106,966
Other receivable	37,935	-	37,935
Prepaid expenses	2,839	-	2,839
Total Current Assets	160,490	206,589	367,079
TOTAL ASSETS	\$ 160,490	\$ 206,589	\$ 367,079
 LIABILITIES AND FUND BALANCES			
Accounts payable	\$ 40,289	\$ -	\$ 40,289
Assessments received in advance	23,804	-	23,804
TOTAL LIABILITIES	64,093	-	64,093
Fund balances	96,397	206,589	302,986
TOTAL LIABILITIES AND FUND BALANCES	\$ 160,490	\$ 206,589	\$ 367,079

See accompanying notes to financial statements

**THE RANCHES HOME
OWNERS' ASSOCIATION
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND BALANCES
For the period ended December 31, 2006**

	Operating Fund	Replacement Fund	Total
REVENUES			
Regular Assessments	\$ 457,967	\$ 148,500	\$ 606,467
Other Income	180,494	-	180,494
Interest Income	-	3,720	3,720
	<u>638,461</u>	<u>152,220</u>	<u>790,681</u>
EXPENSES			
Operating	573,688	-	573,688
Major repairs and replacements	-	71,508	71,508
	<u>573,688</u>	<u>71,508</u>	<u>645,196</u>
EXCESS OF REVENUES OVER EXPENSES	64,773	80,712	145,485
BEGINNING FUND BALANCES	36,301	121,200	157,501
Transfer between funds	(4,677)	4,677	-
ENDING FUND BALANCES	<u>\$ 96,397</u>	<u>\$ 206,589</u>	<u>\$ 302,986</u>

See accompanying notes to financial statements

**THE RANCHES HOME
OWNERS' ASSOCIATION
STATEMENT OF CASH FLOWS
For the Period Ended December 31, 2006**

	<u>Operating Fund</u>	<u>Replacement Fund</u>	<u>Total</u>
<u>Cash Flows from Operating Activities:</u>			
Excess of revenues over expenses	\$ 64,773	\$ 80,712	\$ 145,485
Adjustments to reconcile excess of revenues over expenses to net cash provided by operating activities:			
(Increase) decrease in:			
Assessments receivables	(60,303)	-	(60,303)
Other receivable	(30,406)	-	(30,406)
Prepaid expenses	13,450	-	13,450
Increase (decrease) in:			
Accounts payable	27,993	-	27,993
Bank overdraft	(6,736)	-	(6,736)
Assessments received in advance	8,656	-	8,656
Net cash Provided by Operating Activities	<u>17,427</u>	<u>80,712</u>	<u>98,139</u>
 <u>Cash Flows from Financing Activities:</u>			
Interfund transfers	<u>(4,677)</u>	<u>4,677</u>	<u>-</u>
 Net increase (decrease) in cash	12,750	85,389	98,139
 Beginning Cash Balance	-	121,200	121,200
Ending Cash Balance	<u>\$ 12,750</u>	<u>\$ 206,589</u>	<u>\$ 219,339</u>
 Supplemental Disclosure Information:			
Cash paid during the year for interest	\$ -	\$ -	\$ -
Cash paid during the year for income taxes	\$ -	\$ -	\$ -

See accompanying notes to financial statements

**THE RANCHES HOME
OWNERS' ASSOCIATION
NOTES TO FINANCIAL STATEMENTS**

NOTE A-NATURE OF ORGANIZATION

The Ranches Home Owners' Association is a statutory association incorporated in the State of Utah on June 25, 1998. The Association is responsible for the maintaining, operating and governing of the common property within the development. The Ranches consists of one thousand eight hundred and thirty-eight units, and certain common area and facilities located in Eagle Mountain, Utah.

NOTE B-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 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.

Cash and Cash Equivalents

Cash and cash equivalents consist of cash on deposit in commercial banks.

Member Assessments/Assessments receivable

Association members are subject to monthly 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 levy against any assessment account which is not paid in full as of thirty days from its due date and a late fee in the amount of \$10.00 per month including simple interest at 8% per annum is assessed. The Association also retains legal counsel and places liens on the properties of members whose assessments are fifty-one days or more delinquent. Any excess assessments at year end are retained by the Association for use in the succeeding year. At December 31, 2006 the Association had an allowance for uncollectible accounts of \$35,123. The allowance for doubtful accounts, which is based upon management's evaluation of numerous factors, including a predictive analysis of the outcome of the current portfolio and prior credit loss experience, is deemed adequate to cover reasonably expected losses inherent in outstanding receivables. The Association charges off uncollectible accounts when management estimates no possibility of collecting the related receivable. The Association considers accounts receivable to be past due or delinquent based on contractual terms.

**THE RANCHES HOME
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NOTES TO FINANCIAL STATEMENTS**

NOTE B-SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES-(continued)

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. At December 31, 2006 property not capitalized consists of approximately twenty-seven acres of sidewalks, access roads, and greenbelts.

Income Taxes

The Association qualifies as a tax-exempt homeowners' association under Internal Revenue Code Section 528 for the year ended December 31, 2006. Under that Section, the Association is not taxed on income and expenses related to its exempt purpose, which is the acquisition, construction, management, maintenance, and care of Association property. Net nonexempt function income, which includes earned interest and revenues received from nonmembers, is taxed at 30% by the federal government and 5% by the State of Utah.

Interest Income

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

Use of Estimates in Preparation of Financial Statements

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, 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 C-FUTURE MAJOR REPAIRS

The Association's governing documents require funds to be accumulated for future major repairs and replacements. Accumulated funds, which aggregate approximately \$206,589 at December 31, 2006 are held in separate accounts and are generally not available for operating purposes.

The Association engaged an independent engineer who conducted a study in June 2005 to estimate the remaining useful lives and the replacement costs of the common property components. The Association is funding for such major repairs and replacements over the estimated useful lives of the components based on the study's estimates of current replacements 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.

**THE RANCHES HOME
OWNERS' ASSOCIATION
NOTES TO FINANCIAL STATEMENTS**

NOTE C-FUTURE MAJOR REPAIRS-(continued)

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 D-SIGNIFICANT CONCENTRATIONS OF CREDIT RISK

The Association has cash in excess of FDIC federally insured limits in the amount of \$119,339 as of December 31, 2006.

NOTE D-LEASE OBLIGATION

The office lease expires on March 31, 2008 with current monthly rent of \$1,989.17. The lease has an escalation clause requiring an increase in monthly rental payments of 4% per year. Office rent expense for the year ending December 31, 2006 was \$7,774. The following is a schedule by years of future minimum lease payments required by operating leases that have initial or remaining non-cancellable lease terms extending beyond December 31, 2006:

Rent Period	Rental Rate Per Square Footage	Square Footage	Number of Months	Total
1/1/07 - 3/31/07	\$ 1.29	1,540	3	5,968
4/1/07 - 3/31/08	\$ 1.34	1,540	12	24,825
			Total	30,792

NOTE E-MANAGEMENT AGREEMENT

On December 18, 2006, the Association entered into an agreement with Quality Management Services, Inc. to provide management services for the Association. The agreement expires on December 31, 2007 with a current annual fee of \$180,000 (\$15,000 paid monthly). The fees for the services are set for one year or an increase in properties by 35%, whichever comes first. In the event that the properties increase by 35%, a new payment agreement will be negotiated. In the event that the properties increase by 35% and a new agreement has not been negotiated, then the current agreement will remain in effect.

NOTE F-COMMITMENTS & CONTINGENCIES

On December 30, 2006, the Association was notified by Sandra Vanbloem of formal action against the Association. The action stems from the unfortunate automobile accident which took the life of Lawrence Vanbloem on December 10, 2004. The heirs of his estate are claiming that the accident was caused because Mr. Vanbloem's view of oncoming traffic was obstructed by a sign placed in the median at the intersection where he pulled out. The litigation is still in its early stages, as such, the Association can not estimate the extent of liability they will have to assume to resolve this matter. However, the Association's management does not believe the Association has any liability in this matter and the Association is intending to contest this case vigorously.

SUPPLEMENTARY INFORMATION

THE RANCHES HOME OWNERS' ASSOCIATION SUPPLEMENTARY INFORMATION ON FUTURE MAJOR REPAIRS AND MAINTENANCE For the Period Ended December 31, 2006

The Association's board of directors conducted a study in June 2005 to estimate 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 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. (Amounts are rounded to the nearest thousand dollars).

Components	Estimated Remaining Useful Life (Years)	Estimated Current Replacement Cost
Roofing	4	\$ 4,000
Painted Surfaces	3	24,000
Street Signs	1	12,000
Property Identification	11 to 12	71,000
Privacy Fencing	14	42,000
Rail Fencing	3	21,000
Recreation Equipment	12	267,000
Light Fixtures	12	193,000
Irrigation System	0	9,000
Tree Replacement	3	28,000
Asphalt Path - Overlay	19	169,000
Asphalt Path - Slurry Seal	0	22,000
TOTALS		\$ 862,000