

Raft Island Improvement Association

Audit Report Financial Statements & Supplementary Information June 30, 2016

Cagianut & Company
CERTIFIED PUBLIC ACCOUNTANT
www.hoacpa.com

Members - Community Associations Institute—Washington State
Washington Society of Certified Public Accountants
American Institute of Certified Public Accountants

Independent Auditors' Report

To the Board of Directors and Members
Raft Island Improvement Association
Raft Island, Washington

Report on the Financial Statements

We have audited the accompanying financial statements of Raft Island Improvement Association, which comprise the Balance Sheet as of June 30, 2016, and the related Statement of Changes in Fund Balances, Statement of Revenues and Expenses and Statement of Cash Flows for the year then ended and the related notes to the financial statements.

Association's Responsibility for the Financial Statements

The Association 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.

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 of 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 Raft Island Improvement Association as of June 30, 2016, and the results of its operations and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Other Matter - Required Supplementary Information

Our audit was made for the purpose of forming an opinion on the basic financial statements taken as a whole. We have not applied procedures to determine whether the funds designated for future repairs and replacements are adequate to meet such future costs because that determination is outside the scope of our audit.

Accounting principles generally accepted in the United States of America [GAAP] require that the Supplementary Information on Future Major Repairs 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 and for placing the basic financial statements and related notes 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.

Cagianut & Company, CPA

Bellevue, Washington

September 30, 2016

Raft Island Improvement Association

Balance Sheet
June 30, 2016

	<u>OPERATING FUND</u>	<u>REPLACEMENT FUND</u>	<u>TOTAL</u>
ASSETS			
Cash, including interest bearing deposits	\$ 343,225	\$ 576,934	\$ 920,159
Investments	121,729	377,146	498,874
Assessments Receivable	80,647		80,647
Less: Allowance for Bad Debts	(59,213)		(59,213)
Prepaid Insurance	8,321		8,321
TOTAL ASSETS	<u>\$ 494,708</u>	<u>\$ 954,079</u>	<u>\$ 1,448,787</u>
 LIABILITIES AND FUND BALANCES			
LIABILITIES			
Accounts Payable	\$ 1,801		\$ 1,801
Assessments Received in Advance	54,924		54,924
Accrued Interest Payable	39,830		39,830
USDA Loans Payable	5,237,600		5,237,600
Income Taxes Payable	175		175
TOTAL LIABILITIES	<u>5,334,331</u>		<u>5,334,331</u>
 FUND BALANCES			
Operating	(4,839,623)		(4,839,623)
Replacement		\$ 954,079	954,079
TOTAL FUND BALANCES	<u>(4,839,623)</u>	<u>954,079</u>	<u>(3,885,543)</u>
TOTAL LIABILITIES AND FUND BALANCES	<u>\$ 494,708</u>	<u>\$ 954,079</u>	<u>\$ 1,448,787</u>

See Notes to the Financial Statements

Raft Island Improvement Association
Statement of Changes in Fund Balances
For the Year Ended June 30, 2016

	OPERATING FUND	REPLACEMENT FUND	TOTAL
Balance at the Beginning of the Year	\$ 363,744	\$ (4,417,652)	\$ (4,053,909)
Accumulated Other Comprehensive Income<Loss> on Investments		7,497	7,497
Transfer Between Funds - Accumulated OCI	38,344	(38,344)	
Transfer Between Funds - Cash Accounts	22,303	(22,303)	
Transfer Between Funds - USDA Loans	(5,382,334)	5,382,334	
Excess <Deficiency> of Revenues over Expenses	118,321	42,547	160,868
Balance at the End of the Year	<u>\$ (4,839,623)</u>	<u>\$ 954,079</u>	<u>\$ (3,885,543)</u>

See Notes to the Financial Statements

Raft Island Improvement Association

Statement of Revenues and Expenses

For the Year Ended June 30, 2016

	OPERATING FUND	REPLACEMENT FUND	TOTAL
REVENUES			
General Assessments	\$ 413,762	\$ 29,592	\$ 443,354
Late/Finance Charge/Lien Fees	12,110		12,110
Interest	1,436	10,209	11,645
Realized Gain/(Loss)		2,746	2,746
Miscellaneous	255		255
TOTAL REVENUES	427,563	42,547	470,110
EXPENSES			
Audit & Tax Preparation	4,200		4,200
Bad Debts	19,561		19,561
Federal Taxes	4,067		4,067
Insurance	30,610		30,610
Legal	5,230		5,230
Loan Interest	190,830		190,830
Management	10,694		10,694
Miscellaneous	87		87
Office Supplies	1,039		1,039
Parks & Maintenance	11,077		11,077
Postage	966		966
Reserve Study	2,400		2,400
Roads	24,725		24,725
Utilities	3,756		3,756
TOTAL EXPENSES	309,242		309,242
EXCESS <DEFICIENCY> OF REVENUES OVER EXPENSES	\$ 118,321	\$ 42,547	\$ 160,868

See Notes to the Financial Statements

Raft Island Improvement Association

Statement of Cash Flows
For the Year Ended June 30, 2016

	OPERATING FUND	REPLACEMENT FUND	TOTAL
<i>Cash Flows from Operating Activities:</i>			
Cash from Assessments	\$ 450,632	\$ 29,592	\$ 480,224
Interest Received	1,436	10,209	11,645
Miscellaneous Income	12,365	2,746	15,111
Cash Paid for Services and Products	(297,533)		(297,533)
Net Increase <Decrease> in Cash from Operating Activities	166,900	42,547	209,447
<i>Cash Flows from Investing Activities:</i>			
Purchase of Investments	(121,729)	(246,673)	(368,402)
Sale of Investments	201,964		201,964
<i>Cash Flows from Financing Activities:</i>			
Unrealized Gain/Loss - Current Year		3,949	3,949
Loan Principal Payments	(104,115)		(104,115)
Transfers Between Funds	22,303	(22,303)	
Change in Due Between Funds	(89,327)	89,327	
Net Increase <Decrease> in Cash	75,996	(133,153)	(57,157)
Cash, including interest bearing deposits, at the Beginning of Year	267,229	710,087	977,316
Cash, including interest bearing deposits, at the End of Year	\$ 343,225	\$ 576,934	\$ 920,159

Reconciliation of Excess <Deficiency> of Revenues over Expenses to Net Cash Received by Operations:

Excess <Deficiency> of			
Revenues over Expenses	\$ 118,321	\$ 42,547	\$ 160,868
Decreased Assessments Receivable	30,964		30,964
Increased Bad Debt Allowance	8,016		8,016
Increased Prepaid Insurance	(535)		(535)
Decreased Prepaid Taxes	3,940		3,940
Increased Accounts Payable	901		901
Increased Prepaid Assessments	5,906		5,906
Increased Taxes Payable	175		175
Decreased Accrued Interest Payable	(789)		(789)
Net Increase <Decrease> in Operating Cash	\$ 166,900	\$ 42,547	\$ 209,447

See Notes to the Financial Statements

Raft Island Improvement Association

Notes to the Financial Statements

June 30, 2016

NOTE 1 - ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

General

Raft Island Improvement Association was incorporated November 5, 1984 in the state of Washington as a nonprofit corporation. The Association is responsible for the operation and maintenance of the common property. This is a 226-unit planned residential development located in Gig Harbor, Washington.

Accounting Method

The Association prepares its statements on the accrual basis of accounting whereby income and expenses are recognized when earned and incurred. Fund accounting is employed to properly account for the monies. The Operating Fund is used to pay for all utility, insurance, general maintenance, landscaping, and administrative obligations of the Association. The Replacement Fund has been established to meet the replacement and major repair obligations of the Association with regard to the common area components.

Capitalization Policy

Replacements and improvements to the real property are not capitalized on the books of the Association as the Board does not have the right to sell the common areas and keep the proceeds. Property and equipment acquired by the Association are recorded at cost. The property is depreciated over its estimated useful lives using the straight line method of depreciation. There is no capitalized property at the end of the year.

Assessments Receivable

Association members are subject to 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 Declaration provides for various collection remedies for delinquent assessments including the filing of liens, foreclosing on the unit owner, and obtaining judgment on the assets of the unit owner. The Association uses the allowance method to account for uncollectible assessments receivable.

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.

Cash, including Interest Bearing Deposits

For purposes of the statement of cash flows, Cash, including Interest Bearing Deposits, includes cash on hand, funds on deposit with financial institutions, and investments with original maturities of three months or less.

Fair Value Measurements

The three levels of the fair value hierarchy under ASC 820, Fair Value Measurements and Disclosures, are described below:

Level 1: Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that the Association has the ability to access.

Level 2: Inputs to the valuation methodology include quoted prices for similar assets or liabilities in active markets; quoted prices for identical or similar assets or liabilities in inactive markets; inputs other than quoted prices that are observable for the asset or liability; inputs that are derived principally from or corroborated by observable market data by correlation or other means. If the asset or liability has a specified (contractual) term, the Level 2 input must be observable for substantially the full term of the asset or liability.

Level 3: Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

Investments

Investments include certificates of deposit with original maturities over 90 days, as well as municipal bonds and mutual stock funds. These are level one type investments.

Date of Review

In preparing the financial statements, the Association has evaluated events and transactions for potential recognition or disclosure through the date of the audit report, which is the date that the financial statements were issued or available to be issued.

Raft Island Improvement Association

Notes to the Financial Statements
June 30, 2016

NOTE 2 - REPLACEMENT FUNDING PROGRAM

The Association is currently funding replacement reserve accounts for the future major repair and replacement of Association common areas as disclosed in Note 1. Accumulated funds are held in separate accounts and are generally not available for operating purposes. The funding is based upon a professional reserve study approved by the Board of Directors.

The 2014-2015 reserve study recommended minimum (baseline) monthly allocations to the Replacement Fund of \$9,167. Actual monthly allocations in the current fiscal year were \$2,466. The most recent reserve study recommends monthly allocations to the Replacement Fund in 2016-2017 of \$10,000. The 2016-2017 budgeted monthly reserve contributions are \$2,466.

Funds are being accumulated in the Replacement Fund based on estimates of future needs for repairs and replacements of common property components. Actual expenditures may vary from the estimated future expenditures, and variations may be material. Therefore, the amounts accumulated in the Replacement Fund may not be adequate to meet all future needs for major repairs and replacements. If additional funds are needed, the Association has the right, subject to certain legal limitations, to increase assessments, pass special assessments, or delay replacement if these funds are found to be inadequate for all future costs.

NOTE 3 - FEDERAL INCOME TAXES

Associations may be taxed either as homeowners associations or as regular corporations. For the current year the Association elected to file as a homeowners association using form 1120-H under Internal Revenue Code Section 528. 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 interest, user fees and revenues from non-members is taxed at 30%. Certain expenses were allocated to offset a portion of the taxable income.

The Association's federal tax return is subject to audit by the Internal Revenue Service. The tax returns for the current and prior two fiscal years remain open for examination by the IRS. In evaluating the Association's tax positions and accruals, the Association believes that its estimates are appropriate based on the current facts and circumstances.

NOTE 4 - OWNERS' ASSESSMENTS

Monthly assessments to owners were \$165. The All Saints Center has six lots on which they pay 66.67% of the annual assessment in accordance with a written agreement dated August 29, 2012. Of this amount, a portion was designated to the Replacement Fund.

The annual budget and owners' assessments are determined by the Board of Directors, within certain restrictions. The Association retains excess operating funds at the end of the year, if any, for use in future operating periods.

Raft Island Improvement Association

Notes to the Financial Statements
June 30, 2016

NOTE 5 - BRIDGE REPLACEMENT FUNDING/USDA LOANS PAYABLE

In 1996, the membership approved a multi-year annual special assessment for replacement of the Raft Island Bridge with a new structure. The assessment is due from July 1, 1996 through 2016 with increases of 8.04% each year. The assessment for the current fiscal year is included in the regular assessment in Note 4.

On August 26, 2013, the Association signed a Bond Purchase Agreement and associated Bond and Security Agreement with Northwest Farm Credit Services to provide construction funding of up to \$5,742,400. Included was a \$60,000 commitment fee which was paid in prior fiscal years. Terms called for interest-only payments at 3.2%.

On October 20, 2014, the Association put into place permanent funding to pay off the construction bond in the amount of \$5,392,400. The loan was made or insured by the Consolidated Farm and Rural Development Act, as it was determined that the Association was unable to obtain sufficient credit elsewhere. Assessments of a sufficient amount to pay the loan must be imposed on the membership and they are assigned and pledged to the United States Department of Agriculture (USDA) - Rural Development. Additional security for the loan includes the Bridge and any other properties and assets of the Association. The loan was split into three separate loans and the terms of the loans are as follows:

Loan for \$1,849,400 at a rate not to exceed 4% per year payable over 30 years. There is a requirement to set aside \$887 per month into a reserve account until the accumulated amount is \$106,416.

Loan for \$2,893,000 at a rate not to exceed 3.375% per year payable over 30 years. There is a requirement to set aside \$1,285 per month into a reserve account until the accumulated amount is \$154,140.

Loan for \$650,000 at a rate not to exceed 3.5% per year payable over 30 years. There is a requirement to set aside \$294 per month into a reserve account until the accumulated amount is \$35,178.

At this time, the Board has designated Operating accounts totaling \$289,788 to serve as the required reserve for the loans. These funds will not be available for any other projects.

The Association funded the remaining construction and interest costs from the Replacement Fund. The bridge replacement project was completed in 2014. Principal and interest payments on the loans will continue according to the terms. In the current year, the Board approved reporting the loans in the Operating Fund. Additionally, the loan payments are funded via general assessments and not a separate bridge assessment, as had been done in the past.

Based on borrowing rates currently available to the Association for loans with similar terms and maturities, the fair value of the loan payable is the same as the book value.

The principal payments on the three USDA loans for the next five years are as follows:

2016-17	\$	34,770	\$	59,771	\$	13,207
2017-18		36,175		61,808		13,673
2018-19		37,636		63,915		14,156
2019-20		39,157		66,093		14,655
2020-21		40,738		68,346		15,173
After 2020-21		<u>1,611,284</u>		<u>2,486,877</u>		<u>560,166</u>
Total	\$	<u><u>1,799,760</u></u>	\$	<u><u>2,806,810</u></u>	\$	<u><u>631,030</u></u>

NOTE 6 - INVESTMENTS

The Association classifies its marketable securities as "held to maturity" if it has the positive intent and ability to hold the securities to maturity. Securities classified as held to maturity are carried at amortized cost. All other marketable securities are classified as "available for sale" and are carried at fair value. Currently, the Association is invested in municipal bond and mutual stock funds and they are carried at fair value. The unrealized gain is \$7,497, which has been recorded as Accumulative Other Comprehensive Income/(Loss) in the current year's financial statements.

Raft Island Improvement Association

Notes to the Financial Statements
June 30, 2016

NOTE 7 - UNINSURED CASH BALANCES

The Association's cash deposits are with various financial institutions. All accounts in one financial institution are combined and the maximum FDIC insurance amount per bank is \$250,000. At the end of the year, bank balances exceeded the FDIC limitation by almost \$92,000.

NOTE 8 - CONTINGENCY/ROADS

It is projected that the amount necessary for the anticipated road project may exceed the available monies in the Replacement Fund. The Board has requested bids for the project and these bids will be opened October 3, 2016. The amount of the bid will determine whether a loan is required. It has not been determined whether a special assessment is necessary to repay the loan.

Raft Island Improvement Association

June 30, 2016

Supplementary Information on Future Major Repairs
and Replacements
(Unaudited)

A professional reserve study was prepared on October 5, 2015 by Jeff Samdal & Associates, Inc. to estimate the remaining useful lives and the replacement costs of the components of common property. The estimates were based on current estimated replacement costs. Funding requirements consider an annual inflation rate of 3.0% and interest of 3.0%, net of taxes, on amounts funded for future major repairs and replacements. The following table is based on the study and presents significant information about the components of common property.

Component	Estimated Remaining Useful Life in Years	Estimated Current Replacement Costs	Fund Balance at Year End
Site			
Asphalt overlay of 10% of roads per year for 10 years	1	\$ 79,464	
Complete road replacement	22	2,402,400	
Asphalt repair allotment	1	8,000	
Resurface dock decking with synthetic decking	2	10,400	
Rebuild the dock and pilings	23	85,000	
Replace concrete bulkhead at north beach	28	57,200	
Picnic assets replacement allotment	2	2,000	
Playground equipment replacement	7	5,000	
Rebuild the north beach stairs	9	7,000	
Resurface the tennis court	5	9,200	
Replace entrance sign and upgrade surrounding area	1	4,800	
 TOTAL			 \$ <u><u>954,079</u></u>

Percent Funded as of October 5, 2015 - 59.7%