

Durango Mountain Master Association, Inc.

**Independent Auditor's Report,
Financial Statements, and
Supplementary Information**

April 30, 2008

DURANGO MOUNTAIN MASTER ASSOCIATION, INC.

Table of Contents

April 30, 2008

INDEPENDENT AUDITOR’S REPORT 1

FINANCIAL STATEMENTS:

 Balance Sheet..... 2

 Statement of Revenues, Expenses, and Changes in Fund Balances..... 3

 Statement of Cash Flows 4

 Notes to Financial Statements 5 – 9

SUPPLEMENTARY INFORMATION:

 Future Major Repairs and Replacements (Unaudited) 11

INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
Durango Mountain Master Association, Inc.

We have audited the accompanying balance sheet of *Durango Mountain Master Association, Inc. (the Association)*, as of April 30, 2008, and the related statement of revenues, expenses, and changes in fund balances and cash flows for the year 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 consideration of internal controls over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Association's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and the 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 *Durango Mountain Master Association, Inc.* as of April 30, 2008, and the results of its operations and cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The Schedule of Future Major Replacements and Repairs on page 11 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.



Sacramento, California
November 6, 2008

DURANGO MOUNTAIN MASTER ASSOCIATION, INC.

Balance Sheet

April 30, 2008

	Operating Fund	Replacement Fund	Total
ASSETS			
Current Assets:			
Cash	\$ 155,803	\$ 16,043	\$ 171,846
Assessments receivable	20,422	-	20,422
Related party receivable	122,293	-	122,293
Interfund receivable	-	304,404	304,404
Prepaid expenses and other current assets	9,723	-	9,723
Total current assets	308,241	320,447	628,688
Restricted Cash	120,876	-	120,876
Property and Equipment, Net	874,199	-	874,199
	<u>\$ 1,303,316</u>	<u>\$ 320,447</u>	<u>\$ 1,623,763</u>
LIABILITIES AND FUND BALANCES			
Current Liabilities:			
Accounts payable and accrued expenses	\$ 7,202	\$ -	\$ 7,202
Related party payable	157,031	-	157,031
Interfund payable	304,404	-	304,404
Current maturities of long-term debt	70,413	-	70,413
Total current liabilities	539,050	-	539,050
Security Deposits	120,876	-	120,876
Long-Term Debt, Net of Current Maturities	636,126	-	636,126
Total liabilities	1,296,052	-	1,296,052
Fund Balances	7,264	320,447	327,711
	<u>\$ 1,303,316</u>	<u>\$ 320,447</u>	<u>\$ 1,623,763</u>

DURANGO MOUNTAIN MASTER ASSOCIATION, INC.

Statement of Revenues, Expenses, and Changes in Fund Balances

For the year ended April 30, 2008

	Operating Fund	Replacement Fund	Total
Revenues:			
Real estate transfer fees	\$ 176,013	\$ 161,939	\$ 337,952
Property assessments	204,236	-	204,236
Sales assessments	166,128	-	166,128
Lodging assessments	78,637	-	78,637
Interest and other income	10,210	161	10,371
Total revenues	635,224	162,100	797,324
Expenses:			
Community center operating expense, net	177,360	-	177,360
Landscaping, snow and trash removal	108,283	-	108,283
Janitorial	77,000	-	77,000
Management and accounting fees	67,000	-	67,000
Security	64,000	-	64,000
Shuttle service	62,000	-	62,000
Insurance	21,000	-	21,000
Supplies and materials	20,863	-	20,863
Utilities	20,178	-	20,178
Repairs and maintenance	16,847	-	16,847
Other expense	12,004	1,275	13,279
Pool expenses	11,000	-	11,000
Total expenses	657,535	1,275	658,810
(Deficiency) Excess of Revenues Over Expenses	(22,311)	160,825	138,514
Beginning Fund Balances	29,575	159,622	189,197
Ending Fund Balances	\$ 7,264	\$ 320,447	\$ 327,711

DURANGO MOUNTAIN MASTER ASSOCIATION, INC.

Statement of Cash Flows

For the year ended April 30, 2008

	Operating Fund	Replacement Fund	Total
Cash Flows from Operating Activities:			
Cash received from assessments and real estate transfer fees	\$ 583,691	\$ 161,939	\$ 745,630
Cash paid to suppliers	(628,198)	(1,275)	(629,473)
Interest received	7,785	161	7,946
Net cash from operating activities	<u>(36,722)</u>	<u>160,825</u>	<u>124,103</u>
Cash Flows from Investing Activities:			
Purchase of property and equipment	(22,120)	-	(22,120)
Change in restricted cash	(21,872)	-	(21,872)
Changes in interfund receivables and payables	160,664	(160,664)	-
Net cash from investing activities	<u>116,672</u>	<u>(160,664)</u>	<u>(43,992)</u>
Cash Flows from Financing Activities:			
Principal payments on long-term debt	(61,013)	-	(61,013)
Net cash from financing activities	<u>(61,013)</u>	<u>-</u>	<u>(61,013)</u>
NET CHANGE IN CASH	18,937	161	19,098
Cash, beginning of year	<u>136,866</u>	<u>15,882</u>	<u>152,748</u>
Cash, end of year	<u>\$ 155,803</u>	<u>\$ 16,043</u>	<u>\$ 171,846</u>
Reconciliation of (Deficiency) Excess of Revenues Over Expenses to Net Cash from Operating Activities:			
(Deficiency) Excess of Revenues Over Expenses	\$ (22,311)	\$ 160,825	\$ 138,514
Adjustments to Reconcile (Deficiency) Excess of Revenues Over Expenses to Net Cash from Operating Activities:			
Depreciation	42,888	-	42,888
(Increase) decrease in:			
Assessments receivable	17,570	-	17,570
Related party receivable	(82,046)	-	(82,046)
Prepaid expenses and other current assets	771	-	771
Increase (decrease) in:			
Accounts payable and accrued expenses	(18,623)	-	(18,623)
Related party payable	3,157	-	3,157
Security deposits	21,872	-	21,872
Net cash from operating activities	<u>\$ (36,722)</u>	<u>\$ 160,825</u>	<u>\$ 124,103</u>
Supplemental Disclosure of Cash Flow Information:			
Cash paid during the year for interest	\$ 58,276	\$ -	\$ 58,276

See accompanying notes

DURANGO MOUNTAIN MASTER ASSOCIATION, INC.

Notes to Financial Statements

1. GENERAL:

Durango Mountain Master Association, Inc. (the “Association” or “DMMA”) is a Colorado corporation. The Association was incorporated for the specific and primary purpose to promote the health, safety, and welfare of all members of the Association and to establish and maintain a desirable community and environment for all owners, lessees, and guests. The Association also implements and enforces architectural controls of lots and parcels, and provides for the ownership, management, administration, maintenance, and preservation of common areas, improvements and facilities within the master-planned community known as Durango Mountain Resort.

2. 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. These fees are also available to be used for any operating shortfall that may occur during the fiscal year.

Cash and Cash Equivalents

The Association considers all highly liquid investments with a maturity from the date of purchase of three months or less to be cash equivalents for the purpose of balance sheet and statement of cash flows presentation.

Security Deposits and Restricted Cash

To implement and enforce architectural control over aesthetic issues as specified in the Design Review Guidelines, the Association requires a deposit from each multi-family, mixed-use project, and/or single family residence equal to \$1.00 for every square foot of facility space. This deposit is refunded once the Design Review Board has inspected and approved the completed project and the lot has been re-vegetated and cleaned up. As of April 30, 2008 approximately \$121,000 in security deposits are reflected in restricted cash and the corresponding liability as security deposits

Property and Equipment

The Association capitalizes all property and equipment to which it has title or other evidence of ownership. Property and equipment acquired by the Association is recorded at cost and property contributed to the Association by the developer is recorded at estimated fair value at the date of contribution.

Depreciation

Capitalized common property is depreciated over its estimated useful life of 5 to 27.5 years, using the straight-line method of depreciation.

DURANGO MOUNTAIN MASTER ASSOCIATION, INC.

Notes to Financial Statements

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*:

Member Assessments

Association members are subject to annual 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 significantly delinquent. The Association considers all assessments receivable at April 30, 2008 to be fully collectible. Any excess assessments at year end are retained by the Association for use in the succeeding year.

Revenue Recognition

The Association generates revenue from three major sources, all of which can be used for any Association expenditure including and without limitation, the construction, acquisition or purchase of capital improvements and equipment. These revenue sources are as follows:

Real Estate Transfer Fee

The real estate transfer fee is a 2% fee levied on the buyer of property within the DMMA community based on the fair market value or sales price of the property. Real estate transfer fees are due and payable at the time of sale or transfer.

Sales and Lodging Assessment

The Association levies and collects from each first class member an assessment of 4.0% on all sales of tangible property and services rendered within the Durango Mountain Master Community. Services rendered specifically include the participation of members in any residential rental program. Sales and lodging assessments are recorded in the period the sale is incurred or the service is rendered.

Property Assessment

The property assessment is levied and collected from each property owner within the DMMA community on an annual basis. The property assessment is established by the board of directors, and is allocated to each residential and commercial unit, based on its value in proportion to the total value of all Association encumbered properties.

Income Taxes

Homeowners' associations may be taxed either as homeowners' associations or as regular corporations. For the year ended April 30, 2008, the Association was taxed as a regular corporation and filed Form 1120. As a regular corporation, membership income is exempt from taxation if certain elections are made, and the Association is taxed only on its non-membership income, such as interest earnings, at regular federal and state corporate rates.

Use of 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.

DURANGO MOUNTAIN MASTER ASSOCIATION, INC.

Notes to Financial Statements

3. CONCENTRATIONS:

The Association maintains its cash in bank deposit accounts which, at times, may exceed federally insured limits.

The Association's largest customer is the resort operator and community developer DSC/Purgatory, LLC dba Durango Mountain Resort ("DMR"). As of April 30, 2008, DMR accounted for the following concentrations:

- 86% of total accounts receivable
- 57% of all purchases, and
- 37% of all net sales

4. PROPERTY AND EQUIPMENT:

Property and equipment at April 30, 2008 consisted of the following:

Land	\$	100,000
Building and improvements		903,679
Construction in progress		52,000
Equipment and furnishings		64,065
		<u>1,119,744</u>
Less accumulated depreciation		<u>245,545</u>
	\$	<u><u>874,199</u></u>

Depreciation expense for the year ended April 30, 2008 was \$42,888.

5. LONG-TERM DEBT:

Long-term debt at April 30, 2008 consisted of the following:

Purgatory Village Land, LLC collateralized by buildings and land, monthly payments of \$5,303 including interest at 5.00%, due June 2013.	\$	289,238
First National Bank of Durango, collateralized by buildings and land, monthly payments of \$3,983 including interest at Prime + 1%, due August 2021.		<u>417,301</u>
		706,539
Less current maturities		<u>70,413</u>
	\$	<u><u>636,126</u></u>

The debt agreement between the Association and the First National Bank of Durango contains restrictive covenants with limitations related to certain investing and financing activities. The Association is in compliance with all of their restrictive covenants as of April 30, 2008.

DURANGO MOUNTAIN MASTER ASSOCIATION, INC.

Notes to Financial Statements

5. LONG-TERM DEBT (continued):

Aggregate annual maturities of long-term debt are as follows:

<u>Year Ending April 30:</u>	<u>Amount</u>
2009	\$ 70,413
2010	74,504
2011	78,678
2012	83,030
2013	87,751
Thereafter	<u>312,163</u>
Total	<u>\$ 706,539</u>

Interest expense for the year ended April 30, 2008 was \$58,276.

6. RELATED PARTY TRANSACTIONS:

The Association has contracted with DSC/Purgatory, LLC (dba DMR), who is the resort operator, community developer, and Declarant of the Association. As Declarant, DMR controls the board of directors until such time as the majority of the planned development of the Durango Mountain Resort has been completed. The Association has entered into a management agreement with DMR to manage its operations. Pursuant to this agreement, the Association incurred \$67,000 in management fees during the fiscal year ended April 30, 2008. In addition to the management agreement, the Association contracts with DMR to provide various services to the resort community including landscaping, snow and trash removal, security, shuttle, janitorial and labor costs to operate the community center amenity. Fees paid to DMR for these services were approximately \$364,300 during the fiscal year ended April 30, 2008. The Association receives its sales and lodging revenues from DMR, which amounted to \$244,765 during the fiscal year ended April 30, 2008. At April 30, 2008, the Association owed DMR \$157,031 and had a receivable from DMR of \$122,293.

In addition, the Association has a loan from Purgatory Village Land, LLC, an affiliate of DMR, for the original purchase of the Association's community center land and building. The loan balance at April 30, 2008 was \$289,238.

DURANGO MOUNTAIN MASTER ASSOCIATION, INC.

Notes to Financial Statements

7. FUTURE MAJOR REPAIRS AND REPLACEMENTS:

The Association's governing documents do not require funds to be accumulated for future major repairs and replacements. Accumulated funds, which aggregate approximately \$320,000 (includes a receivable from the operating fund of approximately \$304,000) at April 30, 2008 are held in a separate account and are generally not available for operating purposes.

In prior years, the Association had funded actual major repairs and replacement expenditures from budgeted and accumulated real estate transfer fees not used for operating fund purposes.

The funding program was based on a study performed by the Association's management in October 2008 to retroactively estimate the remaining useful lives and replacement costs of the common property components at April 30, 2008.

The Association is funding such major repairs and replacements over the estimated useful lives of the components based on management's estimates of current replacement costs, considering the only owned facility was newly constructed within the past five years. 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, to increase annual property assessments or levy a special assessment, or it may delay major repairs and replacements until funds are available.

SUPPLEMENTARY INFORMATION

DURANGO MOUNTAIN MASTER ASSOCIATION, INC.

Supplementary Schedule

Future Major Repairs and Replacements (Unaudited)

The Association's management conducted a study in October 2008 retroactive to April 30, 2008 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 fiscal year end. 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).

<u>Components</u>	<u>Estimated Remaining Useful Life (Years)</u>	<u>Estimated Current Replacement Cost</u>
Roof	25	\$ 100,000
Exteriors	20	85,000
Interior finish	15	50,000
Furniture and equipment	15	50,000
Hot tub	10	15,000
Wiring and plumbing	40	<u>50,000</u>
Total		\$ <u><u>350,000</u></u>