

HAWAIIAN SHORES COMMUNITY ASSOCIATION
(A Hawai'i Non-Profit Corporation)

AUDITED FINANCIAL STATEMENTS
(WITH INDEPENDENT AUDITORS' REPORT)

FOR THE YEARS ENDED OCTOBER 31, 2012 AND 2011

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Certified Public Accountants
Member: AICPA
HSCPA

INDEPENDENT AUDITORS' REPORT

To the Board of Directors
Hawaiian Shores Community Association
Pahoa, Hawai'i 96778

We have audited the accompanying statements of financial position of Hawaiian Shores Community Association (a Hawai'i nonprofit corporation) as of October 31, 2012 and 2011 and the related statements of revenue, expenses and change in fund balances, and cash flows for the years 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 audits.

We conducted our audits 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 Hawaiian Shores Community Association as of October 31, 2012 and 2011 and the revenue, expenses and change in fund balances, and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Carbonaro CPA & Associates, Inc.

Hilo, Hawai'i
December 26, 2012

Hawaiian Shores Community Association
Statement of Financial Position
As of October 31, 2012

	Operating Fund	Reserve Fund	Infrastructure Fund	Total
ASSETS				
CURRENT ASSETS				
Operating Checking/Savings (Note 13)	\$ 387,423	\$ -	\$ -	\$ 387,423
Reserve Checking/Savings	-	37,185	-	37,185
Infrastructure Savings	-	-	338,394	338,394
Total Cash and Cash Equivalents	<u>387,423</u>	<u>37,185</u>	<u>338,394</u>	<u>763,002</u>
Accounts Receivable (Note 3)				
Fee Assessments	144,528	-	-	144,528
Attorney Fees	1,800	-	-	1,800
Water Use	17,341	-	-	17,341
Other	16,662	-	-	16,662
Allowance for Doubtful Accounts	(75,000)	-	-	(75,000)
Total Accounts Receivable	<u>105,331</u>	<u>-</u>	<u>-</u>	<u>105,331</u>
Prepaid Expenses	<u>12,581</u>			<u>12,581</u>
Total Current Assets	<u>505,335</u>	<u>37,185</u>	<u>338,394</u>	<u>880,914</u>
PROPERTY AND EQUIPMENT (Note 2)				
Buildings, Furniture and Equipment (Note 9)	2,984,905	-	-	2,984,905
Land	2,645,628	-	-	2,645,628
Vehicles	38,955	-	-	38,955
Work in Progress	135,880	-	-	135,880
	<u>5,805,368</u>	<u>-</u>	<u>-</u>	<u>5,805,368</u>
Less Accumulated Depreciation	(2,480,992)	-	-	(2,480,992)
Net Fixed Assets	<u>3,324,376</u>	<u>-</u>	<u>-</u>	<u>3,324,376</u>
OTHER ASSETS				
Certificate of Deposit (Note 4)	<u>60,550</u>	<u>-</u>	<u>-</u>	<u>60,550</u>
TOTAL ASSETS	<u>\$ 3,890,261</u>	<u>\$ 37,185</u>	<u>\$ 338,394</u>	<u>\$ 4,265,840</u>
LIABILITIES AND NET ASSETS				
CURRENT LIABILITIES				
Accounts Payable	\$ 11,470	\$ -	\$ -	\$ 11,470
Prepaid Assessments	2,448	-	-	2,448
Prepaid Water	8,365	-	-	8,365
Payroll Liabilities	11,699	-	-	11,699
Tenant Water Deposits (Note 5)	4,811	-	-	4,811
Vacation Payable	4,486	-	-	4,486
Current Maturity of HNB Promissory Note (Note 13)	11,170	-	-	11,170
Total Current Liabilities	<u>54,449</u>	<u>-</u>	<u>-</u>	<u>54,449</u>
LONG TERM LIABILITIES				
HNB Promissory Note (Note 13)	<u>42,632</u>			<u>42,632</u>
Total Long Term Liabilities	<u>42,632</u>			<u>42,632</u>
FUND BALANCE (Note 2)				
Unrestricted Net Assets (Note 7)	<u>3,793,180</u>	<u>37,185</u>	<u>338,394</u>	<u>4,168,759</u>
TOTAL LIABILITIES AND NET ASSETS	<u>\$ 3,890,261</u>	<u>\$ 37,185</u>	<u>\$ 338,394</u>	<u>\$ 4,265,840</u>

The accompanying notes are an integral part of these financial statements.

Hawaiian Shores Community Association
Statement of Financial Position
As of October 31, 2011

	Operating Fund	Reserve Fund	Infrastructure Fund	Total
ASSETS				
CURRENT ASSETS				
Operating Checking/Savings	\$ 284,958	\$ -	\$ -	\$ 284,958
Reserve Checking/Savings	-	183,870	-	183,870
Infrastructure Savings	-	-	272,218	272,218
Total Cash and Cash Equivalents	<u>284,958</u>	<u>183,870</u>	<u>272,218</u>	<u>741,046</u>
Accounts Receivable (Note 3)				
Fee Assessments	141,687	-	-	141,687
Attorney Fees	14,845	-	-	14,845
Water Use	14,908	-	-	14,908
Other	12,343	-	-	12,343
Allowance for Doubtful Accounts	(75,000)	-	-	(75,000)
Total Accounts Receivable	<u>108,783</u>	<u>-</u>	<u>-</u>	<u>108,783</u>
Prepaid Expenses	<u>33,620</u>	<u>-</u>	<u>-</u>	<u>33,620</u>
Total Current Assets	<u>427,361</u>	<u>183,870</u>	<u>272,218</u>	<u>883,449</u>
PROPERTY AND EQUIPMENT (Note 2)				
Buildings, Furniture and Equipment	2,881,632	-	-	2,881,632
Land	2,645,628	-	-	2,645,628
Vehicles	38,955	-	-	38,955
Work in Progress (Note 16)	42,790	-	-	42,790
	<u>5,609,005</u>	<u>-</u>	<u>-</u>	<u>5,609,005</u>
Less Accumulated Depreciation	<u>(2,431,249)</u>	<u>-</u>	<u>-</u>	<u>(2,431,249)</u>
Net Capitalized Assets	<u>3,177,756</u>	<u>-</u>	<u>-</u>	<u>3,177,756</u>
TOTAL ASSETS	<u><u>\$ 3,605,117</u></u>	<u><u>\$ 183,870</u></u>	<u><u>\$ 272,218</u></u>	<u><u>\$ 4,061,205</u></u>
LIABILITIES AND NET ASSETS				
CURRENT LIABILITIES				
Accounts Payable	\$ -	\$ -	\$ -	\$ -
Prepaid Assessments	1,120	-	-	1,120
Prepaid Water	5,519	-	-	5,519
Tenant Water Deposits (Note 5)	5,827	-	-	5,827
Vacation Payable	5,390	-	-	5,390
Total Current Liabilities	<u>17,856</u>	<u>-</u>	<u>-</u>	<u>17,856</u>
FUND BALANCE (Note 2)				
Unrestricted Net Assets (Notes 7 and 16)	<u>3,587,261</u>	<u>183,870</u>	<u>272,218</u>	<u>4,043,349</u>
TOTAL LIABILITIES AND EQUITY	<u><u>\$ 3,605,117</u></u>	<u><u>\$ 183,870</u></u>	<u><u>\$ 272,218</u></u>	<u><u>\$ 4,061,205</u></u>

The accompanying notes are an integral part of these financial statements.

Hawaiian Shores Community Association
Statement of Revenue, Expenses and Change in Fund Balances
For the Year Ended October 31, 2012

	Operating Fund	Reserve Fund	Infrastructure Fund	Total
REVENUE				
Annual Assessments	\$ 302,530	\$ 45,325	\$ 52,110	\$ 399,965
Monthly Water Fees (Note 5)	217,745	-	13,528	231,273
Reimbursable Legal Fees	2,740	-	-	2,740
Miscellaneous Income	3,975	-	-	3,975
Transfer Fees	6,300	-	-	6,300
Guest Fees	2,023	-	-	2,023
Water Hookup Fees	4,000	-	-	4,000
Interest Income	294	135	241	670
Reimbursable Water System Damage	478	-	-	478
Total Revenue	540,085	45,460	65,879	651,424
EXPENSES				
Salaries & Wages	189,265	-	-	189,265
Utilities	80,409	-	-	80,409
Maintenance & Repairs	55,026	-	-	55,026
Depreciation	49,743	-	-	49,743
Insurance	32,622	-	-	32,622
Employee Benefits	26,999	-	-	26,999
Legal Fees	21,826	-	-	21,826
Bad Debt Expense	18,072	-	-	18,072
Payroll Expenses	14,788	-	-	14,788
Professional Services	9,855	-	-	9,855
Office Expense	7,642	-	-	7,642
Postage	6,879	-	-	6,879
Board of Directors Expense	4,038	-	-	4,038
Printing	3,265	-	-	3,265
Subscriptions & Trainings	2,052	-	-	2,052
Miscellaneous Expense	1,658	65	65	1,788
Property Taxes	1,442	-	-	1,442
Interest Expense	303	-	-	303
Development	-	-	-	-
Total Expenses	525,884	65	65	526,014
Change in Fund Balances	14,201	45,395	65,814	125,410
Beginning Fund Balance	3,587,261	183,870	272,218	4,043,349
Transfers	191,718	(192,080)	362	-
Ending Fund Balance	\$ 3,793,180	\$ 37,185	\$ 338,394	\$ 4,168,759

The accompanying notes are an integral part of these financial statements.

Hawaiian Shores Community Association
Statement of Revenue, Expenses and Changes in Fund Balances
For the Year Ended October 31, 2011

	Operating Fund	Reserve Fund	Infrastructure Fund	Total
REVENUE				
Annual Assessments	\$ 301,058	\$ 45,255	\$ 52,030	\$ 398,343
Monthly Water Fees (Note 5)	225,196	-	13,988	239,184
Reimbursable Legal Fees	20,850	-	-	20,850
Miscellaneous Income	13,726	-	-	13,726
Transfer Fees	6,000	-	-	6,000
Guest Fees	2,275	-	-	2,275
Water Hookup Fees	2,000	-	-	2,000
Interest Income	531	168	288	987
Reimbursable Water System Damage	105	-	-	105
Total Revenue	571,741	45,423	66,306	683,470
EXPENSES				
Salaries & Wages	208,840	-	-	208,840
Utilities	90,646	-	-	90,646
Depreciation	47,294	-	-	47,294
Maintenance & Repairs	41,312	-	-	41,312
Employee Benefits	37,200	-	-	37,200
Insurance	29,465	-	-	29,465
Bad Debt Expense	25,005	-	-	25,005
Payroll Expenses	15,843	-	-	15,843
Development	14,567	-	-	14,567
Office Expense	10,417	-	-	10,417
Professional Services	8,173	-	-	8,173
Legal Fees	6,449	-	-	6,449
Postage	6,177	-	-	6,177
Board of Directors Expense	4,371	-	-	4,371
Property Taxes	2,281	-	-	2,281
Printing	1,198	-	-	1,198
Subscriptions & Trainings	658	-	-	658
Miscellaneous Expense	416	-	65	481
Total Expenses	550,312	-	65	550,377
Change in Fund Balances	21,429	45,423	66,241	133,093
Beginning Fund Balance	3,453,559	153,321	272,544	3,879,424
Transfers	81,441	(14,874)	(66,567)	-
Prior Period Adjustment (Note 16)	30,832	-	-	30,832
Ending Fund Balance	\$ 3,587,261	\$ 183,870	\$ 272,218	\$ 4,043,349

The accompanying notes are an integral part of these financial statements.

Hawaiian Shores Community Association
Statement of Cash Flows
For the Year Ended October 31, 2012

	Operating Fund	Reserve Fund	Infrastructure Fund	Total
CASH FLOWS FROM OPERATING ACTIVITY				
Change in Fund Balances	\$ 14,201	\$ 45,395	\$ 65,814	\$ 125,410
Adjustments to reconcile changes in net assets with net cash provided by operating activities:				
Add Depreciation and Disposals	49,743	-	-	49,743
Add Bad Debt	18,072	-	-	18,072
Change in Net Accounts Receivable	(14,620)	-	-	(14,620)
Change in Prepaid Expenses	21,039	-	-	21,039
Change in Accounts Payable	11,470	-	-	11,470
Change in Payroll Liabilities	11,699	-	-	11,699
Change in Prepaid Water & Assessments	(5,207)	-	-	(5,207)
Change in Vacation Payable	(904)	-	-	(904)
Net Cash Provided by Operating Activity	<u>105,493</u>	<u>45,395</u>	<u>65,814</u>	<u>216,702</u>
CASH FLOWS FROM INVESTING ACTIVITY				
Purchase of Certificate of Deposit	(60,550)	-	-	(60,550)
Equipment Purchase	(196,363)	-	-	(196,363)
Net Cash Used by Investing Activity	<u>(256,913)</u>	<u>-</u>	<u>-</u>	<u>(256,913)</u>
CASH FLOWS FROM FINANCING ACTIVITY				
Borrowings from HNB Promissory Note	57,500	-	-	57,500
Payments of HNB Promissory Note	(3,698)	-	-	(3,698)
Transfers	191,718	(192,080)	362	-
Net Cash Provided (Used) by Financing Activity	<u>245,520</u>	<u>(192,080)</u>	<u>362</u>	<u>53,802</u>
Net Increase (Decrease) in Cash for the Year	94,100	(146,685)	66,176	13,591
CASH AT BEGINNING OF YEAR	<u>284,958</u>	<u>183,870</u>	<u>272,218</u>	<u>741,046</u>
CASH AT END OF YEAR	<u><u>\$ 379,058</u></u>	<u><u>\$ 37,185</u></u>	<u><u>\$ 338,394</u></u>	<u><u>\$ 754,637</u></u>
Supplemental Cash Flow Information				
Cash Paid for Interest	\$ 303	\$ -	\$ -	\$ 303

The accompanying notes are an integral part of these financial statements.

Hawaiian Shores Community Association
Statement of Cash Flows
For the Year Ended October 31, 2011

	Operating Fund	Reserve Fund	Infrastructure Fund	Total
CASH FLOWS FROM OPERATING ACTIVITY				
Change in Fund Balances	\$ 21,429	\$ 45,423	\$ 66,241	\$ 133,093
Adjustments to reconcile changes in net assets with net cash provided by operating activities:				
Add Depreciation and Disposals	47,294	-	-	47,294
Add Bad Debt	25,005	-	-	25,005
Change in Net Accounts Receivable	(44,775)	-	-	(44,775)
Change in Prepaid Expenses	(28,722)	-	-	(28,722)
Change in Security Deposit	5,000	-	-	5,000
Change in Accounts Payable	5,113	-	-	5,113
Change in Water Deposits	(5,381)	-	-	(5,381)
Change in Prepaid Water & Assessments	(6,334)	-	-	(6,334)
Change in Vacation Payable	(1,093)	-	-	(1,093)
Net Cash Provided by Operating Activity	<u>17,536</u>	<u>45,423</u>	<u>66,241</u>	<u>129,200</u>
CASH FLOWS FROM INVESTING ACTIVITY				
Equipment Purchase	<u>(78,513)</u>	<u>-</u>	<u>-</u>	<u>(78,513)</u>
CASH FLOWS FROM FINANCING ACTIVITY				
Transfers	<u>81,441</u>	<u>(14,874)</u>	<u>(66,567)</u>	<u>-</u>
Net Increase (Decrease) in Cash for the Year	20,464	30,549	(326)	50,687
CASH AT BEGINNING OF YEAR	<u>264,494</u>	<u>153,321</u>	<u>272,544</u>	<u>690,359</u>
CASH AT END OF YEAR	<u><u>\$ 284,958</u></u>	<u><u>\$ 183,870</u></u>	<u><u>\$ 272,218</u></u>	<u><u>\$ 741,046</u></u>
Supplemental Cash Flow Information				
Cash Paid for Interest	\$ -	\$ -	\$ -	\$ -

The accompanying notes are an integral part of these financial statements.

HAWAIIAN SHORES COMMUNITY ASSOCIATION

Notes to the Financial Statements October 31, 2012 and 2011

Note 1. ORGANIZATION

Hawaiian Shores Community Association (the Association) was incorporated as a nonprofit corporation in the State of Hawai'i on July 16, 1971. The Association is located in the Hawaiian Shores Subdivision, District of Puna, County of Hawai'i, comprising 1,294 lots. Each lot owner is subject to covenants, conditions and restrictions as set forth in the Declaration of Covenants, Conditions, and Restrictions-Hawaiian Shores Recreational Estates.

The purpose and activities of the Association are to promote the best interests of the property owners in the subdivision and to promote, strive to improve, maintain, and manage all common and community facilities within the subdivision.

Note 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Method of Accounting: The Association uses the accrual method of accounting for both financial statement reporting and tax return preparation. Under this method of accounting revenue is recognized when earned rather than when received and expenses are recognized when incurred rather than when paid.

Property and Equipment: Real property acquired is reflected on the Association's financial statements. The Association's policy is to capitalize fixed assets to which the useful life is greater than one year and to which the Association holds title in its name. Fixed assets are stated at cost less depreciation, calculated using the straight-line method over the assets' useful lives.

Member Assessments: Owners are subject to a yearly assessment of \$300 to provide funds for the Association's operating expenses, future capital acquisitions, and major repairs and replacements. Any assessments not paid within two months of its effective date will bear interest, retroactive from the effective date, at the rate of 1% per month, or at such other rate as the Board of Directors establish. The Association's by-laws allow the Association to also establish special assessments. Accounts Receivable – Fee Assessments on the balance sheet represent fees due from lot owners. Prepaid Assessments on the balance sheet represent advance payments by owners for future assessments.

Cash and Cash Equivalents: For the purpose of the Statement of Cash Flows, cash is defined as demand deposits, savings accounts, and certificates of deposit with maturities of one year or less.

Income Taxes: The Association is exempt from Federal tax under *Section 501(c)(4)* of the Internal Revenue Code and exempt from State income taxes under *Section 237-23 (b)* of the Hawai'i Revised Statutes. Therefore, no provision for Federal or State income taxes is required for the financial statements.

Use of Estimates: The preparation of financial statements in conformity with generally accepted accounting principles in the United States of America requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

HAWAIIAN SHORES COMMUNITY ASSOCIATION

Notes to the Financial Statements October 31, 2012 and 2011

Note 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Fund Balances: 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 to account for financial resources available for the general operations of the Association.

Reserve Fund-This fund is to account for financial resources related to any emergencies or extraordinary situations and major projects.

Infrastructure Fund-This fund is to be used exclusively to fund the water system and roads.

Note 3. ASSESSMENTS RECEIVABLE

The Association's policy is to place liens on the properties of owners whose annual assessments are in arrears. Assessments receivable of \$180,332 at October 31, 2012 and \$183,783 at October 31, 2011, in the Operating Fund were in arrears and subject to lien. Because of foreclosures against certain property owners which cast doubt on the collectibility of certain assessments, management has established an allowance for doubtful accounts of \$75,000 for this uncertainty. Hence, net accounts receivable at October 31, 2012, amounted to \$105,332 and \$108,783 at October 31, 2011. Total Assessments Receivable past due over 1 year totaled approximately \$103,000 at October 31, 2012 and \$100,000 at October 31, 2011.

Note 4. INVESTMENTS

Hawaiian Shores Community Association has conformed to FASB's *ASC 820-10-50-1* which establishes a fair value hierarchy for inputs used in measuring fair market value that maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that the most observable inputs be used when available. Observable inputs are those that market participants would use in pricing the asset or liability based on the best information available in the circumstances. This fair value hierarchy consists of three broad levels.

- Level 1 inputs consist of unadjusted quoted prices in active markets such as stock exchanges for identical assets and have the highest priority.
- Level 2 inputs consist of significant other observable inputs such as quoted prices for similar assets and liabilities in active markets and inputs that are observable for the asset and liability, either directly or indirectly, for substantially the full term of the financial instrument.
- Level 3 inputs consist of significant unobservable inputs and include situations where there is little, if any, market activity for the investment. The inputs require significant judgment or estimates, such as those associated with discounted cash flow methodologies and appraisals.

HAWAIIAN SHORES COMMUNITY ASSOCIATION

Notes to the Financial Statements
October 31, 2012 and 2011

Note 4. INVESTMENTS (Continued)

There are no liabilities or other assets measured at fair value on a recurring or non-recurring basis. Fair values of assets measured on a recurring basis are as follows:

Assets	Total 10/31/2012	Quoted Prices: Level 1	Significant Other Inputs: Level 2	Significant Non- Observable Inputs: Level 3
Certificates of Deposit	<u>\$ 60,550</u>	<u>\$ 60,550</u>	<u>\$ -</u>	<u>\$ -</u>

Note 5. WATER SYSTEM

The Association owns and operates a water system for the subdivision. According to the Association's by-laws, each lot owner must pay a water hookup fee before starting construction or landscaping. The monthly water service fee is payable on the first day of each month, in advance. On November 1, 2009 the fee was increased to \$50 per month, which is \$47 for the water service charge and \$3 for the Association's Infrastructure Fund for future repairs. The monthly fee charged allows for unlimited use of water.

The Association also requires a security deposit of \$150 from tenants (renters/lessees). This deposit is refundable to tenants when they move out of the subdivision. Total water deposits held by the Association amounted to \$4,811 at October 31, 2012 and \$5,827 at October 31, 2011.

Note 6. SIMPLIFIED EMPLOYEE PENSION PLAN (SEP)

The Association established a Simplified Employee Pension Plan for all eligible employees. As of November 15, 1999, employees are eligible to participate in the Plan upon attaining the age of 21 years and having performed services for the Association for at least three years. All amounts contributed to the employee's SEP Plan will be immediately 100% vested. Contributions by the Association were \$2,450 in fiscal year 2012 and \$3,900 in fiscal year 2011, for eligible employees.

Note 7. NET ASSETS

Hawaiian Shores Community Association has conformed to FASB ASC 958-210-45-9 "Not-for-Profit Entities, Classifications of Net Assets." Accordingly, the Association is required to report information regarding its financial position and activities in three classes of net assets: unrestricted net assets, temporarily restricted net assets, and permanently restricted net assets. There were no temporarily or permanently restricted net assets as of October 31, 2012 and October 31, 2011.

Note 8. CONCENTRATION OF CREDIT RISK

The Association has bank accounts at financial institutions with a combined balance in excess of the maximum insured by the Federal Deposit Insurance Corporation (FDIC) which vary at each institution. Management believes these banks are stable and the risk of loss is minimal.

HAWAIIAN SHORES COMMUNITY ASSOCIATION

Notes to the Financial Statements
October 31, 2012 and 2011

Note 9. POOL UPGRADE

During the fiscal year, Hawaiian Shores Community Association placed into service pool upgrades, including the completed solar system project totaling \$99,941.

Note 10. FUTURE LEASE PAYMENTS

Hawaiian Shores Community Association entered into an operating non-cancelable lease agreement with Xerox Corporation in September 2009, for a new Xerox copy machine. The term of the lease is 60-months. The future non-cancelable portion of this lease is as follows:

2013	\$2,360
2014	\$2,163

The Association also entered into a non-cancelable operating lease with Pitney Bowes Global Financial Services LLC during the fiscal year. The lease agreement is for 23 quarterly payments of \$183. The non-cancelable portion of this lease is as follows:

2013	\$ 732
2014	\$ 732

Note 11. RADIO-READ WATERING SYSTEM

The Association purchased a radio-read water metering system to monitor and assess the water usage of homeowners in the Association. The costs associated with the meters were \$3,017 in the fiscal year ending October 31, 2012 and \$97,368 in the fiscal year ending October 31, 2011 and which have been capitalized.

HAWAIIAN SHORES COMMUNITY ASSOCIATION

Notes to the Financial Statements
October 31, 2012 and 2011

Note 12. INCOME TAXES

The Association is exempt from Federal income taxes under *Section 501(c)(4)* of the Internal Revenue Code and applicable State law.

The accounting standard on accounting for uncertainty in income taxes addresses the determination of whether tax benefits claimed or expected to be claimed on a tax return should be recorded in the financial statements. Under that guidance, the Association may recognize the tax benefit from an uncertain tax position only if it is more likely than not that the tax position will be sustained on examination by taxing authorities based on the technical merits of the position. Examples of tax positions include the tax-exempt status of the Association and various positions related to the potential sources of unrelated business taxable income (UBIT). The tax benefits recognized in the financial statements from such a position are measured based on the largest benefit that has a greater than 50% likelihood of being realized upon ultimate settlement. There were no unrecognized tax benefits identified or recorded as liabilities for fiscal year 2012 and 2011.

The Association files its Forms 990 in the U.S. Federal jurisdiction and the office of the State's Attorney General for the State of Hawai'i. The Association is generally no longer subject to examination by the Internal Revenue Service for years before 2009.

NOTE 13. HNB PROMISSORY NOTE

In May 2012 the Association took out a loan with Hawaiian National Bank. The loan bears interest at a rate of 1.65 percent over the index (1.7 percent at October 31, 2012). Monthly payments of \$1,000 are required based on a five year amortization period, with the final payment due May 2017. The loan is secured by a savings account held at the financial institution. The principal maturities of the debt are as follows:

2013	\$	11,170
2014		11,362
2015		11,557
2016		11,755
2017		7,958
		<u>\$ 53,802</u>

HAWAIIAN SHORES COMMUNITY ASSOCIATION

Notes to the Financial Statements October 31, 2012 and 2011

Note 14. SUBSEQUENT EVENTS

In preparing these financial statements, management has evaluated events and transactions for potential recognition or disclosure through December 26, 2012, the date the financial statements were available for use.

Note 15. RELATED PARTY TRANSACTIONS

K.W. Construction was contracted to renovate and remodel the Community Center (Stables) for the Hawaiian Shores Community Association during the fiscal year ending October 31, 2012. K.W. Construction is owned and operated by the current Treasurer of the Hawaiian Shores Community Association. The amount paid to K.W. Construction was \$44,734 and \$846 in 2011. This includes reimbursements to the Treasurer for the Stables Refurbishing project.

Note 16. PRIOR PERIOD ADJUSTMENT

An adjustment was made to the prior year's financial statements to reflect certain costs associated with the water meter project (See Note 11). During 2011, \$30,832 associated with the water meter project had been expensed when the cost should have been capitalized. The prior period adjustment allows the full value of the project to be capitalized.