

Bailey, Modshire & Company, P.C.

CERTIFIED PUBLIC ACCOUNTANTS

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INDEPENDENT AUDITORS' REPORT

To the Board of Directors
Lake Somerset Property Owners Association
Somerset, MI 49281

We have audited the accompanying Statement of Assets, Liabilities, Reserve and Members' Equity - Cash Basis of the Lake Somerset Property Owners Association as of August 31, 2005 and the related Statement of Revenue and Expenses - Cash Basis and Changes in Members' Equity - Cash Basis 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 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.

As described in the Accounting Policy Note, these financial statements were prepared on the basis of cash receipts and disbursements except that the statements include a provision for depreciation of buildings and equipment. This basis is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the assets, liabilities and members' equity of the Lake Somerset Property Owners Association as of August 31, 2005, and its revenue, expenses and changes in members' equity for the year then ended, on the basis of accounting as described in the Accounting Policy Note.

Our audit was conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The budget information is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has not been subjected to the auditing procedures applied in the audit of the basic financial statements, and, accordingly, we express no opinion on it.

Jonesville, Michigan
November 22, 2005

LAKE SOMERSET PROPERTY OWNERS ASSOCIATION
STATEMENT OF ASSETS, LIABILITIES, RESERVE AND
MEMBERS' EQUITY - CASH BASIS
AUGUST 31, 2005

ASSETS

Current Assets:		
Cash in Checking Account	\$ 2,675	
Cash in Savings Account	37,522	
Cash in Edward Jones Money Market Account	2,027	
Cash in Credit Union Accounts	14,103	
Maintenance Assessments Receivable	<u>31,156</u>	
Total Current Assets		\$ 87,455
Fixed Assets:		
Buildings and Improvements	\$ 42,949	
Equipment and Signs	<u>130,691</u>	
	\$ 173,640	
Less: Accumulated Depreciation	<u>(133,390)</u>	
Net Book Value	\$ 40,250	
Land (Hillandale - Lot #231)	<u>5,820</u>	
Total Fixed Assets - Net Book Value		46,070
Other Assets:		
Edward Jones-Collateralized Mortgage Obligation (Market Value \$24,531 Matures 2034)		<u>25,063</u>
Total Assets		<u><u>\$ 158,588</u></u>

LIABILITIES, RESERVE AND MEMBERS' EQUITY

Liabilities	\$ 0
Reserve for Maintenance Assessments Receivable	31,156
Members' Equity	<u>127,432</u>
Total Liabilities, Reserve and Members' Equity	<u><u>\$ 158,588</u></u>

The accompanying notes are an integral part of this statement.

LAKE SOMERSET PROPERTY OWNERS ASSOCIATION
 BUDGET STATEMENT OF REVENUE AND EXPENSES - CASH BASIS
 FOR THE YEAR ENDED AUGUST 31, 2005

REVENUE	Budget (Unaudited)	Actual	Over (Under) Budget
Assessments	\$ 97,665	\$ 100,123	\$ 2,458
Boat Stickers	0	17,150	17,150
Interest - Assessments	500	975	475
Interest - Bank Accounts	1,000	412	(588)
Interest - Money Market Account & Bond	0	1,352	1,352
Other - Insurance and Gate Keys	1,000	2,428	1,428
Boat Numbers	<u>30</u>	<u>37</u>	<u>7</u>
Total Revenue	\$ 100,195	\$ 122,477	\$ 22,282
Cash on Hand - September 1, 2003	<u>57,845</u>	<u>57,845</u>	<u>0</u>
Total Revenue and Resources	<u>\$ 158,040</u>	<u>\$ 180,322</u>	<u>\$ 22,282</u>
EXPENSES			
<u>Treasurer</u>			
Audit Fees	\$ 2,400	\$ 2,400	\$ 0
Postage	1,400	1,192	(208)
Printing Invoices	4,000	2,374	(1,626)
Accounting	4,600	4,600	0
Telephone	15	0	(15)
Taxes - Property	2,425	2,951	526
Legal and Recording Fees	5,000	1,114	(3,886)
Insurance	6,000	7,945	1,945
Bank Charges	200	0	(200)
Annual Meeting	75	74	(1)
IRS - Taxes	1,000	0	(1,000)
Miscellaneous	<u>400</u>	<u>927</u>	<u>527</u>
Total Treasurer	<u>\$ 27,515</u>	<u>\$ 23,577</u>	<u>\$ (3,938)</u>
<u>Water Quality</u>			
Harvester/Truck Fuel	\$ 600	\$ 1,028	\$ 428
Harvester Maintenance	5,000	3,656	(1,344)
Truck Maintenance	1,500	62	(1,438)
Dredging & Erosion	14,000	0	(14,000)
Harvester Labor	4,000	2,515	(1,485)
Miscellaneous	2,200	1,150	(1,050)
Herbicide	28,000	39,678	11,678
Lake Study	<u>12,000</u>	<u>15,104</u>	<u>3,104</u>
Total Water Quality	<u>\$ 67,300</u>	<u>\$ 63,193</u>	<u>\$ (4,107)</u>

The accompanying notes are an integral part of this statement.

LAKE SOMERSET PROPERTY OWNERS ASSOCIATION
 BUDGET STATEMENT OF REVENUE AND EXPENSES - CASH BASIS
 (CONTINUED)
 FOR THE YEAR ENDED AUGUST 31, 2005

	Budget (Unaudited)	Actual	Over (Under) Budget
<u>Parks</u>			
Dock Repair	\$ 1,400	\$ 573	\$ (827)
Playground Equipment	600	1,100	500
Fence Repair	2,000	1,465	(535)
Port-a-Johns	1,500	1,320	(180)
Trash Pickup	1,000	312	(688)
Consumers Power	1,300	933	(367)
Mowing	5,500	4,350	(1,150)
Picnic Table Repair	850	867	17
Signs & Buoys	1,500	639	(861)
Water Pump and Repair to Parks	1,000	0	(1,000)
Keys & Miscellaneous	2,500	3,807	1,307
Trees & Maintenance of Beaches	<u>2,400</u>	<u>1,403</u>	<u>(997)</u>
Total Parks and Security	<u>\$ 21,550</u>	<u>\$ 16,769</u>	<u>\$ (4,781)</u>
 <u>Security</u>			
Guards	<u>\$ 5,100</u>	<u>\$ 4,765</u>	<u>\$ (335)</u>
 <u>Gazette</u>			
Postage & Printing	<u>\$ 2,500</u>	<u>\$ 1,496</u>	<u>\$ (1,004)</u>
 <u>Fish Planting</u>	<u>\$ 5,000</u>	<u>\$ 5,000</u>	<u>\$ 0</u>
 <u>Community Council</u>	<u>\$ 1,000</u>	<u>\$ 1,050</u>	<u>\$ 50</u>
 <u>Fireworks Display</u>	<u>\$ 400</u>	<u>\$ 400</u>	<u>\$ 0</u>
 <u>Capital Equipment Depreciation</u>	<u>\$ 5,000</u>	<u>\$ 9,726</u>	<u>\$ 4,726</u>
 Total Expenses	<u><u>\$ 135,365</u></u>	<u><u>\$ 125,976</u></u>	<u><u>\$ (9,389)</u></u>

The accompanying notes are an integral part of this statement.

LAKE SOMERSET PROPERTY OWNERS ASSOCIATION
ANALYSIS OF CHANGES IN MEMBERS' EQUITY - CASH BASIS
FOR THE YEAR ENDED AUGUST 31, 2005

Members' Equity - September 1, 2004			\$ 130,931
Deduct: Excess of Expenses over Revenue			
Expenses	\$ 125,976		
Revenue	<u>122,477</u>	<u>3,499</u>	
Members' Equity - August 31, 2005			<u><u>\$ 127,432</u></u>

The accompanying notes are an integral part of this statement.

LAKE SOMERSET PROPERTY OWNERS ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
AUGUST 31, 2005

Description of Reporting Entity

The Lake Somerset Property Owners Association is a Michigan non-stock corporation. Generally speaking, any person or entity who has an equitable interest in any lot and is subject to the restrictive covenants or assessments by the Association is a member. The operations are governed by a nine member Board of Directors with a president at its head. The appointed committees include: Building Control; Water Quality; Parks; Security and Roads; and Public Affairs, Rules and Bylaws.

Federal and State Taxes

The Association is classified as a "Homeowners Association" subject to corporate federal income taxes which accompany that type of entity status. The total income tax liability for the current year is \$-0- and the unused net operating loss from a prior and current year will be carried over to the 2005-2006 fiscal year.

Accounting Policy

The accounting policy of the Association includes the maintenance of records on the cash basis of accounting. Under this basis, revenue and the related assets are recognized when received rather than when earned, and expenses are recognized when paid rather than when the obligation is incurred. The finances are controlled by a budget which is approved by members attending the Annual Meeting, usually in October of each year. The depositories include a non-interest bearing checking account and an interest bearing savings account and a brokerage account with Edward Jones. The balance sheet has been capitalized for unpaid maintenance assessments at August 31, 2005 with an equal amount being shown as "Reserve for Maintenance Assessments Receivable."

Maintenance Assessments Receivable

The maintenance assessment is currently \$85 per lot, billed in March of each year. There are approximately 1,150 billable units (lots). No provision has been made for estimated uncollectible maintenance assessments.

Equipment and Accumulated Depreciation

The costs of depreciable tangible equipment, the storage building, fencing, park improvements, and the pavilion are shown on the balance sheet in the assets section. The equipment includes weed harvesting, park and office equipment. The weed harvesting equipment is being depreciated over 10 years. The park fencing, improvements, and equipment are being depreciated over a 10-year life at straight line rates, and the office and other equipment utilizes accelerated depreciation rates with a 5-year life. The storage building has a 31.5-year life at an accelerated depreciation rate, with a 15 year life straight line method used for the pavilion and a 39 year life for the storage building improvement.

LAKE SOMERSET PROPERTY OWNERS ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
AUGUST 31, 2005

Members' Equity

The Members' Equity of \$127,432 at year-end was a decrease of \$3,499 from the prior year-end balance of \$130,931.

Related Parties

The members of the Board serve as volunteers by virtue of the annual election at each October meeting. The Treasurer is the only paid officer with the fees appearing as "Accounting" in the Treasurer's section of the revenue and expense statement.

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November 22, 2005

To the Board of Directors
Lake Somerset Property Owners Association
Somerset, Michigan

As a result of our audit of the Lake Somerset Property Owners Association for the year ended August 31, 2005, we would like to make the following comments and recommendations:

1. During the 2003-04 year, brokerage accounts were opened at the Jackson office of Edward Jones & Co. The investment made there for \$25,000 in "Mortgage Pass-through Certificates, Series 2005" again bears mentioning. While the interest rate of 5.4% is significantly better than CD's, the principal is subject to stock market fluctuations and should be monitored during your holding period.
2. Our examination of forms #1099 indicated that Kieser and Associates was paid \$600 or more for professional services, and should have been issued that form for 2004.

If we can be of assistance regarding these recommendations, please contact our office.

Respectfully,

Bailey, Hodshire & Company, P.C.
Certified Public Accountants