

THE FRIENDS OF THE CUMBRES & TOLTEC SCENIC RAILROAD, INC.

Financial Statements

December 31, 2006

(With Independent Auditor's Report Thereon)

**REYNOLDS, HIX & CO., P.A.
Certified Public Accountants**

INDEPENDENT AUDITOR'S REPORT

To the Board of Directors of
The Friends of the Cumbres & Toltec Scenic Railroad, Inc.:

We have audited the accompanying statement of financial position of The Friends of the Cumbres & Toltec Scenic Railroad, Inc. (a nonprofit corporation) as of December 31, 2006, and the related statements of activities and cash flows for the year then ended. These financial statements are the responsibility of the Organization'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 Friends of the Cumbres & Toltec Scenic Railroad, Inc. as of December 31, 2006 and the changes in its net assets and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Our audit was conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. Schedules 1 and 2 are presented for purposes of additional analysis and are not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Albuquerque, New Mexico
May 31, 2007

THE FRIENDS OF THE CUMBRES & TOLTEC SCENIC RAILROAD, INC.

Statement of Financial Position

December 31, 2006

Assets	
Current assets:	
Cash	\$ 384,637
Certificate of deposit (note 2)	35,000
Accrued interest	3,765
Grant receivable	25,000
Other receivables	1,815
Merchandise inventory	47,209
Prepaid expense	4,012
Total current assets	<u>501,438</u>
Depreciable assets:	
Building and equipment	212,070
Less accumulated depreciation	<u>51,224</u>
Net depreciable assets	<u>160,846</u>
Other assets:	
Land - Chama	115,500
Land - Antonito	90,000
Historic equipment	77,915
Feasibility study for interpretation center	12,976
Library collection	160,991
Deposits	1,300
Total other assets	<u>458,682</u>
Total assets	<u>\$ 1,120,966</u>

Liabilities and Net Assets

Current liabilities:	
Accounts payable	\$ 49,760
Tenant deposit	550
Note payable-First Community Bank (note 5)	<u>100,000</u>
Total current liabilities	<u>150,310</u>
Net assets:	
Unrestricted	599,397
Temporarily restricted	297,779
Permanently restricted	<u>73,480</u>
Total net assets	<u>970,656</u>
Total liabilities and net assets	<u>\$ 1,120,966</u>

See accompanying notes to financial statements.

THE FRIENDS OF THE CUMBRES & TOLTEC SCENIC RAILROAD, INC.

Statement of Activities

Year ended December 31, 2006

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Support and revenue:				
Member dues	\$ 202,915	-	-	202,915
Contributions	144,306	211,620	8,778	364,704
Work session & charter fees, net of expenses	33,397	-	-	33,397
Merchandise sales, net of expenses	7,032	-	-	7,032
Rental income, net of expenses	(1,370)	-	-	(1,370)
Investment income	1,655	7,713	2,704	12,072
Net assets released - satisfaction of donor restrictions	175,167	(175,167)	-	-
Total support and revenue	<u>563,102</u>	<u>44,166</u>	<u>11,482</u>	<u>618,750</u>
Expenses:				
Program services	182,291	-	-	182,291
Supporting services	152,982	-	-	152,982
Total expenses	<u>335,273</u>	<u>-</u>	<u>-</u>	<u>335,273</u>
Change in net assets	227,829	44,166	11,482	283,477
Net assets at beginning of year	371,568	253,613	61,998	687,179
Net assets at end of year	<u>\$ 599,397</u>	<u>297,779</u>	<u>73,480</u>	<u>970,656</u>

See accompanying notes to financial statements.

THE FRIENDS OF THE CUMBRES & TOLTEC SCENIC RAILROAD, INC.

Statement of Cash Flows

Year ended December 31, 2006

Cash flows from operating activities:	
Change in net assets	\$ 283,477
Adjustments to reconcile change in net assets to net cash from operating activities:	
Non-cash contribution of library	(87,500)
Non-cash contribution of historic equipment	(2,100)
Non-cash contribution of equipment	(1,100)
Non-cash write-off of loan	17,735
Depreciation	6,982
Increase in accrued interest	(1,642)
Increase in grant receivable	(25,000)
Increase in other receivable	(1,119)
Increase in merchandise inventory	(13,338)
Increase in prepaid expenses	(660)
Increase in library collection	(31,649)
Decrease in accounts payable	(2,632)
Increase in tenant deposit	550
Net cash from operating activities	<u>142,004</u>
Cash flow from investing activities:	
Purchase of Chama land and building	(44,375)
Construction of car restoration facility	(18,184)
Purchase of equipment	<u>(10,726)</u>
Net cash used investing activities	<u>(73,285)</u>
Increase in cash	68,719
Cash at beginning of year	315,918
Cash at end of year	<u>\$ 384,637</u>
Supplemental disclosure - interest expense paid	<u>\$ 2,063</u>

See accompanying notes to financial statements.

THE FRIENDS OF THE CUMBRES & TOLTEC SCENIC RAILROAD, INC.

Notes to Financial Statements

December 31, 2006

(1) Nature of Activities and Summary of Significant Accounting Policies

(a) Nature of Activities and Tax Exempt Status

The Friends of the Cumbres & Toltec Scenic Railroad, Inc. (Friends) is a nonprofit corporation devoted to the preservation and interpretation of the Cumbres & Toltec Scenic Railroad, a 64-mile narrow gauge railroad line between Chama, New Mexico and Antonito, Colorado. Friends is exempt from income taxes under Section 501 (c)(3) of the Internal Revenue Code and is not a private foundation.

(b) Financial Statement Presentation

Friends' financial statement presentation is in compliance with Statement of Financial Accounting Standards (SFAS) No. 117, "Financial Statements of Not-for-Profit Organizations." SFAS No. 117 requires that the statement of financial position and the statement of activities report financial information for the following classes of net assets:

- (1) Unrestricted net assets, which are resources available with no restrictions for Friends operations;
- (2) Temporarily restricted net assets, which are resources that, because of donor-imposed restrictions, can be used by Friends in accordance with the specific directions of the donor; and
- (3) Permanently restricted net assets, which are resources that, because of donor-imposed restrictions, must be maintained permanently by Friends with Friends allowed to use part or all of the income derived from the resources.

(c) Contributions

Contributions received are recorded as unrestricted, temporarily restricted or permanently restricted support depending on the existence or nature of any donor restrictions. Donor-restricted contributions are reported as increases in temporarily or permanently restricted net assets depending on the nature of the restrictions. When a restriction expires, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of activities as net assets released from restrictions.

(d) Merchandise Inventory

Merchandise inventory is recorded at cost (first-in, first-out), which does not exceed market value.

THE FRIENDS OF THE CUMBRES & TOLTEC SCENIC RAILROAD, INC.

Notes to Financial Statements

December 31, 2006

(1) Nature of Activities and Summary of Significant Accounting Policies(continued)

(e) Depreciable Assets

Buildings, office equipment and restoration equipment are recorded at cost or fair market value at date of gift and are depreciated using either the straight-line and the declining-balance method over the estimated useful life of the respective assets. Friends' capitalization policy is to capitalize fixed asset acquisitions of \$500 or more.

During 2006, Friends paid \$18,184 in additional costs from temporarily restricted assets for construction of a car restoration facility (CRF) in Antonito, Colorado. The total cost to date for the CRF is \$117,873. The facility was placed in service in 2006.

(f) Other Assets

Other assets, such as land, historic equipment, and library collection are recorded at cost or fair market value at date of gift.

(g) Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results may differ from those estimates.

(h) Donated Services

No amounts have been reflected in the statements for donated services since such services are not of the nature that meet the requirements for recognition in the financial statements. However, a substantial number of members have donated a significant amount of their time in Friends' activities.

(i) Cash Equivalents

For the purpose of the statement of cash flows, Friends considers all short-term debt securities purchased with a maturity of three months or less to be cash equivalents.

(2) Certificate of Deposit

Friends has purchased a certificate of deposit with an issue value of \$35,000 and a maturity date of August 19, 2007.

Interest is paid quarterly with a variable rate based on the prime rate. At December 31, 2006, the rate was 4.75%.

THE FRIENDS OF THE CUMBRES & TOLTEC SCENIC RAILROAD, INC.

Notes to Financial Statements

December 31, 2006

(3) Due from Rio Grande Railway Preservation Corporation

In previous years, Friends made various loans to Rio Grande Railway Preservation Corporation (RGRPC), a New Mexico nonprofit corporation. Friends was a Supported Organization of RGRPC as defined by the Internal Revenue Code. In 2005, the legal and organizational relationship between Friends and RGRPC was terminated and Friends is no longer a Supported Organization of RGRPC.

In 2006, RGRPC ceased operations. For satisfaction of the \$32,435 outstanding loan balance, Friends took possession and title of two flat cars valued at \$14,700 and forgave the remaining \$17,735 of debt.

(4) Fundraising Campaigns Initiated During 2002 and 2006

Since 2002, Friends has conducted a major fundraising campaign referred to as “Another Century of Narrow Gauge Steam”. During 2006, Friends began work on another major fundraising campaign “Another Century of Narrow Gauge Steam-Phase II”. The funds from these campaigns were specifically committed in fundraising brochures to be restricted for:

- 1) Capital for short-term and long-term operating needs of the railroad.
- 2) Historic preservation, C&TS locomotive fleet, interpretation, and public education of the railroad.
- 3) Establishment of a permanent endowment fund in the amount of 10% of all funds raised from this campaign.

Funds raised from these campaigns are considered to be restricted contributions as described in note 1(c).

These fundraising campaigns have resulted in written intentions from supporters of Friends to contribute to Friends in future years. Due to continuing concerns about the future operations of the railroad and future funding by the state legislatures of Colorado and New Mexico, management of Friends considers these written intentions to be conditional promises to give and therefore, has not reported these intentions to contribute as assets of Friends as of December 31, 2006.

(5) Note Payable-First Community Bank

The note payable – First Community Bank is due September 5, 2007, with monthly payments of interest only at 8.25% and is secured by Chama land and building.

THE FRIENDS OF THE CUMBRES & TOLTEC SCENIC RAILROAD, INC.

Notes to Financial Statements

December 31, 2006

(6) Restrictions on Assets

Temporarily restricted net assets are available for the following purposes:

Another Century of Narrow Gauge Steam (ACNGS) for historic preservation, interpretation, public education and operating needs of the railroad	\$ 135,533
Another Century of Narrow Gauge Steam-Phase II (ACNGS II) for historic preservation, C&TS locomotive fleet, interpretation, public education and operating needs of the railroad	26,499
Car Restoration Facility Fund (CRF) for restoring historic pieces of rolling stock in both Antonito, CO & Chama, NM	63,990
Gates Family Foundation for the restoration of Car RPO X54 and Cook Car 053	30,000
Dorman Collection Fund which is to be used for the cataloging and maintenance of the Richard L. Dorman Narrow Gauge Photograph Collection	24,654
Other	17,103
	<u>\$ 297,779</u>
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THE FRIENDS OF THE CUMBRES & TOLTEC SCENIC RAILROAD, INC.

Schedule of Functional Expenses

Year ended December 31, 2006

	Program Services							Supporting Services
	Restoration	Newsletter	Public Relations	Interpretation	Library	Railroad Operations	Total	
Accounting fees	\$ 588	118	118	118	-	-	942	4,348
Advertising and public relations	21	4	3,341	4	-	2,932	6,302	2,875
Bad debt expense	-	-	-	-	-	17,735	17,735	-
Bank/card fees	96	2	2	2	27	-	129	3,337
Bookkeeping	1,535	307	307	307	-	-	2,456	11,362
Conferences/meetings	-	-	327	-	-	-	327	11,404
Contract services	1,477	5,563	274	274	-	-	7,588	10,241
Depreciation	4,707	43	43	43	-	-	4,836	1,598
Dues/subscriptions	(69)	7	297	7	80	-	322	855
Freight/trucking	2,994	-	-	-	-	-	2,994	-
Grants extended	-	-	-	-	-	24,000	24,000	-
Insurance	1,247	90	90	90	1,398	-	2,915	3,317
Mailings/delivery	451	18	102	60	1,082	83	1,796	7,127
Materials/tools/supplies	59,891	-	-	150	320	1,414	61,775	592
Merchandise expense	250	-	-	-	-	-	250	181
Office supplies/copying	1,690	556	283	525	4,410	283	7,747	9,596
Photography/video	-	-	-	-	-	-	-	1,118
Printing/publishing	-	10,480	-	-	-	-	10,480	5,437
Rent	4,658	332	332	332	1,412	-	7,066	12,269
Salaries and benefits	7,809	1,562	1,562	1,562	-	-	12,495	57,782
Taxes	474	-	-	-	-	-	474	-
Telephone	1,463	144	144	144	209	1,817	3,921	5,329
Travel/meals/lodging	476	98	270	82	-	4,393	5,319	4,214
Utilities	422	-	-	-	-	-	422	-
Total	\$ 90,180	19,324	7,492	3,700	8,938	52,657	182,291	152,982

THE FRIENDS OF THE CUMBRES & TOLTEC SCENIC RAILROAD, INC.

Schedule of Supporting Services Expenses

Year ended December 31, 2006

	Management and General	Volunteer Administrative	Fundraising	Membership	Total
Accounting fees	\$ 233	882	294	2,939	4,348
Advertising and public relations	8	31	10	2,826	2,875
Bank/card fees	1	13	4	3,319	3,337
Bookkeeping	614	2,303	768	7,677	11,362
Conferences/meetings	-	-	-	11,404	11,404
Contract services	549	2,055	685	6,952	10,241
Depreciation	86	324	108	1,080	1,598
Dues/subscriptions	14	54	18	769	855
Insurance	179	672	224	2,242	3,317
Mailings/delivery	35	134	98	6,860	7,127
Materials/tools/supplies	-	-	-	592	592
Merchandise expense	-	-	-	181	181
Office supplies/copying	174	657	219	8,546	9,596
Photography/video	-	-	1,118	-	1,118
Printing/publishing	-	-	-	5,437	5,437
Rent	662	2,487	829	8,291	12,269
Salaries and benefits	3,122	11,713	3,904	39,043	57,782
Telephone	288	1,080	360	3,601	5,329
Travel/meals/lodging	161	611	204	3,238	4,214
Total	\$ 6,126	23,016	8,843	114,997	152,982