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Annual
Reports
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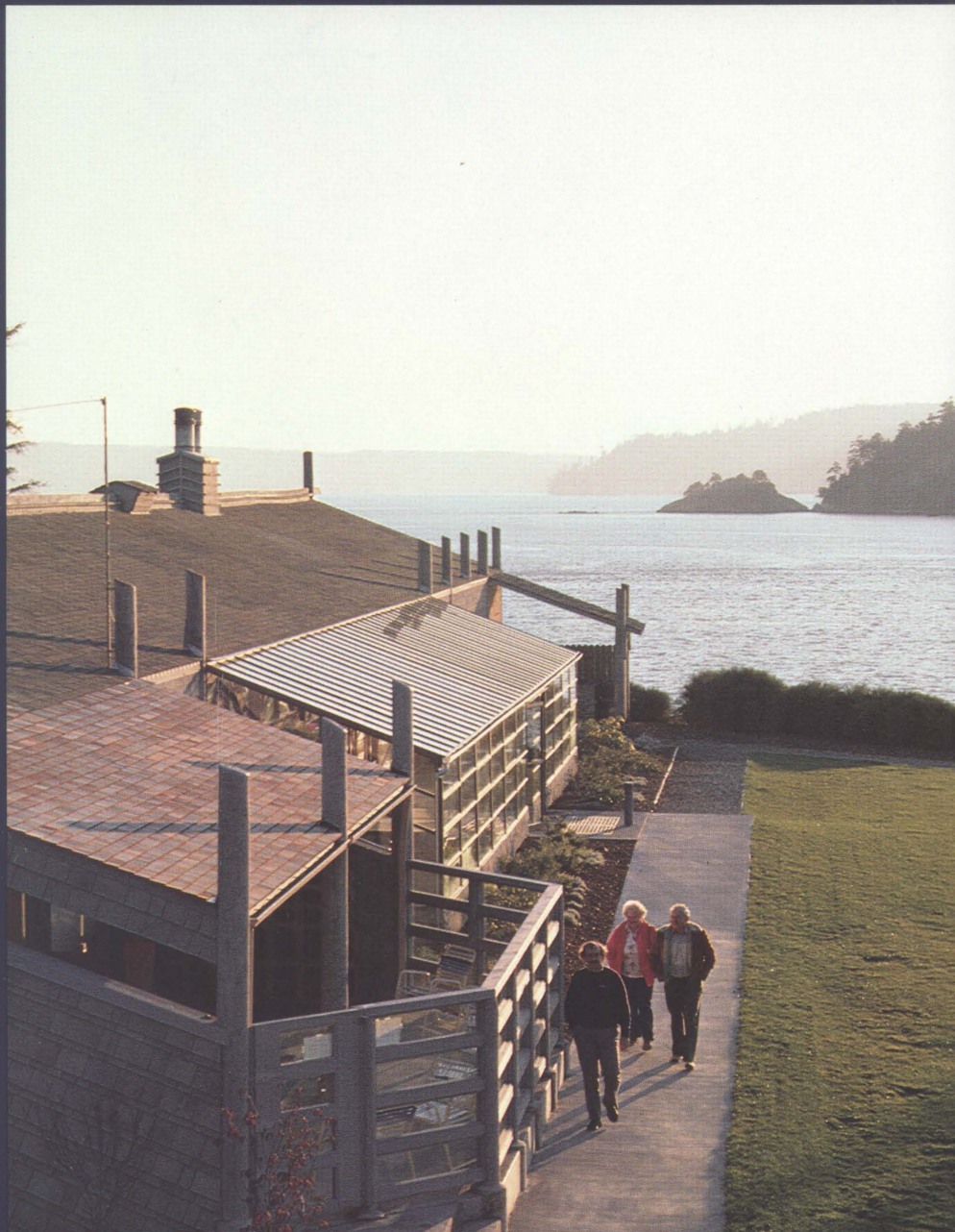
Thousand Trails, Inc.
America's Private
National Park System
1985 Annual Report



■ Thousand Trails is the national leader in the membership campground resort industry. The Company, based in Bellevue, Washington, owns, operates and sells memberships in a network of 43 resorts located in 16 states and in British Columbia, Canada. More than 85,000 families are members of Thousand Trails.

■ Each resort is operated exclusively for members and is a destination for families who love the outdoors and appreciate quality facilities managed by a professional staff. Most members bring their own recreational vehicles, like this family visiting our Verde Valley, Arizona resort. Company-owned, on-site travel trailers are also available for a small nightly fee.

■ The cover photograph of our Hershey, Pennsylvania resort demonstrates the Company's commitment to retaining the unique environment of each location.



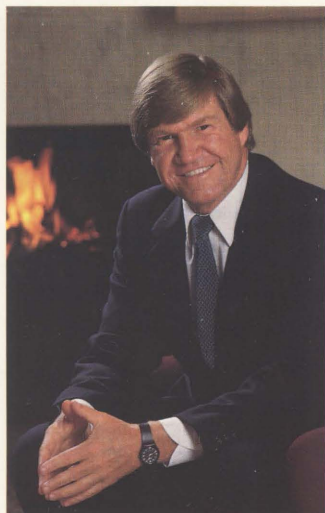
■ Each Thousand Trails resort is distinguished by the beauty of the natural landscape surrounding a carefully developed setting of campsites and facilities such as lodges, swimming pools, sport courts, playgrounds and convenience stores.

■ The lodge at the La Conner, Washington resort was designed to reflect the local Indian architecture.



■ A Thousand Trails member pays an initial membership fee and annual dues. This entitles the member's family to three generations of use of any existing or future locations for an unlimited number of visits of up to two weeks per visit.

■ The Hershey resort is a popular retreat for East Coast members.



Management's Letter to Shareholders

1985 was a difficult year for Thousand Trails. Most of our difficulties related to rapid growth, which produced record revenues and sales, but also resulted in higher marketing and operational costs, reduced profits and our first quarterly loss since 1981. Results for 1985 were also adversely affected by an increase in the rate at which the Company provides for doubtful accounts and an increase in the allowance for doubtful accounts.

We also had many successes in 1985. More than 19,000 new members became part of the Thousand Trails family. We completed our objective of establishing a national network of resorts and have sufficient planned campsite inventory to sell memberships for several years without having to acquire new properties. We are today the leading company in the membership campground industry.

1985 also provided valuable lessons. We learned that it takes time to develop new markets. We learned that rapid growth, although a natural and inevitable part of the maturing process of any organization, needs to be balanced with periods of moderate growth. The problems that occurred in 1985 are being addressed. We know what we need to do and have the drive, patience and focus to succeed. However, solutions take time and 1986 will not be easy. 1986 will be a year of consolidation as the Company shifts from a rapid growth strategy to one of more moderate growth. Our three major objectives in 1986 are:

- To continue providing high quality products and services for our members
- To accelerate the timing of positive cash flow
- To improve profit margins and operating efficiency through more effective management and cost controls

Your Board and the management of Thousand Trails are committed to accomplishing these objectives. We are confident that by establishing Thousand Trails as a major national force in the campground industry, we are building for our shareholders a unique company whose inherent value will be recognized.

To help you understand 1985 and how our Company is positioning itself for the future, we urge you to carefully read the question and answer discussion following this shareholders' letter.

On behalf of the employees of Thousand Trails, we appreciate your continued support.

Sincerely,

C. James Jensen
Chairman of the Board
and Chief Executive Officer

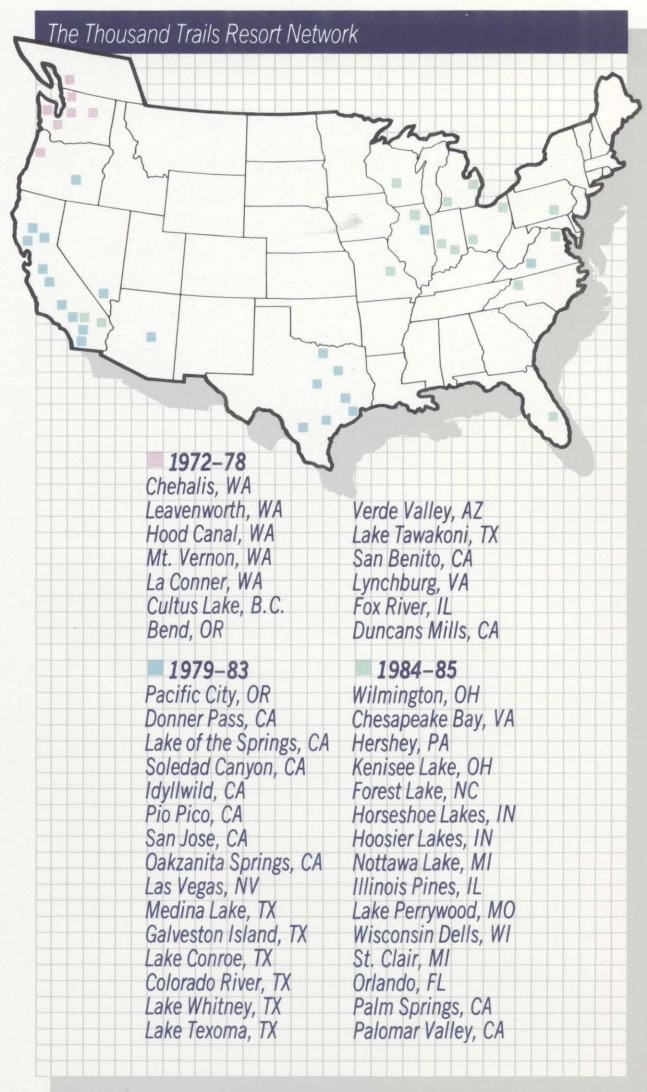
■ What factors led to the Company's decision to expand so rapidly?

■ It has always been our long-term goal to establish a national network of resorts. We have accomplished this goal and today have a national network of 46 properties (43 of which are operational) located in 17 states and British Columbia, Canada. Selling a network rather than individual properties was fundamental to our initial success on the West Coast. The decision to expand rapidly from this market base was necessitated, in our opinion, by the need to develop a comprehensive network of resorts in new geographical areas in order to effectively sell our product.

■ As a result of this expansion, Thousand Trails has achieved national visibility in the consumer market, enhanced product appeal, a larger membership base for future business diversification and enhanced joint venture opportunities with vendors and other third parties. Our recent agreement with Fleetwood Enterprises, Inc., the world's largest manufacturer of recreational vehicles (RVs), is the direct result of our becoming a national company. The specifics of this agreement will be discussed later.

■ While the cost of this expansion has been considerable, most of the dollars invested have been in the acquisition and development of new resorts. As new memberships are sold, these resorts will have an increasing number of dues-paying members, producing income for as long as three generations. Over the next several years, our construction expenditures will be significantly less than in recent years. By simply adding campsites and related amenities at existing resorts, we will have the capacity to serve approximately 270,000 member families, without having to acquire a single new property.

■ 1986 will be a year of consolidation with no new property acquisitions. Our strategy for future years is to expand our business at a more moderate rate than in the past.



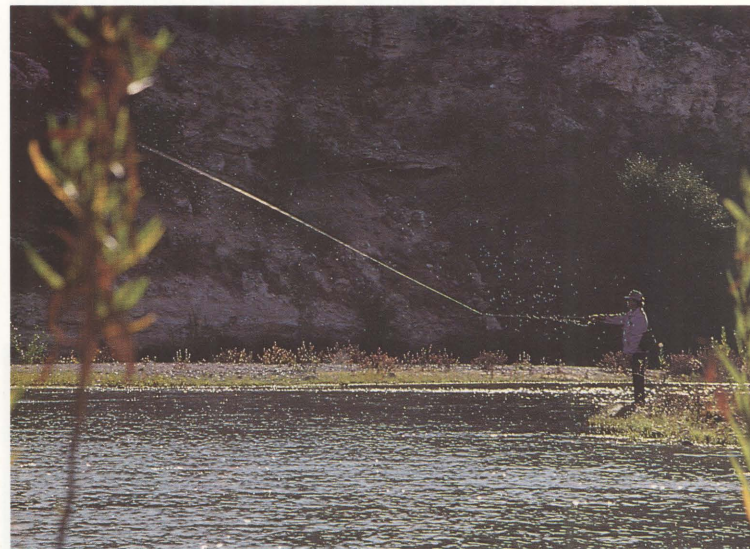
■ What are the benefits of moderate growth?

■ A major benefit is the reduction of the high costs associated with new resort openings. In 1984 and 1985, we invested more than \$100 million in the development of our properties. By greatly reducing new acquisitions and funneling construction dollars into the enhancement of our existing resorts, we will be able to substantially decrease our need for additional borrowings in 1986 and the next several years. Reduced borrowings will allow us to focus on achieving positive cash flow (i.e. when cash received from operations exceeds all cash expended).

■ Another major benefit of moderate growth is that it allows the Company to concentrate on developing its existing network of resorts rather than new properties. This should result in more cost effective sales and resort operations. As our emphasis shifts to becoming better, not just bigger, we should experience greater efficiencies on all fronts.

■ In general, what caused the decrease in profits in 1985?

■ In 1985, we substantially underestimated the time it takes to develop new geographic and demographic markets. The result was lower sales revenues and higher marketing costs than expected. We also experienced a significant increase in contracts receivable losses and, therefore, decided to increase the rate at which we provided for future contract losses, as well as the allowance for doubtful accounts itself. These issues are discussed in more detail in the following questions.



■ Why were marketing costs higher in 1985 and what are you doing to reduce these costs?

■ Although in 1985 a record number of families visited our resorts and received sales presentations, the percentage who purchased a membership declined from what we experienced historically. This resulted in lower sales revenues and higher marketing costs than planned.

■ The increase in marketing costs was primarily due to the impact of our rapid expansion. Sales personnel at our new resorts were not able to effectively service the large flow of potential customers. We also experienced a decrease in the effectiveness of our direct mail marketing, particularly to the non-RV owner. Finally, in our new geographic markets, our membership base was not large enough to generate significant referral business, the Company's most cost-efficient source of sales.

■ We have taken a number of steps to reduce marketing costs. We are placing stronger emphasis on member referral business, including the restructuring of sales compensation to provide greater incentive for sales resulting from this source. The emphasis on referral business should reduce the need for direct mail solicitations, the Company's most costly source of new business. We are also reconfiguring our direct mail data base to enable us to more effectively target our market.

■ In addition, we have developed several programs designed to specifically target the recreational vehicle market. One such program is the Company's Camp USA promotion which is a joint venture between Thousand Trails and Fleetwood Enterprises. This program will offer a free 90-day trial membership to all new purchasers of Fleetwood RVs.



What are your future plans to market memberships to the non-RV owner?

We continue to believe very strongly in the market potential for the non-RV owner. Approximately 23,000 of our members do not own recreational vehicles and, according to our most recent membership survey, have expressed a high level of satisfaction with Thousand Trails.

The need for our product is not limited to those families who own a recreational vehicle, but reflects, in part, the considerable popularity of camping. A recent survey by the U.S. Department of the Interior indicates that 24 percent of a representative sample of Americans camped sometime during the 12 months prior to the survey.

We are continuing to learn more about the profile of those individuals who do not own an RV but have a strong interest in quality outdoor recreational experiences. As we become more sophisticated in understanding this market segment, we should be better able to focus our marketing efforts toward those people who demonstrate a true long-term commitment to our product.

What is your response to the recent legislation regulating the membership campground industry that has been enacted in a number of states during the past several years?

Thousand Trails has taken a leadership role within the industry to support responsible legislation. We have worked directly with legislators and regulators in various states to ensure passage of responsible, fair legislation that protects the consumer without being overly burdensome to the industry. Equitable legislation is necessary not only to protect the consumer but also to protect legitimate operators within the industry from the harm caused by disreputable companies. We believe that the implementation of such legislation is an important step in the maturation of our evolving industry and we will continue to support these efforts.



■ What was the reason for the adjustments to the allowance for losses on membership contracts receivable in 1985?

■ Prior to 1985, our excellent rate of collection on membership contracts receivable had improved each year. Results for 1984 were especially impressive, with accounts delinquent 32 days or more averaging only 1.7 percent. Actual contract losses (i.e. bad debt) in 1984 were less than in 1983, even though the accounts receivable portfolio was substantially larger. Our allowance for doubtful accounts at year end 1984, and the rate at which we provided for future contract losses during the first half of 1985, were based on these results.

■ In May 1985, we became aware that actual bad debt losses in April were higher than projected. In analyzing this change, we initially believed the problem was operational, due to significant employee turnover in the first quarter of 1985 and a new accounts receivable computer system brought on line in early April. As a result, we made changes in our accounts receivable division which were designed to correct these operational problems.

■ We also began developing new analytical tools to better segment our contracts receivable portfolio, not only by type of member (i.e. owners of recreational vehicles vs. non-owners), but geographically as well. At the end of the third quarter, we became convinced that the higher bad debt, while still caused partly by operations, was more a function of an actual increase in contract losses over what had occurred historically. This necessitated our September 30 adjustments. By the end of 1985, with three additional months of information, we were better able to refine our analysis and further increased the reserve.

Thousand Trails Membership Contracts Receivable Table

(Dollars in Thousands)	1981	1982	1983	1984	1985
Average membership contracts receivable	\$30,488	\$46,292	\$71,619	\$115,138	\$166,107
Average 32-day delinquency as a percentage of membership contracts receivable	1.87%	1.79%	1.72%	1.66%	2.51%
Accounts written off as a percentage of average membership contracts receivable	3.7%	2.9%	2.7%	1.6%	4.0%
Membership contracts receivable written off (net)	\$ 1,118	\$ 1,343	\$ 1,899	\$ 1,827	\$ 6,667
Allowance for doubtful accounts	\$ 1,773	\$ 2,671	\$ 4,749	\$ 8,802	\$ 19,779
Allowance for doubtful accounts as a percentage of membership contracts receivable	4.86%	4.76%	5.45%	6.15%	10.46%

What caused the higher contracts receivable losses and what steps have you taken to correct the situation?

It is important to understand that the composition of our contracts receivable portfolio has changed considerably over the past two years as a result of the Company's geographical expansion and sale of memberships to persons who do not own an RV.

Upon analysis, we believe the higher 1985 contract losses were primarily a result of three factors:

- Higher default rate on memberships sold to non-RV owners who have a tendency to use the Company's resorts less than RV owners
- Higher default rate on Texas memberships (21 percent of the total portfolio) which may be related to economic problems in that state
- The negative publicity surrounding the membership campground industry in 1985

In response to the higher contract losses, we substantially increased the allowance for doubtful accounts from 6.1 percent of the portfolio at year end 1984 to 10.5 percent at year end 1985. At December 31, 1985, we had a total of \$19.8 million reserved against a total portfolio of \$189 million. We also increased the rate at which we provide for future contract losses from our historic rate of approximately 5 percent of sales to more than 10 percent. In addition, we segmented our contracts receivable collection efforts geographically, which should allow for greater collection efficiency.

We have also implemented other significant corrective measures including:

- Redirecting our marketing efforts to provide better sales balance between RV owners and non-RV owners
- Establishing new programs designed to obtain higher cash down payments (thus more equity in the membership)
- Developing plans to increase member usage, particularly among non-RV owners, through member orientation, special events and a broad range of social and recreational programs



How would you describe your basic business or product?

Thousand Trails is a nationwide network of membership-based destination campground resorts providing the pleasures of camping, the convenience of modern facilities and the benefits of social interaction in a "country club" environment. All resorts feature 24-hour security, high quality maintenance, a full-time professional staff and a variety of recreational amenities such as lodges, swimming pools, sport courts, hiking trails and playgrounds. Our properties are located in prime outdoor recreational settings, away from big cities and highways, but within a few hours' drive of large metropolitan areas. When developing our resorts, we retain as much of the natural surroundings as possible. Thousand Trails resorts provide members with the opportunity to spend weekends and vacations in quiet, beautiful settings where a variety of recreational and social activities are available for members of all ages.

How do you define your market?

Thousand Trails' market is primarily households headed by individuals who are 45 to 64 years of age. Today, of all Americans of prime working age—that is, over 18 but under 65—one out of every three is in the 45 to 64 age bracket. This age group has a higher per capita income than any other and accounts for more than half of all discretionary income.

We have further refined our market so that we focus on those individuals whose social, economic and demographic profiles correspond with a strong desire for leisure-time outdoor recreation opportunities. From this group comes our target market, owners and users of recreational vehicles and non-RV owners whose demographics and lifestyle interests reflect the characteristics of our current members.

Thousand Trails Membership Survey Table

	Camping*	Vacation**
Percentage who own a recreational vehicle	79.3%	15.0%
Median family income	\$32,800	\$35,000
Percentage who are homeowners	91.0%	86.5%
Years at present residence	14.6	12.3
Of members not retired, years with present employer	14.2	8.6
Average age of primary wage earner	55.3	51.0
Percentage who are retired	45.0%	30.0%

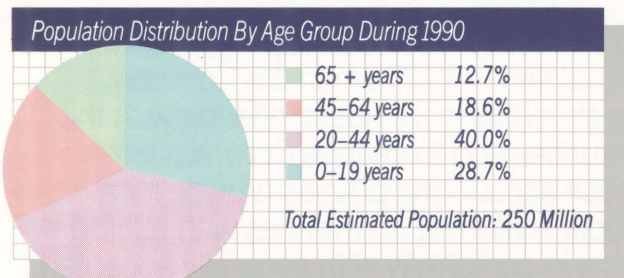
*A camping membership entitles the member's family to use individual campsites without charge and is designed for recreational vehicle owners.

**A vacation membership is designed for members who do not have a recreational vehicle and entitles the member's family to rent Company-owned travel trailers located on the resorts.

What is the future potential for this market?

We believe the market potential for our product is substantial and growing. There are an estimated 7.3 million owners of recreational vehicles in the United States today. A recent study estimates that the membership campground industry has sold approximately 260,000 memberships, or only 3.7 percent of all RV owners. With employment and disposable income up, and gas prices and interest rates down, RV manufacturers are very optimistic about the future and are currently estimating a 10 to 15 percent increase in 1986 sales.

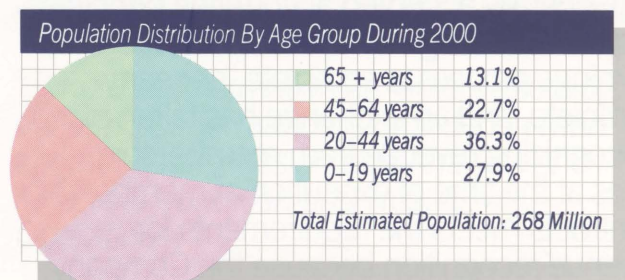
Furthermore, the 45- to 64-year-old age group is projected to increase by 35 percent between 1986 and 2000. This market is characterized by a larger per capita income, greater discretionary spending power and a desire for quality leisure-time activities. According to the September 2, 1985 issue of *Time* magazine, "The 26% of the population over 50 controls three-quarters of the nation's financial assets and, with \$130 billion in discretionary income, half of its spending power."



Source: American Demographics Magazine, July 1984

On the supply side, federal and state budget cutbacks will further reduce the number of public campgrounds. As a result of the Gramm-Rudman Act, the National Park Service has recently proposed cutting \$27 million from its 1986 budget. According to a February 1986 issue of *U.S.A. Today*, "There is little hope of relief in 1987. To combat further cuts, the Park Service has proposed increases of up to 500 percent in park fees." The article also states that the proposed budget calls for the closure of a 236-site campground in Yellowstone National Park, a 300-site campground in Arcadia National Park and three small campgrounds in Yosemite National Park.

These economic and demographic trends indicate a high market potential for our business.



Source: American Demographics Magazine, July 1984

Describe Thousand Trails' accounting policies and why they are appropriate.

Questions regarding Thousand Trails' accounting policies relate primarily to two areas: recognition of revenues from membership sales and the expensing of land and improvement costs.

With respect to revenue recognition, the Company records membership sales, net of an allowance for sales cancellations, upon execution of membership contracts. All costs attributable to membership sales are deducted from the revenue recognized. The execution of a membership contract entitles the member to immediate use of the Company's resorts according to the terms of the contract.

Generally accepted accounting principles require the recognition of revenue when the earnings process is complete, or nearly complete, and an exchange has taken place. Recognizing revenue from membership sales at the time of execution of membership contracts meets the requirements for revenue recognition because the Company has, in essence, transferred a perpetual right to use its real property and received payment of the purchase price, either in cash or a combination of cash and an installment contract with a determinable value. At this point, the earnings process is essentially complete, an exchange has taken place and revenue in the amount of the full sales price is recognized in accordance with generally accepted accounting principles.

Generally accepted accounting principles require that costs of sales and expenses be recognized in the same accounting period as the related sales and revenues. The Company expenses land and improvement costs based on the ratio of memberships sold to total memberships planned by the Company to be available for sale in a defined geographic area. The number of memberships planned for sale is derived from the Company's estimate that its resorts can support and sell ten memberships per campsite without overcrowding. As a result, since inception, land and improvement costs, including estimated costs to fully develop resorts, have been recorded as a cost of membership sales based on this ten-to-one ratio.

Membership sales and resort utilization statistics are reviewed on a regular basis. If the Company changes its estimate of the number of memberships that it can sell because of market or usage constraints, the Company will reassess planned future development at its resorts and, if necessary, change the rate at which it expenses land and improvement costs against subsequent sales.

Thousand Trails' accounting policies were formulated in 1979 when the Company registered its initial public offering with the Securities and Exchange Commission. These accounting policies provide for a proper matching of revenues with related costs in conformity with generally accepted accounting principles and are, therefore, appropriate for our industry.



■ What can the shareholders expect from Thousand Trails in 1986?

■ For Thousand Trails, 1986 will be a year of consolidation and transition. Our emphasis will be on improving cash flow and reducing marketing costs. To help us achieve these objectives, we have planned for a decrease in membership sales from 1985. We do not presently anticipate any further adjustments to our allowance for doubtful accounts, but this allowance and the rate at which the Company currently provides for future contract losses could be adjusted if our experience changes in the future.

■ In the long term, our transition to moderate growth, resulting in a reduced need for additional borrowing, will strengthen the Company financially and position us for a successful future.

■ Further information on factors affecting our 1986 performance is provided in *Management's Discussion and Analysis of Financial Condition and Results of Operations*.



Management's Responsibility for Financial Statements

The financial statements of Thousand Trails, Inc. and subsidiaries, and all other information presented in this annual report, are the responsibility of the management of the Company. The financial statements have been prepared in accordance with generally accepted accounting principles, consistently applied.

Management is responsible for the integrity and objectivity of the financial statements, including estimates and judgments reflected therein, and fulfills this responsibility primarily by establishing and maintaining accounting systems and practices adequately supported by internal accounting controls. Such controls include the selection and training of management and supervisory personnel; an organization structure providing for delegation of authority and establishment of responsibilities, communication of requirements for compliance with approved accounting, control and business practices throughout the organization; and business planning and review. Management believes that the internal accounting controls in use are satisfactory to provide reasonable assurance that the Company's assets are safeguarded, that transactions are executed in accordance with management's authorizations and that the financial records are reliable for the purpose of preparing financial statements.

Independent public accountants are appointed annually by the Company's shareholders to examine the financial statements in accordance with generally accepted auditing standards. Their report appears elsewhere in this annual report. Their examinations include a review of internal accounting controls and a selective review of transactions.

The Audit Committee of the Board of Directors, which consists of three directors who are not officers or employees of the Company, meets regularly with management and the independent public accountants to review matters relating to financial reporting, internal accounting controls and auditing.

Selected Income Statement Data
(In thousands except per share amounts)

<i>Year Ended December 31,</i>	<i>1981</i>	<i>1982</i>	<i>1983</i>	<i>1984</i>	<i>1985</i>
Membership Sales	\$40,006	\$56,454	\$79,971	\$116,983	\$127,603
Gross Profit on Membership Sales	14,422	23,173	31,715	44,960	32,493
Gross Profit on Resort Operations	880	1,298	1,995	2,419	3,715
Net Earnings	3,327	7,761	12,004	19,110	1,788
Primary Earnings Per Share	.47	.97	1.23	1.78	.17
Fully Diluted Earnings Per Share	.45	.89	1.21	1.76	.16

Selected Balance Sheet Data
(In thousands)

<i>December 31,</i>	<i>1981</i>	<i>1982</i>	<i>1983</i>	<i>1984</i>	<i>1985</i>
Current Assets	\$10,967	\$15,981	\$23,666	\$35,479	\$43,908
Current Liabilities	9,395	15,001	22,118	36,090	39,693
Membership Contracts Receivable (Net)	34,696	53,443	82,373	134,351	169,282
Operating Resorts	39,003	56,167	82,282	148,398	200,017
Total Assets	70,822	102,299	151,767	269,770	353,082
Debt:					
Long-Term	22,344	23,183	28,206	33,937	39,006
Senior Subordinated Notes					73,893
Bank Line of Credit	15,855	24,279	25,033	88,317	87,393
Total Deferred Income Taxes	11,437	18,505	29,033	45,053	46,315
Shareholders' Equity	17,865	30,194	60,299	80,917	78,697

Management's Discussion and Analysis of Financial Condition and Results of Operations

The Company acquires, develops, and operates destination campground resorts and sells memberships conveying the right to use these resorts. Memberships are sold either on a cash or an installment basis. All marketing costs and an allowance for estimated losses on installment contracts are recorded currently. Operating resort land and improvement costs, including the Company's estimated costs to develop fully the resorts, are aggregated by geographical area and recorded as a cost of membership sales based upon the ratio of actual memberships sold within each area

to the total memberships planned for sale within the area. Members are assessed annual dues which are intended to cover resort operating costs when approximately 40% of the memberships planned for sale in a geographic area have been sold. The Company derives revenues from membership sales, resort operations (principally membership dues), and interest earned on the receivable portfolio arising from the sale of memberships on an installment basis. Set forth below is a table of the Company's sources of revenue as a percentage of total revenues.

<i>Year Ended December 31,</i>	<i>1981</i>	<i>1982</i>	<i>1983</i>	<i>1984</i>	<i>1985</i>
Sources of revenue:					
Membership sales	82.0%	80.5%	79.8%	78.2%	72.9%
Resort operations	9.8	10.0	10.1	10.6	13.6
Interest income	8.5	9.4	10.1	10.7	13.4
Other	(.3)	.1	—	.5	.1
	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>

Membership sales are made primarily at Company resorts. During 1985, sales activities were conducted at most, but not all operating resorts. Prior to 1983, substantially all membership sales were made to owners of recreational vehicles. During 1983, the Company purchased travel trailers, installed them on its resorts for use by members, and began marketing vacation memberships to individuals who do not have a recreational vehicle. The availability of vacation mem-

berships expanded considerably the number of people capable of utilizing a Thousand Trails membership. Although the vacation membership was designed primarily for individuals who do not have a recreational vehicle, the Company believes that vacation memberships have also been purchased by owners of recreational vehicles who wish to have the ability to rent a Company-owned travel trailer at preferential rates.

During 1985, the Company combined the camping membership formerly offered to owners of recreational vehicles and the vacation membership formerly offered to individuals who do not have a recreational vehicle. The combined membership, called a resort membership, allows the member to rent a Company-owned travel trailer at the preferential rates available to vacation members or, at the member's

option, to use a campsite with a recreational vehicle provided by the member.

The following table provides historical information on membership sales by type of membership, the number of resorts operated by the Company ("operating resorts"), and the number of operating resorts at which memberships are sold ("selling resorts").

<i>Year Ended December 31,</i>	<i>1981</i>	<i>1982</i>	<i>1983</i>	<i>1984</i>	<i>1985</i>
Units of membership sales:					
Camping	7,585	9,743	9,989	8,037	3,108
Vacation	—	377	3,852	10,588	4,400
Resort	—	—	—	—	11,719
Total	<u>7,585</u>	<u>10,120</u>	<u>13,841</u>	<u>18,625</u>	<u>19,227</u>
Operating Resorts:					
Selling	15	16	21	30	37
Non-Selling	—	3	4	6	5
Resorts under initial development	—	2	3	6	1
Total resorts owned	<u>15</u>	<u>21</u>	<u>28</u>	<u>42</u>	<u>43</u>

During the past three years, the Company has rapidly acquired and developed new properties in order to establish a national network of resorts. At December 31, 1985, the Company had 43 resorts (one of which was not yet operational) located in 16 states and British Columbia, Canada. In addition, the Company has acquired three additional properties which are classified on the balance sheet as investment in real estate. The Company has no plans to develop these properties in 1986, although they are available for development or other disposition in subsequent years.

With its national network of resorts in place, the Company has sufficient planned campsite inventory to sell memberships for several years without having to acquire any new properties. As a result, the Company has revised its previously announced plans and does not intend to acquire any new properties during 1986. In addition, the Company plans to spend significantly less on construction in 1986 than it did in 1984 and 1985. By not acquiring new properties and limiting expenditures for construction in 1986, the Company believes

it may achieve positive cash flow in 1987 (i.e., cash received from operations would exceed cash expended). This objective is the basis for management's strategic planning for 1986.

In prior years, the Company has generated growth in membership sales by adding new selling resorts. For 1986, the Company has revised its growth strategy and intends to concentrate its sales efforts on its existing resorts. As noted above, the Company does not intend to acquire any new properties during 1986. Moreover, in an effort to reduce marketing costs and make best use of its available resources, the Company has temporarily discontinued marketing efforts at a number of operating resorts and has focused its sales efforts on its most cost efficient properties. These actions will affect the level of membership sales which can be achieved by the Company.

1986 will be a year of consolidation for the Company with no new property acquisitions and fewer membership sales anticipated than in 1985. The Company's operating results for 1986 will depend primarily upon the level of membership sales achieved and the Company's success in reducing marketing and operational costs.

Membership Sales

Revenues from membership sales during the three years ended December 31, 1983, 1984, and 1985 were \$79,971,000, \$116,983,000, and \$127,603,000, respectively. Increases in revenues from membership sales were a result of increases in the number of memberships sold and increases in the average membership price from \$5,800 in 1983 to \$6,300 in 1984, and to \$6,600 in 1985. Increases in the number of total memberships sold in 1984 and 1985 from the prior periods were due primarily to nine additional selling resorts in 1984 and seven additional selling resorts in 1985, accounting for 25% and 9% of the total memberships sold in such years, respectively, and to the availability of vacation memberships. Although the Company conducted selling activities at seven additional resorts during 1985 and gave sales presentations to a greater number of prospective customers, membership sales in 1985 were lower than anticipated due to a decrease in the conversion percentage—that is, the number of people who purchased a membership as a percentage of the total number of prospective customers who received a sales presentation.

Because of the possibility of sales cancellations, which are defined as members who do not make two payments on their contracts, the Company does not record every membership sale for financial reporting purposes, but rather records actual membership sales net of an estimated provision for future sales cancellations. As a result of this provision, actual membership sales were reduced by \$6,548,000 in 1983, \$8,785,000 in 1984, and \$14,271,000 in 1985. During 1985, the Company experienced higher sales cancellations than in 1984 and 1983. As a result, the Company elected to increase the rate at which it provides for future sales cancellations from 7% of membership sales in 1983, 1984, and the first half of 1985 to 11% of membership sales in the second

half of 1985. In addition, the Company elected to provide an additional \$1,000,000 for future sales cancellations at December 31, 1985. The reasons for the higher sales cancellations in 1985 and the programs implemented by the Company to reduce future sales cancellations are discussed below in connection with the discussion of the Company's provision for doubtful accounts. The Company intends to provide for future sales cancellations at the higher rate until the effectiveness of these programs has been established.

Marketing expenses as a percentage of sales increased from 44.0% in 1983 to 46.3% in 1984, and to 58.1% in 1985. The significant increase in marketing costs as a percentage of sales in 1985 was due primarily to the decrease in the conversion percentage discussed above. The Company believes this decrease was caused by a number of factors, including (1) the Company's rapid expansion, which diluted sales management and shortened the time available to train new salespeople, (2) the higher cost of marketing to individuals who do not have a recreational vehicle, especially in new geographic markets, (3) a decrease in the effectiveness of the Company's direct mail marketing in 1985, and (4) the small membership base at the Company's new selling resorts which was not yet large enough to generate significant member referral business, the Company's most cost-efficient source of sales.

In an effort to reduce marketing costs, the Company has temporarily discontinued marketing efforts at a number of operating resorts and has focused its sales efforts on its most cost efficient properties. The Company has also reduced the amount of direct mail solicitations for the generation of prospective customers and is emphasizing more cost effective programs such as member referrals. In addition, the Company has implemented a number of other programs aimed at reducing marketing costs. The Company's objective is to reduce marketing costs as a percentage of sales in 1986 compared with 1985; however, any reduction is dependent on the success of the actions taken by the Company.

Where fewer than 50% of planned memberships for a resort have been sold, certain resort operations costs are expensed as marketing costs to reflect the support resort operations provide to the Company's sales efforts. These costs increased from \$1,234,000 in 1983 to \$3,040,000 in 1984, and to \$4,562,000 in 1985. The increases were due primarily to the addition of nine new selling resorts in 1984 and seven new selling resorts in 1985.

Resort land and improvement costs attributable to membership sales were \$13,047,000 (16.3% of sales) in 1983, \$17,842,000 (15.3% of sales) in 1984, and \$21,029,000 (16.5% of sales) in 1985. The average land and improvement costs expensed per membership sold in 1983, 1984, and 1985 were approximately \$940, \$940, and \$1090, respectively. The percentage decrease in 1984 compared with 1983 resulted from a \$500 increase in the average membership sales price. The percentage increase in 1985 compared with 1984 was due to the increase in the average land and improvement costs expensed per membership sold. This increase resulted from changes in estimates during 1985 regarding the estimated cost of completing planned improvements. Because of these changes in estimates, the Company expensed an additional \$706,000 of resort land and improvement costs during the fourth quarter of 1985.

The Company expenses resort land and improvement costs based on the ratio of memberships sold to total memberships planned by the Company to be available for sale in each geographic area. The number of memberships planned for sale is derived from the Company's estimate that its resorts can support 10 memberships per campsite without overcrowding and that, on the average, 10 memberships will be sold for each existing and planned campsite. As a result, since inception, the Company has used a 10-to-1 ratio in expensing land and improvement costs attributable to membership sales. For the Company to amortize fully in accordance with its accounting practices the total of incurred and all estimated future land and improvement costs with respect to the 26,702 existing and planned campsites at its current 42 operating resorts, it would be necessary for it to sell approximately 267,020 memberships, of which 85,100 memberships (32%) were outstanding at December 31, 1985. The Company reviews its resort land and improvement costs on an annual basis in order to further define its estimates of the number of memberships which can be sold at each resort and the cost of planned improvements at each resort. If in the future the Company determines that it cannot sell 10 memberships per campsite at one or more resorts, or that it has underestimated the cost to complete planned improvements at one or more resorts, the Company would reassess planned future development at the specific resort or resorts and, if necessary, increase the rate at which it expenses land and

improvement costs against subsequent sales, which would adversely affect profit margins and earnings. In addition, if the Company should determine that the market for one or more resorts is not sufficient to justify further development or operation of the specific resort or resorts, the Company would stop development at, or dispose of, the specific resort or resorts and make a period adjustment to resort land and improvement costs, which would adversely affect profit margins and earnings.

General and administrative expenses as a percentage of membership sales decreased from 14.8% in 1983 to 12.6% in 1984, and increased to 14.6% in 1985. The decrease in 1984 compared with 1983 was primarily the result of economies obtained from an increase in sales. The increase in 1985 compared with 1984 was due primarily to increased staffing at the Company's corporate office for anticipated higher sales volume which did not materialize and additional expenses related to the Company's corporate office facility. Since December 31, 1985, the Company has reduced staffing at its corporate office by approximately 9.8% in an effort to be more cost effective and as a result of the anticipated decrease in membership sales for 1986 compared with 1985.

The Company provides for estimated losses on installment sales based on its historical collection experience. The provision for doubtful accounts as a percentage of membership sales increased from 5.0% in 1983 and 1984 to 13.8% in 1985, primarily as a result of the Company's election to provide an additional \$4,400,000 for future contract losses at September 30, 1985 and an additional \$5,500,000 for future contract losses at December 31, 1985. The \$4,400,000 increase at September 30, 1985 consisted of a quarter-end adjustment to the allowance for doubtful accounts of \$2,600,000 and an increase in the rate at which the Company provides for doubtful accounts from 5.0% to approximately 10% of membership sales. The Company experienced higher delinquencies and contract losses in 1985 compared with 1984 and 1983. Upon analysis, the Company

believes the higher contract losses were primarily attributable to three factors: (1) a higher default rate on memberships sold to individuals who do not have a recreational vehicle, and have a tendency to use the Company's resorts less than owners of recreational vehicles, (2) a higher default rate on installment contracts arising from membership sales in Texas (21% of the total portfolio), which may be related to economic problems in that state, and (3) the negative publicity on the membership campground industry in 1985.

The higher contract losses experienced in 1985 related primarily to membership sales made in 1984. In 1985, the Company offered new members an optional interest rate program at the point of sale which provides for lower interest rates on membership contracts with larger down payments. The average down payment has increased from approximately \$966 in 1984 to approximately \$1153 in 1985. In addition, approximately 73% of installment sales made in 1985 have monthly payments transferred automatically from the member's bank account to a Company bank account under the Company's preauthorized payment program. Only 48% of installment sales made in 1984 utilized this program. Moreover, the Company is currently emphasizing new member programs to reduce delinquencies and contract losses, but will continue to provide for doubtful accounts at a higher rate until the effectiveness of these programs has been established. The Company does not presently anticipate any further adjustments to its allowance for doubtful accounts, but this allowance and the rate at which the Company provides for future contract losses could be increased if the Company experiences higher than anticipated contract losses in the future, which would adversely affect profit margins and earnings.

The Company has been able to offset the impact of inflation on its operations through increases in the membership sales prices and increases in annual dues for new members.

Resort Operations

Revenues from resort operations continued to increase as the base of members grew from 38,120 on January 1, 1983 to 85,100 at December 31, 1985. As a percentage of total revenues, membership dues and other resort revenues increased from 10.1% in 1983 to 13.6% in 1985, and the Company expects this source of revenues to continue to increase as new memberships are sold. After allocating to marketing expenses certain costs related to membership sales (\$1,234,000 in 1983, \$3,040,000 in 1984, and \$4,562,000 in 1985), resort operations generated a profit in 1983 of \$489,000 and incurred losses of \$588,000 and \$539,000 in 1984 and 1985, respectively. Resort operations included a gain from other member services of \$350,000 in 1984 and a loss of \$62,000 in 1985. Other member services consisted primarily of sales of financial and other products to members.

The losses from resort operations in 1984 and 1985 were due primarily to the addition of 11 new operating resorts in 1984 and six new operating resorts in 1985. There are high fixed costs associated with opening and operating a resort until sufficient memberships have been sold to generate self sustaining revenues. Because of these fixed costs, the Company expects a loss from resort operations in 1986. As the membership base grows, however, these costs are expected to be offset by a corresponding increase in dues and other resort revenues.

Interest Income and Expense

The Company charges interest on the unpaid portion of its membership contracts receivable portfolio at fixed rates which averaged approximately 14.8% in 1983, 1984, and 1985. Interest income increased from \$10,147,000 in 1983 to \$16,067,000 in 1984, and to \$23,406,000 in 1985, due to substantial increases in the Company's membership contracts receivable portfolio. The total membership contracts receivable portfolio increased from an average of \$71,619,000 in 1983 to \$115,138,000 in 1984, and to \$166,107,000 in 1985.

The Company finances its acquisition and development of resorts through borrowings under its bank line of credit and seller-financed real estate contracts. Seller financing of resort acquisitions accrues interest at fixed rates, which averaged 8.9% in 1985. Financing under the Company's bank line of credit bears interest at variable rates which averaged 11.5% in 1985.

The average cost to the Company of all borrowed funds over the past three years has varied but increased from 11.7% in 1983 to 11.9% in 1984, and to 13.0% in 1985. The increase in 1985 resulted primarily from the Company's sale in March 1985 of \$75,000,000 of 14½% senior subordinated notes due 1992, which have an effective interest rate of 15.0%. The proceeds from the sale of the notes were used to reduce borrowings under the Company's bank line of credit.

The Company capitalizes interest as a component of the cost of significant improvements to resorts. Interest is capitalized only during periods of major construction activities to prepare a resort for use and during the construction of specific major improvements at subsequent dates. Total interest costs were \$6,411,000 in 1983, \$11,007,000 in 1984, and \$22,078,000 in 1985, of which \$2,454,000, \$5,883,000, and \$5,792,000, respectively, were capitalized.

During 1985, the Company delayed the completion of the initial phase of development at certain of its resorts. Because of this delay, in the fourth quarter, the Company redefined its method of determining when a resort is substantially ready for its intended use, which resulted in a \$1,800,000 charge to earnings in the fourth quarter for interest capitalized in prior quarters.

Happy Trails Resorts

The Company's largest shareholder is developing a recreational vehicle subdivision near Phoenix, Arizona. Under an agreement with this shareholder, the Company is providing sales, marketing, and development services for the project. Compensation to the Company will consist of 50% of the profits arising from the sale of the subdivision lots. Upon sell-out of the lots, title to and the right to operate certain common recreational facilities contiguous to the subdivision will be conveyed to the Company. Costs incurred by the Company in providing sales, marketing, and development services are classified on the balance sheet as other investments and will be recovered ratably from proceeds of the lot sales.

The shareholder has the right to terminate the agreement if cumulative profits from lot sales do not meet certain specified targets each year. The shareholder has waived its right to terminate the agreement based on the Company's failure to meet the specified target for cumulative profits through December 31, 1985. Should the agreement be terminated in future periods for the Company's failure to meet specified profit levels, the Company would be unable to recover its

investment. In addition, the Company would be required to expense its investment in the year the agreement is terminated, which would adversely affect profit margins and earnings in such year.

No profits were recognized during the fourth quarter of 1985 for lot sales at this project. In addition, because of lower than expected sales in 1985 and an increase in the estimated costs to complete the subdivision, the overall profitability of the project was not reasonably determinable at December 31, 1985, and, as a result, the Company reversed approximately \$752,000 of profits which had previously been recognized during the first three quarters of 1985.

Net Earnings

Net earnings were \$12,004,000 in 1983, \$19,110,000 in 1984, and \$1,788,000 in 1985. Increased net earnings in 1983 and 1984 were primarily the result of increased membership sales. The decrease in net earnings in 1985 compared with 1984 was due primarily to lower than expected sales, higher marketing costs, and pretax adjustments during the third and fourth quarters of 1985 totalling \$14,158,000 enumerated above.

Liquidity and Capital Resources

The Company incurs substantial resort acquisition and improvement costs and membership marketing costs prior to and concurrently with membership sales, while members pay for their memberships either entirely in cash at the time of sale or by making a minimum down payment of at least 10% and then paying the balance in installments over periods up to 84 months, with interest averaging 14.7% on installment contracts executed in 1985. For 1985, down payments on financed membership sales averaged 21.0%, and the average installment term was 76 months. The Company financed 92.9% of membership sales in 1985. Revenues from membership sales, net of an allowance for sales cancellations, are recorded in full at the time of sale, while cash flow from installment sales is received over a period of years following the sale.

Cash received from sales, resort operations, and collections on membership contracts receivable has increased from period to period but has not kept pace with the growth of membership sales. Down payments and cash sales as a percentage of membership sales were 34.7% in 1983, 26.1% in 1984, and 27.1% in 1985. The Company has developed incentive programs intended to accelerate cash flow by

encouraging members to pay their installment contracts in full prior to maturity. These incentive programs generated additional cash of approximately \$2,249,000 in 1983, \$9,800,000 in 1984, and \$12,735,000 in 1985.

Below is a table showing a historical summary of cash received and expended as it relates to operations of the Company.

<i>Year ended December 31,</i>	<i>1983</i>	<i>1984</i>	<i>1985</i>
Cash received from operations		(In thousands)	
Membership sales	\$ 27,738	\$ 30,549	\$ 34,517
Collections on contracts receivable including interest	28,619	44,060	67,626
Dues and resort revenues	10,507	15,586	21,191
Other	211	1,288	324
	67,075	91,483	123,658
Principal operating expenditures	(52,782)	(74,906)	(111,186)
Cash provided by operations before debt service and resort acquisition and development	14,293	16,577	12,472
Cash expended for resort acquisition and development	(20,609)	(59,316)	(44,112)
Interest expense	(3,957)	(4,984)	(15,678)
Principal payments on debt related to resort properties	(4,337)	(4,688)	(7,839)
Cash used in operations	<u><u>\$ (14,610)</u></u>	<u><u>\$ (52,411)</u></u>	<u><u>\$ (55,157)</u></u>

Although cash received from sales, resort operations, and collections on membership contracts receivable has increased over the past three years, it has not been sufficient to fund the Company's operations because of expenditures relating to increases in membership sales, the expansion and improvement of the Company's resort network, and the additional cost of the debt required to finance this growth.

In 1985, the Company spent more as a percentage of membership sales than in previous years on marketing, general and administrative, and resort operations expenses, as the Company was not as cost-effective in generating prospective customers and also spent more in an effort to lay the foundation for expected future years' growth in membership sales by adding personnel and data processing systems. In 1984 and 1985, the Company spent \$59,316,000 and \$44,112,000, respectively, for resort acquisition and development compared with \$20,609,000 in 1983. Interest expense

and principal payments on debt related to resort properties have also increased due to the growth in the Company's resort network, the additional debt required to finance this growth, and the higher cost of such debt.

The Company also spent \$4,331,000, \$13,480,000, and \$12,668,000 in 1983, 1984, and 1985, respectively, for purchase of construction and operating equipment, a portion of which was financed through borrowings secured by such equipment. These expenditures include approximately \$1,384,000 in 1983, \$6,774,000 in 1984, and 5,425,000 in 1985 for purchase of rental trailers.

During 1985, the Company purchased 602,500 shares of its outstanding common stock pursuant to its previously announced program to purchase up to 1,000,000 shares from time to time at the current market price. The total cost to the Company was \$7,020,000. The Company does not

intend to purchase additional stock in 1986.

The Company has relied upon external financing to provide cash to fund working capital and the rapid expansion of its resort network, as follows:

<i>Year ended December 31,</i>	<i>1983</i>	<i>1984</i>	<i>1985</i>
Issuance of common stock (net of repurchases)	\$17,756,000	\$ 989,000	\$ (3,995,000)
Bank borrowings (net of repayments)	851,000	63,284,000	(924,000)
14% senior subordinated notes due 1992 (net of discount)	—	—	71,555,000
	<u>\$18,607,000</u>	<u>\$64,273,000</u>	<u>\$66,636,000</u>

The Company has taken several actions intended to reduce its cash requirements in 1986 compared with prior years. The Company does not plan to acquire any new properties in 1986. The Company also plans to spend significantly less on construction in 1986 than it did in 1984 and 1985. During 1986, the Company anticipates spending no more than \$20,000,000 for additional development of its 43 resorts. The Company does not anticipate a need to acquire additional rental trailers in 1986. In addition, the Company has taken a number of steps designed to reduce marketing and operational costs in 1986 and plans to continue its incentive programs to encourage members to pay their installment contracts in full prior to maturity.

On December 31, 1985, the Company's unused sources of liquidity consisted principally of \$995,000 in cash and approximately \$22,607,000 of additional borrowing capacity under its \$110,000,000 bank line of credit. The Company's bank line of credit includes a \$50,000,000 revolving working capital credit line, a \$50,000,000 term loan restricted to acquisition and development of resorts, and a \$10,000,000 working capital term loan. At December 31, 1985, the Company had borrowed \$48,993,000 of the revolving credit line, \$28,400,000 of the \$50,000,000 term loan, and all of the \$10,000,000 term loan. During the third quarter of 1985, the revolving credit line was reduced from \$65,000,000 to \$50,000,000. The Company does not expect to increase its existing \$110,000,000 bank line of credit during 1986. However, the Company will continue to pursue alternatives to its current line of credit which would provide lower interest rates and increased flexibility.

The Company has generated additional liquidity through the deferral of income taxes, principally as a result of reporting membership sales on the installment method for income tax purposes. Income taxes may continue to be deferred and additional liquidity thereby provided as long as the Company continues to use the installment method for income tax purposes and continues to expand its membership contracts receivable portfolio. The United States Treasury Department has proposed, and the United States House of Representatives has passed, legislation which, if adopted, could limit tax deferral by the Company and others which use the installment method. In addition, other legislative changes, judicial decisions, or administrative rulings, positions, or regulations could preclude use of the installment method by the Company, perhaps with retroactive effect. In the event that any of the foregoing were to occur, the Company's liquidity, capital resources, and results of operations could be adversely affected.

The Company believes its capital requirements through the end of 1986 will be met by the remaining borrowing capacity under its existing \$110,000,000 bank line of credit, deferral of income taxes, and cash generated by operations. Should the Company require working capital in excess of these sources, the Company would consider additional debt financing and/or the sale of equity securities.

Thousand Trails, Inc. and Subsidiaries **Consolidated Balance Sheets**

<i>Assets December 31,</i>	<i>1984</i>	<i>1985</i>
Current Assets:		
Cash	\$ 1,644,000	\$ 995,000
Membership contracts receivable, net of allowance of \$1,797,000 and \$3,897,000	27,426,000	33,357,000
Inventory and other assets	6,409,000	9,556,000
Total Current Assets	35,479,000	43,908,000
Membership Contracts Receivable, net of allowance of \$7,005,000 and \$15,882,000	106,925,000	135,925,000
Operating Resorts:		
Land	28,981,000	35,259,000
Improvements	119,417,000	164,758,000
	148,398,000	200,017,000
Costs attributable to membership sales	(55,661,000)	(76,251,000)
	92,737,000	123,766,000
Resorts Under Initial Development	9,830,000	5,181,000
Resort Operating Equipment, net of accumulated depreciation of \$2,217,000 and \$4,180,000	9,356,000	14,594,000
Construction and Other Equipment, net of accumulated depreciation of \$2,902,000 and \$4,478,000	5,596,000	6,392,000
Investment in Real Estate	3,203,000	10,284,000
Other Investments	812,000	4,554,000
Other Assets	5,832,000	8,478,000
	<u>\$269,770,000</u>	<u>\$353,082,000</u>

<i>Liabilities and Shareholders' Equity December 31,</i>	<i>1984</i>	<i>1985</i>
Current Liabilities:		
Accounts payable	\$ 5,980,000	\$ 5,297,000
Accrued salaries and related taxes	5,654,000	5,118,000
Accrued interest and other liabilities	2,229,000	5,977,000
Prepaid membership dues and rental revenues	3,671,000	6,464,000
Current portion of long-term debt	9,359,000	7,711,000
Deferred income taxes	9,197,000	9,126,000
Total Current Liabilities	36,090,000	39,693,000
Long-Term Debt	112,895,000	192,581,000
Deferred Income Taxes	35,856,000	37,189,000
Deferred Rental Revenue and Other Liabilities	4,012,000	4,922,000
Commitments and Contingencies (Note H)		
Shareholders' Equity:		
Common stock, no par value—		
Authorized, 15,000,000 shares		
Issued and outstanding, 10,658,476 and 10,308,847 shares	30,934,000	26,940,000
Retained earnings	49,983,000	51,757,000
	80,917,000	78,697,000
	<u>\$269,770,000</u>	<u>\$353,082,000</u>

See notes to consolidated financial statements.

Thousand Trails, Inc. and Subsidiaries **Consolidated Statements of Earnings**

<i>Year ended December 31,</i>	<i>1983</i>	<i>1984</i>	<i>1985</i>
Membership Sales	\$79,971,000	\$116,983,000	\$127,603,000
Costs Attributable to Membership Sales:			
Marketing expenses	35,209,000	54,181,000	74,081,000
Resort land and improvement costs	13,047,000	17,842,000	21,029,000
General and administrative expenses	11,827,000	14,693,000	18,602,000
Provision for doubtful accounts	3,977,000	5,880,000	17,644,000
	64,060,000	92,596,000	131,356,000
Income (Loss) from Membership Sales	15,911,000	24,387,000	(3,753,000)
Resort Operations:			
Membership dues	7,355,000	10,551,000	15,452,000
Resort revenue and rental income	2,749,000	5,264,000	8,382,000
	10,104,000	15,815,000	23,834,000
Less:			
Maintenance and operations expense	5,709,000	10,107,000	15,305,000
Cost of resort revenue	2,400,000	3,289,000	4,814,000
General and administrative expenses	1,506,000	3,007,000	4,254,000
	9,615,000	16,403,000	24,373,000
Income (Loss) from Resort Operations	489,000	(588,000)	(539,000)
Other Income (Expense):			
Interest income	10,147,000	16,067,000	23,406,000
Interest expense	(3,957,000)	(5,124,000)	(16,286,000)
Other	42,000	654,000	152,000
	6,232,000	11,597,000	7,272,000
Earnings before Deferred Income Taxes	22,632,000	35,396,000	2,980,000
Deferred Income Taxes	10,628,000	16,286,000	1,192,000
Net Earnings	<u>\$12,004,000</u>	<u>\$ 19,110,000</u>	<u>\$ 1,788,000</u>
Net Earnings Per Share:			
Primary	<u>\$1.23</u>	<u>\$1.78</u>	<u>\$.17</u>
Fully diluted	<u>\$1.21</u>	<u>\$1.76</u>	<u>\$.16</u>

See notes to consolidated financial statements.

Thousand Trails, Inc. and Subsidiaries
Consolidated Statements of Shareholders' Equity

	Shares	Amount	Retained earnings
Balance, January 1, 1983	8,209,239	\$11,252,000	\$18,942,000
Debenture conversions	116,704	296,000	
Issuance of common stock	1,871,202	17,810,000	
Foreign currency translation			(5,000)
Net earnings			12,004,000
Balance, December 31, 1983	10,197,145	29,358,000	30,941,000
Debenture conversions	230,135	587,000	
Exercise of stock options	231,196	989,000	
Foreign currency translation			(68,000)
Net earnings			19,110,000
Balance, December 31, 1984	10,658,476	30,934,000	49,983,000
Exercise of stock options	252,871	3,026,000	
Purchase and retirement of treasury stock	(602,500)	(7,020,000)	
Foreign currency translation			(14,000)
Net earnings			1,788,000
Balance, December 31, 1985	<u>10,308,847</u>	<u>\$26,940,000</u>	<u>\$51,757,000</u>

See notes to consolidated financial statements.

Thousand Trails, Inc. and Subsidiaries
Consolidated Statements of Changes in Financial Position

<i>Year ended December 31,</i>	<i>1983</i>	<i>1984</i>	<i>1985</i>
Operations:			
Cash received—			
Membership sales	\$27,738,000	\$30,549,000	\$34,517,000
Collections on contracts receivable, including interest	28,619,000	44,060,000	67,626,000
Dues and resort revenues	10,507,000	15,586,000	21,191,000
Other	211,000	1,288,000	324,000
	67,075,000	91,483,000	123,658,000
Cash expended—			
Marketing expenses	32,832,000	48,653,000	73,144,000
General and administrative expenses	11,325,000	12,510,000	17,061,000
Resort maintenance and operations	8,625,000	13,743,000	20,981,000
	52,782,000	74,906,000	111,186,000
Cash provided by operations before debt service and resort acquisition and development	14,293,000	16,577,000	12,472,000
Cash expended for resort acquisition and development	(20,609,000)	(59,316,000)	(44,112,000)
Interest expense	(3,957,000)	(4,984,000)	(15,678,000)
Principal payments on debt related to resort properties	(4,337,000)	(4,688,000)	(7,839,000)
Cash used in operations	(14,610,000)	(52,411,000)	(55,157,000)
Other Sources (Uses) of Cash:			
Issuance of common stock	17,756,000	989,000	3,025,000
Issuance of debentures, net of discount of \$1,196,000 and related costs of \$2,250,000			71,555,000
Treasury stock acquired			(7,020,000)
Proceeds (repayments) of borrowings collateralized by contracts receivable	851,000	63,284,000	(924,000)
Purchase of resort operating equipment, net of related borrowings of \$1,302,000, \$3,165,000 and \$5,199,000	(1,711,000)	(5,953,000)	(3,892,000)
Purchase of construction and other equipment, net of related borrowings of \$86,000, \$96,000 and \$334,000	(1,232,000)	(4,266,000)	(3,243,000)
Increase (decrease) in notes payable and credit line arrangements	(1,109,000)	(306,000)	219,000
Other investments			(4,216,000)
Other, net	122,000	(463,000)	(996,000)
	14,677,000	53,285,000	54,508,000
Increase (Decrease) in Cash	67,000	874,000	(649,000)
Cash:			
Beginning of year	703,000	770,000	1,644,000
End of year	<u>\$ 770,000</u>	<u>\$ 1,644,000</u>	<u>\$ 995,000</u>

See notes to consolidated financial statements.

Thousand Trails, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Three Years Ended December 31, 1985

Note A **Significant Accounting Policies:**

General

The Company and its subsidiaries operate membership-based destination campground resorts in the United States and Canada. All significant intercompany transactions and balances have been eliminated in the accompanying financial statements.

Revenue recognition

The Company sells memberships for cash or on an installment basis. Membership sales, net of an allowance for sales cancellations, are recorded in full upon execution of membership contracts. Installment sales require a down payment of at least 10% of the sales price. All marketing costs and an allowance for estimated contract collection losses and sales cancellations (based on historical loss occurrence rates) are recorded currently.

Certain membership contracts provide for prepaid use by members of Company-owned rental trailers. Revenue attributable to prepaid use is recorded as deferred rental revenue and recognized over the period of expected use.

Members are assessed annual dues which are used for resort maintenance and operations, member services and related general and administrative expenses. The Company establishes dues at rates intended to fully provide for such expenses when active memberships sold reach approximately 40% of total memberships available for sale. Membership contracts provide for annual adjustment of dues to reflect increases in the Consumer Price Index.

Operating resorts

Operating resort land and improvement costs, including the estimated costs to fully develop the resorts, are aggregated by geographical area and recorded as a cost of membership sales based upon the ratio of actual memberships sold within each area to the total memberships planned for sale within the area. The maximum number of memberships which will be sold in a geographical area is determined based on members' historical use of the Company's resorts in that area. The Company currently plans to sell ten memberships for each campsite. Resort utilization statistics are reviewed on a regular basis, and the number of total planned memberships available for sale will be revised if future experience indicates the ten-to-one ratio is no longer appropriate. As of December 31, 1985, the Company had 85,100 members, which represented approximately one-third of the total memberships planned for sale on its 42 operating resorts.

Resorts under initial development

Resorts under initial development are classified as operating resorts when development has been completed to the extent that the resorts are available for regular use by members.

Investment in real estate

Real estate acquired for potential future development as resorts and real estate acquired in excess of that necessary for operating resorts is classified as investment in real estate. Real estate contiguous to operating resorts is infrequently used but is generally available for use by members until disposition or further development. Certain parcels of the real estate contiguous to operating resorts are subject to land use permits obtained in connection with development of the resorts. Prior to disposition or development of such parcels, the Company will be required to obtain waivers or modifications of such permits from local governmental authorities.

Depreciation

Depreciation of equipment is provided on the straight-line method over the assets' respective useful lives which range from three to ten years.

Foreign currency translation

The Company translates the financial statements of its Canadian subsidiary into U. S. dollars at exchange rates in effect as of the balance sheet dates. Unrealized translation gains and losses are included in retained earnings.

Earnings per share

Earnings per share of common stock is computed based on weighted average common and equivalent shares outstanding during the year. Stock options, warrants and rights to purchase stock are included in the computation of earnings per share when dilutive.

Reclassifications

Certain reclassifications have been made in the 1983 and 1984 financial statements to conform with 1985 classifications.

Note B
Membership Contracts Receivable:

Membership contracts receivable bear interest at an average rate of 14.8% and currently are written with initial terms of 10 to 84 months (average 76 months in 1985). The Company has no obligation to refund monies received or provide further services to members in the event a membership is cancelled for nonpayment of contractual obligations.

Scheduled aggregate annual principal payments on membership contracts are as follows:

<i>Year ending December 31,</i>	
1986	\$37,254,000
1987	35,257,000
1988	32,671,000
1989	28,466,000
1990	24,191,000
1991	20,007,000
1992	11,215,000

The Company received principal payments in excess of the scheduled payments in 1983, 1984 and 1985 of \$2,249,000, \$9,800,000 and \$12,735,000, respectively, by utilizing early payment incentive programs.

Substantially all membership contracts receivable are pledged as collateral for debt.

Note C
Other Investments:

The Company's largest shareholder is developing a recreational vehicle subdivision near Phoenix, Arizona. Under an agreement with the shareholder, the Company is providing sales, marketing and development services for the project. Compensation to the Company will consist of 50% of the profits arising from the sale of the subdivision lots. Upon sellout of the lots, title to and the right to operate certain common recreational facilities contiguous to the subdivision will be transferred to the Company. Costs incurred by the Company in providing sales, marketing and development services are classified as other investments and are being recovered ratably from proceeds of the lot sales.

The shareholder has the right to terminate the agreement if cumulative profits from lot sales do not meet certain specified amounts each year. The shareholder has waived its right to terminate the agreement based on the Company's failure to meet the specified target for cumulative profits through December 31, 1985. Should the agreement be terminated in future periods for failure to meet specified profit levels, the Company would be unable to recover its investment.

Note D
Long-Term Debt and Line of Credit:

Long-term debt and line of credit consist of the following:

December 31,	1984	1985
14.625% senior subordinated notes due 1992, interest paid semi-annually (effective rate 15.0%), net of discount of \$1,107,000	\$ —	\$ 73,893,000
Real estate contracts, 6.5% to 15.0% (average 8.9%), payable in monthly installments of \$587,000 and \$611,000 including interest	28,604,000	29,975,000
Equipment and other contracts, 8.8% to 18.6% (average 10.6%), payable in monthly installments of \$182,000 and \$240,000 including interest	3,955,000	7,139,000
Notes, 6.0% to 12.25% (average 9.2%), payable in monthly installments of approximately \$46,000 and \$125,000 including interest	1,378,000	1,892,000
	33,937,000	112,899,000
Line of credit	88,317,000	87,393,000
	122,254,000	200,292,000
Current portion	(9,359,000)	(7,711,000)
	<u>\$112,895,000</u>	<u>\$192,581,000</u>

Substantially all of the Company's assets are pledged as collateral for the above debt. Aggregate annual principal payments over the next five years are as follows:

Year ending December 31,	
1986	\$ 7,711,000
1987	12,672,000
1988	8,553,000
1989	13,441,000
1990	10,586,000

The Company's \$110,000,000 bank line of credit is provided by several financial institutions and includes a \$50,000,000 revolving working capital credit line, a \$50,000,000 term loan restricted to acquisition and development of resorts and a \$10,000,000 working capital term loan. Borrowings under the credit line may not exceed 70% of the aggregate amount of the Company's qualifying membership contracts receivable. At December 31, 1985, qualifying membership contracts receivable totaled \$186,014,000 which would permit the Company to borrow the maximum line of credit. The Company is restricted from payment of cash dividends without the institution's approval.

The \$50,000,000 revolving credit line, which may be converted at the option of the Company or the bank to a term loan payable over 36 months, accrued interest during 1985 at the prime lending rate plus .25% (9.75% as of December 31, 1985). Effective February 1, 1986, the interest rate on the revolving credit line was increased to the prime lending rate

plus 1%. The Company had borrowed \$48,993,000 of the revolving credit line as of December 31, 1985. None of the amount due under the revolving credit line is included in the current portion of long-term debt. The bank can at its option cease making additional advances under the revolving credit line, in which case the outstanding revolving balance would convert to a three-year term loan.

The \$50,000,000 term loan is comprised of two \$25,000,000 components. The first \$25,000,000 component bears interest at the 26-week Treasury bill rate plus 3.5% (12.0% as of December 31, 1985). The Company had borrowed the entire \$25,000,000 as of December 31, 1985. The second \$25,000,000 component of this term loan bears interest at a fixed rate of 14.875%. The Company had borrowed \$3,400,000 of this second \$25,000,000 component as of December 31, 1985. The entire term loan is payable in 12 monthly principal installments of \$400,000 commencing June 1987, with the remaining balance due in equal principal payments over 72 months. The financial institution funding this loan owned approximately 23% of the Company's common stock on December 31, 1985. Interest paid to this financial institution for the three years ended December 31, 1985 was \$694,000, \$1,424,000 and \$1,366,000, respectively.

As of December 31, 1985, the Company had borrowed all of the \$10,000,000 working capital term loan which bears interest at 14.875%. This loan is payable in five equal annual principal installments commencing in 1988.

Note E
Deferred Income Taxes:

The provision for deferred income taxes consists of the following:

<i>Year ended December 31,</i>	<i>1983</i>	<i>1984</i>	<i>1985</i>
Federal	\$ 9,539,000	\$14,434,000	\$ 794,000
Foreign and state	1,089,000	1,852,000	398,000
	<u>\$10,628,000</u>	<u>\$16,286,000</u>	<u>\$1,192,000</u>

Investment tax credits are recorded as a reduction of the income tax provision in the year available. The income tax provision was reduced by investment tax credits of \$226,000 in 1983, \$934,000 in 1984, and \$318,000 in 1985. In each of

the three years, the Company's tax provision was reduced by \$140,000 from an 85% dividend received deduction.

The tax effect of items reported in different periods for financial statement and income tax purposes is as follows:

<i>Year ended December 31,</i>	<i>1983</i>	<i>1984</i>	<i>1985</i>
Installment sales	\$13,309,000	\$18,514,000	\$6,639,000
Capitalized interest	211,000	1,379,000	440,000
Resort land and improvement costs	(4,033,000)	(1,877,000)	(1,608,000)
Decrease (increase) in tax basis net operating loss carryforward	977,000	(2,079,000)	(4,839,000)
Excess of tax over book depreciation and effect of accounting for capital leases as operating leases for tax purposes	130,000	457,000	783,000
Other, net	34,000	(108,000)	(223,000)
	<u>\$10,628,000</u>	<u>\$16,286,000</u>	<u>\$1,192,000</u>

Note F
Incentive Stock Plans:

Stock option plans

The Company has two stock option plans under which common stock is reserved for issuance to officers and key employees. Under the 1979 plan, options are exercisable 25% each year commencing one year after the date of grant and expire after ten years. Under the 1980 plan, options are

exercisable in full commencing one year after the date of grant and expire after five years. Options are priced at not less than the market price of the Company's common stock at the date of grant.

Information with respect to options granted under the plans is as follows:

<i>Options outstanding</i>						
	<i>Authorized</i>	<i>Available for grant</i>	<i>Shares</i>	<i>Price per share</i>	<i>Options currently exercisable</i>	<i>Exercised</i>
Balance at						
January 1, 1985	1,162,575	190,186	290,865	\$2.37-\$15.33	57,530	681,524
Options forfeited		87,275	(87,275)			
Options granted		(205,900)	205,900		(11,570)	11,570
Options exercised			(11,570)		(19,952)	
Options exercisable during year					1,406	
Balance at						
December 31, 1985	<u>1,162,575</u>	<u>71,561</u>	<u>397,920</u>	<u>\$2.37-\$7.00</u>	<u>27,414</u>	<u>693,094</u>

On October 25, 1985, with approval of the Board of Directors, the Company offered stock options priced at \$7.00 per share (the fair market value of a share of the Company's common stock on that date) in substitution of all outstanding stock options with exercise prices in excess of \$7.00.

Stock purchase plans

Since 1982, the Company has reserved 975,000 shares for issuance under a stock purchase plan for officers and key employees. The plan provides for sale of common stock to participants on a cash or installment basis at a price not less than market value. Shares sold on the installment basis are issued and recorded in the financial statements upon receipt of payment. Of the shares reserved for issuance under the plan, 347,250 shares were sold in 1983 at an average of \$10.54 per share, 113,375 shares were sold in 1984 at an average of \$15.27 per share, and 88,400 shares were sold

in 1985 at an average of \$15.63 per share. On October 25, 1985, with approval of the Board of Directors, the Company offered to modify outstanding installment contracts under the plan to reduce the purchase price to \$7.00 per share (the fair market value of a share of the Company's common stock on that date). During 1983, 1984 and 1985, 215,491, 88,743 and 37,676 shares, respectively, were issued under the plan.

In November 1983 and April 1984, the Company sold 150,000 shares of common stock to its President on an installment basis at an average of \$15.71 per share. During 1984 and 1985, these shares were paid for and issued. The Company repurchased these shares upon resignation of the President in May 1985, at fair market value.

Note G
Post-Employment Agreements:

During 1983, the Company entered into post-employment agreements with certain key officers. The agreements provide for pre-retirement death benefits, post-employment consulting, retirement benefits and an agreement not to compete. Costs to the Company under these agreements were \$275,000 in 1983, \$300,000 in 1984 and \$686,000 in 1985.

Note H
Commitments and Contingencies:

The Company has operating lease obligations of approximately \$975,000 annually until 1994.

Certain of the Company's resorts have been developed and must be operated in compliance with the provisions of applicable land use permits. Management believes the Company is in compliance with such permits and, in the future, will make applications for new permits or for modifications of existing permits as considered necessary for resort operations or for further development.

The Company is involved in a dispute with the Arizona Department of Revenue regarding the application of a 4% privilege transaction tax to membership sales and dues assessments made in Arizona. The Company is also involved in a dispute with the Washington Department of Revenue regarding the application of a 1.5% business and occupation tax to interest income from membership contracts sold outside the state of Washington. In addition, the Company has been notified by the Virginia Department of Revenue that it believes the Company's membership sales and dues assessments in Virginia are subject to a 4% retail sales tax. The Company has not collected or accrued for these state taxes. The Company is in the process of contesting the application of these state taxes, and management believes the eventual outcome will not have a material impact on the Company's operations or financial position.

The sales and marketing activities of the Company are regulated by certain state and federal consumer protection laws. Prior to commencing sales and marketing activities in a new state, the Company reviews its sales and marketing practices in light of the state's consumer protection laws to ensure that its practices comply with such laws. Despite this review, in one state in which the Company commenced sales and marketing activities in 1984, the state's Attorney General's office has taken the position that certain of the Company's sales and marketing practices violate the state's consumer protection laws. Although the Company does not believe its sales and marketing practices violate such laws, it is negotiating with the state's Attorney General's office in an attempt to reach a mutually agreeable settlement. If a settlement is not reached, the state's Attorney General's office has threatened to take legal action against the Company to enjoin the practices which it believes violate the state's consumer protection laws and to seek monetary damages and penalties. Management believes the eventual outcome will not have a material impact on the Company's operations or financial position.

The Company has received an access letter dated August 29, 1985 from the Federal Trade Commission (FTC) which required the Company to furnish to the FTC certain information with respect to the sales and marketing practices of the Company. The Company has not been notified whether or not the FTC intends to take any action against the Company as a result of its investigation. The Company believes its sales and marketing practices are in compliance with the federal consumer protection laws enforced by the FTC.

On February 26, 1986, the Company was served with a purported class action complaint filed in Seattle in federal district court naming the Company, two of its principal officers, and its independent auditors as defendants. The complaint alleges claims under Section 10(b) of the Securities Exchange Act of 1934, Rule 10b-5 promulgated thereunder, and certain common law principles based on alleged misrepresentations by the Company in certain financial disclosures, including reports filed with the Securities and Exchange Commission, in 1985 and seeks unspecified damages. No discovery has been initiated to date and no in-depth investigation of the asserted claims has been made. However, the Company has reviewed the complaint with legal counsel and, based on this preliminary review, believes that it has meritorious defenses and that the lawsuit will not have a material impact on the Company's operations or financial position.

Note I
Costs and Expenses:

The Company capitalizes interest as a component of the cost of significant improvements to resorts. Total interest costs were \$6,411,000 in 1983, \$11,007,000 in 1984, and \$22,078,000 in 1985, of which \$2,454,000, \$5,883,000 and \$5,792,000, respectively, were capitalized.

Certain resort operating costs which support sales activity are charged to marketing expense in regions where

less than 50% of planned memberships have been sold.

These costs are as follows:

<i>Year ended December 31,</i>	
1983	\$1,234,000
1984	3,040,000
1985	4,562,000

Note J
Quarterly Financial Information (unaudited):

The following table sets forth quarterly financial information (in thousands except per share data).

	<i>First quarter</i>	<i>Second quarter</i>	<i>Third quarter</i>	<i>Fourth quarter</i>
1984:				
Membership sales	\$17,725	\$32,725	\$42,649	\$23,884
Gross profit	6,700	13,630	17,062	7,568
Earnings before taxes	5,129	11,400	14,715	4,152
Net earnings	2,641	5,871	7,650	2,948
Earnings per share—				
Primary	\$.25	\$.55	\$.70	\$.28
Fully diluted	.25	.54	.70	.27
1985:				
Membership sales	\$22,053	\$39,051	\$43,439	\$23,060
Gross profit	6,725	12,149	11,813	1,806
Earnings (loss) before taxes	5,862	8,338	1,937	(13,157)
Net earnings (loss)	3,102	4,425	1,026	(6,765)
Earnings (loss) per share—				
Primary	\$.29	\$.41	\$.10	\$(.66)
Fully diluted	.29	.41	.10	(.66)

The Company experienced higher than expected sales cancellations and contract losses in the second half of 1985, resulting in an increase in its allowance for sales cancellations and doubtful accounts of \$4,400,000 in the third quarter and \$6,500,000 in the fourth quarter.

As a result of changes in estimates regarding the total number of planned campsites to be constructed at the Company's resorts and the estimated cost of completing planned facilities, the Company's resort land and improvement costs increased by \$706,000 in the fourth quarter.

No profits were recognized during the fourth quarter for sales which occurred at the recreational vehicle subdivision near Phoenix, Arizona. In addition, because of lower than

expected sales in the fourth quarter of 1985 and an increase in the estimated costs to complete the subdivision, the overall profitability of the project was not reasonably determinable at December 31, 1985 and, as a result, the Company reversed approximately \$752,000 of profits which had previously been recognized during the first three quarters.

During 1985, the Company delayed the completion of the initial phase of development at certain of its resorts. Because of this, the Company redefined its method of determining when a resort is substantially ready for its intended use, resulting in a \$1,800,000 charge to earnings in the fourth quarter for interest capitalized in prior quarters.

Supplemental Information—Financial Reporting and Changing Prices (unaudited)

As a result of the impact of inflation on American business enterprises, the Financial Accounting Standards Board issued pronouncements requiring certain disclosures of the effects of changing prices on business enterprises. These statements require businesses to report the effects of changing prices on inventories, property and equipment, cost of sales, depreciation and amortization. Information on a current cost basis is not applicable to the Company's income-producing real estate related operations. Consequently, the supplementary information presented herein is intended to show the effect of a rise in the general price level on the exchange value or purchasing power of the dollar, called general inflation.

The consolidated statement of earnings is presented for constant dollars and was derived by restating costs of land and improvements, depreciation and amortization using the Consumer Price Index for all urban consumers. The cost of land and improvements applicable to 1985 membership sales increased by \$1,240,000 and total depreciation increased by \$202,000.

The five-year comparison summarizes the effects of changing prices on the results of operations for the last five years. The summary indicates that sales have increased in real terms over the past five years, although at a lower rate than reported on a historical cost basis. In order to continue to provide shareholders with real growth, the Company must continue to improve productivity of its existing assets and personnel, as well as identify new opportunities for growth.

The information presented must be used with care. As with the traditional historical cost method of accounting, the reported results must be related to the results of other business enterprises. Constant dollar calculations involve the use of assumptions, approximations and estimates. The results should be viewed in that context and not as precise indicators of the effects of inflation.

Consolidated net assets adjusted for general inflation are as follows (in thousands):

	<i>As reported</i>	<i>Adjusted for general inflation</i>
Operating resorts and resorts under initial development, net	\$128,947	\$142,966
Resort operating, construction and other equipment	20,986	22,878
Other assets and investments	203,149	200,952
Liabilities	(274,385)	(270,027)
Net assets	<u>\$ 78,697</u>	<u>\$ 96,769</u>

Consolidated Statement of Earnings Adjusted for Changing Prices
(In thousands except per share data)

Year ended December 31, 1985		
	As reported	Adjusted for general inflation
Membership sales	\$127,603	\$127,603
Resort land and improvements cost	21,029	22,269
Marketing, general and administrative expenses	92,683	92,812
Provision for bad debts	17,644	17,644
Loss from membership sales	(3,753)	(5,122)
Revenues from resort operations	23,834	23,834
Costs and expenses of resort operations	24,373	24,446
Loss from resort operations	(539)	(612)
Other income and expenses, net	7,272	7,272
Earnings before deferred income taxes	2,980	1,538
Deferred income taxes	1,192	1,192
Net earnings	\$ 1,788	\$ 346
Earnings per common share	\$.16	\$.03
Gain from decline in the purchasing power of net amounts owed	—	\$2,006

Five-year summary of selected financial data is as follows (stated in average 1985 dollars) (in thousands except per share data):

Year ended December 31,	1981	1982	1983	1984	1985
Membership sales	\$47,320	\$62,918	\$86,349	\$121,157	\$127,603
Year-end data:					
Market price per common share	\$3.06	\$9.85	\$16.27	\$15.32	\$8.12
Average Consumer Price Index	272.4	289.1	298.4	311.1	322.2

**Thousand Trails, Inc. and Subsidiaries
Report on Examination of
Consolidated Financial Statements
Three Years Ended December 31, 1985**

**Board of Directors and Shareholders
Thousand Trails, Inc.
Bellevue, Washington**

We have examined the consolidated balance sheets of Thousand Trails, Inc. and subsidiaries as of December 31, 1984 and 1985, and the related statements of earnings, shareholders' equity and changes in financial position for each of the three years in the period ended December 31, 1985. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the consolidated financial statements referred to above present fairly the financial position of Thousand Trails, Inc. and subsidiaries as of December 31, 1984 and 1985, and the results of their operations and the changes in their financial position for each of the three years in the period ended December 31, 1985, in conformity with generally accepted accounting principles applied on a consistent basis.

Touche Ross & Co.

Touche Ross & Co.
Certified Public Accountants
Seattle, Washington
March 6, 1986

Thousand Trails, Inc. and Subsidiaries

Corporate Officers



Thousand Trails, Inc. (left to right): Kathy Hornsby, Vice President and Corporate Secretary; Craig Kirsch, Senior Vice President and Chief Financial Officer; Jim Jensen, Chairman of the Board and Chief Executive Officer; Jim Claus, Vice President, Finance. Not pictured, Julie Brooks, Vice President and General Counsel.



Ron Bidleman, President, Outdoor Enterprises, Inc.* (left); Jerry Andres, President, Happy Trails Resorts, Inc.*



Thousand Trails Resorts, Inc.* (left to right): Bob Mayes, President; Howard Behar, Senior Vice President, Sales and Marketing; Duke Campbell, Senior Vice President, Administration; Don Kent, Vice President, Marketing; Al Schriber, Vice President, Membership Administration.

*Wholly owned subsidiaries of Thousand Trails, Inc.

Directors

Thomas J. Cable
General Partner
Cable, Howse & Ragen, Inc., Seattle, WA

Gary H. Driggs
President & Chief Executive Officer
Western Savings & Loan Association, Phoenix, AZ

Kingdon J. Dunham
The Boeing Company, retired

Jerry D. Horn
Chairman & Chief Executive Officer
General Nutrition Corporation, Pittsburgh, PA

C. James Jensen
Thousand Trails, Inc.

Charles E. Swanson
Encyclopaedia Britannica, Inc., retired

Milton G. Kuolt II
Chairman & Chief Executive Officer
Horizon Air, Seattle, WA

Robert M. Mayes
Thousand Trails, Inc.

J. Paul Meyer
The Boeing Company, retired

James F. Nordstrom
President
Nordstrom, Inc., Seattle, WA

Edwin M. Stanley
Chairman
Management Compensation Group, Portland, OR

J.P. Weyerhaeuser III
Weyerhaeuser Company, retired

Shareholder Information

Annual Meeting
Thursday, June 26
3 p.m.
15325 S.E. 30th Place
Bellevue, WA 98007

Dividend Policy

The Company has paid no cash dividends and anticipates that for the foreseeable future it will continue to retain its earnings for use in the business. The indenture under which the Company's senior subordinated notes were issued limits the payment of cash dividends, and the Company's bank line of credit prohibits the payment of cash dividends without the bank's approval.

Stock Market Activity

The Company's common stock is traded over-the-counter under the symbol TRLS. The following table sets forth the high and low closing bid prices in the NASDAQ National Market System for the Company's common stock as reported by NASDAQ for the fiscal years 1984 and 1985.

Bid	High	Low
1984		
First Quarter	17 $\frac{1}{4}$	13
Second Quarter	21 $\frac{1}{4}$	15 $\frac{3}{4}$
Third Quarter	26 $\frac{1}{8}$	18 $\frac{1}{2}$
Fourth Quarter	28	14 $\frac{3}{8}$
1985		
First Quarter	20 $\frac{1}{8}$	14 $\frac{7}{8}$
Second Quarter	19 $\frac{1}{2}$	13 $\frac{3}{8}$
Third Quarter	15 $\frac{5}{8}$	6 $\frac{3}{4}$
Fourth Quarter	9	5 $\frac{1}{2}$

Transfer Agent and Registrar
The First Jersey National Bank
One Exchange Place
Jersey City, New Jersey 07302

Independent Accountants
Touche Ross & Co.
30th Floor
1111 Third Ave.
Seattle, WA 98101

Corporate Headquarters
15325 SE 30th Place
Bellevue, WA 98007

Form 10-K

The Company files an Annual Report with the Securities and Exchange Commission on Form 10-K, pursuant to the Securities Exchange Act of 1934. Shareholders may obtain a copy of this report without charge by writing:

Craig Kirsch, Chief Financial Officer
Thousand Trails, Inc.
15325 SE 30th Place
Bellevue, WA 98007

Investor Relations Counsel
Kekst and Company
437 Madison Ave.
New York, NY 10022

■ **Thousand Trails, Inc.**

15325 S.E. 30th Place
Bellevue, WA 98007