

WILLAMETTE VALLEY VINEYARDS INC  
Form 10QSB  
August 16, 2004

SECURITIES AND EXCHANGE COMMISSION  
Washington, DC 20549

---

FORM 10-QSB

---

Quarterly Report Pursuant to Section 13 or 15 (d) of the  
Securities Exchange Act of 1934

For the Quarter Ended June 30, 2004

Commission File Number 0-21522

WILLAMETTE VALLEY VINEYARDS, INC.

(Exact name of registrant as specified in charter)

Oregon	93-0981021
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)

---

8800 Enchanted Way, S.E., Turner, Oregon 97392  
(503)-588-9463

(Address, including Zip code, and telephone number,  
including area code, of registrant's principal executive offices)

---

Indicate by check mark whether the registrant (1) has filed, all reports  
required to be filed by Section 13 or 15(d) of the Securities Exchange Act of  
1934 during the preceding 12 months (or for such shorter period that the  
registrant was required to file such reports) and (2) has been subject to such  
filing requirements for the past 90 days.

YES                       NO

Number of shares of common stock outstanding as of June 30, 2004  
4,485,978 shares, no par value

Transitional Small Business Disclosure                       YES                       NO

WILLAMETTE VALLEY VINEYARDS, INC.  
INDEX TO FORM 10-QSB

Part I - Financial Information

# Edgar Filing: WILLAMETTE VALLEY VINEYARDS INC - Form 10QSB

Item 1--Financial Statements

Balance Sheet

Statement of Operations

Statement of Cash Flows

Notes to Consolidated Financial Statements

Item 2--Management's Discussion and Analysis of Financial Condition and Results of Operations

Item 3--Controls and Procedures

Part II - Other Information

Item 1--Exhibits and Reports of Form 8-K

Item 5--Other Information

Signatures

PART 1 FINANCIAL INFORMATION  
ITEM 1

Financial Statements

WILLAMETTE VALLEY VINEYARDS, INC.  
Balance Sheet

	June 30, 2004 (unaudited)	December 31, 2003
<b>ASSETS</b>		
Current assets		
Cash and cash equivalents	\$ 67,876	\$ 213,681
Accounts receivable trade, net	616,206	796,836
Inventories	7,785,779	7,335,378
Prepaid expenses and other current assets	60,909	46,565
Income taxes receivable	-	81,670
Deferred income taxes	174,323	174,323
Total current assets	8,705,093	8,648,453
Vineyard development cost, net	1,700,671	1,698,970
Inventories	552,414	552,414
Property and equipment, net	4,551,972	4,698,915
Notes receivable from officer and other	68,374	66,134
Debt issuance costs, net	60,676	62,805
Other assets	207,416	215,148
Total assets	\$15,846,616	\$15,942,839
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
Current liabilities		

Edgar Filing: WILLAMETTE VALLEY VINEYARDS INC - Form 10QSB

Line of credit	\$ 1,034,407	\$ 1,130,516
Current portion of long-term debt	250,291	250,291
Accounts payable	796,981	752,219
Accrued expenses	445,511	459,219
Income taxes payable	49,108	-
Grapes payable	514,293	669,714
Total current liabilities	<u>3,090,591</u>	<u>3,261,959</u>
Long-term debt	2,559,134	2,693,108
Distributor obligation	1,500,000	1,500,000
Deferred rent liability	120,390	108,995
Deferred gain	387,251	399,743
Deferred income taxes	300,856	300,856
Total liabilities	<u>7,958,222</u>	<u>8,264,661</u>
Shareholders' equity		
Common stock, no par value - 10,000,000 shares authorized, 4,485,978 and 4,479,478 shares issued and outstanding at June 30, 2004 and December 31, 2003	7,181,639	7,167,589
Retained earnings	706,755	510,589
Total shareholders' equity	<u>7,888,394</u>	<u>7,678,178</u>
Total liabilities and shareholders' equity	<u>\$15,846,616</u>	<u>\$15,942,839</u>

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

WILLAMETTE VALLEY VINEYARDS, INC.

Statement of Operations

(unaudited)

	Three months ended June 30,		Six months ended June 30,	
	2004	2003	2004	2003
Net revenues				
Case revenue	\$ 2,096,773	\$ 1,545,706	\$ 3,931,383	\$ 2,883,892
Custom crush-facility lease- bulk revenue	7,041	8,640	16,057	163,815
Total net revenues	<u>2,103,814</u>	<u>1,554,346</u>	<u>3,947,440</u>	<u>3,047,707</u>
Cost of sales				
Case	1,061,808	744,882	1,945,827	1,375,339
Bulk	-	6,324	-	121,611
Total cost of sales	<u>1,061,808</u>	<u>751,206</u>	<u>1,945,827</u>	<u>1,496,950</u>
Gross margin	1,042,006	803,140	2,001,613	1,550,757
Selling, general and administrative expenses	846,570	670,176	1,539,933	1,294,341
Net operating income	<u>195,436</u>	<u>132,964</u>	<u>461,680</u>	<u>256,416</u>
Other income (expense)				
Interest income	1,346	1,313	2,548	2,627
Interest expense	(75,440)	(86,411)	(151,822)	(173,532)
Other income				

Edgar Filing: WILLAMETTE VALLEY VINEYARDS INC - Form 10QSB

(expense)	-	1,076	14,538	26,999
Net income before income taxes	121,342	48,942	326,944	112,510
Income tax	48,537	19,611	130,778	45,038
Net income	72,805	29,331	196,166	67,472
Retained earnings beginning of period	633,950	410,510	510,589	372,369
Retained earnings end of period	\$ 706,755	\$ 439,841	\$ 706,755	\$ 439,841
Basic earnings per common share	\$ .02	\$ .01	\$ .04	\$ .02
Diluted earnings per common share	\$ .02	\$ .01	\$ .04	\$ .02
Weighted average number of basic common shares outstanding	4,485,780	4,474,854	4,484,030	4,473,663
Weighted average number of diluted common shares outstanding	4,567,637	4,474,854	4,565,887	4,473,663

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

WILLAMETTE VALLEY VINEYARDS, INC.

Statement of Cash Flows

(unaudited)

	Six months ended June 30,	
	2004	2003
Cash flows from operating activities:		
Net income	\$ 196,166	\$ 67,472
Reconciliation of net income to net cash provided by (used in) operating activities:		
Depreciation and amortization	325,541	363,721
Loss (gain) on disposal of fixed assets	1,898	(3,004)
Stock issued for compensation	11,500	8,819
Changes in assets and liabilities:		
Accounts receivable trade	180,630	66,817
Inventories	(450,401)	94,242
Prepaid expenses and other current assets	(14,344)	12,173
Note receivable	(2,240)	(2,075)
Other assets	7,732	8,657
Accounts payable	44,762	(135,935)
Accrued commissions and payroll costs	(13,708)	1,640
Income taxes payable	130,778	(24,084)
Grape payables	(155,421)	(303,555)
Deferred rent liability	11,395	11,396
Deferred gain	(12,492)	(12,492)
Net cash provided by operating activities	261,796	153,792

## Edgar Filing: WILLAMETTE VALLEY VINEYARDS INC - Form 10QSB

Cash flows from investing activities;		
Additions to property and equipment	(130,518)	(70,238)
Vineyard development expenditures	(40,462)	(6,057)
Proceeds from the sale of property and equipment	-	15,128
Investments	-	1,000
Net cash used in investing activities	(170,980)	(60,167)
Cash flows from financing activities:		
Debt issuance costs	(9,088)	(12,710)
Net decrease in line of Credit balance	(96,109)	(307,097)
Proceeds from stocks options exercised	2,550	-
Repayments of long-term debt	(133,974)	(129,565)
Net cash used in financing activities	(236,621)	(449,372)
Net decrease in cash and cash equivalents	(145,805)	(355,747)
Cash and cash equivalents:		
Beginning of period	213,681	632,183
End of period	\$ 67,876	\$ 276,436
	=====	=====

The accompanying notes are an integral part of these financial statements.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### 1) BASIS OF PRESENTATION

The accompanying unaudited financial statements as of and for the three and six months ended June 30, 2004 and 2003, have been prepared in conformity with accounting principles generally accepted in the United States. The financial information as of December 31, 2003, is derived from the audited financial statements presented in the Willamette Valley Vineyards, Inc. (the "Company") Annual Report on Form 10-KSB for the year ended December 31, 2003. Certain information or footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted, pursuant to the rules and regulations of the Securities and Exchange Commission. In the opinion of management, the accompanying financial statements include all adjustments necessary (which are of a normal and recurring nature) for the fair presentation of the results of the interim periods presented. The accompanying financial statements should be read in conjunction with the Company's audited financial statements for the year ended December 31, 2003, as presented in the Company's Annual Report on Form 10-KSB.

Operating results for the three and six months ended June 30, 2004, are not necessarily indicative of the results that may be expected for the entire year ending December 31, 2004, or any portion thereof.

The Company has a single operating segment consisting of the retail, in-state self-distribution and out of state sales departments. These departments have similar economic characteristics, offer comparable products to customers, and utilize similar processes for production and distribution.

Basic earnings per share are computed based on the weighted-average number of common shares outstanding each period. Diluted earnings per share are computed using the weighted average number of shares of common stock and dilutive common equivalent shares outstanding during the year. Common equivalent shares from

## Edgar Filing: WILLAMETTE VALLEY VINEYARDS INC - Form 10QSB

stock options and other common stock equivalents are excluded from the computation when their effect is anti-dilutive. There were total common stock equivalent shares of 81,857 shares included in the computation of dilutive earnings per share for the three and six-month period ended June 30, 2004. Options to purchase shares of common stock outstanding at June 30, 2003 were not included in the computation of diluted earnings per share for the three and six-month period ended June 30, 2003 because the exercise prices were greater than fair value.

### 2) STOCK BASED COMPENSATION

The Company accounts for the employee and director stock options in accordance with provisions of Accounting Principles Board (APB) Opinion No. 25, Accounting for Stock Issued to Employees. Pro forma disclosures as required under SFAS No. 123, Accounting for Stock Based Compensation, and as amended by SFAS No. 148, Accounting for Stock Based Compensation - Transition and Disclosure, are presented below.

Had compensation cost for the Company's stock option plans been determined based on the fair value at the grant date for awards consistent with the provisions of SFAS No. 123, the Company's net earnings would have been reduced to the pro forma amounts indicated as follows for the three and six months ended June 30:

		Three months ended June 30, 2004 (unaudited)	2003 (unaudited)	Six months ended June 30, 2004 (unaudited)	2003 (unaudited)
		_____	_____	_____	_____
Net income, as reported	\$	72,805	\$ 29,331	\$ 196,166	\$ 67,472
Add stock-based employee compensation expense included in reported net income, net of related tax effects		-	-	11,500	8,819
Deduct total stock based employee compensation expense determined under fair value based method for all awards, net of related tax effects		(5,124)	(5,948)	(18,033)	(20,715)
Pro forma net income	\$	67,681	\$ 23,383	\$ 189,633	\$ 55,576
Earnings per share:					
Basic -					
as reported	\$	0.02	\$ 0.01	\$ 0.04	\$ 0.02
Basic - pro forma	\$	0.02	\$ 0.01	\$ 0.04	\$ 0.01
Diluted -					
as reported	\$	0.02	\$ 0.01	\$ 0.04	\$ 0.02
Diluted - pro forma	\$	0.01	\$ 0.01	\$ 0.04	\$ 0.01

## Edgar Filing: WILLAMETTE VALLEY VINEYARDS INC - Form 10QSB

For purposes of disclosure, the Black-Scholes option pricing model was used to calculate fair values for stock options granted. The estimated fair value of the options is amortized to expense over the options' vesting period.

### 3) INVENTORIES BY MAJOR CLASSIFICATION ARE SUMMARIZED AS FOLLOWS:

	June 30, 2004 (unaudited)	December 31, 2003
	<u>                    </u>	<u>                    </u>
Winemaking and packaging materials	\$ 140,181	\$ 80,886
Work-in-progress (costs relating to unprocessed and/or bulk wine products)	2,136,742	1,982,469
Finished goods (bottled wines and related products)	6,061,270	5,824,437
	<u>8,338,193</u>	<u>7,887,792</u>
Less: amounts designated for distributor	(552,414)	(552,414)
	<u>                    </u>	<u>                    </u>
Current inventories	\$ 7,785,779	\$ 7,335,378
	=====	=====

### 4) PROPERTY AND EQUIPMENT CONSIST OF THE FOLLOWING:

	June 30, 2004 (unaudited)	December 31, 2003
	<u>                    </u>	<u>                    </u>
Land and improvements	\$ 984,256	\$ 976,838
Winery building and hospitality center	4,647,272	4,577,467
Equipment	4,979,294	4,933,329
	<u>10,610,822</u>	<u>10,487,634</u>
Less accumulated depreciation	(6,058,850)	(5,788,719)
	<u>                    </u>	<u>                    </u>
	\$ 4,551,972	\$ 4,698,915
	=====	=====

### 5) SUBSEQUENT EVENTS:

None.

## ITEM 2

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

#### Forward Looking Statement:

This Management's Discussion and Analysis of Financial Condition and Results of Operation and other sections of this Form 10-QSB contain forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These forward-looking statements involve risks and uncertainties that are based on current expectations, estimates and projections about the Company's business, and beliefs and assumptions made by management. Words such as "expects," "anticipates," "intends," "plans," "believes," "seeks,"

## Edgar Filing: WILLAMETTE VALLEY VINEYARDS INC - Form 10QSB

"estimates" and variations of such words and similar expressions are intended to identify such forward-looking statements. Therefore, actual outcomes and results may differ materially from what is expressed or forecasted in such forward-looking statements due to numerous factors, including, but not limited to: availability of financing for growth, availability of adequate supply of high quality grapes, successful performance of internal operations, impact of competition, changes in wine broker or distributor relations or performance, impact of possible adverse weather conditions, impact of reduction in grape quality or supply due to disease, impact of governmental regulatory decisions, and other risks detailed below as well as those discussed elsewhere in this Form 10-QSB and from time to time in the Company's Securities and Exchange Commission filings and reports. In addition, such statements could be affected by general industry and market conditions and growth rates, and general domestic economic conditions.

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

#### Overview

Revenues increased in the three and six months ended June 30, 2004 compared to the prior year period, particularly in the six month period where total revenue increased 30%. This was due primarily to increased sales through the Bacchus Fine Wines and out of state sales departments. While total costs of sales and selling, general and administrative expenses also increased in both the three and six months periods, net operating income increased approximately 47% for the three months ended June 30, 2004 and 80% for the six months ended June 30, 2004, compared in each case to the prior year period. Net income before taxes increased 148% and 191% for the three and six month periods ended June 30, 2004 compared to the prior year periods and earnings per share doubled in each of the three and six month periods ended June 30, 2004 compared to the prior year period. This was due entirely to the increase in our net revenue for those periods.

We expect revenues to increase in the future because of the continued growth of Bacchus Fine Wines. We also expect total costs of sales and selling, general and administrative expense to increase.

The Company has hired a viticulture consultant to improve vineyard care and increase wine quality. The winemaker and vineyard manager have spent one day each week with her this quarter, resulting in a number of vineyard improvements including using straw under the vine rows to increase natural soil nutrition and as well as using other organic methods of improving vine health. These activities have resulted in higher per acre costs. We believe these higher costs will be offset by increased quality of grapes, which should result in our wines demanding premium pricing, and increasing revenues.

The gross margin is higher than expected, elevating profitability. As our distribution in Oregon of wines produced by others grows, we expect this gross margin to fall. Therefore, we believe conclusions should not be drawn by this Quarter's favorable gross margin.

Also in this quarter, the Company favorably resolved its review of invoices to the out-of-state distribution network and bill-backs received by this network and credits taken against Company invoices by this network. This review resulted in the reduction of sample and sales allowance expenses and thereby providing a one time increase in profitability in this quarter.

As a result of the Sarbanes-Oxley Act and accompanying regulations relating to public company financial reporting, we are expecting to incur significantly greater costs, including accounting, legal and consulting fees in the future. We anticipate these fees will reduce the Company's profitability in future



## Edgar Filing: WILLAMETTE VALLEY VINEYARDS INC - Form 10QSB

periods.

Revenues from Bacchus Fine Wines, the Company's wholesale wine distribution department, increased 54% in the 2nd Quarter of 2004 compared to the same period in 2003. At the same time, expenses attributable to Bacchus' operations increased at a higher rate(68%) and exceeded planned expenses for the three months ended June 30, 2004 compared to the prior year period. We believe we are in an infrastructure building stage, which will be supported by increased sales in the future, thereby spreading these new fixed costs over greater volume and increasing profitability. Sales of Company produced products through Bacchus Fine Wines increased 8% and sales of products produced by other wineries increased 570% in the three months ended June 30, 2004 compared to the prior year period.

Out-of-state sales to distributors increased 36% for the three months ended June 30, 2004 compared to the prior year period with lower selling costs than in the comparable prior year period, as well as budget. The unusual sale of the remaining stock of 2002 Pinot gris to United Airlines for its First Class Cabin wine service on international and transcontinental flights in the three months ended June 30, 2004 contributed to these positive results. This same wine was named in USA Today as one of the top white wines of summer, in an article written March 26, 2004, titled, "The Pours of Summer". We believe the Company will need to increase sales expenses, in particular out-of-state travel to distributor markets, to increase retail and restaurant account calls to remain competitive with other wine producers. These additional costs could reduce future profitability.

Retail revenues were down 6% in the three months ended June 30, 2004 compared to the prior year period due primarily to lower direct sales made by the Company's key customer sales representatives. Staff turnover with vacancies in these positions is the primary reason for these lower sales. Higher tasting room sales in the three months ended June 30, 2004 compared to the prior year period did not completely offset the direct sale revenue reductions. Results have improved at the Tualatin winery as compared to the prior year since we leased a portion of the facility to our former head winemaker which generated rent income of \$6,909 and \$15,924, respectively for the three and six months ended June 30, 2004.

The Company's wines continued to receive strong reviews from prominent reviewers. Willamette Valley Vineyards 2003 Pinot gris received an "Exceptional" rating from renowned wine critic Dan Berger and was awarded the "Sweepstakes White" wine, one of the top awards from among 1,600 wines submitted at the Long Beach Grand Cru.

### RESULTS OF OPERATIONS

#### Revenue

The Company's revenues are summarized as follows:

	Three months ended June 30,		Six months ended June 30,	
	2004	2003	2004	2003
Tasting Room Sales and Rental Income	\$ 331,363	\$ 351,414	\$ 659,122	\$ 647,081
On-site and off-site festivals	11,766	21,826	61,735	64,997
In state sales	1,171,162	758,465	2,072,989	1,348,997
Out of state sales	649,470	478,770	1,246,648	926,806
Bulk wine/				

Edgar Filing: WILLAMETTE VALLEY VINEYARDS INC - Form 10QSB

Misc. sales	7,041	8,640	16,057	163,815
Total Revenue	<u>2,170,802</u>	<u>1,619,115</u>	<u>4,056,551</u>	<u>3,151,696</u>
Less Excise Taxes	66,988	64,769	109,111	103,989
Net Revenue	<u>\$ 2,103,814</u>	<u>\$ 1,554,346</u>	<u>\$ 3,947,440</u>	<u>\$ 3,047,707</u>
	=====	=====	=====	=====

Tasting room and retail sales, and rental income for the three months ending June 30, 2004 decreased 6% to \$331,363 in 2004 from \$351,414 for the comparable period in 2003. For the six months ended June 30, 2004 sales increased 2% over the comparable prior year period. Tasting room and retail sales decreased during the second quarter of 2004 due in part to staff turnover and vacancies in key customer sales.

On-site and off-site festival sales for the three months ended June 30, 2004 decreased 46% to \$11,766 from \$21,826 compared to the prior year period, and decreased 5% for the six months ended June 30, 2004 compared to the prior year period. These decreases are due primarily to the continuing focus away from on-site and off-site events, in favor of telephone, mail order and retail sales.

Sales in the state of Oregon, through the Company's independent sales force and through direct sales from the winery, increased 54% to \$1,171,162 in the three months ended June 30, 2004 from \$758,465 as compared to the prior year period. Sales through the Company's independent sales force alone for the three months ended June 30, 2004 increased 60% to \$949,675 from \$593,566 from the comparable prior year period. The Company's direct instate sales to our largest customer increased 153% to \$193,067 from \$76,328 in the three months ended June 30, 2004 compared to the prior year period. These increases are largely the result of the improved sales management and broader product lines presented through the development of Bacchus Fine Wines.

Out-of-state sales in the three months ended June 30, 2004 increased 36% to \$649,470 from \$478,770 compared to the prior year period. During the six months ended June 30, 2004, sales increased 35% compared to the prior year period. The higher sales are a result of increased promotional allowances offered to distributors by the Company that are resulting in higher depletions by the Company's distributors.

Excise taxes

The Company's excise taxes increased in the three months ended June 30, 2004 to \$66,988 from \$64,769 compared to the prior year period, and increased to \$109,111 from \$103,689 for the six months ended June 30, 2004 compared to the prior year period. This was due largely to the increased sales in the three months ended June 30, 2004, increasing overall sales volumes and taxes paid by volume.

In February and March of 2004, the Alcohol and Tobacco Tax and Trade Bureau of the U.S. Treasury Department audited the Company's excise tax. The preliminary result of this audit was back excise taxes due principally to the Company's incorrect application of the federal small winery tax credit. Congress previously increased wine taxes from 17 cents to \$1.07 per gallon but provided a 90-cent exemption for small wineries on the first 100,000 gallons produced. This credit declines when production surpasses 150,000 gallons by 1% for every additional 1,000 gallons. The Company's error in the application of this credit may also result in penalty and interest assessments due in part to the requirement that tax returns must be accurately filed every two weeks. Although sales declined in 2002, the tax rate on those sales actually rose due to the processing of the large amount of grape tonnage in the past several

## Edgar Filing: WILLAMETTE VALLEY VINEYARDS INC - Form 10QSB

years. Although the exact amount of any back taxes, accrued interest and penalties, if any, is not known, we included in accrued expenses for December 31, 2003 and June 30, 2004, an estimate of \$80,000 in relation to expected back excise taxes due.

### Gross Margin

As a percentage of net revenue, gross margin decreased to 50% in the three months ended June 30, 2004 as compared to 52% in the comparable prior year period. Gross margin for the six months ended June 30, 2004 and the comparable prior year period was approximately 51%. While the Company is continuing its focus on, and improved distribution of, higher margin products, as well as continuing to reduce grape and production costs, we anticipate the Company's increased representation of brands other than its own through its Oregon sales force will further erode the gross margins due to the lower margins associated with selling those brands.

### Selling, General and Administrative Expense

Selling, general and administrative expenses increased to \$846,570 in the three months ended June 30, 2004 from \$670,176 in the comparable prior year period. Selling, general and administrative expenses increased to \$1,539,933 for the six months ended June 30, 2004 from \$1,294,341 for the comparable prior year period. As a percentage of net revenue from winery operations, selling, general and administrative expenses decreased to 40% in the three months ended June 30, 2004 from 43% in the comparable prior year period, and to 39% in the six months ended June 30, 2004 from 42% in the comparable prior year period, primarily as a result of increased revenues.

### Interest Income, Other Income and Expense

Interest income increased to \$1,346 for the three months ended June 30, 2004 from \$1,313 for the comparable prior year period. Interest expense decreased to \$75,440 for the three months ended June 30, 2004 compared to \$86,411 in the comparable prior year period. Interest income decreased to \$2,548 the six months ended June 30, 2004 compared to \$2,627 for the comparable prior year period. Interest expense decreased to \$151,822 for the six months ended June 30, 2004 compared to \$173,532 in the comparable prior year period. Interest costs were lower primarily due to less debt outstanding during the period.

The Company's other income is summarized as follows:

	Three months ended June 30, 2004	2003	Six months ended June 30, 2004	2003
	_____	_____	_____	_____
Gain on Tualatin bare land sale	\$ -	\$ -	\$ -	\$ 3,004
Farm Credit interest rebate	-	-	14,504	22,617
Miscellaneous rebates	-	1,076	34	1,378
	_____	_____	_____	_____
Other income (expense)	\$ -	\$ 1,076	\$ 14,538	\$ 26,999

### Income Taxes

## Edgar Filing: WILLAMETTE VALLEY VINEYARDS INC - Form 10QSB

As the Company experienced a net profit for the three and six months ended June 30, 2004, we accrued \$48,537 in income tax expense for the three months ended June 30, 2004, making the total accrued \$130,778 for the six months ended June 30, 2004. The Company's estimated tax rate for the three and six months ended June 30, 2004 was 40 percent.

### Liquidity and Capital Resources

At June 30, 2004, the Company had a working capital balance of \$5.6 million and a current ratio of 2.82:1. At December 31, 2003, the Company had a working capital balance of \$5.4 million and a current ratio of 2.65:1. The Company had a cash balance of \$67,876 at June 30, 2004.

Total cash provided by operating activities in the six months ended June 30, 2004 was \$261,796 compared to \$153,792 in the prior year period. Cash provided by operating activities in the six months ended June 30, 2004 was comprised of net income of \$196,166 plus depreciation of \$325,541 less changes in assets and liabilities and other non-cash charges of \$259,911. Cash provided by operating activities in the six months ended June 30, 2003 was comprised of net income of \$67,472 plus depreciation of \$363,721 less changes in assets and liabilities and other non-cash charges of \$277,401.

Total cash used in investing activities in the six months ended June 30, 2004 was \$170,980 compared to \$60,167 in the prior year period. Cash used in investing activities comprised of property and equipment additions and vineyard development costs.

Total cash used in financing activities in the six months ended June 30, 2004 was \$236,621 compared to \$449,372 in the prior year period. Cash used in financing activities was primarily comprised of payments on the long term debt (2004 \$133,974 and 2003 \$129,565) and payments on the line of credit (2004 \$96,109 and 2003 \$307,097).

At June 30, 2004, the line of credit balance was \$1,034,407 compared to \$1,130,516 on December 31, 2003. The Company's loan agreement with GE Commercial Distribution Finance Corporation contains certain restrictive financial covenants with respect to total equity, debt-to-equity and debt coverage, which must be maintained by the Company on a quarterly basis. As of June 30, 2004, the Company was in compliance with all of the financial covenants.

As of June 30, 2004, the Company had a total long-term debt balance of \$2,809,425 owed primarily to Farm Credit Services. This debt was used to finance the Hospitality Center, invest in winery equipment to increase the Company's winemaking capacity, complete the storage facility, and purchase Tualatin Vineyards.

At June 30, 2004, the Company owed \$514,293 on grape contracts. A large portion is owed to a single grape grower, which will be paid as the wine made from those grapes is sold.

The Company believes that cash flow from operations and funds available under credit facilities will be sufficient to meet the Company's liquidity requirements for the next 12 months.

### Critical Accounting Policies:

The discussion and analysis of our financial condition and results of operations are based upon our financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets,

## Edgar Filing: WILLAMETTE VALLEY VINEYARDS INC - Form 10QSB

liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. On an on-going basis, we evaluate our estimates, including those related to revenue recognition, collection of accounts receivable, valuation of inventories, and amortization of vineyard development costs. We base our estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances. Actual results may differ from these estimates under different assumptions or conditions. A description of our critical accounting policies and related judgments and estimates that affect the preparation of our financial statements is set forth in our Annual Report on Form 10-KSB for the year ended December 31, 2003.

### ITEM 3

#### Controls and Procedures

a) We carried out an evaluation, under the supervision and with the participation of the Chief Executive Officer, Chief Financial Officer and other management personnel, of the effectiveness of our disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) of the Securities and Exchange Act of 1934. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that the our disclosure controls and procedures as of June 30, 2004 were effective to ensure that information required to be disclosed by the Company in reports that it files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission's rules and forms.

The Company does not expect that its disclosure controls and procedures will prevent all error and all fraud. A control procedure, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control procedure are met. Because of the inherent limitations in all control procedures, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the control. The Company considered these limitations during the development of it disclosure controls and procedures, and will continually reevaluate them to ensure they provide reasonable assurance that such controls and procedures are effective.

b) There were no changes in the Company's internal control procedures over financial reporting that occurred during the three months ended June 30, 2004 that have materially affected, or are reasonably likely to materially affect, the our internal control over financial reporting.

### PART II.

#### OTHER INFORMATION

#### Item 1

##### Exhibits and Reports on Form 8-K.

a) The exhibits filed herewith are listed in the Exhibit Index following the signature page of this report.

b) No reports on Form 8-K were filed during the three months ended June 30, 2004.

### ITEM 5

#### Other Information

Non-Audit Fees:

