



CERTIFIED PUBLIC ACCOUNTANT

BRADFORD G. BENTON

Independent Auditor's Report

Board of Directors
Park Paseo Homeowners Association:

We have audited the accompanying balance sheet of Park Paseo Homeowners Association as of December 31, 2003, and the related statements of revenues and expenses and changes in fund balances, and cash flows for the year then ended. These financial statements are the responsibility of the Association's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Park Paseo Homeowners Association as of December 31, 2003 and the results of its operations and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The supplementary information on future major repairs and replacements on page 7 is not a required part of the basic financial statements but is supplementary information required by the American Institute of Certified Public Accountants. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

A handwritten signature in cursive script that reads "Bradford G. Benton".

February 12, 2004

PARK PASEO HOMEOWNERS ASSOCIATION

BALANCE SHEET

DECEMBER 31, 2003

ASSETS

	Operating Fund	Replace- ment Fund	Total
<u>Assets</u>			
Cash and cash equivalents	\$ 176,754	\$ 4,261	\$ 181,015
Investments	93,553	416,389	509,942
Assessments receivable	3,902		3,902
Interest receivable	1,354		1,354
Prepaid income taxes	1,525		1,525
Total assets	<u>\$ 277,088</u>	<u>\$420,650</u>	<u>\$ 697,738</u>

LIABILITIES AND FUND BALANCES

<u>Liabilities</u>			
Accounts payable	\$ 4,867	\$ -	\$ 4,867
Prepaid assessments	12,200		12,200
Total liabilities	<u>17,067</u>	<u>-</u>	<u>17,067</u>
<u>Fund balance</u>			
Accumulated excess of revenues over expenses	272,993	420,650	693,643
Accumulated other comprehensive income			
Net unrealized losses on investment (Franklin Fund)	<u>(12,972)</u>	<u></u>	<u>(12,972)</u>
Total fund balance	<u>260,021</u>	<u>420,650</u>	<u>680,671</u>
Total liabilities and fund balance	<u>\$ 277,088</u>	<u>\$420,650</u>	<u>\$ 697,738</u>

See accompanying notes to financial statements.

PARK PASEO HOMEOWNERS ASSOCIATION

STATEMENT OF REVENUES AND EXPENSES AND

CHANGES IN FUND BALANCES

For the year ended December 31, 2003

	Operating Fund	Replace- ment Fund	Total
<u>Revenues</u>			
Member assessments	\$ 396,669	\$ 60,831	\$ 457,500
Interest	12,452		12,452
Late charges and lien fees	5,649		5,649
Other charges to owners	9,299		9,299
Other	6,797	528	7,325
Total revenues	<u>430,866</u>	<u>61,359</u>	<u>492,225</u>
<u>Expenses</u>			
Utilities	51,373		51,373
Landscape maintenance	164,166		164,166
Pool and spa	20,122		20,122
Lifeguards	18,784		18,784
Common areas	37,260	25,164	62,424
Security	46,867		46,867
Management fees	56,184		56,184
Insurance	15,828		15,828
Legal and professional	7,152	8,460	15,612
Income taxes	4,216		4,216
Print, postage, & supplies	10,674		10,674
Newsletter	2,828		2,828
Other	6,264		6,264
Total expenses	<u>441,718</u>	<u>33,624</u>	<u>475,342</u>
Excess of revenues over expenses	(10,852)	27,735	16,883
Beginning fund balances	<u>283,845</u>	<u>392,915</u>	<u>676,760</u>
ENDING FUND BALANCES	<u><u>\$ 272,993</u></u>	<u><u>\$ 420,650</u></u>	<u><u>\$ 693,643</u></u>

See accompanying notes to financial statements.

PARK PASEO HOMEOWNERS ASSOCIATION

STATEMENT OF CASH FLOWS

For the year ended December 31, 2003

	Operating Fund	Replace- ment Fund	Total
Excess (deficiency) of revenues over expenses	\$ (10,852)	\$ 27,735	\$ 16,883
Adjustments to reconcile excess (deficiency) of revenues over expenses to net cash provided (used) by operating activities:			
(Increase)/Decrease in:			
Assessments receivable	3,184		3,184
Interest receivable	1,542		1,542
Prepaid income taxes	629		629
Increase/(Decrease) in:			
Accounts payable	(11)		(11)
Prepaid assessments	7,947		7,947
Income taxes payable	-		-
Total adjustments	<u>13,291</u>	<u>-</u>	<u>13,291</u>
Net cash provided (used) by operating activities	2,439	27,735	30,174
Cash flows from investing activities:			
Purchase of investments (CDs)	80,373	(28,469)	51,904
Net unrealized loss on investment	<u>(3,099)</u>		<u>(3,099)</u>
Net increase/(decrease) in cash and cash equivalents	79,713	(734)	78,979
Cash and cash equivalents at beginning of year	<u>97,041</u>	<u>4,995</u>	<u>102,036</u>
Cash and cash equivalents at end of year	<u>\$ 176,754</u>	<u>\$ 4,261</u>	<u>\$ 181,015</u>

See accompanying notes to financial statements.

PARK PASEO HOMEOWNERS ASSOCIATION

NOTES TO FINANCIAL STATEMENTS

1. Organization and Summary of Significant Accounting Policies

a) Organization

Park Paseo Homeowners Association (the Association) was organized as a nonprofit corporation in 1977 in the state of California. Its purpose is to provide management and maintenance of the common areas within the development, which is located in the city of Irvine, California. The development consists of 625 single family dwellings.

b) Fund Accounting

The Association's operations are segregated between operating funds and replacement funds. The operating fund is used to account for normal maintenance and service operations related to the common area. Disbursements from the operating fund are generally at the discretion of the Board of Directors. The replacement fund is utilized to account for the long-term major repair and replacement requirements of the Association. Disbursements from the replacement fund may be made only for their designated purpose.

c) Property and Equipment

Real property and common areas acquired from the developer and related improvements to such property are not recorded in the Association's financial statements.

d) Interest Earned

The Association's policy is to allocate to the operating fund interest earned on all replacement fund cash and investment accounts.

e) Cash and Cash Equivalents

Certificates of deposit with a maturity of three months or less at the time of purchase are considered to be cash equivalents. Those with a maturity over three months at the time of purchase are classified as investments.

f) Use of Estimates

Management uses estimates and assumptions in preparing financial statements in accordance with generally accepted accounting principles. Those estimates and assumptions affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, and the reported revenues and expenses. Actual results could vary from the estimates that were used.

g) FDIC Insurance Limits

The Association funds on deposit at financial institutions did not exceed the \$100,000 federally insured limit during the period.

PARK PASEO HOMEOWNERS ASSOCIATION

NOTES TO FINANCIAL STATEMENTS

2. Summary of Cash and Cash Equivalents at December 31, 2003

<u>Bank</u>	<u>Interest Rate</u>	<u>Maturity Date</u>	<u>Operating Fund</u>	<u>Replacement Fund</u>	<u>Total</u>
Cash and cash equivalents consist of:					
Washington Mutual:					
Checking	0.22%		\$ 52,372	\$ -	\$ 52,372
Savings	1.04%		16,105		16,105
Wells Fargo			14,680		14,680
Petty Cash			500		500
Smith Barney:					
Money Fund	0.94%		93,097	4,261	97,358
Total cash and equivalents			<u>\$176,754</u>	<u>\$ 4,261</u>	<u>\$ 181,015</u>
Investments consist of the following:					
Franklin Adjustable US Govt. Securities					
Fund - at current value (a) (b)		N/A	\$ -	\$166,389	\$ 166,389
World Savings	2.08%	06/16/04	93,553		93,553
Smith Barney CDs:					
PNB Financial	1.50%	04/08/04		80,000	80,000
Western Bank	1.25%	07/09/04		80,000	80,000
Edward Jones:					
Bank of Russell County	1.70%	01/14/05		90,000	90,000
Total investments			<u>\$ 93,553</u>	<u>\$416,389</u>	<u>\$ 509,942</u>

(a) The investment in the Franklin Adjustable U S Government Securities Fund is recorded at fair market value. The corresponding unrealized gain or loss in the fair market value in relation to cost is accounted for as a separate item in the fund balance section of the balance sheet.

(b) This is a mutual fund that invests primarily in adjustable-rate, mortgage-backed securities, or other securities collateralized by, or representing an interest in, mortgages, issued or guaranteed by the U.S. government, its agencies or instrumentalities.

3. Owners' Assessments

Monthly assessments to owners during 2003 were \$61.00. Of this amount, \$8.09 was allocated to the replacement fund during the year. At December 31, 2003 all assessments receivable were deemed to be collectible.

The annual budget and owners' assessments were determined by the Board of Directors. Currently, the Association retains excess operating funds at the end of the operating year, if any, for use in future operating periods.

PARK PASEO HOMEOWNERS ASSOCIATION

NOTES TO FINANCIAL STATEMENTS

4. Future Major Repairs and Replacements

The Association has established a policy of assessing members monthly and accumulating funds based on current estimated replacement costs. Accumulated funds are held in separate savings accounts and are generally not available for expenditures for normal operations.

In November 2003 the Association retained an independent company, which specializes in conducting reserve studies, to estimate the remaining useful lives and the replacement costs of the components of common property. The estimates were based on current estimated replacement costs. The study concluded that the Association's funds available for reserves at December 31, 2003 were adequate. The table included in the unaudited supplementary information of Future Major Repairs and Replacements is based on the study.

The Board of Directors has included \$71,479 in the 2004 budget for reserves, which is the amount recommended by the study referred to above.

Funds are being accumulated in the replacement fund based on estimates of future needs for repairs and replacements of common property components. Actual expenditures may vary from the estimated future expenditures, and the variations may be material. Therefore, amounts accumulated in the replacement fund may not be adequate to meet all future needs for major repairs and replacements. If additional funds are needed, the Association has the right to increase regular assessments, pass special assessments, or delay major repairs and replacements until funds are available.

5. Income Taxes

Homeowners' associations may be taxed either as homeowners' associations or as regular corporations. As a regular corporation, membership income is exempt from taxation if certain elections are made, and the Association is taxed only on its nonmembership income, such as interest earnings, at regular federal and state corporate rates. Under the homeowners' association election, the Association is taxed on its nonexempt function income, such as interest earnings, at a flat rate of 30% for federal and the regular corporate rate for state. Exempt function income, which consists primarily of member assessments, is not taxable.

For the year ended December 31, 2003 the Association filed as a homeowner association.

Income taxes consist of:

	<u>Federal</u>	<u>State</u>	<u>Total</u>
Income taxes	\$ 3,109	\$ 1,107	\$ 4,216
less payments made	<u>(3,970)</u>	<u>(1,771)</u>	<u>(5,741)</u>
Balance due (prepaid)	<u>\$ (861)</u>	<u>\$ (664)</u>	<u>\$ (1,525)</u>