

**APR 16 2012**  
**2012**

**NOTICE**

**DATE:** April 12, 2012

**TO:** Park Paseo Homeowners Association  
Membership

**FROM:** Park Paseo Homeowners Association  
Board of Directors

**RE:** Audit

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Enclosed, please find the audited financial statements as prepared by Inouye, Shively & Longtin for the Park Paseo Homeowners Association, for the fiscal year ending December 31, 2011. Please file these documents with the rest of your Association paperwork.



Member:  
American Institute  
of Certified Public  
Accountants

Member:  
California Society  
of Certified Public  
Accountants

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## INDEPENDENT AUDITOR'S REPORT

To the Board of Directors and Members of  
Park Paseo Homeowners Association

We have audited the accompanying balance sheet of Park Paseo Homeowners Association as of December 31, 2011, and the related statements of revenues, 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 audit.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Park Paseo Homeowners Association as of December 31, 2011, 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.

As discussed in Note 4 to the financial statements, the Board of Directors is funding for major repairs and replacements based on recommendations of a study conducted to determine current estimates of major repairs and replacements that may be required in the future. Because actual expenditures may vary from estimated future expenditures, it is not presently determinable whether amounts accumulated in the replacement fund will be adequate to meet all future needs for major repairs and replacements.

To the Board of Directors and Members of  
Park Paseo Homeowners Association

Accounting principles generally accepted in the United States of America require that the supplementary information on future major repairs and replacements on page 9 be presented to supplement the basic financial statements. Such information, although not part of the basic financial statements, is required by the Financial Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or any other form of assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or any other form of assurance.

Inouye, Shively & Longtin

*Inouye, Shively & Longtin*

Laguna Hills, California  
April 9, 2012

**PARK PASEO HOMEOWNERS ASSOCIATION  
BALANCE SHEET  
AS OF DECEMBER 31, 2011**

	Operating Fund	Replacement Fund	Total
<b>Assets</b>			
Cash and cash equivalents	\$ 133,720	\$ 211,937	\$ 345,657
Short-term investments	-	348,528	348,528
Assessments receivable	10,118	-	10,118
Interest receivable	-	659	659
Prepaid expenses	15,149	-	15,149
Interfund account	(95,591)	95,591	-
<b>Total assets</b>	<b>63,396</b>	<b>656,715</b>	<b>720,111</b>
<b>Liabilities</b>			
Accounts payable	16,261	-	16,261
Prepaid assessments	11,110	-	11,110
Income taxes payable	373	-	373
	27,744	-	27,744
Accumulated excess revenues over expenses	47,526	656,715	704,241
Accumulated other comprehensive income - Unrealized loss on investments	(11,874)	-	(11,874)
<b>Fund balances</b>	<b>35,652</b>	<b>656,715</b>	<b>692,367</b>
<b>Total liabilities and fund balances</b>	<b>\$ 63,396</b>	<b>\$ 656,715</b>	<b>\$ 720,111</b>

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THE FINANCIAL STATEMENTS.

**PARK PASEO HOMEOWNERS ASSOCIATION  
STATEMENT OF REVENUES AND EXPENSES  
AND CHANGES IN FUND BALANCES  
FOR THE YEAR ENDED DECEMBER 31, 2011**

	Operating Fund	Replacement Fund	Total
<b>Revenues</b>			
Member assessments	\$ 481,020	\$ 141,480	\$ 622,500
Interest income	-	3,422	3,422
Laundry income	6,476	-	6,476
Other income	25,324	-	25,324
<b>Total revenues</b>	<b>512,820</b>	<b>144,902</b>	<b>657,722</b>
<b>Expenses</b>			
Property protection	51,484	-	51,484
Landscape	164,289	-	164,289
Custodial	8,027	-	8,027
Pool maintenance	35,206	1,232	36,438
General maintenance and repairs	46,811	-	46,811
Electricity	26,853	-	26,853
Water	26,048	-	26,048
Gas	11,635	-	11,635
Management fees	34,330	-	34,330
General manager payroll	64,634	-	64,634
Accounting	2,810	-	2,810
Legal and collection	3,378	-	3,378
Insurance	17,240	-	17,240
Refuse collection	1,357	-	1,357
Pest control	957	-	957
Printing and postage	8,989	-	8,989
Reserve analysis	1,700	-	1,700
General and administrative	7,521	-	7,521
Fencing	-	4,170	4,170
Clubhouse	-	23,140	23,140
Trellis	-	42,124	42,124
Recreation areas	-	18,527	18,527
Income taxes	1,077	195	1,272
<b>Total expenses</b>	<b>514,346</b>	<b>89,388</b>	<b>603,734</b>
<b>Excess (deficiency) of revenues over expenses</b>	<b>(1,526)</b>	<b>55,514</b>	<b>53,988</b>
<b>Beginning fund balances</b>	<b>49,052</b>	<b>601,201</b>	<b>650,253</b>
<b>Ending fund balances</b>	<b>\$ 47,526</b>	<b>\$ 656,715</b>	<b>\$ 704,241</b>

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THE FINANCIAL STATEMENTS.

**PARK PASEO HOMEOWNERS ASSOCIATION  
STATEMENT OF CASH FLOWS  
FOR THE YEAR ENDED DECEMBER 31, 2011**

	Operating Fund	Replacement Fund	Total
<b>Cash flows from operating activities</b>			
Excess (deficiency) of revenues over expenses	\$ (1,526)	\$ 55,514	\$ 53,988
Adjustments to reconcile excess (deficiency) of revenues over expenses to net cash provided by (used in) operating activities			
Recovery of bad debts	(6,476)	-	(6,476)
Increase in assessments receivable	(299)	-	(299)
Decrease in other receivable	9,072	-	9,072
Decrease in accrued interest receivable	-	17	17
Increase in prepaid expenses	(14,535)	-	(14,535)
Increase in accounts payable	3,932	-	3,932
Decrease in accounts payable	-	(4,954)	(4,954)
Decrease in prepaid assessments	(11,240)	-	(11,240)
Increase in income tax payable	373	-	373
Total adjustments	(19,173)	(4,937)	(24,110)
Net cash provided by (used in) operating activities	(20,699)	50,577	29,878
<b>Cash flows from investing activities</b>			
Proceeds from disposition of short-term investments	-	44,153	44,153
Net cash provided by investing activities	-	44,153	44,153
<b>Cash flows from financing activities</b>			
Change in interfund payable balances	37,224	(37,224)	-
Net cash provided by (used in) financing activities	37,224	(37,224)	-
Net increase in cash and cash equivalents	16,525	57,506	74,031
Cash and cash equivalents at beginning of year	117,195	154,431	271,626
Cash and cash equivalents at end of year	\$ 133,720	\$ 211,937	\$ 345,657
Income taxes paid	\$ 113	\$ -	\$ 113

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THE FINANCIAL STATEMENTS.

**PARK PASEO HOMEOWNERS ASSOCIATION**  
**NOTES TO FINANCIAL STATEMENTS**  
**DECEMBER 31, 2011**

**NOTE 1 - ORGANIZATION**

Park Paseo Homeowners Association ("Association") is a nonprofit mutual benefit corporation organized for the purposes of maintaining and preserving common property of the Park Paseo community. The Association consists of 625 residential units occupying a site in Irvine, California. The Association was incorporated on June 9, 1977.

**NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

- (a) Principles of Accounting: The books and records for the Association are maintained on a modified accrual basis of accounting. For these audited financial statements, adjustments have been made at the year end to convert the Association's records to the full accrual basis of accounting. The tax returns are also reported on the accrual basis of accounting.
- (b) Funds: The Association uses fund accounting which requires that funds, such as operating funds and funds designated for future major repairs and replacements, be classified separately for accounting and reporting purposes. Disbursements from the operating fund are generally at the discretion of the Board of Directors and property manager. Disbursements from the replacement fund generally may be made only for their designated purposes.
- (c) Recognition of assets and depreciation policy: Real property contributed to the Association by the developer has not been recorded for financial statement purposes since the Association's governing documents impose severe limitations on its disposition. The Association recognizes personal property assets at cost. The property is depreciated over its estimated useful life using the straight line method of depreciation.
- (d) Cash equivalents and short-term investments: Cash equivalents consist primarily of certificates of deposit and other securities with original maturities of 90 days or less. Certificates of deposit and other securities with original maturities over 90 days are classified as short-term investments. Cash equivalents and short-term investments are stated at cost.
- (e) Interest earned: The Board's policy is to allocate to the replacement fund interest earned on all replacement fund cash accounts.
- (f) Estimates: The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

**NOTE 3 - OWNERS' ASSESSMENTS**

During fiscal 2011, assessments to owners were \$622,500 of which \$141,480 was designated to the replacement fund. The annual budget and owners' assessments are determined by the Board of Directors. 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 - CONTINUED**  
**DECEMBER 31, 2011**

**NOTE 4 - FUTURE MAJOR REPAIRS AND REPLACEMENTS**

The Association's governing documents require that funds be accumulated for future major repairs and replacements. Substantially all accumulated funds are held in separate savings or short-term investment accounts and are generally not available for expenditures for normal operations.

A study was conducted on November 17, 2011 by Reserve Data Analysis 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. Funding requirements consider an annual inflation rate of 3%, scheduled annual funding increase of 3%, and interest at 1% net of taxes of 30%, on amounts funded for future major repairs and replacements.

The table included in the unaudited supplementary information on Future Major Repairs and Replacements is based on the study.

The Board of Directors is funding for major repairs and replacements over the remaining useful lives of the components based on the study's estimates of current replacement costs and considering amounts previously accumulated in the replacement fund. Accordingly, the study's recommended funding requirement of \$152,700 has been included in the Association's 2012 budget. The study recommends an ideal cash balance in the amount of \$814,088. As of December 31, 2011, the actual available replacement fund cash balance was \$560,465, however, as of December 31, 2011 the operating fund owed the replacement fund \$95,591. Please see Note 8.

Funds are being accumulated in the replacement fund based on estimated future costs for repairs and replacements of common property components. Actual expenditures may vary from the estimated amounts 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.

**NOTE 5 - FEDERAL AND STATE TAXES**

The Association qualifies as a tax-exempt homeowners association under Internal Revenue Code Section 528 for the year ended December 31, 2011. Under that Section, the Association is not taxed on income and expenses related to its exempt purpose, which is the acquisition, construction, management, maintenance, and care of Association property. Net nonexempt function income, which includes earned interest and revenues received from nonmembers, is taxed at 30% by the federal government and at 8.84% by the State of California.

The Association has not recorded deferred tax assets or liabilities due to the fact that there is no material difference between the financial accounting and tax basis of the Association's assets and liabilities. If there were differences in the basis, a liability or benefit would be recognized based on the expected tax rate in the years in which the differences would be reversed.

The Association's federal income tax return for fiscal year end 2008, 2009, 2010, and 2011 may be subject to examination by the Internal Revenue Service, generally for three years after they were filed.



**PARK PASEO HOMEOWNERS ASSOCIATION**  
**NOTES TO FINANCIAL STATEMENTS - CONTINUED**  
**DECEMBER 31, 2011**

**NOTE 6 - ASSESSMENTS RECEIVABLE**

As of December 31, 2011, the Association had delinquent assessments receivable of \$10,118. The Association's Declaration provides for various collection remedies for delinquent assessments including the filing of liens, foreclosing on the unit owner, and obtaining judgment on other assets of the unit owner. Delinquent assessments may be secured by a lien on the property against which assessments are made and the Association has the power to foreclose the property of any owner who fails to pay assessments.

The Association writes off receivable balances once all collection alternatives have been exhausted.

It is the opinion of the Association that an allowance for doubtful accounts is not necessary since all accounts are considered fully collectible.

**NOTE 7 - INVESTMENTS**

The Association's investments consist of certificates of deposit with original maturities over 90 days. The investments are considered to be held to maturity which range from January to December 2012. Investment income is recorded as it is earned. The investments are carried at cost.

The Association also has an investment in a Franklin Adjustable U.S. Government Securities Fund which is recorded at fair market value. The corresponding unrealized 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. This mutual fund is not FDIC insured, although it invests primarily in mortgages guaranteed by the U.S. government.

**NOTE 8 - SUBSEQUENT EVENTS**

Management has evaluated subsequent events through April 9, 2012, the date the financial statements were available to be issued. While the operating fund owed the replacement fund \$95,591 as of December 2011, the replacement fund has been paid back in full beginning in January 2012.

PARK PASEO HOMEOWNERS ASSOCIATION  
 SUPPLEMENTARY INFORMATION ON FUTURE MAJOR  
 REPAIRS AND REPLACEMENTS  
 AS OF DECEMBER 31, 2011  
 (UNAUDITED)

A study was conducted on November 17, 2011 by Reserve Data Analysis 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. Replacement costs and useful lives can be found in published manuals such as construction estimators, appraisal handbooks, and valuation guides. Remaining lives are calculated from the useful lives and ages of assets, and adjusted according to conditions such as design, manufacture quality, usage, exposure to the elements and maintenance history. Funding requirements consider an annual inflation rate of 3%, scheduled annual funding increase of 3%, and interest at 1% net of taxes of 30%, on amounts funded for future major repairs and replacements. The study recommends an annual funding amount of \$148,656 of which \$152,700 has been included in the 2012 budget. The ideal cash replacement fund balance was \$814,088, per the reserve study. As of December 31, 2011, the actual available replacement fund cash balance was \$560,465.

The following table is based on the study and presents significant information about the components of common property:

Components	Estimated Remaining Useful Lives (Years)	Estimated Current Replacement Costs
Parking lot	0 - 6	\$ 16,398
Roofs	11 - 49	36,873
Painting	2 - 13	35,336
Fencing	19 - 28	190,062
Lighting	1 - 10	127,029
Pool	1 - 10	278,735
Clubhouse	0 - 25	306,096
Tennis court	0 - 14	64,187
Recreation area	0 - 15	105,948
Trellis	2 - 29	56,685
Signs	0	4,102
Landscape	0 - 1	39,000
Irrigation	0 - 1	69,904
Termite control	0	4,780
Total		<u>\$ 1,335,135</u>