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APR 19 2014

NOTICE

DATE: April 17, 2014
TO: Park Paseo Homeowners Association Membership
FROM: Park Paseo Homeowners Association Board of Directors
RE: Audit

Enclosed, please find the audited financial statements as prepared by Inouye, Shively, Longtin & Klatt for the Park Paseo Homeowners Association, for the fiscal year ending December 31, 2013. Should you have any questions on this material, please contact management. Please file these documents with the rest of your Association paperwork. Thank you.



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To the Board of Directors of
Park Paseo Homeowners Association

INDEPENDENT AUDITOR'S REPORT

Report on the Financial Statements

We have audited the accompanying financial statements of Park Paseo Homeowners Association, which comprise the balance sheet as of December 31, 2013, and the related statements of revenues, expenses, and changes in fund balance, and cash flows for the year then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

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 involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Board of Directors
Park Paseo Homeowners Association

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, 2013, 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.

Emphasis of Matter

Our audit was made for the purpose of forming an opinion on the basic financial statements taken as a whole. We have not applied procedures to determine whether the funds designated for future major repairs and replacements as discussed in Note 4 are adequate to meet such future costs because that determination is outside the scope of our audit. Our opinion on the financial statements is not modified with respect to this matter.

Disclaimer of Opinion on Required Supplementary Information

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 provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Inouye, Shively, Longtin & Klatt

Inouye, Shively, Longtin & Klatt

Laguna Hills, CA
April 14, 2014

PARK PASEO HOMEOWNERS ASSOCIATION
BALANCE SHEET
AS OF DECEMBER 31, 2013

	<u>Operating Fund</u>	<u>Replacement Fund</u>	<u>Total</u>
Assets			
Cash and cash equivalents	\$ 192,500	\$ 257,463	\$ 449,963
Investments	-	440,000	440,000
Assessments receivable	19,434	-	19,434
Allowance for doubtful accounts	(9,578)	-	(9,578)
Accrued interest receivable	-	862	862
Prepaid expenses	789	84	873
Interfund account	(44,945)	44,945	-
Total assets	<u>158,200</u>	<u>743,354</u>	<u>901,554</u>
Liabilities			
Accounts payable	12,915	-	12,915
Prepaid assessments	12,503	-	12,503
Income taxes payable	10	79	89
	<u>25,428</u>	<u>79</u>	<u>25,507</u>
Fund balances	<u>132,772</u>	<u>743,275</u>	<u>876,047</u>
Total liabilities and fund balances	<u>\$ 158,200</u>	<u>\$ 743,354</u>	<u>\$ 901,554</u>

See independent auditors' report and accompanying notes to financial statements.

PARK PASEO HOMEOWNERS ASSOCIATION
STATEMENT OF REVENUES, EXPENSES,
AND CHANGES IN FUND BALANCES
FOR THE YEAR ENDED DECEMBER 31, 2013

	<u>Operating Fund</u>	<u>Replacement Fund</u>	<u>Total</u>
Revenues			
Member assessments	\$ 501,189	\$ 136,311	\$ 637,500
Interest income	-	1,788	1,788
Clubhouse rental	10,850	-	10,850
Other income	12,600	-	12,600
Total revenues	<u>524,639</u>	<u>138,099</u>	<u>662,738</u>
Expenses			
Landscape services	136,661	35,030	171,691
Pool/spa services	45,851	144,754	190,605
General maintenance and repairs	51,340	-	51,340
Security/patrol services	41,384	-	41,384
Pest control	1,488	-	1,488
Janitorial services	14,314	-	14,314
Water	28,825	-	28,825
Electricity	29,153	-	29,153
Gas	12,106	-	12,106
Telephone	3,860	-	3,860
Refuse	1,831	-	1,831
Management fees	60,000	-	60,000
Office supplies/printing/postage	17,621	-	17,621
Insurance	14,710	-	14,710
Legal and collection	5,223	-	5,223
Audit and tax preparation	1,800	-	1,800
Reserve study	2,215	-	2,215
General and administrative	22,003	95	22,098
Provision for doubtful accounts	5,729	-	5,729
Clubhouse	-	5,344	5,344
Income tax	26	483	509
Total expenses	<u>496,140</u>	<u>185,706</u>	<u>681,846</u>
Excess (deficiency) of revenues over expenses	28,499	(47,607)	(19,108)
Beginning fund balances	104,273	790,882	895,155
Ending fund balances	<u>\$ 132,772</u>	<u>\$ 743,275</u>	<u>\$ 876,047</u>

See independent auditors' report and accompanying notes to financial statements.

PARK PASEO HOMEOWNERS ASSOCIATION
STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED DECEMBER 31, 2013

	<u>Operating Fund</u>	<u>Replacement Fund</u>	<u>Total</u>
Cash flows from operating activities:			
Excess (deficiency) of revenues over expenses	\$ 28,499	\$ (47,607)	\$ (19,108)
Adjustments to reconcile excess (deficiency) of revenues over expenses to net cash provided by (used in) operating activities			
Increase in net assessments receivable	(4,775)	-	(4,775)
Increase in accrued interest receivable	-	(532)	(532)
Decrease (increase) in prepaid expenses	(714)	279	(435)
Decrease in accounts payable	(658)	-	(658)
Increase in prepaid assessments	353	-	353
Decrease in refundable deposits	(250)	-	(250)
Increase in income taxes payable	-	79	79
Total adjustments	<u>(6,044)</u>	<u>(174)</u>	<u>(6,218)</u>
Net cash provided by (used in) operating activities	22,455	(47,781)	(25,326)
Cash flows from investing activities:			
Purchase of investments	-	(329,000)	(329,000)
Net cash used in investing activities	-	(329,000)	(329,000)
Cash flows from financing activities:			
Change in interfund payable balances	36,856	(36,856)	-
Net cash provided by (used in) financing activities	36,856	(36,856)	-
Net increase (decrease) in cash and cash equivalents	59,311	(413,637)	(354,326)
Cash and cash equivalents at beginning of year	133,189	671,100	804,289
Cash and cash equivalents at end of year	<u>\$ 192,500</u>	<u>\$ 257,463</u>	<u>\$ 449,963</u>
Supplemental disclosures			
Income taxes paid	<u>\$ 26</u>	<u>\$ 125</u>	<u>\$ 151</u>

See independent auditors' report and accompanying notes to financial statements.

PARK PASEO HOMEOWNERS ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2013

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 and was incorporated on June 9, 1977.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

- (a) Basis 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, if any, is depreciated over its estimated useful life using the straight line method of depreciation.
- (d) Cash Equivalents and 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 investments. Cash equivalents and 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 - MEMBER ASSESSMENTS

During the year ended December 31, 2013, assessments to owners were \$637,500 of which \$136,311 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, 2013

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 investment accounts and are generally not available for expenditures for normal operations.

A study was conducted on November 18, 2013 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 2%, scheduled annual funding increase of 2%, 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, \$143,976 (an amount greater than the study's recommended funding requirement of \$123,663) has been included in the Association's 2014 budget. The study recommends an ideal cash balance in the amount of \$855,100. As of December 31, 2013, the actual available replacement fund cash balance was \$698,325.

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.

As of December 31, 2013, the operating fund owed the replacement fund \$44,945.

NOTE 5 - INCOME TAXES

The Association qualifies as a tax-exempt homeowners association under Internal Revenue Code Section 528 for the year ended December 31, 2013. 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 recognizes tax benefits only to the extent that it believes it is more likely than not that its tax positions will be sustained upon examination by taxing authorities. The Association has not been examined by taxing authorities. However, the Association's tax returns for fiscal year end 2010, 2011, 2012, and 2013 may be subject to examination by taxing authorities, generally for three years after they are filed. Management believes that all of its tax positions will be sustained if examined by taxing authorities, therefore no additional tax liabilities or related penalties and interest due to uncertain tax positions have been recorded.

PARK PASEO HOMEOWNERS ASSOCIATION
NOTES TO FINANCIAL STATEMENTS - CONTINUED
DECEMBER 31, 2013

NOTE 6 - ASSESSMENTS RECEIVABLE

As of December 31, 2013, the Association had delinquent assessments receivable of \$19,434. The Association's governing documents provide 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.

It is the opinion of the Association that the allowance for doubtful accounts of \$9,578 is adequate to cover any accounts that may eventually be uncollectible. The allowance was computed by adding all receivable amounts in the 90 day category.

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

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 February 2014 to October 2015. Investment income is recorded as it is earned. The investments are carried at cost.

NOTE 8 - CONCENTRATION OF CREDIT RISK

An investment in a money market fund is neither insured nor guaranteed by the Federal Deposit Insurance Corporation (FDIC) or any other government agency. As of December 31, 2013, the Association had approximately \$202,000 deposited in a money market fund at Morgan Stanley, and approximately \$49,000 deposited in a federated government money market fund at Comerica Bank. Investments held by the federated government money market fund are obligations of, or backed by, the U. S. government or its agencies.

NOTE 9 - SUBSEQUENT EVENTS

The Association has evaluated subsequent events and transactions for potential recognition or disclosure in the financial statements through April 14, 2014, the date the financial statements were available to be issued.

PARK PASEO HOMEOWNERS ASSOCIATION
SUPPLEMENTARY INFORMATION ON FUTURE MAJOR
REPAIRS AND REPLACEMENT
AS OF DECEMBER 31, 2013
(UNAUDITED)

A study was conducted on November 18, 2013 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 2%, scheduled annual funding increase of 2%, 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 \$123,663, although \$143,976 has been included in the 2014 budget. The ideal cash replacement fund balance was \$855,100, per the reserve study. As of December 31, 2013, the actual available replacement fund cash balance was \$698,325.

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	1-4	\$ 16,767
Roofs	0-47	66,506
Painting	0-21	36,871
Fencing	17-26	198,974
Lighting	0-8	151,345
Pools	0-13	330,255
Clubhouse	0-23	304,694
Tennis court	1-12	67,370
Rec area	0-13	116,214
Trellis	3-27	59,357
Signs	0-3	4,232
Landscape	0-2	39,000
Irrigation	2-14	55,542
Termite control	1	4,986
Total		<u>\$ 1,452,113</u>