

Schonwit & Company

Certified Public Accountants

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April 26, 2013

Cypress Homeowners Association
c/o Accell Property Management
23046 Avienda de la Carlota, Suite 700
Laguna Hills, CA 92653

To the Board of Directors:

Enclosed you will find the final version of the financial statements for Cypress Homeowners Association. These statements should be distributed to the owners, in their **entirety**. If you should have any questions, please contact our office for further explanation.

Again, it has been a pleasure providing service for your Association.

Very truly yours,



Schonwit & Company

Enclosures

CYPRESS HOME OWNERS ASSOCIATION
COMPARATIVE FINANCIAL STATEMENTS
DECEMBER 31, 2012 AND 2011

CYPRESS HOME OWNERS ASSOCIATION

Table of Contents

| | |
|--|------------|
| Independent Auditors' Report | Pages 3-4 |
| Balance Sheet with Comparative Totals | Page 5 |
| Statement of Revenues, Expenses and Changes in Fund Balances with Comparative Totals | Page 6 |
| Statement of Cash Flows with Comparative Totals | Page 7 |
| Notes to Financial Statements | Pages 8-11 |
| Supplementary Information on Future Major Repairs and Replacements | Page 12 |

INDEPENDENT AUDITORS' REPORT

To the Owners
Cypress Home Owners Association

Report on the Financial Statements

We have audited the accompanying financial statements of Cypress Home Owners Association, which comprise the balance sheet as of December 31, 2012, and the related statements of revenues, expenses and changes in fund balances, and cash flows for the year then ended, and the related notes to the financial statements. The prior year summarized comparative information is presented for comparative purposes only and has been extracted from the Cypress Home Owners Association's financial statements presented by fund for 2012 on which we expressed an unmodified opinion in our report dated March 19, 2012.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of the 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. 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 auditors' judgment, including the assessment of 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.

Opinion

In our opinion the financial statements referred to above present fairly, in all material respects, the financial position of Cypress Home Owners Association as of December 31, 2012, 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.

Other Matters

A current study of the Association's replacement funding program indicates that the Association is underfunded. Accordingly, it may be necessary to increase assessments, pass special assessments, or delay future repair or replacement obligations until sufficient funds are available.

Report on Supplementary Information

Accounting principles generally accepted in the United States of America require that supplementary information on future major repairs and replacements on page 12 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the American Institute of Certified Public Accountants, who considers it to be an essential part of financial reporting and for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. Such information was not audited or reviewed by us and, accordingly, we do not express an opinion or provide any assurance on it.

Schonwit & Co.
SCHONWIT & COMPANY

April 14, 2013

CYPRESS HOME OWNERS ASSOCIATION
BALANCE SHEET
AS OF DECEMBER 31, 2012
(WITH COMPARATIVE TOTALS FOR 2011)

| | <u>2012</u> | | | <u>2011</u> |
|--|---------------------------|-----------------------------|-------------------|-------------------|
| | <u>Operating Fund</u> | <u>Replacement Fund</u> | <u>Total</u> | <u>Total</u> |
| ASSETS | | | | |
| Cash and cash equivalents [Note 7] | \$ 190,659 | \$ 394,278 | \$ 584,937 | \$ 451,799 |
| Member assessments receivable, less allowance for doubtful collections of \$103,300 at 12/31/12 and \$93,200 at 12/31/11 | 18,671 | -- | 18,671 | 17,112 |
| Investments [Note 8] | -- | 51,002 | 51,002 | 50,697 |
| Accrued interest receivable | -- | 11 | 11 | 19 |
| Prepaid insurance | 74,174 | -- | 74,174 | 65,557 |
| Prepaid taxes | 412 | -- | 412 | 2,418 |
| Due (to)/from fund | <u>(62,711)</u> | <u>62,711</u> | <u>--</u> | <u>--</u> |
| Total Assets | <u>\$ 221,205</u> | <u>\$ 508,002</u> | <u>\$ 729,207</u> | <u>\$ 587,602</u> |
| LIABILITIES | | | | |
| Accounts payable | \$ 11,954 | \$ 15,325 | \$ 27,279 | \$ 17,865 |
| Prepaid assessments | 17,504 | -- | 17,504 | 7,703 |
| Income taxes payable | <u>10</u> | <u>--</u> | <u>10</u> | <u>10</u> |
| Total Liabilities | 29,468 | 15,325 | 44,793 | 25,578 |
| FUND BALANCES | <u>191,737</u> | <u>492,677</u> | <u>684,414</u> | <u>562,024</u> |
| TOTAL LIABILITIES AND FUND BALANCES | <u>\$ 221,205</u> | <u>\$ 508,002</u> | <u>\$ 729,207</u> | <u>\$ 587,602</u> |

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

CYPRESS HOME OWNERS ASSOCIATION
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN FUND BALANCES
FOR THE YEAR ENDED DECEMBER 31, 2012
(WITH COMPARATIVE TOTALS FOR 2011)

| | <u>2012</u> | | | <u>2011</u> |
|---|-----------------------|-------------------------|-------------------|-------------------|
| | <u>Operating Fund</u> | <u>Replacement Fund</u> | <u>Total</u> | <u>Total</u> |
| REVENUES | | | | |
| Member assessments | \$ 564,200 | \$ 290,800 | \$ 855,000 | \$ 825,000 |
| Interest | -- | 1,752 | 1,752 | 1,754 |
| Other income | 9,178 | -- | 9,178 | 13,316 |
| Total Revenues | <u>573,378</u> | <u>292,552</u> | <u>865,930</u> | <u>840,070</u> |
| EXPENSES | | | | |
| Utilities: | | | | |
| Electricity | 33,470 | -- | 33,470 | 33,523 |
| Water | 61,010 | -- | 61,010 | 54,937 |
| Gas | 2,076 | -- | 2,076 | 1,565 |
| Refuse | 60,695 | -- | 60,695 | 60,034 |
| Maintenance: | | | | |
| Landscape maintenance and supplies | 86,031 | -- | 86,031 | 83,353 |
| Irrigation repairs | 1,262 | -- | 1,262 | 1,659 |
| Tree maintenance | 8,250 | -- | 8,250 | 7,630 |
| Pool service, supplies and repairs | 19,477 | 4,124 | 23,601 | 24,985 |
| Janitorial service and supplies | 5,337 | -- | 5,337 | 7,460 |
| Pest control | 5,328 | -- | 5,328 | 5,058 |
| Roof repairs | 3,589 | 179,556 | 183,145 | 56,082 |
| Plumbing repairs | 6,411 | 1,084 | 7,495 | 9,186 |
| Other common area maintenance | 10,037 | -- | 10,037 | 20,469 |
| Painting | -- | 17,050 | 17,050 | 94,675 |
| Wood repairs | -- | 15,075 | 15,075 | 46,350 |
| Asphalt work | -- | 6,270 | 6,270 | 4,373 |
| Clubhouse | -- | 9,104 | 9,104 | -- |
| Water heater | -- | 4,035 | 4,035 | -- |
| Administrative: | | | | |
| Insurance | 134,802 | -- | 134,802 | 141,328 |
| Management fees | 41,484 | -- | 41,484 | 41,484 |
| Professional fees | 1,299 | -- | 1,299 | 5,018 |
| Income taxes [Note 4] | 448 | -- | 448 | 298 |
| Postage and printing expense | 3,855 | -- | 3,855 | 4,575 |
| Other administrative expenses | 7,886 | -- | 7,886 | 3,325 |
| Bad debt expense | 14,495 | -- | 14,495 | 10,668 |
| Total Expenses | <u>507,242</u> | <u>236,298</u> | <u>743,540</u> | <u>718,035</u> |
| EXCESS OF REVENUES OVER EXPENSES | 66,136 | 56,254 | 122,390 | 122,035 |
| Beginning Fund Balances | <u>125,601</u> | <u>436,423</u> | <u>562,024</u> | <u>439,989</u> |
| Ending Fund Balances | <u>\$ 191,737</u> | <u>\$ 492,677</u> | <u>\$ 684,414</u> | <u>\$ 562,024</u> |

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

CYPRESS HOME OWNERS ASSOCIATION
STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED DECEMBER 31, 2012
(WITH COMPARATIVE TOTALS FOR 2011)

| | <u>2012</u> | | | <u>2011</u> |
|---|-----------------------|-------------------------|-------------------|-------------------|
| | <u>Operating Fund</u> | <u>Replacement Fund</u> | <u>Total</u> | <u>Total</u> |
| Excess of revenues over expenses: | \$ 66,136 | \$ 56,254 | \$ 122,390 | \$ 122,035 |
| Adjustments to reconcile excess of revenues over expenses to net cash provided by operating activities: | | | | |
| (Increase)/decrease in member assessments receivable | (1,559) | -- | (1,559) | 13,270 |
| Decrease in accrued interest receivable | -- | 8 | 8 | 13 |
| Increase in prepaid insurance | (8,617) | -- | (8,617) | (38,997) |
| (Increase)/decrease in prepaid taxes | 2,006 | -- | 2,006 | (2,418) |
| Increase/(decrease) in accounts payable | (5,911) | 15,325 | 9,414 | 585 |
| Increase/(decrease) in prepaid assessments | 9,801 | -- | 9,801 | (9,831) |
| Decrease in income taxes payable | -- | -- | -- | (1,259) |
| Net cash provided by operating activities | <u>61,856</u> | <u>71,587</u> | <u>133,443</u> | <u>83,398</u> |
| Cash provided/(used) by investing activities: | | | | |
| Acquisition of certificates of deposit | -- | (51,002) | (51,002) | (50,697) |
| Maturity of certificates of deposit | -- | 50,697 | 50,697 | 50,193 |
| Net cash flows from investing activities | <u>--</u> | <u>(305)</u> | <u>(305)</u> | <u>(504)</u> |
| Net increase in cash | 61,856 | 71,282 | 133,138 | 82,894 |
| Cash at beginning of year | <u>128,803</u> | <u>322,996</u> | <u>451,799</u> | <u>368,905</u> |
| Cash at end of year | <u>\$ 190,659</u> | <u>\$ 394,278</u> | <u>\$ 584,937</u> | <u>\$ 451,799</u> |

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

CYPRESS HOME OWNERS ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2012

NOTE 1. ORGANIZATION

Cypress Home Owners Association [the Association] is a statutory homeowners association which was organized as a non-profit mutual benefit corporation in February 1965. The purpose of the Association is primarily to maintain, preserve and control the common areas of the Association. The Association consists of 250 residential units and is located in Cypress, California.

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(a) Principles of Accounting - The books and records for the Association are maintained the accrual basis of accounting. The tax returns are also reported on the accrual basis of accounting.

(b) Capitalization Policy and Depreciation – In accordance with industry standards, the Association has not capitalized in the financial statements the common area real property acquired at its inception from the developer. Replacements and improvements to the real property which are directly associated with the units are also not capitalized. They are instead charged directly to either operating or replacement funds in the period they are incurred.

Significant capital assets not directly associated with the units, referred to as personal property assets, are capitalized and depreciated over their estimated useful life using the straight-line method of depreciation. During the year ended December 31, 2012, there were no significant personal property additions.

(c) Fund Accounting - The Association's accompanying financial statements have been prepared using fund accounting. Under this method of accounting, funds are separated into two categories, the operating fund and the replacement fund. Disbursements from the replacement fund generally may be made only for designated repair or replacement of major common area components. Disbursements from the operating fund are at the discretion of the Board of Directors and generally are for on-going repairs, maintenance, and administrative functions.

(d) Investment Income - The Board's policy is to allocate interest earned on replacement fund cash and investment accounts to the replacement fund, and to pay the related income taxes out of the operating fund.

(e) Use of Estimates - The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the period. Actual results could differ from those estimates.

(f) Subsequent Events - Subsequent events have been evaluated through April 14, 2013, which is the date the financial statements were available to be issued.

NOTE 3. COMPARATIVE FINANCIAL STATEMENTS

The financial statements include certain prior year summarized comparative information in total, but not by fund. Such information does not include sufficient detail to constitute a presentation in conformity with generally accepted accounting principles. Accordingly, such information should be read in conjunction with the Association's financial statements for the year ended December 31, 2011, from which the summarized information was derived.

CYPRESS HOME OWNERS ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2012

NOTE 4. INCOME TAXES

The Association may elect to file its federal income tax return as either a regular corporation [under Internal Revenue Code Section 277] or as a homeowners association [under Internal Revenue Code Section 528]. For the year ended December 31, 2012, the Association elected to file as a regular corporation using certain provisions available to membership organizations. For California purposes, the Association also qualifies for tax exempt status as a homeowners association and pays a tax of 8.84% on income not related to membership dues and assessments. For the year ended December 31, 2012, the federal and California income tax expense was \$332 and \$116, respectively.

The Association utilizes the liability method of accounting for income taxes. Under the liability method deferred income tax assets and liabilities are provided based on the difference between the financial statements and tax basis of assets and liabilities measured by the currently enacted tax rates in effect for the years in which these differences are expected to reverse. Because there is no material difference between the financial accounting and tax basis of the Association's assets and liabilities, the Association has not recorded any deferred tax assets or liabilities.

The Association has adopted accounting standards for the accounting for uncertainty in income taxes. These standards provide guidance for the accounting and disclosure about uncertain tax positions taken by an association. Management believes that all of the positions taken by the Association in its federal and state income tax returns are more likely than not to be sustained upon examination. The Association's tax returns are subject to examination by the Internal Revenue Service and the California Franchise Tax Board, generally for three years and four years, respectively after they are filed.

NOTE 5. ASSESSMENTS AND ASSESSMENTS RECEIVABLE

Association members are subject to paying assessments to fund for the Association's operating expenses, future capital acquisitions, and major repairs and replacements. Assessments receivable at December 31, 2012 represent assessments and other fees due from owners. The Association's governing documents provide for various collection remedies for delinquent assessments, including filing of liens on the owner's unit, foreclosing on the unit owner, or obtaining judgment on other assets of the unit owner. At December 31, 2012, the Association has recorded an allowance for uncollectible assessments of \$103,300. This allowance represents an estimated amount which was calculated using historical collection information.

For the year ended December 31, 2012, the Association's monthly assessment was \$285 per unit. For 2013, the monthly assessment is budgeted to remain at \$285 per unit.

NOTE 6. REPLACEMENT FUNDING PROGRAM

In accordance with the Association's governing documents, which require that funds be accumulated for future major repairs and replacements, the Association has established certain amounts as reserves for future capital expenditures. Members' assessments relating to the replacement funding program are considered capital contributions from members' dues and as such are restricted in usage. Disbursements are to be made only if specifically approved by the Board of Directors.

CYPRESS HOME OWNERS ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2012

NOTE 6. REPLACEMENT FUNDING PROGRAM – (CONTINUED)

An independent study of the Association's replacement funding program, which was conducted in May 2012, indicates that the Association is underfunded. Accordingly the study recommends a contribution to the replacement fund of approximately \$214,731 for 2013. The study's recommendations were based on estimates of remaining useful lives, current replacement costs, and amounts accumulated in the replacement funds. For the year ended December 31, 2012, the Association funded \$290,800 from assessments to the replacement fund. The 2013 budget includes a provision for replacement funding of \$299,565. The table included in the unaudited supplementary information on future major repairs and replacements is based on the study.

Replacement funds are being accumulated based on estimates of future needs 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 funds may not be adequate to meet all future needs for major repairs and replacements. If additional funds are needed, the Association has the right, subject to the Association's governing documents, to pass special assessments, increase monthly assessments, or delay replacement until funds are available.

NOTE 7. SCHEDULE OF CASH BALANCES

Generally, certificates of deposit and other debt securities with original maturities less than 90 days are considered cash equivalents, while certificates of deposits and debt securities with maturities over 90 days are considered "investments."

At December 31, 2012 and 2011, the Association maintained cash balances at the following institutions:

| <u>Operating Fund:</u> | <u>2012</u> | <u>2011</u> |
|-----------------------------------|-------------------|-------------------|
| City National Bank - checking | <u>\$ 190,659</u> | <u>\$ 128,803</u> |
| <u>Replacement Fund:</u> | | |
| City National Bank - money market | \$ 217,084 | \$ 147,108 |
| State Farm Bank - money market | <u>177,194</u> | <u>175,888</u> |
| Total Cash - Replacement Fund | <u>\$ 394,278</u> | <u>\$ 322,996</u> |

CYPRESS HOME OWNERS ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2012

NOTE 8. INVESTMENTS

The Association's investments consist of certificates of deposit with original maturities over 90 days. Investment income from these investments is recorded when earned or accrued. The investments are considered to be held to maturity and are carried at cost, which approximates the fair value.

At December 31, 2012 and 2011, the Association's investment is as follows:

| <u>Replacement Fund:</u> | <u>2012</u> | <u>2011</u> |
|---------------------------------|------------------|------------------|
| State Farm Bank - 0.4%, 8/12/13 | <u>\$ 51,002</u> | <u>\$ 50,697</u> |

NOTE 9. SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION

There were no cash payments for income taxes for the year ended December 31, 2012. No interest was paid and there were no non-cash investing or financing transactions during the year.

CYPRESS HOME OWNERS ASSOCIATION
 REQUIRED SUPPLEMENTARY INFORMATION
 ON FUTURE MAJOR REPAIRS & REPLACEMENTS
 AS OF DECEMBER 31, 2012
 (UNAUDITED)

An independent reserve study was conducted in May 2012 to estimate the remaining useful lives and the replacement costs of the components of common property. The study was based upon representations by the Board of Directors and the experience and knowledge of the independent reserve analyst. The estimates were based on current replacement costs adjusted for an annual inflation rate of 3.0%. These estimates are used as a foundation in arriving at recommended funding requirements, based upon cash and investments which have been allocated for future repairs and replacements, earning a yield on investments of 1.0%.

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

| <u>Common Area Component</u> | <u>Estimated Remaining Useful Lives</u> | <u>Estimated Current Replacement Costs</u> | <u>2013 Recommended Funding Requirement</u> | <u>Study's Recommended Fund Balance</u> |
|---------------------------------------|---|--|---|---|
| Painting | 0-6 years | \$ 443,254 | \$ 87,646 | \$ 102,774 |
| Roofs | 0-49 years | 2,295,541 | 98,686 | 844,363 |
| Pools/spas | 0-10 years | 63,469 | 7,801 | 27,169 |
| Fences/gates | 4-8 years | 36,771 | 2,469 | 27,254 |
| Irrigation controllers | 3 years | 108,150 | 7,261 | 91,928 |
| HVAC - clubhouse | 4 years | 12,742 | 3,270 | 10,192 |
| Tot lot equipment | 1 year | 37,139 | 3,325 | 34,663 |
| Decks | 9 years | 16,223 | 1,089 | 8,922 |
| Clubhouse furniture | 8 years | 3,300 | 222 | 1,980 |
| Clubhouse interior | 2-10 years | 34,500 | 856 | 33,147 |
| Concrete | 1 year | 5,405 | 1,816 | 4,056 |
| Water heaters - clubhouse | 0 years | 2,596 | 290 | 2,596 |
| | Total | <u>\$ 3,059,090</u> | <u>\$ 214,731</u> | <u>\$ 1,189,044</u> |
| Replacement Fund balance at 12/31/12: | | | | <u>\$ 492,677</u> |