

**MISSION GROVE HOMEOWNERS ASSOCIATION**

Independent Accountant's Review Report,  
Financial Statements and Supplementary Information

Year Ended August 31, 2015

**MISSION GROVE HOMEOWNERS ASSOCIATION**  
Year Ended August 31, 2015

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**BHLF**

**BONG HILLBERG LEWIS FISCHESSEY LLP**

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**INDEPENDENT ACCOUNTANT'S REVIEW REPORT**

Board of Directors and Members  
Mission Grove Homeowners Association

We have reviewed the accompanying balance sheet of Mission Grove Homeowners Association (the Association) as of August 31, 2015, and the related statements of revenues, expenses, and changes in fund balance and cash flows for the year then ended. A review includes primarily applying analytical procedures to management's financial data and making inquiries of Association management. A review is substantially less in scope than an audit, the objective of which is the expression of an opinion regarding the financial statements as a whole. Accordingly, we do not express such an opinion.

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 and for designing, implementing, and maintaining internal control relevant to the preparation and fair presentation of the financial statements.

Our responsibility is to conduct the review in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants. Those standards require us to perform procedures to obtain limited assurance that there are no material modifications that should be made to the financial statements. We believe that the results of our procedures provide a reasonable basis for our report.

Based on our review, we are not aware of any material modifications that should be made to the accompanying financial statements in order for them to be in conformity with accounting principles generally accepted in the United States of America.

Accounting principles generally accepted in the United States of America require that the information about future major repairs and replacements of common property be presented to supplement the basic financial statements. Such information, although not a 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 compiled the required supplementary information without audit or review, and, accordingly, we do not express an opinion or provide any assurance on it.

*Bong Hillberg Lewis Fischesser LLP*

Walnut Creek, California  
October 21, 2015

# MISSION GROVE HOMEOWNERS ASSOCIATION

## Balance Sheet August 31, 2015

	<u>Operations</u> <u>Fund</u>	<u>Replacement</u> <u>Fund</u>	<u>Total</u> <u>Funds</u>
<b>ASSETS</b>			
Cash and cash equivalents	\$ 103,639	\$ 638,417	\$ 742,056
Certificates of deposit	-	1,227,000	1,227,000
Member receivables, net	18,837	-	18,837
Prepaid expenses	<u>23,263</u>	<u>-</u>	<u>23,263</u>
Total assets	<u>\$ 145,739</u>	<u>\$ 1,865,417</u>	<u>\$ 2,011,156</u>
<b>LIABILITIES</b>			
Accounts payable	\$ 20,910	\$ -	\$ 20,910
Assessments received in advance	34,737	-	34,737
Deferred cable easement income	<u>13,300</u>	<u>-</u>	<u>13,300</u>
Total liabilities	<u>68,947</u>	<u>-</u>	<u>68,947</u>
<b>FUND BALANCE</b>	<u>76,792</u>	<u>1,865,417</u>	<u>1,942,209</u>
Total liabilities and fund balance	<u>\$ 145,739</u>	<u>\$ 1,865,417</u>	<u>\$ 2,011,156</u>

See independent accountant's review report and notes to financial statements.

# MISSION GROVE HOMEOWNERS ASSOCIATION

## Statement of Revenues, Expenses and Changes in Fund Balances Year Ended August 31, 2015

	Operations Fund	Replacement Fund	Total Funds
<b>REVENUES</b>			
Member assessments	\$ 792,800	\$ 370,000	\$ 1,162,800
Laundry income	83,554	-	83,554
Late charges and other income	23,879	-	23,879
Cable easement income	5,700	-	5,700
Investment income	29	5,316	5,345
	<u>905,962</u>	<u>375,316</u>	<u>1,281,278</u>
<b>TOTAL REVENUES</b>			
<b>EXPENSES</b>			
<b>Administrative</b>			
Salaries, wages, and payroll taxes	72,633	-	72,633
Insurance	70,360	-	70,360
Management	63,000	-	63,000
Other administration	6,555	-	6,555
Office, printing and postage	5,364	-	5,364
Legal, accounting and consulting	4,742	-	4,742
Bad debt	3,147	-	3,147
Licenses	1,584	-	1,584
Collection costs	1,309	-	1,309
	<u>228,694</u>	<u>-</u>	<u>228,694</u>
Total administrative			
<b>Common Area Maintenance</b>			
Maintenance, common areas	108,660	-	108,660
Security services	70,598	-	70,598
Landscape maintenance	67,242	-	67,242
Plumbing maintenance and repair	34,500	-	34,500
Maintenance supplies	20,986	-	20,986
Pool and spa maintenance and repair	9,066	-	9,066
Roof maintenance	7,824	-	7,824
Custodial services	7,766	-	7,766
Entry system	4,710	-	4,710
Landscape maintenance, trees	3,850	-	3,850
Pest control	3,752	-	3,752
Fire alarm and safety system	3,157	-	3,157
Lighting and electrical	2,220	-	2,220
Painting	1,486	-	1,486
Landscape maintenance, irrigation	1,074	-	1,074
Locks and keys	823	-	823
	<u>347,714</u>	<u>-</u>	<u>347,714</u>
Total common area maintenance			

See independent accountant's review report and notes to financial statements.

# MISSION GROVE HOMEOWNERS ASSOCIATION

## Statement of Revenues, Expenses and Changes in Fund Balances Year Ended August 31, 2015

	<u>Operations Fund</u>	<u>Replacement Fund</u>	<u>Total Funds</u>
<b>Utilities</b>			
Water and sewer	162,376	-	162,376
Gas and electricity	118,675	-	118,675
Garbage collection	59,099	-	59,099
Telephone	5,581	-	5,581
	<u>345,731</u>	<u>-</u>	<u>345,731</u>
<b>Major Repairs and Replacements</b>			
Roofs	-	150,014	150,014
Trees and trimming	-	20,350	20,350
Equipment, fitness	-	14,546	14,546
Mailboxes	-	12,000	12,000
Other major repairs and replacements	-	6,651	6,651
	<u>-</u>	<u>203,561</u>	<u>203,561</u>
<b>TOTAL EXPENSES</b>	<u>922,139</u>	<u>203,561</u>	<u>1,125,700</u>
Excess (Deficiency) of Revenues Over Expenses	(16,177)	171,755	155,578
<b>Fund Balance, Beginning of Year</b>	<u>92,969</u>	<u>1,693,662</u>	<u>1,786,631</u>
<b>Fund Balance, End of Year</b>	<u>\$ 76,792</u>	<u>\$ 1,865,417</u>	<u>\$ 1,942,209</u>

See independent accountant's review report and notes to financial statements.

# MISSION GROVE HOMEOWNERS ASSOCIATION

## Statement of Cash Flows Year Ended August 31, 2015

	Operations Fund	Replacement Fund	Total Funds
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>			
Excess (deficiency) of revenues over expenses	\$ (16,177)	\$ 171,755	\$ 155,578
Adjustments to reconcile excess (deficiency) of revenues over expenses to net cash provided (used) by operating activities			
Bad debt	3,147	-	3,147
(Increase) decrease in assets:			
Member receivables	(10,805)	-	(10,805)
Prepaid expenses	(4,729)	-	(4,729)
Increase (decrease) in liabilities			
Accounts payable	241	-	241
Assessments received in advance	9,031	-	9,031
Deferred cable easement income	(5,700)	-	(5,700)
Net cash provided (used) by operating activities	(24,992)	171,755	146,763
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>			
Purchases of certificates of deposit	-	(1,227,000)	(1,227,000)
Proceeds from sale of certificates of deposit	-	1,528,000	1,528,000
Net cash provided by investing activities	-	301,000	301,000
<b>NET CHANGE IN CASH AND CASH EQUIVALENTS</b>	(24,992)	472,755	447,763
<b>CASH AND EQUIVALENTS</b>			
Beginning of year	128,631	165,662	294,293
End of year	\$ 103,639	\$ 638,417	\$ 742,056

See independent accountant's review report and notes to financial statements.

# MISSION GROVE HOMEOWNERS ASSOCIATION

## Notes to Financial Statements

### 1. THE ASSOCIATION

Mission Grove Homeowners Association (the Association) is a common interest development located in San Jose, California which consists of 380 residential dwellings and certain common area property. The Association was organized as a nonprofit mutual-benefit corporation in February 1984 to provide for management, maintenance and architectural control of the individual dwellings and the common area property. The Association is governed by a member-elected Board of Directors which is responsible for enforcing provisions of the governing documents, which include covenants, conditions and restrictions (CC&Rs), bylaws, and rules and regulations. Major decisions, as determined by the CC&Rs, are referred to the Association owners as a whole.

### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

**Basis of Accounting** - The accompanying financial statements have been prepared on the accrual basis of accounting, in accordance with accounting principles generally accepted in the United States of America, whereby revenues are recognized when earned and expenses are recognized when incurred.

**Fund Accounting** - The Association's governing documents provide certain guidelines for governing its financial activities. To ensure the observance of limitations and restrictions on the use of financial resources, the Association maintains its accounts using fund accounting. Financial resources are classified for accounting and reporting purposes in two funds established according to their nature and purpose.

**Operations Fund** - This fund is used to account for the financial resources available for the general day-to-day operations of the Association.

**Replacement Fund** - This fund is used to accumulate financial resources designated for future major repairs and replacements.

**Use of Estimates** - The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect certain amounts and disclosures. Consequently, actual results may differ from such estimates.

**Cash and cash equivalents** - The Association considers cash on hand, demand deposits with financial institutions, money market accounts and all short-term investments with original maturities of ninety days or less to be included in cash and cash equivalents. The Association places its cash and temporary cash investments with high credit quality institutions. Periodically, such deposits may be in excess of federally insured limits.

**Certificates of Deposit** - Certificates of deposit are those with original maturities greater than ninety days and are stated at cost which approximates fair market value.

**Member receivables** - Member receivables represent aggregate amounts due from unit owners which may include regular assessments, late fees, fines, reimbursement assessments and other charges. The Association's policy is to retain legal counsel and place liens on the properties of homeowners whose assessments are delinquent. In certain instances, foreclosure may be necessary. Management assesses the aging of the member receivables annually and reserves an allowance for doubtful accounts based generally on member accounts greater than 90 days outstanding. The allowance for doubtful accounts was \$23,000 at August 31, 2015.



**MISSION GROVE HOMEOWNERS ASSOCIATION**  
**Notes to Financial Statements**

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

**Real and personal common property** - Real and personal common property acquired by the original owners from the developer is not recognized in the Association's financial statements, in accordance with prevalent industry practice, because it is commonly owned by the individual Association members and its disposition by the Board of Directors is restricted. Similarly, major repairs, replacements and improvements to real and personal property are not recognized.

**Member assessments** - Association members are subject to annual assessments, payable in equal monthly installments, to provide funds for the Association's operating expenses and major repairs and replacements. In addition to regular annual assessments, special or emergency assessments may be imposed by the Association's Board of Directors under certain circumstances without member approval. Generally, any excess assessments at year end are retained by the Association for use in the succeeding year.

**Deferred cable revenues** - The Association has entered into a services agreement with a local cable service provider to provide broadband communication services to the Association for a five year term. The Association recognizes cable revenue ratably over the term of the contract.

**Interest earned** - Interest earned on operating and replacement funds is retained in said respective funds.

**Income taxes** - The Association elects annually to be taxed as either a corporation under Internal Revenue Code (IRC) 277 or as a homeowners association under IRC 528 in its tax filing with the Internal Revenue Service (IRS). Form 1120 is used when filing as a corporation and Form 1120-H is used when filing as a homeowners association.

For the year ended August 31, 2015, the Association elected to file Form 1120 and be taxed as a regular corporation. By doing so, the Association is taxed at graduated rates from 15% to 39% on net nonmembership income, less directly related expenses.

The Association is taxed by the California Franchise Tax Board (FTB) at a rate of 8.84% on its net nonmembership income. The Association has qualified as a tax-exempt entity with the FTB under California Revenue and Taxation Code 23701.

As of August 31, 2015, periods subsequent to 2011 are subject to audit by various taxing authorities; however there are currently no audits for any tax periods in progress.

The Association's policy is to classify income tax related interest and penalties in interest expense and other expenses, respectively. The Association has not recognized any interest and penalties in the year ended August 31, 2015.

**3. FUTURE MAJOR REPAIRS AND REPLACEMENTS**

The governing documents of the Association and California state law (Civil Code Section 1365) require that funds be accumulated for future major repairs and replacements. Accumulated cash, cash equivalents and investments, if any, are required to be held in separate accounts are generally not available for expenditures for normal operations.

In June 2013 a component study update, with a site-visit was completed by John D. Beatty & Company 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 component cost inflation rate of 3% and an interest rate of 1/2% earned on cash and investments on amounts funded for future major repairs and replacements. The table included as supplemental information on page 9 on future major repairs and replacements is based on the aforementioned study.

See independent accountant's review report.

**MISSION GROVE HOMEOWNERS ASSOCIATION**  
**Notes to Financial Statements**

**3. FUTURE MAJOR REPAIRS AND REPLACEMENTS (CONTINUED)**

The Board is funding for major repairs and replacements over the remaining useful lives of the components based on the study's estimates of future replacement costs and considering amounts previously accumulated in the replacement fund. The Board of Directors has adopted a funding model known as a threshold funding plan based on the funding recommendations included in the aforementioned component study. Accordingly, the Board has approved an annual contribution of \$370,000 in the 2016 operating budget. Additional information regarding the Association's funding model may be found in the annually-prepared pro forma operating budget and/or the assessment and reserve funding disclosure summary.

Funds are being accumulated in the replacement fund based on estimated future costs for repairs and replacement of common property components. Actual expenditures and investment income 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, subject to the constraints in its governing documents and California civil code, to increase regular assessments, pass special assessments, or delay major repairs and replacements until funds are available.

**4. COMMITMENTS**

The Association enters into contracts for management and/or maintenance services in the normal course of its business operations. These contracts are generally cancelable on thirty to ninety days' advance notice.

**5. SUBSEQUENT EVENTS**

The Association's management has reviewed the results of operations for the period of time from its year ended August 31, 2015 through October 21, 2015, the date the financial statements were available to be issued, and has determined that no adjustments are necessary to the amounts reported in the accompanying financial statements nor subsequent events have occurred, the nature of which would require disclosure.

**SUPPLEMENTAL INFORMATION**

## MISSION GROVE HOMEOWNERS ASSOCIATION

### Supplementary Information on Future Major Repairs and Replacements August 31, 2015

In June 2013 a component study update, with a site-visit was completed by John D. Beatty & Company 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 derived from actual contractor prices or by using standard industry estimating techniques and have not been updated since that date. Funding requirements consider an annual component cost inflation rate of 3% and an interest rate of 1/2% earned on cash and investments on amounts funded for future major repairs and replacements.

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

<b>Major Components</b>	<b>Estimated Remaining Useful Lives (Years)</b>	<b>Estimated Current Replacement Costs</b>
Building exteriors	1 - 23	\$ 593,109
Fencing & walls	1	107,974
Gates	1 - 24	79,015
Landscaping	1 - 13	54,167
Laundry rooms	3 - 4	17,070
Light fixtures	1 - 17	14,901
Mechanical systems - HVAC	5 - 14	7,590
Mechanical systems - water	1 - 2	38,275
Paved surfaces	1 - 13	338,813
Recreational building	1 - 7	38,528
Recreational facilities	1 - 5	53,629
Roofing systems - flat roofs	1 - 8	2,946,708
Other	1 - 13	25,139
Total Estimated Current Replacement Cost as of August 31, 2015		\$ 4,314,918
Replacement fund cash and investments at August 31, 2015		\$ 1,865,417

See independent accountant's review report.