

**The Mediterranean Villas Homeowners Association
Financial Statements
For the Year Ended December 31, 2018**

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Independent Auditor's Report

To the Board of Directors of The Mediterranean Villas Homeowners Association

We have audited the accompanying financial statements of The Mediterranean Villas Homeowners Association (the "Association") which comprise the balance sheet as of December 31, 2018, 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 the 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 from 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.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of The Mediterranean Villas Homeowners Association as of December 31, 2018, and 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 a Matter on Future Major Repairs and Replacements

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

Disclaimer of Opinion of Required Supplementary Information

Accounting principles generally accepted in the United States of America require that Supplementary Information on Future Repairs and Replacements 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 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 the 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.

Newman & Associates, CPA, PC

Newman & Associates, CPA, PC

Bellevue, Washington

August 01, 2019

The Mediterranean Villas Homeowners Association
Balance Sheet
December 31, 2018

	Operating Fund	Replacement Fund	Total
Assets			
Cash and cash equivalents	\$ 331,783	\$ 325,015	\$ 656,798
Investments		249,195	249,195
Assessments receivable	1,130		1,130
Prepaid insurance	679		679
Prepaid expenses	175		175
Total assets	\$ 333,767	\$ 574,210	\$ 907,977
Liabilities			
Accounts payable	\$ 8,815	\$ -	\$ 8,815
Prepaid assessments	33,908		33,908
Income taxes payable	2,107		2,107
Total liabilities	44,830	-	44,830
Fund balances	288,937	574,210	863,147
Total liabilities and fund balances	\$ 333,767	\$ 574,210	\$ 907,977

The accompanying notes are an integral part of the financial statements
(See Independent Auditor's Report)

The Mediterranean Villas Homeowners Association
Statement of Revenue and Expenses and Changes in Fund Balances
For the Year Ended December 31, 2018

	Operating Fund	Replacement Fund	Total
Revenues			
Owners assessments	\$ 270,000	\$ 72,000	\$ 342,000
Rental income	6,276		6,276
Interest	343	6,712	7,055
Other member income	1,196		1,196
Total revenues	<u>277,815</u>	<u>78,712</u>	<u>356,527</u>
Expenses			
Utilities			
Electricity and gas	2,272		2,272
Water and sewer	31,229		31,229
	<u>33,501</u>	-	<u>33,501</u>
Maintenance			
Landscape and irrigation	115,599		115,599
Tree trimming and removal	8,389		8,389
Common area repairs and maintenance	11,927		11,927
Pest control	357		357
Fences and walls	3,903		3,903
	<u>140,175</u>	-	<u>140,175</u>
Administrative			
Insurance	9,175		9,175
Administrative expense	2,302		2,302
Accounting services	14,880		14,880
Legal and professional	3,048		3,048
Licenses, permits, fees and taxes	10		10
Property tax	886		886
Federal taxes	3,259		3,259
	<u>33,560</u>	-	<u>33,560</u>
Total expenses	<u>207,236</u>	<u>-</u>	<u>207,236</u>
Excess (deficit) of revenues over (under) expenses	70,579	78,712	149,291
Beginning fund balances	251,252	462,604	713,856
Interfund transfers	(32,894)	32,894	-
Ending fund balances	<u>\$ 288,937</u>	<u>\$ 574,210</u>	<u>\$ 863,147</u>

The accompanying notes are an integral part of the financial statements
(See Independent Auditor's Report)

The Mediterranean Villas Homeowners Association
Statement of Cash Flows
For the Year Ended December 31, 2018

	<u>Operating Fund</u>	<u>Replacement Fund</u>	<u>Total</u>
Excess (deficit) of revenues over (under) expenses	\$ 70,579	\$ 78,712	\$ 149,291
Adjustments to reconcile excess (deficit) of revenues over (under) expenses to net cash provided (used) by operating activities			
Decrease (Increase) in operating assets:			
Accounts receivable	(519)		(519)
Prepaid expenses	(152)		(152)
Prepaid income tax	152		152
Increase (decrease) in operating liabilities:			
Accounts payable	283		283
Prepaid assessments	908		908
Income taxes payable	2,107		2,107
Total adjustments	<u>2,779</u>	<u>-</u>	<u>2,779</u>
Net cash provided (used) by operating activities	<u>73,358</u>	<u>78,712</u>	<u>152,070</u>
Cash provided (used) by investing activities			
Change in investments		1,739	1,739
Net cash provided (used) by investing activities	<u>-</u>	<u>1,739</u>	<u>1,739</u>
Cash provided (used) by financing activities			
Interfund transfers	(32,894)	32,894	-
Net cash provided (used) by financing activities	<u>(32,894)</u>	<u>32,894</u>	<u>-</u>
Net increase (decrease) in cash and cash equivalents	40,464	113,345	153,809
Beginning cash and cash equivalents	291,319	211,670	502,989
Ending cash and cash equivalents	<u><u>331,783</u></u>	<u><u>\$ 325,015</u></u>	<u><u>\$ 656,798</u></u>
SUPPLEMENTAL DISCLOSURE			
Income taxes paid			\$ -
Interest paid			\$ -

The accompanying notes are an integral part of the financial statements
(See Independent Auditor's Report)

The Mediterranean Villas Homeowners Association
Notes to Financial Statements
For the Year Ended December 31, 2018

1. Organization

The Mediterranean Villas Homeowners Association (the "Association") was incorporated on September 19, 2002 as a nonprofit corporation under the laws of Washington, for the purposes of maintaining and preserving common property. The Association consists of 228 residential homes and is located in Pasco, Washington.

2. Summary of Significant Accounting Policies

Basis of Accounting

The Association maintains its financial records on the accrual basis of accounting, which recognizes revenues when earned and expenses when incurred.

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires the board of directors 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 reporting period. Actual results could differ significantly from those estimates.

Fund Accounting

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 designated purposes.

Capital Assets and Depreciation Policy

The Association has not capitalized real and personal common area property contributed by the developer. Replacements and improvements to real property are also not capitalized; rather, they are charged to the respective fund in the period the cost is incurred. Significant personal property assets are capitalized and depreciated over their estimated lives using straight-line depreciation.

Cash and Cash Equivalents

Cash and cash equivalents include the Association's cash, checking accounts, money market funds and investments in certificates of deposit with original maturities of 90 days or less.

Investments

Investments consist of certificates of deposit and other securities and investment accounts with original maturities of more than 90 days.

Subsequent Events

Subsequent events have been evaluated through August 01, 2019, which is the date the financial statements were available to be issued.

The Mediterranean Villas Homeowners Association
Notes to Financial Statements
For the Year Ended December 31, 2018

3. Assessments and Assessments Receivable

Association members are subject to monthly assessments to provide funds for the Association's operating expenses, future capital acquisitions, and major repairs and replacements. Assessments receivable represent fees due from owners. The Association's governing documents provide for various collection remedies for delinquent assessments and fees, including filing of liens on an owner's unit, foreclosing on a unit owner, and obtaining a legal judgment on an owner's other assets. Any excess operating funds are retained at the end of the fiscal year for use in future periods. After the Association has exhausted all efforts to collect delinquent accounts, the Board of Directors may elect to write off uncollectible balances.

4. Future Major Repairs and Replacements

The Association's governing documents require funds to be accumulated for future major repairs and replacements. Accumulated funds are held in separate bank accounts and are generally not available for expenditures for normal operations.

The board of directors conducted a reserve study to estimate the remaining useful lives and the replacement costs of the components of common property. The table included in the unaudited Supplementary Information on Future Major Repairs and Replacements is based on this study.

The Association is funding such major repairs and replacements over the estimated useful lives of the components based on the study's estimates of current replacement costs, considering amounts previously accumulated in the replacement fund. Actual expenditures, however, may vary from estimated amounts and the variations may be material. Therefore, amounts accumulated in the replacement fund may or may not be adequate to meet future needs. If additional funds are needed, however, the Association has the right, subject to its governing documents, to increase regular assessments or to levy special assessments, or it may delay major repairs and replacements until funds are available.

5. Federal Income Taxes

Associations may be taxed either as homeowners associations or as regular corporations. For the current year the Association elected to file as a homeowners association using form 1120-H under Internal Revenue Code Section 528. Under that Section, the Association is not taxed on income and the expenses related to its exempt purpose, which is the acquisition, construction, management, maintenance and care of Association property. Net nonexempt function income which includes interest, user fees and revenues from non-members is taxed at 30%. Certain expenses were allocated to offset a portion of the taxable income.

The Association's federal tax return is subject to audit by the Internal Revenue Service. The tax returns for the current and prior two fiscal years remain open for examination by the IRS. In evaluating the Association's tax positions and accruals, the Association believes that its estimates are appropriate based on the current facts and circumstances.

The Mediterranean Villas Homeowners Association
Supplementary Information on Future Major Repairs and Replacements
December 31, 2018
(Unaudited)

The Association's board of directors, in conjunction with a reserve study expert, conducted a reserve study dated September 5, 2018 to estimate the remaining useful lives and the replacement costs of the components of common property. Replacement costs were based on the estimated costs to repair or replace the common property components on the date of the study.

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

Study Component	Estimated remaining useful lives	Estimated current replacement costs
Indoor common area	3-14	\$ 70,657
Outdoor common area	0-16	139,909
Heating and landscaping	0-6	39,527
Entrance maintenance	0-9	46,457
Painting	0-20	2,038,464
Miscellaneous	0-29	140,505
		<u>\$ 2,475,519</u>
Replacement fund balance at December 31, 2018		<u>\$ 574,210</u>
<u>Other Assumptions:</u>		
Interest rate		<u>1.41%</u>
Inflation rate		<u>2.29%</u>

See the Balance Sheet for replacement fund cash, cash equivalents and investments balances at December 31, 2018.