

**STREAM HOUSE COMMUNITY ASSOCIATION  
COMPARATIVE FINANCIAL STATEMENTS  
DECEMBER 31, 2011 AND 2010**

STREAM HOUSE COMMUNITY ASSOCIATION

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# Schonwit & Company

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### INDEPENDENT AUDITORS' REPORT

To the Owners  
Stream House Community Association

We have audited the accompanying balance sheet of Stream House Community Association, a California mutual benefit corporation, 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. The prior year summarized comparative information is presented for comparative purposes only and has been extracted from the Stream House Community Association's financial statements presented by fund for 2010 on which we expressed an unqualified opinion in our report dated March 16, 2011.

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 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.

A recent 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/replacement obligations until sufficient funds are available.

In our opinion the accompanying financial statements referred to above present fairly, in all material respects, the financial position of Stream House Community 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.

The supplementary information on future major repairs and replacements that accompanies the basic financial statements is not a required part of the basic financial statements but is supplementary information required by the American Institute of Certified Public Accountants. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

*Schonwit & Co.*

SCHONWIT & COMPANY

February 20, 2012

STREAM HOUSE COMMUNITY ASSOCIATION  
BALANCE SHEET  
AS OF DECEMBER 31, 2011  
(WITH COMPARATIVE TOTALS FOR 2010)

	2011			2010
	Operating Fund	Replacement Fund	Total	Total
<b>ASSETS</b>				
Cash and cash equivalents [Note 7]	\$ 39,273	\$ 101,042	\$ 140,315	\$ 141,238
Member assessments receivable, less allowance for doubtful collection of \$10,900 at 12/31/11 and \$15,200 at 12/31/10	12,489	-	12,489	10,708
Prepaid insurance	105	-	105	207
Prepaid taxes	480	-	480	480
Due (to)/from fund	(1,542)	1,542	-	-
Total Assets	<u>\$ 50,805</u>	<u>\$ 102,584</u>	<u>\$ 153,389</u>	<u>\$ 152,633</u>
<b>LIABILITIES</b>				
Accounts payable	\$ 28,562	\$ -	\$ 28,562	\$ 25,520
Prepaid assessments	2,271	-	2,271	3,817
Income taxes payable	10	-	10	10
Total Liabilities	30,843	-	30,843	29,347
<b>FUND BALANCES</b>	<u>19,962</u>	<u>102,584</u>	<u>122,546</u>	<u>123,286</u>
<b>TOTAL LIABILITIES AND FUND BALANCES</b>	<u>\$ 50,805</u>	<u>\$ 102,584</u>	<u>\$ 153,389</u>	<u>\$ 152,633</u>

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

STREAM HOUSE COMMUNITY ASSOCIATION  
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN FUND BALANCES  
FOR THE YEAR ENDED DECEMBER 31, 2011  
(WITH COMPARATIVE TOTALS FOR 2010)

	2011			2010
	Operating Fund	Replacement Fund	Total	Total
<b>REVENUES</b>				
Member assessments	\$ 401,076	\$ 136,764	\$ 537,840	\$ 537,840
Special assessment [Note 5]	--	26,892	26,892	--
Interest	--	45	45	104
Other income	5,045	--	5,045	5,539
Total Revenues	<u>406,121</u>	<u>163,701</u>	<u>569,822</u>	<u>543,483</u>
<b>EXPENSES</b>				
Utilities:				
Electricity	65,449	--	65,449	66,777
Water	49,873	--	49,873	44,542
Gas	2,453	--	2,453	2,482
Refuse	11,535	--	11,535	12,604
Maintenance:				
Landscape maintenance and supplies	99,104	--	99,104	73,460
Stream and stream pumps	25,157	--	25,157	32,426
Patrol services	3,700	--	3,700	3,303
Lighting maintenance and supplies	5,604	--	5,604	6,556
Pool service, supplies and repairs	4,969	--	4,969	5,541
Janitorial service and supplies	2,281	--	2,281	2,813
Pest control	13,268	--	13,268	10,882
Plumbing repairs	6,609	--	6,609	--
Other common area maintenance	36,519	--	36,519	26,485
Replacement fund [Note 9]	--	167,878	167,878	68,113
Administrative:				
Insurance	34,292	--	34,292	33,567
Management fees	34,800	--	34,800	33,600
Professional fees	2,584	--	2,584	4,459
Income taxes [Note 4]	10	--	10	10
Postage and printing expense	2,029	--	2,029	1,376
Other administrative expenses	980	--	980	171
Amortization expense	--	--	--	375
Interest expense	--	--	--	803
Bad debt expense	1,468	--	1,468	10,325
Total Expenses	<u>402,684</u>	<u>167,878</u>	<u>570,562</u>	<u>440,670</u>
<b>EXCESS OF REVENUES OVER/(UNDER) EXPENSES</b>	3,437	(4,177)	(740)	102,813
<b>Beginning Fund Balances</b>	29,680	93,606	123,286	20,473
<b>Interfund Transfer</b>	(13,155)	13,155	--	--
<b>Ending Fund Balances</b>	<u>\$ 19,962</u>	<u>\$ 102,584</u>	<u>\$ 122,546</u>	<u>\$ 123,286</u>

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

STREAM HOUSE COMMUNITY ASSOCIATION  
STATEMENT OF CASH FLOWS  
FOR THE YEAR ENDED DECEMBER 31, 2011  
(WITH COMPARATIVE TOTALS FOR 2010)

	<u>2011</u>			<u>2010</u>
	<u>Operating Fund</u>	<u>Replacement Fund</u>	<u>Total</u>	<u>Total</u>
<b>Excess of revenues over/(under) expenses:</b>	\$ 3,437	\$ (4,177)	\$ (740)	\$ 102,813
Adjustments to reconcile excess of revenues over/(under) expenses to net cash provided/(used) by operating activities:				
Amortization expense	-	-	-	375
(Increase)/decrease in member assessments receivable	(1,781)	-	(1,781)	2,368
(Increase)/decrease in prepaid insurance	102	-	102	(1)
Increase/(decrease) in accounts payable	3,042	-	3,042	(2,669)
Decrease in accrued interest payable	-	-	-	(160)
Decrease in prepaid assessments	(1,546)	-	(1,546)	(593)
Change in due to/(from) fund	14,697	(14,697)	-	--
Net cash provided/(used) by operating activities	<u>17,951</u>	<u>(18,874)</u>	<u>(923)</u>	<u>102,133</u>
Cash provided by investing activities:				
Acquisition of certificates of deposit	-	-	-	--
Maturity of certificates of deposit	-	-	-	30,148
Net cash flows from investing activities	<u>-</u>	<u>-</u>	<u>-</u>	<u>30,148</u>
Cash used by financing activities:				
Principal loan payments	-	-	-	(43,608)
Interfund transfer	(13,155)	13,155	-	--
Net increase/(decrease) in cash	4,796	(5,719)	(923)	88,673
Cash at beginning of year	<u>34,477</u>	<u>106,761</u>	<u>141,238</u>	<u>52,565</u>
Cash at end of year	<u>\$ 39,273</u>	<u>\$ 101,042</u>	<u>\$ 140,315</u>	<u>\$ 141,238</u>

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

STREAM HOUSE COMMUNITY ASSOCIATION  
NOTES TO FINANCIAL STATEMENTS  
DECEMBER 31, 2011

NOTE 1.      ORGANIZATION

Stream House Community Association [the Association] is a statutory homeowners association which was organized as a non-profit mutual benefit corporation in February 1982. The purpose of the Association is primarily to maintain, preserve and control the common areas of the Association. The Association consists of 166 residential units and is located in Orange, California.

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 financial statements, adjustments have been made at December 31, 2011 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)      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, 2011, 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 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 February 20, 2012, 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, 2010, from which the summarized information was derived.

STREAM HOUSE COMMUNITY ASSOCIATION  
NOTES TO FINANCIAL STATEMENTS  
DECEMBER 31, 2011

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, 2011, the Association elected to file as a homeowners association, where generally the association is taxed only on income unrelated to membership dues and assessments [such as interest income less related expenses]. 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, 2011, the federal and California income tax expense was \$0 and \$10, 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, 2011 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, 2011, the Association has recorded an allowance for uncollectible assessments of \$10,900. This allowance represents an estimated amount which was calculated using historical collection information.

For the year ended December 31, 2011, the Association's monthly assessment was \$270 per unit. Additionally, the Association collected a one-time special assessment of \$162 per unit for asphalt work throughout the Association. For 2012, the monthly assessment is budgeted to remain at \$270 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.



STREAM HOUSE COMMUNITY ASSOCIATION  
NOTES TO FINANCIAL STATEMENTS  
DECEMBER 31, 2011

NOTE 6. REPLACEMENT FUNDING PROGRAM – (CONTINUED)

An independent study of the Association's replacement funding program, which was conducted in 2012, indicates that the Association is underfunded. Accordingly, the study recommends a contribution to the replacement fund of approximately \$258,960 for 2012. 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, 2011, the Association funded \$136,764 from regular assessments and \$26,892 from the special assessment to the replacement fund. The 2012 budget includes a provision for replacement funding of \$124,140 (\$62.32 per unit per month). 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, 2011 and 2010, the Association maintained cash balances at the following institutions:

<u>Operating Fund:</u>	<u>2011</u>	<u>2010</u>
Wells Fargo Bank - checking	\$ 39,273	\$ 27,085
Sunwest Bank - checking	-	7,392
	<u>          </u>	<u>          </u>
Total Cash - Operating Fund	<u>\$ 39,273</u>	<u>\$ 34,477</u>
<u>Replacement Fund:</u>		
Sunwest Bank - savings	<u>\$ 101,042</u>	<u>\$ 106,761</u>

NOTE 8. SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION

There were no cash payments for income taxes for the year ended December 31, 2011. There were no non-cash investing or financing transactions during the year.

STREAM HOUSE COMMUNITY ASSOCIATION  
NOTES TO FINANCIAL STATEMENTS  
DECEMBER 31, 2011

NOTE 9. REPLACEMENT FUND EXPENDITURES

Replacement fund expenditures for the years ended December 31, 2011 and 2010 are as follows:

	<u>2011</u>	<u>2010</u>
Asphalt work	\$ 49,889	\$ --
Deck repairs	35,090	4,523
Rain gutter and roof maintenance	23,575	26,944
Concrete work	23,332	5,198
Lighting/electrical repairs	9,674	-
Dry rot/termite repairs	9,159	8,257
Painting	5,753	7,825
Plumbing repairs	3,069	-
Window repairs/replacements	2,480	-
Landscape	1,750	-
Mailboxes	1,712	-
Drywall repairs	917	-
Storage closets	908	-
Stucco repairs	570	-
Stream repairs	--	13,048
Doors	--	1,340
Waterproofing wall	--	978
	<u>\$ 167,878</u>	<u>\$ 68,113</u>
Total		

STREAM HOUSE COMMUNITY ASSOCIATION  
 REQUIRED SUPPLEMENTARY INFORMATION  
 ON FUTURE MAJOR REPAIRS & REPLACEMENTS  
 AS OF DECEMBER 31, 2011  
 (UNAUDITED)

An independent reserve study was conducted in 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 3.5%. 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% (net of taxes).

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>Study's Recommended Fund Balance</u>
Painting	0-3 years	\$ 506,200	\$ 436,750
Lighting	0 years	20,700	20,700
Roofs	0-4 years	611,300	595,960
Pool/spa.	0-7 years	24,700	18,260
Asphalt	3-4 years	223,600	181,720
Tree maintenance	0 years	31,100	31,100
Irrigation controllers	0-3 years	20,100	19,600
Patio furnitures	0 years	4,500	4,500
Termite	0 years	3,800	3,800
Streams	0-7 years	123,200	94,320
Mailboxes	0 years	16,200	16,200
Decks	0-5 years	377,400	289,310
Fences/railings	0-7 years	64,300	61,840
Doors	6 years	78,000	57,420
Gates	1 year	12,200	11,340
Bridge	21 years	10,000	3,310
	Total	<u>\$ 2,127,300</u>	<u>\$ 1,846,130</u>
Replacement Fund balance at 12/31/11:			<u>\$ 102,584</u>
Study's recommended funding requirement for 2012:			<u>\$ 258,960</u>