

NEWPORT HILLS COMMUNITY ASSOCIATION

Audited Financial Statements

For The Year Ended December 31, 2023

TABLE OF CONTENTS

	PAGE
INDEPENDENT AUDITORS' REPORT	3-4
BALANCE SHEET	5
STATEMENT OF REVENUE, EXPENSES AND ASSOCIATION FUNDS	6
STATEMENT OF CASH FLOWS	7
NOTES TO FINANCIAL STATEMENTS	8-11
SUPPLEMENTAL INFORMATION	12
SUPPLEMENTAL INFORMATION ON FUTURE MAJOR REPAIRS	13

OWENS, MOSKOWITZ AND ASSOCIATES, INC.

CERTIFIED PUBLIC ACCOUNTANTS

27792 EL LAZO

LAGUNA NIGUEL, CALIFORNIA 92677

TELEPHONE: (949) 851-5020

E-MAIL: bob@raocpa.com Web Site: www.raocpa.com

MEMBER:
AMERICAN INSTITUTE
OF CERTIFIED
PUBLIC ACCOUNTANTS

MEMBER:
CALIFORNIA SOCIETY
OF CERTIFIED PUBLIC
ACCOUNTANTS

INDEPENDENT AUDITOR'S REPORT

Board of Directors
Newport Hills Community Association

Opinion

We have audited the accompanying financial statements of Newport Hills Community Association (a California corporation), which comprise the balance sheet as of December 31, 2023, and the related statements of revenue, expenses and association funds, and cash flows for the year then ended, and the related notes to the financial statements.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Newport Hills Community Association as of December 31, 2023, and the results of its operations and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Basis for Opinion

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of our report. We are required to be independent of Newport Hills Community Association and to meet our other ethical responsibilities in accordance with the relevant ethical requirements relating to our audit. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Future Major Repairs and Replacement

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 replacement as discussed in Note 3 are adequate to meet such future costs because that determination is outside the scope of our audit. Our opinion is not modified with respect to that matter.

Responsibilities of Management 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, and for 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.

In preparing the financial statements, management is required to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about Newport Hills Community Association's ability to continue as a going concern within one year after the date that the financial statements are available to be issued.

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance but is not absolute assurance and therefore is not a guarantee that an audit conducted in accordance with generally accepted auditing standards will always detect a material misstatement when it exists. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. Misstatements are considered material if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgment made by a reasonable user based on the financial statements.

In performing an audit in accordance with generally accepted auditing standards, we:

- Exercise professional judgment and maintain professional skepticism throughout the audit.
- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements.
- Obtain an understanding of internal control relevant to the audit 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 Newport Hills Community Association's internal control. Accordingly, no such opinion is expressed.
- Evaluate the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluate the overall presentation of the financial statements.
- Conclude whether, in our judgment, there are conditions or events, considered in the aggregate, that raise substantial doubt about Newport Hills Community Association's ability to continue as a going concern for a reasonable period of time.

We are required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit, significant audit findings, and certain internal control related matters that we identified during the audit.

Disclaimer of Opinion on Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the information on future major repairs and replacements of common property on page 13 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, which 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 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.

Owens, Moskowitz and Associates, Inc.

April 17, 2024

Owens, Moskowitz and Associates, Inc.

NEWPORT HILLS COMMUNITY ASSOCIATION
BALANCE SHEET
DECEMBER 31, 2023

	OPERATING FUND	REPLACEMENT FUND	TOTAL
ASSETS			
Cash	\$ 507,196	\$ 752,836	\$ 1,260,032
Short-Term Investments	-	1,071,223	1,071,223
Assessments Receivable	2,610	-	2,610
Interest Receivable	-	2,077	2,077
Prepaid Insurance	9,564	-	9,564
Due From/(Due To) Other Funds	110,018	(110,018)	-
Total Assets	\$ 629,388	\$ 1,716,118	\$ 2,345,506
LIABILITIES AND ASSOCIATION FUNDS			
Liabilities			
Accounts Payable	\$ 15,930	\$ -	\$ 15,930
Prepaid Assessments	248,552	-	248,552
Refundable Deposits	272,902	-	272,902
Deferred Assessments (Assessments Received In Advance - Replacement Fund)	-	1,716,118	1,716,118
Income Taxes Payable	13,996	-	13,996
Total Liabilities	551,380	1,716,118	2,267,498
Commitments	-	-	-
Association Funds	78,008	-	78,008
Total Liabilities And Association Funds	\$ 629,388	\$ 1,716,118	\$ 2,345,506

SEE INDEPENDENT AUDITORS' REPORT AND ACCOMPANYING NOTES

NEWPORT HILLS COMMUNITY ASSOCIATION
STATEMENT OF REVENUE, EXPENSES AND ASSOCIATION FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2023

	OPERATING FUND	REPLACEMENT FUND	TOTAL
REVENUE			
Assessments	\$ 586,099	\$ (5,192)	\$ 580,907
Interest Income	158	61,207	61,365
Swim Program Income	9,688	-	9,688
Clubhouse/Recreation Center Rental	18,459	-	18,459
Release of Swim Team Account	(91,774)	-	(91,774)
Other Income	11,850	-	11,850
Total Revenue	534,480	56,015	590,495
EXPENSES			
Landscape Maintenance	114,530	16,065	130,595
On-site Manager	83,000	-	83,000
Administrative	17,974	-	17,974
Legal And Audit	35,787	-	35,787
Insurance	21,337	-	21,337
Pool	30,949	-	30,949
Rubbish Collection	7,080	-	7,080
Pest Control	995	-	995
Telephone	8,132	-	8,132
Painting	-	9,500	9,500
General Maintenance	23,128	26,377	49,505
Reserve Study	900	-	900
Gas	69,250	-	69,250
Electricity	33,560	-	33,560
Water	40,874	-	40,874
Custodial	36,989	-	36,989
Clubhouse Security	88,425	-	88,425
Plumbing	-	1,193	1,193
Clubhouse/Pool Management	30,766	-	30,766
Payroll and Related Expenses	22,448	-	22,448
Lighting and Electrical	4,293	2,880	7,173
Income Tax	13,996	-	13,996
Total Expenses	684,413	56,015	740,428
Excess (Deficiency) of Revenue Over Expenses	(149,933)	-	(149,933)
Association Funds Balance Beginning of Year	227,941	-	227,941
Association Funds Balance End of Year	\$ 78,008	\$ -	\$ 78,008

SEE INDEPENDENT AUDITORS' REPORT AND ACCOMPANYING NOTES

NEWPORT HILLS COMMUNITY ASSOCIATION
STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED DECEMBER 31, 2023

	OPERATING FUND	REPLACEMENT FUND	TOTAL
Cash Flows From Operating Activities:			
Cash Received From Members	\$ 557,208	\$ 185,301	\$ 742,509
Cash Paid To Suppliers of Goods And Services	(675,691)	(56,015)	(731,706)
Architectural Deposits Collected	55,213	-	55,213
Interest Received	158	59,258	59,416
Income Taxes Paid	(5,187)	-	(5,187)
Net Cash Provided By (Used In) Operating Activities	(68,299)	188,544	120,245
Cash Flows From Investing Activities:			
Maturity (Purchase) of Short-Term Investments	-	(428,673)	(428,673)
Cash Flows From Financing Activities:			
Interfund Borrowings	4,710	(4,710)	-
Net Increase (Decrease) In Cash And Cash Equivalents	(63,589)	(244,839)	(308,428)
Cash And Cash Equivalents At Beginning of Year	570,785	997,675	1,568,460
Cash And Cash Equivalents At End of Year	\$ 507,196	\$ 752,836	\$ 1,260,032

RECONCILIATION OF EXCESS OF REVENUE OVER EXPENSES
TO NET CASH PROVIDED BY OPERATING ACTIVITIES

Excess (Deficiency) of Revenue Over Expenses	\$ (149,933)	\$ -	\$ (149,933)
Adjustments To Reconcile Excess (Deficiency) of Revenue Over Expenses To Net Cash Provided By Operating Activities:			
Change In Assessments Receivable	(657)	-	(657)
Change In Interest Receivable	-	(1,949)	(1,949)
Change In Prepaid Insurance	(845)	-	(845)
Change In Accounts Payable	(4,429)	-	(4,429)
Change In Deferred Assessments	-	190,493	190,493
Change In Prepaid Assessments	23,543	-	23,543
Change In Architectural Deposits	55,213	-	55,213
Change In Income Tax Payable	8,809	-	8,809
Net Cash Provided By (Used In) Operating Activities	\$ (68,299)	\$ 188,544	\$ 120,245

SEE INDEPENDENT AUDITORS' REPORT AND ACCOMPANYING NOTES

NEWPORT HILLS COMMUNITY ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2023

NOTE 1 NATURE OF ORGANIZATION

Newport Hills Community Association was incorporated on April 13, 1970, in the state of California. It is responsible for the operation and maintenance of the common property within the development, which is located in the city of Newport Beach, California. The development consists of 532 residential units.

NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Method of Accounting

The books of Newport Hills Community Association are maintained on the modified cash basis of accounting with entries made to convert them to the accrual basis for audit and tax purposes.

Fund Accounting

The Association's governing documents provide certain guidelines for governing its financial activities. To ensure 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 the following funds established according to their nature and purpose:

- Operating fund - This fund is used to account for financial resources available for the general operations of the Association.
- Replacement fund - This fund is used to accumulate financial resources designated for future major repairs and replacements.

Deferred Assessments (Assessments received in advance-replacement fund)

The Association recognizes revenue from members as the related performance obligations are satisfied. Deferred assessments (assessments received in advance-replacement fund) are recorded when the Association has the right to receive payment in advance of the satisfaction of performance obligations related to replacement reserve assessments. The activity in deferred assessments (assessments received in advance-replacement fund) during 2023 was as follows:

Deferred Assessments, at January 1, 2023	\$ 1,525,625
Assessments Budgeted for Replacement Reserve	185,301
Interest Earned on Reserve Bank Accounts	61,207
Revenue Released to Match Reserve Expenses	<u>(56,015)</u>
Deferred Assessments, at December 31, 2023	<u>\$ 1,716,118</u>

Cash Equivalents and Short-term 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 short-term investments. Cash equivalents and short-term investments are stated at cost, which approximates market value.

The Association maintains bank accounts at various financial institutions. During the course of the year, the accounts may fluctuate over the FDIC insured amount.

SEE INDEPENDENT AUDITORS' REPORT

NEWPORT HILLS COMMUNITY ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2023
(CONTINUED)

NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Member Assessments

Association members are subject to semi-annual assessments to provide funds for the Association's operating expenses and major repairs and replacements. Assessment revenue is recognized as the related performance obligations are satisfied at transaction amounts expected to be collected. The Association's performance obligations related to its operating assessments is satisfied over time on a daily pro-rata basis using the input method. The performance obligations related to the replacement fund assessments are satisfied when these funds are expended for their designated purpose. Assessments receivable at the balance sheet date are stated at the amounts expected to be collected from outstanding assessments from unit owners. The Association's policy is to retain legal counsel and place liens on the properties of homeowners whose assessments are ninety days or more delinquent. Any excess assessments at year end are retained by the Association for use in the succeeding year. The balances of assessments receivable as of the beginning and end of the year were \$1,953 and \$2,610, respectively.

Use of Estimates

The Association uses estimates and assumptions in preparing these financial statements in accordance with generally accepted accounting principles. Those estimates and assumptions affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, and the reported revenues and expenses. Actual results could vary from the estimates that were used.

Credit Losses Implementation

In June 2016, the FASB issued ASU 2016-13, *Financial Instruments – Credit Losses (Topic 326)*. This guidance represents a significant change in the accounting model for credit losses by requiring immediate recognition of management's estimates of "current expected credit losses". Under the prior model, losses were recognized only as they were incurred, which FASB has noted delayed recognition of expected losses that might not yet have met the threshold of being probable. The new model is applicable to all financial instruments that are not accounted for at fair value through net income, thereby bringing consistency in accounting treatment across different types of financial instruments and requiring consideration of a broader range of variables when forming loss estimates. The Association adopted this standard on January 1, 2023 by using a "Loss rate approach – Individual Evaluation". An allowance for expected credit losses is established for any account that is six months or older which has historically been reliable. The cumulative effect of adopting this new accounting policy resulted in no change to the beginning of the year allowance for expected credit losses or the operating fund balance.

Management believes that the historical loss information it has compiled is a reasonable basis on which to determine expected credit losses of assessments receivables held at December 31, 2023 because the composition of the member receivables at that date is consistent with that used in developing the historical credit-loss percentages (i.e. the similar risk characteristics of its members and its lending practices have not changed significantly over time). Accordingly, the allowance for expected credit losses at December 31, 2023 totaled \$-0-.

Property and Equipment

Real property and common areas acquired by the original homeowners from the developer are owned by the individual owners in common and are not capitalized on the Association's financial statements.

Replacements and improvements to the real property and common areas also belong to the owners and are not capitalized on the Association's financial statements.

SEE INDEPENDENT AUDITORS' REPORT

NEWPORT HILLS COMMUNITY ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2023
(CONTINUED)

NOTE 3 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 accounts and are generally not available for operating purposes. It is the Association's policy to allocate interest earned on such funds to the replacement fund. Since the actual costs are dependent upon the frequency of occurrence and future costs, there is no assurance that this fund is adequate.

A study of the Association's funding program for the replacement of Association common areas, projected to December 31, 2023, indicates the Association's ideal cash replacement fund balance was \$ 1,842,880 at that date. The study recommends a 2024 contribution to the replacement fund of \$ 228,326 (\$ 35.77 per owner per month). The 2024 budgeted contribution is \$ 228,326.

The preparation of such a study involves significant estimates by the persons preparing the study, and these estimates are subject to annual revision for changing prices, circumstances and assumptions. If actual replacement costs exceed funds available, or where replacement of common areas is necessary where no fund has been previously established, the Association has the right to increase the monthly assessments, pass special assessments, or delay replacement until funds are available.

NOTE 4 INCOME TAXES

The Association is a corporation that is potentially taxable on all of its net income, including unspent member assessments. However, under state and federal filing elections, the Association may choose to be taxed only on its net non-membership income, which includes interest income.

The State of California allows qualifying homeowner associations to file an election to be taxed under special rules. Under this election, income from members (such as assessments) is exempt from taxation.

Federal law offers a similar election, which must be made annually. However, net non-membership income under this election is taxed at a flat rate of 30%. If the Association chooses to file as a regular corporation, it may still exclude from taxation its net membership income by making certain elections. Tax at the regular corporate tax rate is generally lower. Some of these elections, however, have come under IRS attack and certain issues are yet to be clarified.

In 2023, the Association filed as a regular corporation for federal taxes, since it had an excess of maintenance expenses over membership source income. That excess may be carried over to future periods to offset future membership source income when the Association files as a regular corporation. This election is not related to the issues involved in the IRS audits.

Regardless of how the Association files its taxes, non-membership income (interest) may not be offset with membership expenses (such as common area maintenance costs). That is why the Association's taxable income can be greater than its net income as recorded in the financial statements.

Accounting principles generally accepted in the United States of America require management to evaluate tax positions taken by the Association and recognize a tax liability if the Association has taken an uncertain position that more likely than not would not be sustained upon examination by the IRS. Management has analyzed the tax positions taken by the Association and has concluded that as of December 31, 2023, there are no uncertain positions taken or expected to be taken that would require recognition of a liability or disclosure in the financial statements. The Association is subject to routine audits by taxing jurisdictions; however, there are currently no audits in progress. The Association's management believes it is no longer subject to income tax examinations for years prior to 2019.

SEE INDEPENDENT AUDITORS' REPORT

NEWPORT HILLS COMMUNITY ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2023
(CONTINUED)

NOTE 4 INCOME TAXES (Continued)

Federal and California income taxes have been accrued based on the taxable portion of the income reported in the accompanying financial statements. Income taxes for the current year were:

2023 INCOME TAXES	FEDERAL	STATE TAX	STATE FEE	TOTAL
Income Taxes	\$ 11,253	\$ 2,743	\$ -	\$ 13,996
Less: Estimated payments	-	-	-	-
Income tax payable	\$ 11,253	\$ 2,743	\$ -	\$ 13,996

NOTE 5 ASSESSMENTS

During 2023, assessments were billed at a rate of \$ 725 per unit semi-annually. Effective January 1, 2024, the rate increased to \$ 800 per unit semi-annually.

NOTE 6 INTERFUND ACCOUNT

The interfund account represents the amount one fund owes another fund. Various scenarios may cause this situation which include, but are not limited to, one fund paying the expenses of another fund, one fund borrowing from another fund, or the operating fund not paying the full annual budgeted contribution amount to the replacement fund.

NOTE 6 RELATED PARTY TRANSACTIONS

During 2023, the Association's on-site manager paid for miscellaneous maintenance, administrative expenses and reserve expenses on behalf of the Association and received total reimbursements of \$9,873.

During 2023, the Association's clubhouse and pool manager paid for miscellaneous maintenance and administrative expenses on behalf of the Association and received total reimbursements of \$1,022.

Beach & Bay Lighting is owned by the Association's clubhouse/pool manager. During 2023, the Association used this vendor for holiday decoration. The Association paid the vendor \$ 3,100 during the year.

Philco is owned by the Association's on-site manager. During 2023, the Association used this vendor to provide general maintenance replacement work. The Association paid the vendor \$3,660 during the year.

NOTE 7 SWIM TEAM ACCOUNT

During 2023, the swim team stopped operating under the Association's tax identification number. As such, the swim team controlled account has been removed from the Association's financials.

NOTE 8 SUBSEQUENT EVENTS

The date to which events occurring after December 31, 2023, the date of the most recent balance sheet, have been evaluated for possible adjustment to the financial statements or disclosure is April 17, 2024, which is the date on which the financial statements were issued.

SEE INDEPENDENT AUDITORS' REPORT

SUPPLEMENTAL INFORMATION

NEWPORT HILLS COMMUNITY ASSOCIATION
 SUPPLEMENTAL INFORMATION ON FUTURE MAJOR REPAIRS
 AND REPLACEMENTS
 DECEMBER 31, 2023
 (UNAUDITED)

The board of directors contracted an independent consultant who conducted a August 25, 2023 study, projected to December 31, 2023, to estimate the remaining useful lives and replacement costs of the components of common property. Funding requirements include an inflation factor of 2.5% and an interest rate of 2.5%.

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

<u>Components</u>	<u>Estimated Remaining Useful Lives</u>	<u>Estimated Current Replacement Cost</u>	<u>2024 Funding Requirement</u>	<u>Recommended Fund Balances</u>
Clubhouse Roofs	1 year	\$ 130,648	\$ 9,198	\$ 124,275
Painting	0 to 1 year	96,521	23,096	90,399
Lighting	4 to 21 years	60,330	4,048	23,533
Fencing/Walls	0 to 10 years	393,627	24,508	324,515
Pool/Pool Area/Wader	0 to 14 years	588,601	54,648	382,975
Clubhouse	0 to 17 years	605,018	48,188	297,835
Grounds	0 to 14 years	797,300	56,870	541,372
Guardhouse	0 years	4,300	790	4,300
Contingency	n/a	-	6,980	53,676
		<u>\$ 2,676,345</u>	<u>\$ 228,326</u>	<u>\$ 1,842,880</u>

As shown above, the study recommends a cash replacement balance of \$1,842,880 as of December 31, 2023 and contributions to reserves of \$228,326 during 2024. The Association's total replacement fund total assets at December 31, 2023 were \$1,716,118 or 93.12% of the recommended balance.