

**NELLIE GAIL RANCH OWNERS' ASSOCIATION
FINANCIAL STATEMENTS
FOR THE YEAR ENDED SEPTEMBER 30, 2018**

**NELLIE GAIL RANCH OWNERS' ASSOCIATION
FINANCIAL STATEMENTS
For the Year Ended September 30, 2018**

TABLE OF CONTENTS

Independent Auditor's Report 1

Balance Sheet..... 2

Statement of Revenues and Expenses and Changes in Fund Balances 3

Statement of Cash Flows 4

Notes to Financial Statements 5-7

Supplementary Information 8

Independent Auditor's Report

To the Board of Directors of Nellie Gail Ranch Owners' Association

We have audited the accompanying financial statements of Nellie Gail Ranch Owners' Association (the "Association"), which comprise the balance sheet as of September 30, 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 Nellie Gail Ranch Owners' Association as of September 30, 2018, and 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.

Emphasis of a Matter – Future Major Repairs and Replacements

Our audit was made for the purpose of forming an opinion on the basis financial statements, taken as a whole. We have not applied procedures to determine whether the funds designated for future repairs and replacements (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 the Supplementary Information on Future Repairs and Replacements on page 8 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

Carlsbad, California
December 10, 2018

NELLIE GAIL RANCH OWNERS' ASSOCIATION
BALANCE SHEET
September 30, 2018

	<u>Operating Fund</u>	<u>Replacement Fund</u>	<u>Equestrian Fund</u>	<u>Swim Fund</u>	<u>Tennis Fund</u>	<u>Total</u>
Assets						
Cash and cash equivalents	\$ 1,224,526	\$ 384,430	\$ 283,882	\$ 87,861	\$ 306,828	\$ 2,287,527
Investments		3,321,081				3,321,081
Assessments receivable	76,945		-			76,945
Allowance for doubtful accounts	(50,435)					(50,435)
Interest receivable		27,909				27,909
Prepaid insurance	34,501		8,926			43,427
Fixed assets	480,768		742,552	563,578	844,247	2,631,145
Accumulated depreciation	(365,525)		(609,159)	(475,591)	(686,408)	(2,136,683)
Deferred expenses	24,000					24,000
Total Assets	<u>\$ 1,424,780</u>	<u>\$ 3,733,420</u>	<u>\$ 426,201</u>	<u>\$ 175,848</u>	<u>\$ 464,667</u>	<u>\$ 6,224,916</u>
Liabilities						
Accounts payable	\$ 33,042	\$ -	\$ 17,468	\$ 3,111	\$ 3,869	\$ 57,490
Payroll payable	15,347					15,347
Prepaid assessments	161,588					161,588
Paid time off payable	41,952					41,952
Income Tax payable	1,801					1,801
Deposits	367,701		60,376			428,077
Total liabilities	<u>621,431</u>	<u>-</u>	<u>77,844</u>	<u>3,111</u>	<u>3,869</u>	<u>706,255</u>
Fund balances	<u>803,349</u>	<u>3,733,420</u>	<u>348,357</u>	<u>172,737</u>	<u>460,798</u>	<u>5,518,661</u>
Total liabilities and fund balances	<u>\$ 1,424,780</u>	<u>\$ 3,733,420</u>	<u>\$ 426,201</u>	<u>\$ 175,848</u>	<u>\$ 464,667</u>	<u>\$ 6,224,916</u>

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

**NELLIE GAIL RANCH OWNERS' ASSOCIATION
STATEMENT OF REVENUES AND EXPENSES AND
CHANGES IN FUND BALANCES
For the Year Ended September 30, 2018**

	Operating Fund	Replacement Fund	Equestrian Fund	Swim Fund	Tennis Fund	Total
Revenues						
Owners' assessments	\$ 1,836,188	\$ 247,200	\$ -	\$ 136,022	\$ -	\$ 2,219,410
Equestrian center income		110,400	648,584			758,984
Swim club income		59,400		23,271		82,671
Tennis club income		78,000			70,560	148,560
Newsletter	88,458					88,458
Cell tower revenue	109,685					109,685
Interest	3,876	46,006	-			49,882
Maintenance revenue from Association			24,000			24,000
Other member income	208,685		124,506		83,421	416,612
Total revenues	<u>2,246,892</u>	<u>541,006</u>	<u>797,090</u>	<u>159,293</u>	<u>153,981</u>	<u>3,898,262</u>
Expenses						
Utilities						
Electricity and gas	2,732		15,866	51,463	39,595	109,656
Water and sewer	60,447		16,047	5,804	3,000	85,298
Trash removal	15,019			600	600	16,219
Telephone, cable, internet and website	11,451		2,934	1,783	2,387	18,555
	89,649	-	34,847	59,650	45,582	229,728
Common area and equestrian						
Landscape and irrigation	508,509		15,483	2,292	11,126	537,410
Tree trimming	5,280		5,625	875	6,093	17,873
Trail maintenance	169,125					169,125
Common area repairs and maintenance	39,062		94,827	5,576	9,869	149,334
Pool and spa				23,553		23,553
Pest control	15,995		8,308	971	2,179	27,453
Janitorial	31,935		1,900	9,045	3,940	46,820
Emergency preparedness and security	196,600					196,600
Feed and shavings			302,374			302,374
	966,506	-	428,517	42,312	33,207	1,470,542
Administrative						
Insurance	70,860		811	11,653		83,324
Accounting	45,146					45,146
Payroll and related expenses	562,071		357,442	16,442	82,390	1,018,345
Administrative expense	98,933		14,921	-	-	113,854
Operating contingency	10,471					10,471
Newsletter expense	54,258					54,258
Legal and professional	215,240			11,475		226,715
Collection costs	9,725					9,725
Social activities	70,013					70,013
Property tax, Licenses and permits	760		400	678		1,838
Income tax expense	5,605					5,605
Capital expenditures	73,483		5,875	-		79,358
Depreciation expense	10,175		4,731	1,781	9,720	26,407
	1,226,740	-	384,180	42,029	92,110	1,745,059
Major repairs and replacements		180,042				180,042
Total expenses	<u>2,282,895</u>	<u>180,042</u>	<u>847,544</u>	<u>143,991</u>	<u>170,899</u>	<u>3,625,371</u>
Excess(deficit) of revenues over(under) expenses	(36,003)	360,964	(50,454)	15,302	(16,918)	272,891
Beginning fund balances	839,352	3,372,456	398,811	157,435	477,716	5,245,770
Ending fund balances	<u>\$ 803,349</u>	<u>\$ 3,733,420</u>	<u>\$ 348,357</u>	<u>\$ 172,737</u>	<u>\$ 460,798</u>	<u>\$ 5,518,661</u>

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

NELLIE GAIL RANCH OWNERS' ASSOCIATION
STATEMENT OF CASH FLOWS
For the Year Ended September 30, 2018

	<u>Operating Fund</u>	<u>Replacement Fund</u>	<u>Equestrian Fund</u>	<u>Swim Fund</u>	<u>Tennis Fund</u>	<u>Total</u>
Excess(deficit) of revenues over(under) expenses	\$ (36,003)	\$ 360,964	\$ (50,454)	\$ 15,302	\$ (16,918)	\$ 272,891
Adjustments to reconcile excess(deficit) of revenues over(under) expenses to net cash provided(used) by operating activities						
Assessments receivable	32,780	-	22,132	-	-	54,912
Allowance for doubtful accounts	(52,080)	-	-	-	-	(52,080)
Interest receivable	-	(22,303)	-	-	-	(22,303)
Other receivable	11	-	-	-	-	11
Prepaid insurance	7,948	-	(8,926)	-	-	(978)
Prepaid taxes	1,910	-	-	-	-	1,910
Deferred expenses	73,483	-	-	-	-	73,483
Depreciation	10,175	-	4,731	1,781	9,720	26,407
Accounts payable	(13,755)	-	2,940	(2,073)	187	(12,701)
Payroll payable	(2,918)	-	-	-	-	(2,918)
Prepaid assessments	3,560	-	-	-	-	3,560
Paid time off payable	5,020	-	-	-	-	5,020
Income taxes payable	1,801	-	-	-	-	1,801
Deposits	32,302	-	4,350	-	-	36,652
Net cash provided(used) by operating activities	<u>100,237</u>	<u>(22,303)</u>	<u>25,227</u>	<u>(292)</u>	<u>9,907</u>	<u>112,776</u>
Cash provided(used) by investing activities:						
Increase in investments	-	(1,192,683)	-	-	-	(1,192,683)
Net cash flows from investing activities	<u>-</u>	<u>(1,192,683)</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(1,192,683)</u>
Cash provided(used) by financing activities:						
Net cash flows from financing activities	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
Net increase(decrease) in cash and cash equivalents	64,234	(854,022)	(25,227)	15,010	(7,011)	(807,016)
Cash and cash equivalents at beginning of year	1,160,292	1,238,452	309,109	72,851	313,839	3,094,543
Cash and cash equivalents at end of year	<u>\$ 1,224,526</u>	<u>\$ 384,430</u>	<u>\$ 283,882</u>	<u>\$ 87,861</u>	<u>\$ 306,828</u>	<u>\$ 2,287,527</u>
SUPPLEMENTAL DISCLOSURE						
Income taxes paid						\$ 6,400
Interest paid						<u>\$ -</u>

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

NELLIE GAIL RANCH OWNERS' ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
For the Year Ended September 30, 2018

1. Organization

Nellie Gail Ranch Owners' Association (the "Association") was incorporated on November 19, 1976 as a mutual benefit corporation under the laws of California, for the purposes of maintaining and preserving common property. The Association consists of 1,407 residential homes and is located in Laguna Hills, California.

2. Summary of Significant Accounting Policies

Basis of Accounting

The Association maintains its financial records on the cash basis of accounting, which recognizes revenues when received and expenses when paid. Adjustments at the end of the fiscal year result in these financial statements being presented on the full accrual basis of accounting.

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 require signatures from the board of directors or officers as specified by California Civil Code, and generally may be made only for designated purposes. The Association maintains additional funds for Equestrian, Swim and Tennis.

Investment Income

The board's policy is to account for interest income in the fund in which it is earned. The Association pays related income taxes from the operating fund.

Property, Equipment and Depreciation Policy

The Association has not capitalized real and personal common area property contributed by the developer. Property and equipment purchased by the association has been recorded at cost, and depreciated using the straight-line method over estimated useful lives ranging from five to thirty years.

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.

NELLIE GAIL RANCH OWNERS' ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
For the Year Ended September 30, 2018

Subsequent Events

Subsequent events have been evaluated through December 10, 2018, which is the date the financial statements were available to be issued.

3. Assessments and Assessments Receivable

Association members are subject to quarterly assessments of \$398 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. The Association records an allowance for doubtful accounts to reflect an estimate of accounts that may not be collectible, which includes receivables greater than 90 days old.

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 Association's board of directors, in conjunction with a reserve study expert, conducted a reserve study dated August 13, 2018 to estimate the remaining useful lives and the replaces costs of the components of the common property. Replace costs were based on the estimated costs to repair or replace the common property components on the date of the 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 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. Income Taxes

The Association has federal tax-exempt status under Internal Revenue Code Section 501(c)(4), and is exempt from federal income taxes on all non-business activities. The Association has not met the criteria to file as a homeowners' association for its California income tax return, and is taxed as a regular corporation for state purposes. The Internal Revenue Service and the California Franchise Tax Board can examine the Association's income tax returns generally up to three years and four years, respectively. The Association has not been examined by taxing authorities. The Association's tax positions have been in place beyond the statutes of limitations; and the Board has considered that the tax positions the Association has taken will be sustained if examined by taxing authorities.

NELLIE GAIL RANCH OWNERS' ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
For the Year Ended September 30, 2018

6. Compensated Absence Liability

Employees of the Association are entitled to paid vacation, paid sick days and personal days off, depending on job classification, length of service, and other factors. The estimated liability for paid time off has been accrued in the amount of \$41,952.

7. Pension Plan

The Association's Simple IRA plan covers employees who have completed at least three months of service. The Association matches 100% of employee contributions up to 3% of compensation. The plan administrator is Assembly Pointe Financial. During the year ended September 30, 2018, the Association contributed \$17,194 to the plan.

8. Tennis, Swim Club and Equestrian Facilities License Agreements

In October 2011, the Association entered into an agreement to lease the tennis courts to provide services and/or conduct activities related to tennis instruction to the Members. The agreement was restructured in October 2018 for the period November 1, 2018 through October 2019. The agreement directs all Tennis Club Membership dues to the Association. In addition, the service provider pays the Association a fixed annual fee of \$10,000 for rights to run the Summer Tennis Camp.

In November 2011, the Association entered into a license agreement with a licensee to provide services and/or conduct activities related to swim program services to the Participant Members. The contract was renewed in October 2018, to extend the term through September 30, 2019. The Service Provider is required to pay a flat monthly usage fee for swim team practice of \$2,550, as well as a monthly amount equivalent to 20% of the swim lesson revenues.

The Association entered into a license agreement in September, 2015 with a service provider for the use of certain amenities and areas of the Association's equestrian facilities for the purpose of providing equestrian training and instruction. During the year ended September 30, 2018, the service provider paid a monthly fee of \$2,220. In October 2018, the Association renewed the one-year arrangement via a service agreement with Hayden Show Jumping and Riding School (Trainer), with monthly fees totaling \$2,420.

9. Contingent Liabilities and Litigation

The Association has ongoing claims made against it that result from the normal operations of the Association. The Association believes that it has adequate legal defense and insurance to be sufficiently protected from potentially adverse legal consequences.

10. Deferred Expenses

Through the year ended September 30, 2018, the Association incurred clubhouse renovation architectural, permitting and other planning costs totaling \$24,000. These costs have been accounted for as work in progress, and will be recognized upon completion of the clubhouse renovation project.

NELLIE GAIL RANCH OWNERS' ASSOCIATION
SUPPLEMENTARY INFORMATION ON FUTURE MAJOR
REPAIRS AND REPLACEMENTS
For the Year Ended September 30, 2018
(Unaudited)

The Association's board of directors, in conjunction with a reserve study expert, conducted a reserve study dated August 13, 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 - HOA	Estimated remaining useful lives	Estimated current replacement costs	Study recommended annual funding requirement	Study recommended fund balance
Paved surfaces	0-9	\$ 261,500	18840	\$ 213,650
Landscape	0-10	257,400	31752	191,472
Office components	0-10	115,100	11412	84,580
Grounds	0-24	618,350	109992	405,345
Dapple grey	0-5	163,500	9768	133,938
Gallup park	0-18	154,025	7620	110,506
Hidden trail	0-5	74,150	5028	58,196
Hundred foot arena	0-5	46,330	2076	40,218
Moulton Park	0-16	131,450	6156	117,535
Cabot Arena	0-18	96,460	7356	47,295
		<u>1,918,265</u>	<u>210,000</u>	<u>1,402,735</u>
Study Component - Equine		1,738,792	153,600	1,104,021
Study Component - Swim		577,650	59,400	339,239
Study Component - Tennis		851,485	81,600	652,772
		<u>\$ 5,086,192</u>	<u>\$ 504,600</u>	<u>\$ 3,498,767</u>
Replacement fund balance at September 30, 2018				<u><u>\$ 3,733,420</u></u>
Other Assumptions:				
Interest rate				<u>1.00%</u>
Inflation rate				<u>3.00%</u>