

TREO MAINTENANCE ASSOCIATION

DATE: April 2023
TO: Treo Maintenance Association
FROM: Rina Sagal, Community Manager

Dear Homeowner:

In accordance with California Civil Code Section 5305 this notice is to advise you that the Annual Audit for the fiscal year end December 31, 2022 has been completed. This audit was prepared by an independent CPA firm, Owens, Moskowitz and Associates, Inc. and has been accepted by the Board of Directors. You may view a copy of the complete audit at www.myhoa.com/treo.

Please be advised, as a property owner, you have the right under California Civil Code Section 4950 to obtain copies of minutes of the Board of Directors meetings for a nominal fee. You may send your request in writing to the Board of Directors in care of Management at the address below.

The meetings of the Board of Directors are scheduled to be held on a regular basis on the third Tuesday of the odd months via zoom. These meeting dates are subject to change or cancellation if there is a lack of quorum of the Board. Please call StoneKastle Community Management to confirm the meeting you plan to attend.

Should you have any questions, regarding the enclosed information, please contact the Board, in writing or attend a Board meeting.

TREO MAINTENANCE ASSOCIATION

Audited Financial Statements

For The Year Ended December 31, 2022

OWENS, MOSKOWITZ AND ASSOCIATES, INC.

CERTIFIED PUBLIC ACCOUNTANTS

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OF CERTIFIED PUBLIC
ACCOUNTANTS

INDEPENDENT AUDITOR'S REPORT

Board of Directors
Treo Maintenance Association

Opinion

We have audited the accompanying financial statements of Treo Maintenance Association (a California corporation), which comprise the balance sheet as of December 31, 2022, 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 Treo Maintenance Association as of December 31, 2022, 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 Treo Maintenance 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.

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 Treo Maintenance 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 Treo Maintenance 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 Treo Maintenance 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.

March 27, 2023

Owens, Moskowitz and Associates, Inc.

TREC MAINTENANCE ASSOCIATION
BALANCE SHEET
DECEMBER 31, 2022

	OPERATING FUND	REPLACEMENT FUND	TOTAL
ASSETS			
Cash	\$ 35,578	\$ 922,025	\$ 957,603
Short-Term Investments	-	400,000	400,000
Assessments Receivable	32,251	-	32,251
Less: Allowance For Doubtful Accounts	(27,332)	-	(27,332)
Interest Receivable	-	2,574	2,574
Prepaid Taxes	1,653	-	1,653
Prepaid Insurance	3,604	-	3,604
Total Assets	\$ 45,754	\$ 1,324,599	\$ 1,370,353
LIABILITIES AND ASSOCIATION FUNDS			
Liabilities			
Accounts Payable	\$ 2,711	\$ -	\$ 2,711
Prepaid Assessments	25,063	-	25,063
Deferred Assessments (Assessments Received In Advance - Replacement Fund)	-	1,324,599	1,324,599
Total Liabilities	27,774	1,324,599	1,352,373
Commitments	-	-	-
Association Funds	17,980	-	17,980
Total Liabilities And Association Funds	\$ 45,754	\$ 1,324,599	\$ 1,370,353

SEE INDEPENDENT AUDITORS' REPORT AND ACCOMPANYING NOTES

TREO MAINTENANCE ASSOCIATION
STATEMENT OF REVENUE, EXPENSES AND ASSOCIATION FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2022

	OPERATING FUND	REPLACEMENT FUND	TOTAL
	<u> </u>	<u> </u>	<u> </u>
REVENUE			
Assessments	\$ 219,096	\$ 134,635	\$ 353,731
Price Adjustment - Bad Debt	(17,506)	-	(17,506)
Interest Income	25	7,631	7,656
Other Income	8,641	-	8,641
Total Revenue	210,256	142,266	352,522
EXPENSES			
Landscape Maintenance	112,709	-	112,709
Management Fees	19,200	-	19,200
Administrative	8,578	-	8,578
Legal And Audit	11,716	-	11,716
Insurance	29,552	-	29,552
Pest Control	3,465	-	3,465
Painting	-	32,175	32,175
General Maintenance	20,484	10,843	31,327
Reserve Study	700	-	700
Electricity	8,367	-	8,367
Water	19,192	-	19,192
Pavements	-	2,134	2,134
Fence	-	6,994	6,994
Lighting and Electrical	5,082	-	5,082
Plumbing	4,301	-	4,301
Roof and Decks	5,775	90,120	95,895
Income Tax	1,778	-	1,778
Total Expenses	250,899	142,266	393,165
Deficiency of Revenue Over Expenses	(40,643)	-	(40,643)
Association Funds Balance Beginning of Year	58,623	-	58,623
Association Funds Balance End of Year	\$ 17,980	\$ -	\$ 17,980

SEE INDEPENDENT AUDITORS' REPORT AND ACCOMPANYING NOTES

TREC MAINTENANCE ASSOCIATION
STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED DECEMBER 31, 2022

	OPERATING FUND	REPLACEMENT FUND	TOTAL
Cash Flows From Operating Activities:			
Cash Received From Members	\$ 225,497	\$ 153,504	\$ 379,001
Cash Paid To Suppliers of Goods And Services	(241,010)	(142,266)	(383,276)
Interest Received	25	5,229	5,254
Net Cash Provided By (Used In) Operating Activities	(15,488)	16,467	979
Cash Flows From Investing Activities:			
Maturity of Short-Term Investments	-	400,000	400,000
Net Increase (Decrease) In Cash And Cash Equivalents	(15,488)	416,467	400,979
Cash And Cash Equivalents At Beginning of Year	51,066	505,558	556,624
Cash And Cash Equivalents At End of Year	\$ 35,578	\$ 922,025	\$ 957,603

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

Deficiency of Revenue Over Expenses	\$ (40,643)	\$ -	\$ (40,643)
Adjustments To Reconcile Deficiency of Revenue Over Expenses To Net Cash Provided By Operating Activities:			
Change In Assessments Receivable	11,316	-	11,316
Change In Interest Receivable	-	(2,402)	(2,402)
Change In Prepaid Insurance	3,581	-	3,581
Change In Prepaid Expenses	5,701	-	5,701
Change In Prepaid Taxes	1,778	-	1,778
Change In Accounts Payable	(1,171)	-	(1,171)
Change In Deferred Assessments	-	18,869	18,869
Change In Prepaid Assessments	3,950	-	3,950
Net Cash Provided By (Used In) Operating Activities	\$ (15,488)	\$ 16,467	\$ 979

SEE INDEPENDENT AUDITORS' REPORT AND ACCOMPANYING NOTES

TREGO MAINTENANCE ASSOCIATION
 NOTES TO FINANCIAL STATEMENTS
 FOR THE YEAR ENDED DECEMBER 31, 2022

NOTE 1 NATURE OF ORGANIZATION

Trego Maintenance Association was incorporated on January 13, 2005, 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 Irvine, California. The development consists of 135 residential units.

NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Method of Accounting

The books of Trego Maintenance 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 2022 was as follows:

Deferred Assessments, at January 1, 2022	\$	1,305,730
Assessments Budgeted for Replacement Reserve		153,504
Revenue Released to Match Reserve Expenses		<u>(134,635)</u>
Deferred Assessments, at December 31, 2022	\$	<u>1,324,599</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.

TREO MAINTENANCE ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 2022
(CONTINUED)

NOTE 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Member Assessments

Association members are subject to monthly 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. At December 31, 2022, the Association had delinquent assessments of \$32,051, where an allowance for uncollectible accounts is deemed necessary.

The Association treats uncollectible assessments as credit losses. Methods, inputs, and assumptions used to evaluate when assessments are considered uncollectible include consideration of past experience and susceptibility to factors outside the Association's control. The balances of assessments receivable as of the beginning and end of the year were \$26,060 and \$32,051, respectively.

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.

Credit Losses

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. Although this change affects any entity holding financial instruments (ie: trade receivables or investments in debt securities) the financial services industry by its nature bears the most exposure. The effect of adoption of this standard will be to accelerate the recognition of credit losses. The effective date of this standard is for years beginning after December 15, 2023, with early adoption allowed. We do not plan an early adoption of this standard.

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.

SEE INDEPENDENT AUDITORS' REPORT

TREC MAINTENANCE ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 2022
(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, 2022, indicates the Association's ideal cash replacement fund balance was \$ 1,503,707 at that date. The study recommends a 2023 contribution to the replacement fund of \$ 180,500 (\$ 111.42 per owner per month). The 2023 budgeted contribution is \$ 180,504.

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 2022, 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 recent 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, 2022, 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 2018.

SEE INDEPENDENT AUDITORS' REPORT

TREO MAINTENANCE ASSOCIATION
NOTES TO FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 2022
(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:

2022 INCOME TAXES	FEDERAL	STATE TAX	STATE FEE	TOTAL
Income Taxes	\$ 1,163	\$ 615	\$ -	\$ 1,778
Less: Credit from prior year return	(2,680)	(751)	-	(3,431)
Prepaid tax	\$ 1,517	\$ 136	\$ -	\$ 1,653

NOTE 5 ASSESSMENTS

During 2022, assessments were billed at a rate of \$ 230 per unit per month. Effective January 1, 2023, the rate increased to \$ 250 per unit per month.

NOTE 6 BALCONY INSPECTION

On August 30, 2019, Senate Bill No. 326 added Civil Code section 5551 (the "Code") to the Davis-Stirling Act. The Code adds a requirement for homeowners associations with buildings with three or more multifamily dwellings to perform inspections of balconies and other exterior structural elements that the association has an obligation to maintain. The exterior structural elements primarily include any load bearing components (i.e. balconies, decks, stairways, walkways, railings) that extend beyond the exterior walls of the building that are supported by wood or wood-based products and are more than six feet above the ground. Inspections must be performed by a licensed structural engineer or architect. The first inspection must be completed by the end of 2024 with continuing inspections required every nine years.

NOTE 7 CONTINGENCY

In March 2020, the World Health Organization declared the novel strain of coronavirus (COVID-19) a global pandemic. As a result, economic uncertainties have arisen that may adversely affect the Association. However, the financial impact, if any, cannot be reasonably estimated at this time.

NOTE 8 SUBSEQUENT EVENTS

The date to which events occurring after December 31, 2022, the date of the most recent balance sheet, have been evaluated for possible adjustment to the financial statements or disclosure is March 27, 2023, which is the date on which the financial statements were issued.

SEE INDEPENDENT AUDITORS' REPORT

SUPPLEMENTAL INFORMATION

TREC MAINTENANCE ASSOCIATION
 SUPPLEMENTAL INFORMATION ON FUTURE MAJOR REPAIRS
 AND REPLACEMENTS
 DECEMBER 31, 2022
 (UNAUDITED)

The board of directors contracted an independent consultant who conducted a September 9, 2022 study, projected to December 31, 2022, 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 1.5%.

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>2023 Funding Requirement</u>	<u>Recommended Fund Balances</u>
Streets	0 to 4 years	\$ 151,681	\$ 11,432	\$ 126,229
Roofs - Tile Repairs	0 years	20,407	18,465	20,407
Painting	0 to 4 years	315,209	50,864	257,714
Gates/Railing/Walls	4 to 18 years	364,869	17,194	239,254
Lighting	8 to 12 years	144,100	6,090	87,141
Decks/Doors	3 to 23 years	654,019	38,823	382,434
Building Exterior	2 to 18 years	316,335	19,863	176,170
Grounds	3 to 11 years	48,500	3,036	29,401
Termite Control	4 years	174,375	9,475	141,161
Contingency	n/a	-	5,257	43,797
		<u>\$ 2,189,495</u>	<u>\$ 180,500</u>	<u>\$ 1,503,707</u>

As shown above, the study recommends a cash replacement balance of \$1,503,707 as of December 31, 2022 and contributions to reserves of \$180,500 during 2023. The Association's total replacement fund total assets at December 31, 2022 were \$1,324,599 or 88.09% of the recommended balance.