

Bluegrass Owners Association

Audit Report Financial Statements & Supplementary Information December 31, 2017

Cagianut & Company
CERTIFIED PUBLIC ACCOUNTANT
www.hoacpa.com

Members - Community Associations Institute—Washington State
Washington Society of Certified Public Accountants
American Institute of Certified Public Accountants

Independent Auditors' Report

To the Board of Directors and Members
Bluegrass Owners Association
Everett, Washington

Report on the Financial Statements

We have audited the accompanying financial statements of Bluegrass Owners Association, which comprise the Balance Sheet as of December 31, 2017, and the related Statement of Changes in Fund Balances, Statement of Revenues and Expenses and Statement of Cash Flows for the year then ended and the related notes to the financial statements.

Association's Responsibility for the Financial Statements

The Association 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 of 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 Bluegrass Owners Association as of December 31, 2017, 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 of America.

Other Matter - Required Supplementary Information

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 repairs and replacements are adequate to meet such future costs because that determination is outside the scope of our audit.

Accounting principles generally accepted in the United States of America [GAAP] require that the Supplementary Information on Future Major Repairs 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 and for placing the basic financial statements and related notes 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.

Cagianut & Company, CPA

Bellevue, Washington

May 1, 2018

Bluegrass Owners Association

Balance Sheet
December 31, 2017

	<u>OPERATING FUND</u>	<u>REPLACEMENT FUND</u>	<u>TOTAL</u>
ASSETS			
Cash, including interest bearing deposits	\$ 56,987	\$ 851,737	\$ 908,723
Assessments Receivable	42,599		42,599
Less: Allowance for Bad Debts	(6,019)		(6,019)
Prepaid Insurance	59,476		59,476
Utility Billing Receivable	11,535		11,535
Insurance Claim Receivable	34,629		34,629
Other Receivable	5,324		5,324
Fixed Assets	211,819		211,819
Less: Accumulated Depreciation	(78,324)		(78,324)
Due Between Funds	11,038	(11,038)	
TOTAL ASSETS	<u>\$ 349,062</u>	<u>\$ 840,699</u>	<u>\$ 1,189,761</u>
 LIABILITIES AND FUND BALANCES			
LIABILITIES			
Accounts Payable	\$ 11,073		\$ 11,073
Assessments Received in Advance	23,826		23,826
Mortgage Payable #R101	112,727		112,727
Security Deposits Held	4,392		4,392
Insurance Claim Payable	43,472		43,472
Income Taxes Payable	34		34
TOTAL LIABILITIES	<u>195,524</u>		<u>195,524</u>
 FUND BALANCES			
Operating	153,537		153,537
Replacement		\$ 840,699	\$ 840,699
TOTAL FUND BALANCES	<u>153,537</u>	<u>840,699</u>	<u>994,236</u>
TOTAL LIABILITIES AND FUND BALANCES	<u>\$ 349,062</u>	<u>\$ 840,699</u>	<u>\$ 1,189,761</u>

See Notes to the Financial Statements

Bluegrass Owners Association
Statement of Changes in Fund Balances
For the Year Ended December 31, 2017

	OPERATING FUND	REPLACEMENT FUND	TOTAL
Balance at the Beginning of the Year	\$ 298,882	\$ 621,938	\$ 920,820
Transfer Between Funds	(150,000)	150,000	
Excess <Deficiency> of Revenues over Expenses	4,655	68,761	73,416
Balance at the End of the Year	\$ 153,537	\$ 840,699	\$ 994,236

See Notes to the Financial Statements

Bluegrass Owners Association
Statement of Revenues and Expenses
For the Year Ended December 31, 2017

	OPERATING FUND	REPLACEMENT FUND	TOTAL
REVENUES			
Assessments	\$ 467,429	\$ 207,940	\$ 675,369
Late & NSF Fees	5,475		5,475
Utility Reimbursement	145,113		145,113
Legal Fees	14,073		14,073
Cable Income	8,358		8,358
Interest	197	2,017	2,214
Rental Units	29,679		29,679
Insurance Claim Proceeds	90,982		90,982
Miscellaneous	5,539		5,539
TOTAL REVENUES	766,844	209,957	976,801
EXPENSES			
Bad Debts	4,723		4,723
Electricity	16,941		16,941
Federal Taxes	1,834		1,834
Insurance	78,609		78,609
Insurance Claims	85,070		85,070
Landscape	79,370		79,370
Legal	15,950		15,950
Legal - Collections	16,729		16,729
Life Safety Systems	13,356		13,356
Management	63,706		63,706
Miscellaneous	30,135		30,135
Payroll	82,467		82,467
Payroll Taxes & Benefits	14,457		14,457
Rental Units	16,367		16,367
Repairs & Maintenance	37,725		37,725
Submetering Fees	8,553		8,553
Trash	27,931		27,931
Unit #R101 Depreciation	6,997		6,997
Unit #R101 Mortgage Interest	5,631		5,631
Water & Sewer	135,637		135,637
Window, Siding & Roof Cleaning	20,000		20,000
Replacement Fund Expenses			
Chimney Covers		10,222	10,222
Clubhouse Furniture Replacement		5,699	5,699
Concrete/Curb Repair/Replacement		7,110	7,110
Parking Space Addition		225	225
Pool Resurface		45,220	45,220
Reserve Contingency Expense		64,829	64,829
Vinyl Siding Clean/Inspect		7,890	7,890
TOTAL EXPENSES	762,189	141,196	903,385
EXCESS <DEFICIENCY> OF REVENUES OVER EXPENSES	\$ 4,655	\$ 68,761	\$ 73,416

See Notes to the Financial Statements

Bluegrass Owners Association
Statement of Cash Flows
For the Year Ended December 31, 2017

	OPERATING FUND	REPLACEMENT FUND	TOTAL
<i>Cash Flows from Operating Activities:</i>			
Cash from Assessments	\$ 450,352	\$ 207,940	\$ 658,292
Interest Received	197	2,017	2,214
Miscellaneous Income	299,219		299,219
Income Taxes Paid	(1,115)		(1,115)
Interest Paid	(5,631)		(5,631)
Cash Paid for Services and Products	(728,060)	(141,196)	(869,256)
Net Increase <Decrease> in Cash from Operating Activities	14,961	68,761	83,722
<i>Cash Flows from Financing Activities:</i>			
Loan Principal Payments	(9,579)		(9,579)
Transfers Between Funds	(150,000)	150,000	
Change in Due Between Funds	(7,989)	7,989	
Net Increase <Decrease> in Cash	(152,607)	226,750	74,143
Cash, including interest bearing deposits, at the Beginning of Year	209,594	624,987	834,580
Cash, including interest bearing deposits, at the End of Year	<u>\$ 56,987</u>	<u>\$ 851,737</u>	<u>\$ 908,723</u>

Reconciliation of Excess <Deficiency> of Revenues over Expenses to Net Cash Received by Operations:

Excess <Deficiency> of Revenues over Expenses	\$ 4,655	\$ 68,761	\$ 73,416
Increased Assessments Receivable	(25,145)		(25,145)
Increased Bad Debt Allowance	4,674		4,674
Decreased Prepaid Insurance	166		166
Decreased Prepaid Taxes	685		685
Decreased Prepaid Expenses	8,970		8,970
Increased Insurance Claim Receivable	(34,629)		(34,629)
Increased Other Receivable	(105)		(105)
Adjust for Depreciation	7,773		7,773
Decreased Accounts Payable	(3,657)		(3,657)
Increased Prepaid Assessments	8,068		8,068
Increased Taxes Payable	34		34
Increased Insurance Claim Payable	43,472		43,472
Net Increase <Decrease> in Operating Cash	<u>\$ 14,961</u>	<u>\$ 68,761</u>	<u>\$ 83,722</u>

See Notes to the Financial Statements

Bluegrass Owners Association

Notes to the Financial Statements
December 31, 2017

NOTE 1 - ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

General

Bluegrass Owners Association was incorporated March 22, 2006 in the state of Washington as a nonprofit corporation. The Association is responsible for the operation and maintenance of the common property. This is a 221-unit condominium development located in Everett, Washington.

Accounting Method

The Association prepares its statements on the accrual basis of accounting whereby income and expenses are recognized when earned and incurred. Fund accounting is employed to properly account for the monies. The Operating Fund is used to pay for all utility, insurance, general maintenance, landscaping, and administrative obligations of the Association. The Replacement Fund has been established to meet the replacement and major repair obligations of the Association with regard to the common area components.

Capitalization Policy

Replacements and improvements to the real property are not capitalized on the books of the Association as title is held by the members as a fractional interest as tenants in common. Property and equipment acquired by the Association are recorded at cost. The property is depreciated over its estimated useful lives using the straight line method of depreciation.

Assessments Receivable

Association members are subject to assessments to provide funds for the Association's operating expenses, future capital acquisitions, and major repairs and replacements. Assessments receivable at the balance sheet date represent fees due from unit owners. The Association's Declaration provides for various collection remedies for delinquent assessments including the filing of liens, foreclosing on the unit owner, and obtaining judgment on the assets of the unit owner. The Association uses the allowance method to account for uncollectible assessments receivable, which approximates the net realizable value.

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 reporting period. Actual results could differ from those estimates.

Cash, including Interest Bearing Deposits

For purposes of the statement of cash flows, Cash, including Interest Bearing Deposits, includes cash on hand, funds on deposit with financial institutions, and investments with original maturities of three months or less.

Fair Value Measurements

The three levels of the fair value hierarchy under ASC 820, Fair Value Measurements and Disclosures, are described below:

Level 1: Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that the Association has the ability to access.

Level 2: Inputs to the valuation methodology include quoted prices for similar assets or liabilities in active markets; quoted prices for identical or similar assets or liabilities in inactive markets; inputs other than quoted prices that are observable for the asset or liability; inputs that are derived principally from or corroborated by observable market data by correlation or other means. If the asset or liability has a specified (contractual) term, the Level 2 input must be observable for substantially the full term of the asset or liability.

Level 3: Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

Date of Review

In preparing the financial statements, the Association has evaluated events and transactions for potential recognition or disclosure through the date of the audit report, which is the date that the financial statements were issued or available to be issued.

Bluegrass Owners Association

Notes to the Financial Statements
December 31, 2017

NOTE 2 - REPLACEMENT FUNDING PROGRAM

The Association is currently funding for the future major repair and replacement of Association common areas as disclosed in Note 1. Accumulated funds are held in separate accounts and are generally not available for operating purposes. The funding is based upon a professional reserve study approved by the Board of Directors.

There were significant changes between the Required Supplementary Information presented in the prior audit and in the current audit. The Association had an updated reserve study prepared and it was determined that reserve component asset remaining lives and replacement costs required revision. Three of the most significant changes were: 1) adding of siding replacement to the funding plan due to the fact that the remaining useful life is now within the scope of the report, 2) adding windows/glass doors replacement to the funding plan due to the fact that the remaining useful life is now within the scope of the report, and 3) adding fire alarm system replacement to the funding plan with a one-time allowance for upgrading the system in six buildings. These changes have been approved by the Board of Directors.

Funds are being accumulated in the Replacement Fund based on estimates of future needs for repairs and replacements of common property components. Actual expenditures may vary from the estimated future expenditures, and variations may be material. Therefore, the amounts accumulated in the Replacement Fund 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 certain legal limitations, to increase assessments, pass special assessments, or delay replacement if these funds are found to be inadequate for all future costs.

NOTE 3 - FEDERAL INCOME TAXES

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

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

NOTE 4 - OWNERS' ASSESSMENTS

Monthly assessments to owners varied by unit. Of this amount, a portion was designated to the Replacement Fund.

The annual budget and owners' assessments are determined by the Board of Directors, within certain restrictions. The Association retains excess operating funds at the end of the year, if any, for use in future operating periods.

Bluegrass Owners Association

Notes to the Financial Statements
December 31, 2017

NOTE 5 - MORTGAGE PAYABLE

The Association purchased a unit within the complex on February 8, 2007 as noted in Note 7. The purchase price was \$190,000 and there were closing costs of \$2,419. The purchase was financed with a bank loan. The interest rate was 7.84% and the monthly payments were \$1,583. The interest rate is subject to change; the current interest rate is 4.92% and the monthly payments are \$1,279. The loan matures in February, 2027.

Based on borrowing rates currently available to the Association for loans with similar terms and maturities, the fair value of the loan payable is the same as the book value.

The principal payments for the next five years are as follows:

2018	\$	10,496
2019		10,557
2020		11,088
2021		11,646
2022		12,232
After 2022		56,708
	\$	<u>112,727</u>

NOTE 6 - SHERIFF'S/TRUSTEE SALES AND RENTAL UNITS

The Association obtained a unit at a Sheriff's Sale in May of 2011. No value has been assigned to the unit nor has the unit been included in the assets of the Association. The unit has been a rental since then.

A second unit was obtained by a Trustee Sale February 28, 2014 and immediately rented out. No value has been assigned to the unit nor has the unit been included in the assets of the Association.

NOTE 7 - FIXED ASSETS/ASSOCIATION-OWNED UNIT

The Association acquired the manager unit, R101 in 2007 at a cost of \$192,419. In addition, the Association purchased Garage #311 in 2015 for a cost of \$19,400.

Association-Owned Unit #R101	\$	192,419
Garage #311	\$	19,400
	\$	<u>211,819</u>
Less: Accumulated Depreciation	\$	<u>(78,324)</u>
	\$	<u>133,495</u>

NOTE 8 - RELATED PARTY TRANSACTIONS - MANAGEMENT COMPANY

The management company provided payroll services to the Association including providing contract personnel services. The Association paid \$98,347 to the management company in 2017 for this service.

Bluegrass Owners Association
December 31, 2017
Supplementary Information on Future Major Repairs
and Replacements
(Unaudited)

An update "with-site-visit" reserve study was prepared on December 1, 2017 by Association Reserves for the period January 1, 2018 to December 31, 2018 to estimate the remaining useful lives and the replacement costs of the components of common property. The estimates were based on current estimated replacement costs. Funding requirements consider an annual inflation rate of 3.0% and interest of 1.0%, net of taxes, on amounts funded for future major repairs and replacements. The following table is based on the study and presents significant information about the components of common property.

Component	Estimated Remaining Useful Life in Years	Estimated Current Replacement Costs	Fund Balance at Year End
Special Projects			
Fire Alarm System - 2018 Replace	0	\$ 32,500	
Fire Alarm System - 2019 Replace	1	32,500	
Fire Alarm System - 2020 Replace	2	32,500	
Fire Alarm System - 2021 Replace	3	32,500	
Fire Alarm System - 2022 Replace	4	32,500	
Fire Alarm System - 2023 Replace	5	32,500	
Fire Sprinkler Piping - Replace	0	45,000	
Site/Grounds			
Concrete/Curb - Repair/Replace	4	5,500	
Asphalt, Phase 1 - Resurface	25	71,600	
Asphalt, Phase 2 - Resurface	28	152,000	
Asphalt - Seal/Repair	0	30,300	
Entry Gates - Repair/Replace	10	10,950	
Entry Gate Operators - Replace	9	6,050	
Gate Access Panel - Replace	2	3,250	
Metal Fence - Replace	36	67,800	
Metal Rail - Replace	12	6,900	
Trash Enclosures - Repair/Replace	19	2,800	
Pole Lights - Replace	12	24,100	
Mailboxes - Replace	15	12,050	
Storage Shed - Replace	12	5,500	
Recreation/Clubhouse			
Pool Deck - Resurface	12	38,050	
Pool Fence - Repair/Replace	12	9,800	
Pool/Spa - Resurface	11	22,000	
Pool Tile/Coping - Replace	23	18,500	
Pool/Spa Heaters - Replace	6	7,650	
Basketball Equipment - Replace	10	3,250	
Chain Link Fence - Replace	12	8,850	
Play Equipment - Replace	4	6,550	
Exercise Equipment - Replace	0	8,750	
Clubhouse Interior Walls - Repaint	0	11,500	
Clubhouse Flooring - Replace	10	12,300	
Clubhouse Carpet - Replace	0	8,540	
Clubhouse Kitchen - Refurbish	10	6,600	
Clubhouse Appliances - Replace	5	3,850	
Clubhouse Bathrooms - Refurbish	10	6,600	
Clubhouse HVAC - Repair/Replace	6	4,400	
Clubhouse Furniture - Replace	14	5,000	
Resident Managers Unit - Refurbish	3	3,800	
Building Exterior			
Roof: Comp Shingle - Repair/Replace	14	574,000	
Roof: Comp Shingle - Repair/Replace	14	190,500	
Gutters/Downspouts - Repair/Replace	14	107,650	
Chimney Covers/Flue Caps - Replace	14	64,450	

continued on next page

Bluegrass Owners Association
December 31, 2017
Supplementary Information on Future Major Repairs
and Replacements
(Unaudited)

Component	Estimated Remaining Useful Life in Years	Estimated Current Replacement Costs	Fund Balance at Year End
Building Exterior - CONT.			
Siding: Vinyl - Repair/Replace	28	\$ 1,772,500	
Siding: Vinyl - Clean/Inspect	0	14,850	
Exterior Surfaces - Paint/Caulk	3	133,000	
Windows/Glass Doors - Replace	28	827,500	
Decks/Landings - Seal/Repair	1	91,950	
Deck/Stair Rail - Replace	28	189,000	
Exterior Lights - Replace	8	36,000	
Systems			
Fire Alarm Panels - Repair/Replace	17	24,000	
Trash Compactor - Repair/Replace	6	37,250	
TOTAL			\$ 840,699

Percent Funded as of January 1, 2018 - 39.1%