

**LAKE MISSION VIEJO ASSOCIATION**

***FINANCIAL STATEMENTS***

**DECEMBER 31, 2006**

**WITH**

**INDEPENDENT AUDITOR'S REPORT  
AND SUPPLEMENTARY INFORMATION**

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**INDEPENDENT AUDITOR'S REPORT****Board of Directors  
Lake Mission Viejo Association**

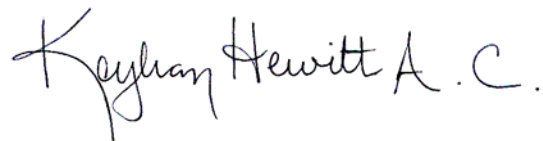
We have audited the accompanying balance sheet of Lake Mission Viejo Association (the "Association"), a California non-profit corporation, as of December 31, 2006, and the related statements of revenues, expenses and changes in fund balance, and cash flows for the year then ended. These financial statements are the responsibility of the Association's Board of Directors. Our responsibility is to express an opinion on these statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards of 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 includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Lake Mission Viejo Association as of December 31, 2006, and the results of its operations and its cash flows for the year then ended in conformity with generally accepted accounting principles of the United States of America.

The supplementary information on future major repairs and replacements as of December 31, 2006 is not a required part of the basic financial statements of Lake Mission Viejo Association, but is supplementary information required by the American Institute of Certified Public Accountants. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the method of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion or any other form of assurance on it.

February 8, 2007



**LAKE MISSION VIEJO ASSOCIATION  
BALANCE SHEET  
DECEMBER 31, 2006**

**ASSETS**

	<u>Operating Fund</u>	<u>Replacement Fund</u>	<u>Capital Expansion Fund</u>	<u>Contingency Fund</u>	<u>Total</u>
<b>CURRENT ASSETS</b>					
Cash and cash equivalents	\$ 1,542,020	\$ 283,305	\$ 15,331	\$ -	\$ 1,840,656
Investments, net	-	2,576,000	1,327,000	250,000	4,153,000
Assessments receivable, net of allowance for uncollectible assessments of \$86,961	47,710	-	-	-	47,710
Prepaid expenses and other current assets	45,364	-	-	-	45,364
	<u>\$ 1,635,094</u>	<u>\$ 2,859,305</u>	<u>\$ 1,342,331</u>	<u>\$ 250,000</u>	<u>\$ 6,086,730</u>

**LIABILITIES AND FUND BALANCE**

<b>CURRENT LIABILITIES</b>					
Accounts payable and accrued expenses	\$ 96,548	\$ -	\$ -	\$ -	\$ 96,548
Accrued payroll and related expenses	238,310	-	-	-	238,310
Deferred revenues	1,290,462	-	-	-	1,290,462
Other payables	9,774	-	-	-	9,774
	<u>1,635,094</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>1,635,094</u>
<b>COMMITMENTS AND CONTINGENCIES</b>					
<b>FUND BALANCE</b>	<u>-</u>	<u>2,859,305</u>	<u>1,342,331</u>	<u>250,000</u>	<u>4,451,636</u>
	<u>\$ 1,635,094</u>	<u>\$ 2,859,305</u>	<u>\$ 1,342,331</u>	<u>\$ 250,000</u>	<u>\$ 6,086,730</u>

**LAKE MISSION VIEJO ASSOCIATION**  
**STATEMENT OF REVENUES, EXPENSES AND CHANGES IN FUND BALANCE**  
**FOR THE YEAR ENDED DECEMBER 31, 2006**

	<u>Operating Fund</u>	<u>Replacement Fund</u>	<u>Capital Expansion Fund</u>	<u>Contingency Fund</u>	<u>Total</u>
<b>REVENUES</b>					
Assessments	\$ 4,551,416	\$ 201,858	\$ 237,856	\$ -	\$ 4,991,130
Boat rental and storage	265,431	-	-	-	265,431
Interest	227,912	-	-	-	227,912
Recreation and sales	214,710	-	-	-	214,710
Other	279,097	-	-	-	279,097
	<u>5,538,566</u>	<u>201,858</u>	<u>237,856</u>	<u>-</u>	<u>5,978,280</u>
<b>EXPENSES</b>					
Concerts and special events	312,168	-	-	-	312,168
Consulting and outside services	331,568	-	-	-	331,568
Bad Debt	14,400	-	-	-	14,400
Fish stocking	121,088	-	-	-	121,088
General and administrative	365,851	-	-	-	365,851
Insurance	147,535	-	-	-	147,535
Lake refill and quality management	166,552	-	-	-	166,552
Maintenance and repairs	349,409	120,497	1,518	13,847	485,271
Professional services	93,422	-	-	-	93,422
Salaries and related	2,963,189	-	-	-	2,963,189
Utilities	188,444	-	-	-	188,444
	<u>5,053,626</u>	<u>120,497</u>	<u>1,518</u>	<u>13,847</u>	<u>5,189,488</u>
<b>EXCESS (DEFICIENCY) OF</b>					
<b>REVENUES OVER EXPENSES</b>	484,940	81,361	236,338	(13,847)	788,792
<b>BEGINNING FUND BALANCE</b>					
	-	2,527,944	903,512	231,388	3,662,844
<b>INTERFUND TRANSFERS</b>					
	<u>(484,940)</u>	<u>250,000</u>	<u>202,481</u>	<u>32,459</u>	<u>-</u>
<b>ENDING FUND BALANCE</b>					
	<u>\$ -</u>	<u>\$ 2,859,305</u>	<u>\$ 1,342,331</u>	<u>\$ 250,000</u>	<u>\$ 4,451,636</u>

**LAKE MISSION VIEJO ASSOCIATION  
STATEMENT OF CASH FLOWS  
FOR THE YEAR ENDED DECEMBER 31, 2006**

	<u>Operating Fund</u>	<u>Replacement Fund</u>	<u>Capital Expansion Fund</u>	<u>Contingency Fund</u>	<u>Total</u>
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>					
Excess (deficiency) of revenues over expenses	\$ 484,940	\$ 81,361	\$ 236,338	\$ (13,847)	\$ 788,792
Adjustments to reconcile excess (deficiency) of revenues over expenses to net cash provided by operating activities:					
Interfund transfers	(484,940)	250,000	202,481	32,459	-
(Increase) decrease in:					
Assessment receivable	(21,066)	-	-	-	(21,066)
Prepaid expenses and other assets	11,554	-	-	-	11,554
Increase (decrease) in:					
Accounts payable and accrued expenses	15,638	-	-	-	15,638
Accrued payroll and related expenses	60,769	-	-	-	60,769
Deferred revenues	137,327	-	-	-	137,327
Other payables	446	-	-	-	446
	<u>204,668</u>	<u>331,361</u>	<u>438,819</u>	<u>18,612</u>	<u>993,460</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>					
Redemptions of investments	-	2,132,100	903,512	231,388	3,267,000
Purchase of investments	-	<u>(2,576,000)</u>	<u>(1,327,000)</u>	<u>(250,000)</u>	<u>(4,153,000)</u>
	-	<u>(443,900)</u>	<u>(423,488)</u>	<u>(18,612)</u>	<u>(886,000)</u>
<b>NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS</b>	204,668	(112,539)	15,331	-	107,460
<b>BEGINNING CASH AND CASH EQUIVALENTS</b>	<u>1,337,352</u>	<u>395,844</u>	<u>-</u>	<u>-</u>	<u>1,733,196</u>
<b>ENDING CASH AND CASH EQUIVALENTS</b>	<u>\$ 1,542,020</u>	<u>\$ 283,305</u>	<u>\$ 15,331</u>	<u>\$ -</u>	<u>\$ 1,840,656</u>

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**LAKE MISSION VIEJO ASSOCIATION  
SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES  
FOR THE YEAR ENDED DECEMBER 31, 2006**

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**Organization**

Lake Mission Viejo Association (the “Association”) was incorporated in California in November 1976. The Association is responsible for the operation and maintenance of the common property within the development. The development consists of residential units and apartment units located in Mission Viejo, California. At December 31, 2006, the development consisted of 23,518 units.

**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 management. Disbursements from the replacement, capital expansion, and contingency funds, generally may be made only for designated purposes.

**Use of Estimates**

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

**Concentration of Credit Risk**

Cash balances are maintained at several banks. Accounts at each institution are insured by the Federal Deposit Insurance Corporation (“FDIC”) up to \$100,000. Periodically, due to the Association’s assessment billing cycle, operating cash accounts may exceed the FDIC limits.

**Cash and Cash Equivalents**

Cash and cash equivalents consist of highly liquid investments with maturities of three months or less when purchased. The Association’s cash equivalent balances as of December 31, 2006 totaled approximately \$600,000, all of which is kept in Monarch funds, which invest in government securities and are not FDIC insured.

**Investments and Interest Earnings**

Investments consist of time certificates of deposit with annual interest rates ranging from 4.0% to 5.2%. Investments are recorded at amortized cost, which approximates fair market value. The Association intends to hold all investments until maturity. All interest earnings are allocated to and recorded in the operating fund.

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**LAKE MISSION VIEJO ASSOCIATION  
SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES  
(CONTINUED)**

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**Assessments**

Association members are subject to assessments to provide funds for the Association's operating expenses and replacement fund requirements. Assessments receivable at the balance sheet date represent fees due from members. The Association's governing documents and legislated laws provide for various collection remedies for delinquent assessments including late charges, filing of liens, foreclosing on the member's property within the Association, and obtaining judgment on other assets of the member.

**Allowance for Uncollectible Assessments**

Allowance for uncollectible assessments is based upon historical experience and management's evaluation of outstanding assessments receivable at year-end.

**Prepaid Assessments**

Assessments collected in advance are deferred and recognized as revenue in the year in which the related services are rendered.

**Property and Equipment**

The developer of the Association donated the majority of the property and equipment. Valuation of these items was made as of the date of transfer to the Association. Personal property purchased by the Association and replacements and improvements to the real property are not capitalized and are expensed as incurred. The expense is charged to either the replacement or the capital expansion funds, in accordance with the guidelines within those funds.

**Income Taxes**

The Association has obtained exemption from taxation under Internal Revenue Code §501(c)(4) and related California Revenue and Taxation Code sections. Accordingly, no provision for Federal or state taxes has been made in the accompanying financial statements.

**Replacement Fund**

The Association's governing documents require that funds be accumulated for future major repairs and replacements. Accumulated funds are kept in separate accounts and are generally not available for normal operations. Disbursements are to be made only if specifically approved by the Board of Directors.

An independent study (the "Study") of the Association's replacement fund was conducted in June 2006, for the purpose of estimating the remaining useful lives and the replacement costs of the components of common property. The table included in the accompanying unaudited supplemental information on Future Major Repairs and Replacements is based upon the Study.



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**LAKE MISSION VIEJO ASSOCIATION  
NOTES TO FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2006**

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**NOTE 1: COMMITMENTS AND CONTINGENCIES**

**Replacement Fund**

The Association is funding for major repairs and replacements over the remaining useful lives of the components based on the Study's estimates of current replacement costs and considering amounts previously accumulated in the replacement fund. Accordingly, the funding requirement of approximately \$480,000 has been included in the 2007 budget.

For year ended December 31, 2006 the contributions, in addition to the budgeted amounts, to the replacement fund totaled approximately \$250,000.

Funds are being accumulated in the repair and replacement fund based on estimates of future needs for repairs and replacements of common area property components. Actual expenditures and investment income may vary from the estimated amounts, and the variations may be material. Therefore, amounts accumulated in the repair and replacement fund may not be sufficient to meet all future repairs and replacements. If additional funds are necessary, the Association has the right to increase regular assessments, approve special assessments, or delay major repairs and replacements until funds are available.

**Capital Expansion and Contingency Funds**

The Association has established a policy to accumulate funds for capital expansion and other unforeseen expenses. Annually the Association includes nominal amounts in the budget for capital expansion and contingency funds. In accordance with the Association's policy, upon completion of accounting at each year-end, any excess operating income is transferred to the capital expansion and contingency funds. For year ended December 31, 2006 the contributions, in addition to the budgeted amounts, to the capital expansion and contingency funds totaled approximately \$202,000 and \$32,000, respectively.

**Litigation**

At times, the Association is involved in litigation arising out of the normal course of business. Management, after consultation with outside counsel, believes there is no likelihood that the Association will incur any material loss as a result of these lawsuits. Therefore no provision for loss resulting from these lawsuits has been made in the accompanying financial statements.

**SUPPLEMENTARY INFORMATION**  
*(Unaudited)*

**DECEMBER 31, 2006**

**LAKE MISSION VIEJO ASSOCIATION  
SUPPLEMENTARY INFORMATION ON FUTURE MAJOR  
REPAIRS AND REPLACEMENTS  
DECEMBER 31, 2006  
(Unaudited)**

In June 2006, an independent study was conducted to estimate the remaining useful lives and future replacement costs of the components of the common area property. An independent company that specializes in the development of these funding programs performed the study. The funding program considers an annual inflation rate of 3% on the replacement cost on amounts funded for future repairs and replacements. Replacement costs were based on the estimated costs to repair or replace the common property components at the date of the study. The Association has not adjusted for changes in the estimated replacement costs, if any, since the date of the study.

The following information is based on the study and presents significant information about the components of common property at December 31, 2006. The reserve study should be referred to for a more complete description of the Association's assets and estimates used.

<u>Component</u>	<u>Estimated Remaining Useful Lives (Years)</u>	<u>Estimated Current Replacement Cost</u>	<u>Replacement Fund Balance</u>
Automobiles	2 to 7	\$ 143,370	\$ 94,202
Carpeting	1 to 2	29,816	25,110
Small equipment	0 to 8	129,836	76,845
Snack bar equipment	0 to 17	145,100	102,046
Asphalt	0 to 2	1,881,084	1,050,536
Boats	0 to 8	328,215	242,410
Boat motors	0 to 3	54,120	39,249
Tractors	0 to 3	64,585	54,339
Sand	0	82,500	82,500
Carts	0 to 5	111,325	72,260
Maintenance equipment	0 to 21	183,175	83,129
Fencing	3 to 25	496,543	92,931
Recreation Structures	0 to 11	992,820	167,946
Access and irrigation equipment	0 to 2	45,755	43,333
Lighting	1 to 17	202,880	172,720
Lake equipment	1 to 3	70,235	51,167
Air conditioning equipment	0 to 7	52,005	35,957
Other			372,625
		<u>\$ 5,013,364</u>	<u>\$ 2,859,305</u>