

**Royal Oaks Residential
Community Owners Association, Inc.
(A Texas Non-Profit Corporation)**

Financial Statements

December 31, 2019

Canady & Canady, LLC
Certified Public Accountants
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Independent Auditor's Report

To the Board of Directors of
Royal Oaks Residential Community Owners Association, Inc.

Report on the Financial Statements

We have audited the accompanying financial statements of Royal Oaks Residential Community Owners Association, Inc., which comprise the balance sheet as of December 31, 2019, and related statements of revenues, expenses and changes in fund balances 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.

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Independent Auditor's Report (Continued)

To the Board of Directors of
Royal Oaks Residential Community Owners Association, Inc.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Royal Oaks Residential Community Owners Association, Inc. as of December 31, 2019, 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.

Disclaimer of Opinion on Required Supplementary Information

Accounting principles generally accepted in the United States of America require that Supplementary Information on Future Major Repairs and Replacements on page 10 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 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.

Canady & Canady LLC

Houston, Texas

July 1, 2020

Royal Oaks Residential Community Owners Association, Inc.
Balance Sheet
December 31, 2019

| | <u>Operating Fund</u> | <u>Replacement Fund</u> | <u>Total</u> |
|--|----------------------------|-----------------------------|----------------------------|
| Assets | | | |
| Cash | \$ 1,680,420 | \$ 2,146,182 | \$ 3,826,602 |
| Assessments receivable, net of allowance for doubtful accounts of \$5,000 | 51,022 | - | 51,022 |
| Due from operating fund | - | 134,156 | 134,156 |
| Prepaid expenses | 6,969 | - | 6,969 |
| Other deposits | 1,936 | - | 1,936 |
| Total Assets | <u><u>\$ 1,740,347</u></u> | <u><u>\$ 2,280,338</u></u> | <u><u>\$ 4,020,685</u></u> |
| Liabilities and Fund Balances | | | |
| Assessments received in advance | \$ 1,043,357 | \$ - | \$ 1,043,357 |
| Accrued expenses | 114,483 | - | 114,483 |
| Due to replacement fund | 134,156 | - | 134,156 |
| Homeowner refundable deposits | 42,243 | - | 42,243 |
| Deferred revenue- trash reimbursement | 48,470 | - | 48,470 |
| Other liabilities | 54,781 | - | 54,781 |
| Total Liabilities | 1,437,490 | 0 | 1,437,490 |
| Fund Balances | <u>302,857</u> | <u>2,280,338</u> | <u>2,583,195</u> |
| Total Liabilities and Fund Balances | <u><u>\$ 1,740,347</u></u> | <u><u>\$ 2,280,338</u></u> | <u><u>\$ 4,020,685</u></u> |

See accompanying notes to financial statements.

Royal Oaks Residential Community Owners Association, Inc.
Statement of Revenues, Expenses and Changes in Fund Balance
For the Year Ended December 31, 2019

| | Operating Fund | Replacement Fund | Total |
|-------------------------------|---------------------------|-----------------------------|---------------------|
| | <u> </u> | <u> </u> | <u> </u> |
| Revenues | | | |
| Assessments | \$ 2,322,019 | \$ 416,731 | \$ 2,738,750 |
| Trash reimbursement | 70,859 | - | 70,859 |
| Compliance | 36,075 | - | 36,075 |
| Gate and access fees | 17,720 | - | 17,720 |
| Legal | 13,434 | - | 13,434 |
| Interest | 5,705 | 6,062 | 11,767 |
| Late fees and penalty | 9,800 | - | 9,800 |
| Other income | 1,312 | - | 1,312 |
| Total Revenues | <u>2,476,924</u> | <u>422,793</u> | <u>2,899,717</u> |
| Expenses | | | |
| Security | 916,485 | - | 916,485 |
| Landscaping | 473,846 | - | 473,846 |
| Office and administrative | 434,445 | - | 434,445 |
| Capital improvements | - | 279,146 | 279,146 |
| Trash removal | 212,756 | - | 212,756 |
| Repairs and maintenance | 195,768 | - | 195,768 |
| Utilities | 114,328 | - | 114,328 |
| Insurance | 50,577 | - | 50,577 |
| Legal and professional fees | 40,771 | - | 40,771 |
| Management fees | 24,897 | - | 24,897 |
| Property taxes | 5,420 | - | 5,420 |
| Bad debt | 2,603 | - | 2,603 |
| Total Expenses | <u>2,471,896</u> | <u>279,146</u> | <u>2,751,042</u> |
| Excess of | | | |
| Revenues over Expenses | 5,028 | 143,647 | 148,675 |
| Fund Balances | | | |
| Beginning of year | <u>297,829</u> | <u>2,136,691</u> | <u>2,434,520</u> |
| End of year | <u>\$ 302,857</u> | <u>\$ 2,280,338</u> | <u>\$ 2,583,195</u> |

See accompanying notes to financial statements.

Royal Oaks Residential Community Owners Association, Inc.
Statement of Cash Flows
For the Year Ended December 31, 2019

| | <u>Operating Fund</u> | <u>Replacement Fund</u> | <u>Total</u> |
|--|---------------------------|-----------------------------|------------------|
| Cash Flows from Operating Activities | | | |
| Excess of revenues over expenses | \$ 5,028 | \$ 143,647 | \$ 148,675 |
| Adjustments to reconcile excess of revenues over expenses to net cash (used) provided by operating activities: | | | |
| Bad debt | 2,603 | - | 2,603 |
| Decrease (increase) in: | | | |
| Assessments receivable | 13,379 | - | 13,379 |
| Prepaid expenses | 1,672 | - | 1,672 |
| Refundable deposit | (1,936) | - | (1,936) |
| Increase (decrease) in: | | | |
| Assessments received in advance | 297,806 | - | 297,806 |
| Accounts payable | (1,385) | - | (1,385) |
| Accrued expenses | (5,387) | (33,175) | (38,562) |
| Homeowners refundable deposits | (40,510) | - | (40,510) |
| Deferred revenue- trash reimbursement | 48,470 | - | 48,470 |
| Other liabilities | 34,555 | - | 34,555 |
| Net cash provided by operating activities | 354,295 | 110,472 | 464,767 |
| Cash Flows from Financing Activities | | | |
| Interfund borrowing | 172,964 | (172,964) | - |
| Net increase (decrease) in cash and cash equivalents | 527,259 | (62,492) | 464,767 |
| Cash and cash equivalents at beginning of year | 1,153,161 | 2,208,674 | 3,361,835 |
| Cash and Cash Equivalents at End of Year | <u>\$ 1,680,420</u> | <u>\$ 2,146,182</u> | <u>3,826,602</u> |
| Supplemental Disclosure | | | |
| Income taxes paid | \$ - | \$ - | \$ - |
| Interest paid | \$ - | \$ - | \$ - |

See accompanying notes to financial statements.

Royal Oaks Residential Community Owners Association, Inc.
Notes to Financial Statements
December 31, 2019

Note 1 - Organization

Royal Oaks Residential Community Owners Association, Inc. (the Association) is a Texas non-profit corporation incorporated on February 25, 2000, for the purpose of providing for management, maintenance, preservation, operation and architectural control of the properties that may be brought within the jurisdiction of the Association. The Association is comprised of 875 residential units in Harris County, Texas.

Note 2 - Management's Review

In preparing the financial statements, the Association has evaluated the events and transactions for potential recognition or disclosure through July 1, 2020, the date that the financial statements were available to be issued.

Note 3 - Summary of Significant Accounting Policies

Funds

The Association uses fund accounting which requires funds allocated for future major repairs and replacements be classified separately from funds available for general operations. 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 account for financial resources designated for future repairs and replacements.

Cash and Cash Equivalents

Cash includes cash and cash equivalents of short-term, highly liquid investments which are readily convertible into cash within ninety days of purchase.

The Association maintains its cash balances in a financial institution located in Houston, Texas. Accounts at the institution are secured by the Federal Deposit Insurance Corporation (FDIC) up to \$250,000. As of December 31, 2019, \$858,943 was not insured by FDIC.

Assessments

Association members are subject to annual assessments to provide funds for the Association's operating expenses and major repairs and replacements. Assessments receivable at the balance sheet date represent fees due from unit members. Any excess assessments at year end are retained by the Association for use in the succeeding year. Income received in advance is deferred and amortized over the period to which it relates.

Royal Oaks Residential Community Owners Association, Inc.
Notes to Financial Statements
December 31, 2019

Note 3 - Summary of Significant Accounting Policies (Continued)

Assessments Received in Advance

Assessments received in advance at the balance sheet date represent payments received from association members during the current year, which relate to maintenance assessments for the subsequent year.

Federal Income Tax

The Association was granted an exemption from federal income tax on August 2, 2019. The Association qualified as a social welfare organization as described in section 501(c) (4) of the Internal Revenue Code.

The Association adopted the revision to ASC 740 regarding accounting for uncertainty in income taxes. An entities status, including its status as a tax exempt not-for-profit entity, is included in the definition of a tax position. The Association's tax filings are subject to audit. The Association's federal income tax returns for 2019, 2018, and 2017 remain open to examination by the Internal Revenue Service. In evaluating the Association's tax provisions and accruals, the Association believes that its estimates are appropriate based on current facts and circumstances.

Texas State Franchise Tax and Sales Tax

The Association is exempt from Texas Franchise tax and sales tax as qualifying 501(c) (4).

Property and Equipment

Real property and common areas acquired from the developer and related improvements to such property are not reflected on the Association's financial statements. In accordance with the American Institute of Certified Public Accounts guidelines, the Association only capitalizes common real properties to which it has title or other evidence of ownership and either of the following conditions are met:

- The Association can dispose of the property, at the discretion of its board of directors, for cash or claims to cash, with the Association retaining the proceeds.
- The property is used by the Association to generate significant cash flows from members on the basis of usage or from nonmembers.

At December 31, 2019, the Association did not meet either of the guidelines requiring property and equipment to be capitalized.

Royal Oaks Residential Community Owners Association, Inc.
Notes to Financial Statements
December 31, 2019

Note 3 - Summary of Significant Accounting Policies (Continued)

Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

Fair Value of Financial Instruments

The Association's financial instruments are cash and cash equivalents, accounts receivable, prepaid expenses and accounts payable. The recorded values of the cash and cash equivalents, investments, accounts receivable, prepaid expenses and accounts payables approximate their fair values based on their short-term nature.

Trash Reimbursement

The Association entered into an agreement with Harris County Municipal Utility District on June 3, 2019 for trash reimbursement program. MUD periodically reimburse a portion of the trash expenses paid by the Association. This agreement shall be in force for a period of one year.

Note 4 - Assessments Receivable

Assessments receivable represents fees due prior to December 31, 2019. The Association's policy is to retain legal counsel to pursue collection matters when assessments become past due. Accounts are deemed delinquent when payment is not received within 30 days of billing. Accounts are charged to operations when they are deemed uncollectible based upon periodic reviews of aging and collections. Bad debts are provided on the allowance method based on management's evaluation of outstanding accounts receivable. As of December 31, 2019, the allowance for doubtful account was \$5,000.

Note 6 – Operating Lease

The Association entered into an operating lease on April 25, 2019. The monthly rental schedule for the renewal period is as follows:

| Period | Rate/SF | Monthly Rent | Annual Rent |
|---------------|----------------|---------------------|--------------------|
| Months 1-2 | \$ - | \$ - | \$ - |
| Months 2-12 | 9.50 | 1,140.00 | 13,680.00 |
| Months 13-24 | 9.79 | 1,174.20 | 14,090.40 |
| Months 25-36 | 10.08 | 1,209.60 | 14,515.20 |
| Months 37-48 | 10.38 | 1,245.60 | 14,947.20 |
| Months 49-62 | 10.69 | 1,282.80 | 15,393.30 |

Royal Oaks Residential Community Owners Association, Inc.
Notes to Financial Statements
December 31, 2019

Note 7 - Future Major Repairs and Replacements

The Association's governing documents requires funds to be accumulated for future major repairs and replacements. Accumulated funds are generally not available for operating purposes.

The Association conducted a study in 2019 to determine the remaining useful lives of the components of common property and current estimates of costs of major repairs and replacements that may be required in the future. Funds are being accumulated based on estimates of future needs for repairs and replacements of common assets. Actual expenditures may vary from the estimated future expenditures, and the variations may be material. Therefore, amounts accumulated in the replacement fund may not be adequate to meet all future needs for major repairs and replacements. When replacement funds are needed to meet future needs for major repairs and replacements, the Association has the right to increase regular assessments, pass special assessments, or delay major repairs and replacements until funds are available. The effect on the future assessments has not been determined at this time.

Note 8 – Subsequent Events

In preparing the financial statements, the Associations management has evaluated events and transactions for potential recognition or disclosure through July 1, 2020, the date that the financial statements were available to be issued. No events have occurred which would have a material effect on the financial statements of the Association as of that date.

Royal Oaks Residential Community Owners Association, Inc.
Supplementary Information on Future Major Repairs and Replacements (Unaudited)
December 31, 2019

The Association hired an outside firm to conduct study in July 2019 and revised in September 2019 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 including an inflation factor of 2.2%. As of December 31, 2019, the Association's reserve fund balance was \$2,280,338. The following information is based on the study and presents significant information about the components of common property.

| <u>Components</u> | <u>Remaining Useful Life (Years)</u> | <u>Replacement Cost</u> |
|---|--------------------------------------|------------------------------------|
| Property Site Elements | | |
| Bridges, Capital Repairs | 3 | \$ 127,348 |
| Concrete Streets (Incl. Curbs), Partial | 2 to 30+ | 3,419,664 |
| Gate Entry System, Cameras | 0 | 122,635 |
| Gate Entry System, Kiosk Entry Panels | 13 | 65,033 |
| Gate Entry System, Loop Detectors, Phased | 1 to 10 | 60,150 |
| Gate Entry System, Readers, Phased | 1 to 10 | 307,581 |
| Gate Entry System, Scanners | 11 | 23,651 |
| Gate Operators, Phased | 1 to 10 | 877,080 |
| Gates | 3 | 423,857 |
| Irrigation System | 21 | 621,855 |
| Light Poles and Fixtures | 10 | 147,930 |
| Pavers, Masonry, Main Entrance | 5 | 94,502 |
| Perimeter Walls, Panelized Masonry, Partial, Through 2038 | 1 to 30+ | 2,192,937 |
| Perimeter Walls, Panelized Masonry, Partial, 2039-2049 | 20 to 30+ | 3,502,731 |
| Playground Equipment | 4 | 113,849 |
| Playground, Rest Room, Renovation | 11 | 10,164 |
| Playground, Shade Structures, Partial | 24 to 30+ | 48,890 |
| Play Surface, Artificial Turf | 9 | 117,505 |
| Signage, Renovation, Main Entrance | 11 | 60,626 |
| Signage, Replacement, Street and Traffic, Phased | 2 to 14 | 102,443 |
| Sport Court, Light Poles and Fixtures | 20 | 13,599 |
| Sport Court, Surface Replacement | 25 | 73,966 |
| Guard House and Office Elements | | |
| Exterior Renovation, Main Guard House | 5 | 29,568 |
| Furniture, Offices | 0 | 64,605 |
| Interior Renovation, Main Guard House (2019 is Budgeted) | 0 | 264,957 |
| Roofs, Concrete Tiles (Incl. Playground Rest Room) | 11 | 19,819 |
| Westpark South Guard House, Replacement (Incl. Concrete, Landscape) | 0 | 100,000 |
| Windows and Doors, Main Guard House | 16 | 19,123 |
| Total | | <u><u>\$ 13,026,068</u></u> |