

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

Financial Statements

December 31, 2020

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, 2020, 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)

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, 2020, 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 11 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

April 29, 2021

Royal Oaks Residential Community Owners Association, Inc.
Balance Sheet
December 31, 2020

	<u>Operating Fund</u>	<u>Replacement Fund</u>	<u>Total</u>
Assets			
Cash	\$ 1,632,275	\$ 2,584,732	\$ 4,217,007
Assessments receivable, net of allowance for doubtful accounts of \$11,000	55,649	-	55,649
Due from replacement fund	9,260	-	9,260
Prepaid expenses	6,889	-	6,889
Right-of-use asset	42,946	-	42,946
Other deposits	1,936	-	1,936
Total Assets	<u>\$ 1,748,955</u>	<u>\$ 2,584,732</u>	<u>\$ 4,333,687</u>
Liabilities and Fund Balances			
Assessments received in advance	\$ 1,104,571	\$ -	\$ 1,104,571
Accrued expenses	153,914	-	153,914
Due to operating fund	-	9,260	9,260
Homeowner refundable deposits	25,297	-	25,297
Deferred revenue - trash reimbursement	73,499	-	73,499
Lease liability	42,946	-	42,946
Other liabilities	8,900	-	8,900
Total Liabilities	<u>1,409,127</u>	<u>9,260</u>	<u>1,418,387</u>
Fund Balances	<u>339,828</u>	<u>2,575,472</u>	<u>2,915,300</u>
Total Liabilities and Fund Balances	<u>\$ 1,748,955</u>	<u>\$ 2,584,732</u>	<u>\$ 4,333,687</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, 2020

	<u>Operating</u> <u>Fund</u>	<u>Replacement</u> <u>Fund</u>	<u>Total</u>
Revenues			
Assessments	\$ 2,339,890	\$ 398,860	\$ 2,738,750
Trash reimbursement	105,221	-	105,221
Gate and access fees	36,520	-	36,520
Insurance claim	26,602	-	26,602
Interest	2,914	23,549	26,463
Late fees and penalty	16,651	-	16,651
Compliance	12,111	-	12,111
Legal	3,881	-	3,881
Other income	3,304	-	3,304
Total Revenues	<u>2,547,094</u>	<u>422,409</u>	<u>2,969,503</u>
Expenses			
Security	956,818	-	956,818
Landscaping	461,348	-	461,348
Office and administrative	393,834	-	393,834
Repairs and maintenance	234,062	-	234,062
Trash removal	203,021	-	203,021
Utilities	127,422	-	127,422
Capital improvements	-	127,275	127,275
Insurance	44,908	-	44,908
Legal and professional fees	36,803	-	36,803
Management fees	24,897	-	24,897
Lease expenses	20,021	-	20,021
Bad debt	6,834	-	6,834
Property taxes	155	-	155
Total Expenses	<u>2,510,123</u>	<u>127,275</u>	<u>2,637,398</u>
Excess of Revenues over Expenses	36,971	295,134	332,105
Fund Balances			
Beginning of year	302,857	2,280,338	2,583,195
End of year	<u>\$ 339,828</u>	<u>\$ 2,575,472</u>	<u>\$ 2,915,300</u>

See accompanying notes to financial statements.

Royal Oaks Residential Community Owners Association, Inc.
Statement of Cash Flows
For the Year Ended December 31, 2020

	<u>Operating</u> <u>Fund</u>	<u>Replacement</u> <u>Fund</u>	<u>Total</u>
Cash Flows from Operating Activities			
Excess of revenues over expenses	\$ 36,971	\$ 295,134	\$ 332,105
Adjustments to reconcile excess of revenues over expenses to net cash provided by operating activities:			
Bad debt	6,834	-	6,834
(Increase) decrease in:			
Assessments receivable	(11,461)	-	(11,461)
Prepaid expenses	80	-	80
Right-of-use asset	(42,946)	-	(42,946)
Increase (decrease) in:			
Assessments received in advance	61,214	-	61,214
Accrued expenses	39,431	-	39,431
Homeowners refundable deposits	(16,946)	-	(16,946)
Deferred revenue- trash reimbursement	25,029	-	25,029
Lease liability	42,946	-	42,946
Other liabilities	(45,881)	-	(45,881)
Net cash provided by operating activities	<u>95,271</u>	<u>295,134</u>	<u>390,405</u>
Cash Flows from Financing Activities			
Interfund fund borrowing	(143,416)	143,416	-
Net cash (used) provided by financing activities	<u>(143,416)</u>	<u>143,416</u>	<u>-</u>
Net (decrease) increase in cash and cash equivalents	<u>(48,145)</u>	<u>438,550</u>	<u>390,405</u>
Cash and cash equivalents at beginning of year	<u>1,680,420</u>	<u>2,146,182</u>	<u>3,826,602</u>
Cash and Cash Equivalents at End of Year	<u><u>\$ 1,632,275</u></u>	<u><u>\$ 2,584,732</u></u>	<u><u>4,217,007</u></u>

See accompanying notes to financial statements.

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

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 April 29, 2021, 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 various financial institution. Accounts at the institution are secured by the Federal Deposit Insurance Corporation (FDIC) up to \$250,000. As of December 31, 2020, \$1,343,685 was not insured by FDIC.

Certificate of Deposit

Certificates of deposits are recorded at cost, and are held in a financial institutions Financial Services. Accounts at the institutions are secured by the Securities Investor Protection Corporation (SIPC) up to \$500,000. As of December 31, 2020, all the balances of Certificate of Deposit were insured by SIPC. The Association's policy is to hold investments until maturity; therefore, there are no gains or losses recognized on the accompanying Statements of Revenues and Expenses.

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

Note 3 - Summary of Significant Accounting Policies (Continued)

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.

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.

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, 2020, the Association did not meet either of the guidelines requiring property and equipment to be capitalized.

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.

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

Note 3 - Summary of Significant Accounting Policies (Continued)

Adoption of the New Lease Accounting Guidance in ASU No. 2019-02

At the beginning of the first quarter of 2020, the Association adopted the Financial Accounting Standards Board's (the "FASB") Accounting Standards Update ("ASU") No. 2016-02, Leases (Topic 842) ("ASU 2016-02"), and additional ASUs issued to clarify and update the guidance in ASU 2016-02 (collectively, the "new leases standard"), which modifies lease accounting for lessees to increase transparency and comparability by recording lease assets and liabilities for operating leases and disclosing key information about leasing arrangements. The Association adopted the new leases standard utilizing the modified retrospective transition method, under which amounts in prior periods presented were not restated. For contracts existing at the time of adoption, the Association elected to not reassess (i) whether any are or contain leases, (ii) lease classification, and (iii) initial direct costs. Upon adoption, the Association recorded \$42,946 of right-of-use ("ROU") assets and \$ 42,946 of lease liability on its Balance Sheet.

Contract Liabilities (Assessments Received In Advance-Replacement Fund)

The Association recognizes revenue from members as the related performance obligations are satisfied. A contract liability (assessments received in advance-replacement fund) is recorded when the Association has the right to receive payment in advance of the satisfaction of performance obligations related to replacement reserve assessments. The balances of contract liabilities (assessments received in advance-replacement fund) as of the beginning and end of the year are \$0 and \$0, respectively.

Note 4 - Assessments Receivable

Assessments receivable represents fees due prior to December 31, 2020. 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, 2020, the allowance for doubtful account was \$11,000.

Note 5 - Trash Reimbursement

The Association entered into an agreement with Harris County Municipal Utility District on July 27, 2020 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 6 – Lease

The Association has obligations under operating leases for its management office. The leases expire at five years and two month following the first day of the month after the Commencement date, June 1, 2019 and provide for renewal options of three (3) years. In the normal course of business, it is expected that these leases will be renewed or replaced by leases on other properties.

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

Note 6 – Lease (Continued)

The Association agrees to pay to Landlord the monthly payments of base rent as below, the applicable sales or use or excise tax, pro rata share of operating expenses, real estate taxes, and insurance etc.:

Period	Rate/SF	Monthly Rent	Annual Rent
Months 1-2	\$ -	\$ -	\$ -
Months 3-12	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

The following is table presents future minimum lease payments and the impact of discounting:

	Annual Rent
2021	14,338.00
2022	14,767.00
2023	15,208.00
2024	<u>6,414.00</u>
Future minimum lease payments	<u>50,727.00</u>
Impact of discounting	(7,781.00)
Present value of lease liabilities	<u><u>42,946.00</u></u>

The weighted-average remaining lease term and weighted-average discount rate were as follows:

Weighted-average remaining lease term	3 years
Weighted-average discount rate	5%

The total rent expense prior to the adoption of ASC 842 is \$5,700.

Note 7 - Federal Income Tax

The Association is exempt from Federal income taxes under 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 2020, 2019, and 2018 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.

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

Note 8 - State Franchise Tax

The Association is exempt from Texas franchise tax as specified under Section 171.082 of the Texas Tax Code as a homeowners' association.

Note 9 – FASB ASC 606 New Accounting Guidance Implementation

The Financial Accounting Standards Board (FASB) issued new guidance that created Topic 606, Revenue from Contracts with Customers, in the Accounting Standards Codification (ASC). Topic 606 supersedes the revenue recognition requirements in FASB ASC 972-605, Real Estate—Common Interest Realty Associations, Revenue Recognition, and requires the recognition of revenue when promised goods or services are transferred to customers in an amount that reflects the consideration to which a CIRA expects to be entitled in exchange for those goods or services.

The Association applied the new guidance using the practical expedient provided in Topic 606 that allows the guidance to be applied only to contracts that were not complete as of January 1, 2020. Adoption of the new guidance resulted in changes to our accounting policies for assessment revenue and contract liabilities (assessments received in advance-replacement fund), as previously described.

Note 10 - 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 11 – Subsequent Events

In preparing the financial statements, the Associations management has evaluated events and transactions for potential recognition or disclosure through April 29, 2021, 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, 2020

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, 2020, the Association's reserve fund balance was \$2,575,472. 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>