Falls Creek Ranch Association
Accounting, Budgeting and Financial Reporting Policies
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Accounting, Budgeting and Financial Reporting Policies:

Fiscal Year

The fiscal year of the Association begins on August 1 of each year and ends on July 31 of the following year.

Accounting Method

The Association prepares its financial statements on the accrual basis of accounting. Under this method of accounting, revenue is recognized when assessments are earned (rather than received) and expenses are recognized when goods or services are received or incurred, whether paid or not.

> Example: Annual dues assessments are generally received in August (beginning of fiscal year) for those making one payment, or one-half in August and one-half in February for those paying in two installments. Prior to adopting accrual basis of accounting, all dues received were recorded as income in the month received, thus distorting reported net income. Under the accrual basis, total annual dues are recorded on the Balance Sheet at beginning of year as Accounts Receivable (asset) with an offsetting entry to Unearned Assessments (liability). 1/12th of the total dues are then recorded as revenue each month (a debit entry to Unearned Assessments and a credit entry to Revenues) regardless of when payments are received. As payments come in, they are debited to Cash and credited to Accounts Receivable. The result being a much

more accurate reflection of net income each month and month-to-date.

Capitalization Policy

- **Financial Reporting** - The Association's policy is to capitalize personal property and equipment that has cost of $1,000 or higher, and estimated useful life of 1 year or longer. Expenditures less than $1,000 or with a useful life of less than one year shall be expensed in the fiscal year incurred. (This policy also satisfies the Association's Bylaws (Para. 7.3 (c) which requires the Association to maintain a record of any capital expenditure in excess of $1,000.)

- **Reserve Component Asset** – For purposes of reserve funding (for future repairs / replacement of existing capital assets) the Association's policy is to include in a Reserve Component List only those assets that meet the following criteria:
    1. Are a common property maintenance responsibility
    2. Have a limited life
    3. Have a predictable remaining life
    4. Be above a minimum threshold cost of $5,000.

  A Fixed Asset Depreciation Schedule shall be maintained for all expenditures capitalized for financial reporting. Those capitalized assets (shown on the Fixed Asset Depreciation Schedule) that meet the criteria for including on the Reserve Component List shall be added to the Reserve Component list each year when that list is updated during the Reserve Study and budget preparation process.

Fund Accounting

The Association maintains its accounts using fund accounting. Financial resources are classified for accounting and financial reporting in the following funds established according to their nature and purpose:

0perating Fund – this fund is used to account for financial resources available for the general operation and maintenance of the Association.

Capital Reserve Fund – this fund is used to accumulate financial resources designated for future major repairs and replacements of existing common property elements.

Grant Reserve Fund – this fund is used to account for grant resources available for those specific needs and requirements associated with specific grants.

Budgeting:

Budgets shall be prepared on the Fund Accounting basis with separate sections for Operating Fund, Reserve Fund and Grant Fund.

Income: Total HOA dues assessments shall be allocated between the Operating Fund and the Reserve Fund based on the approved Reserve Funding plan for that budget year.

Capital Expenditures: Budgeted capital projects (see Capitalization Policy) that "repair or replace an existing Reserve Component asset included in the Reserve Component Inventory" shall be included in the Reserve Fund budget section as an authorized use of reserve funds as per the Reserve Policy. All other budgeted capital projects (not meeting that criteria) shall be included in the Operating Fund section.

All budgeted capital projects shall use an assigned balance sheet fixed asset account code, rather than an "expense" account code.

Projected end of budget year cash balances: Shall be included in each budget fund section. This is to determine if budgeted income less budgeted expenditures (both capital and expense) plus beginning cash in bank will result in a positive end of budget year cash balance. Assuming "actual" expenditures incurred are close to "budgeted" and there are no significant "budget variances".

Budget Updating: Because "actual" expenditures will seldom equal "best guess" budgeted expenditures, there will likely be budget variances which at times may be material and if "negative" significantly reduce projected year end cash balances.

> Examples: A major piece of equipment fails earlier than planned (not budgeted) and needs to be replaced. Unexpected weather-related extra drainage or road work. Higher than estimated final bids on capital projects. Or on the positive side, it may be determined that a planned capital project is no longer necessary or can be deferred.

Therefore the budget shall be updated periodically to reflect significant budget variances and revised end of year projected cash balances. If negative cash balances are projected in the budget update, and noticed in time, the board may be able to take pro-active steps to avoid a negative year end cash balance by deferring certain capital projects that can be deferred, cutting expenses that can be cut, or worst case call for a special assessment to avoid a year-end cash deficit.