

**Sixty-01 Association of Apartment Owners
Financial Statements
For the Year Ended December 31, 2018**

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Financial Statements
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Independent Auditor's Report

To the Board of Directors of Sixty-01 Association of Apartment Owners

We have audited the accompanying financial statements of Sixty-01 Association of Apartment Owners (the "Association") which comprise the balance sheet as of December 31, 2018, and the related statements of revenues, expenses, and changes in fund balance 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.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Sixty-01 Association of Apartment Owners as of December 31, 2018, and 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.

Emphasis of a Matter - Special Assessment

As discussed in Note 4 to the financial statements, the most recent reserve study states that a special assessment of \$30,400,000 is needed to fund projects anticipated in the coming years. Our opinion is not modified with respect to this matter.

Emphasis of a Matter on Future Major Repairs and Replacements

Our audit was made for the purpose of forming an opinion on the basic financial statement, taken as a whole. We have not applied procedures to determine whether the funds designated for future repairs and replacements as discussed in Note 4 are adequate to meet such future costs, because such determination is outside the scope of our audit. Our opinion is not modified with respect to this matter.

Disclaimer of Opinion of Required Supplementary Information

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

Newman & Associates, CPA, PC

Bellevue, Washington

May 15, 2019

Sixty-01 Association of Apartment Owners
Balance Sheet
December 31, 2018

	<u>Operating Fund</u>	<u>Replacement Fund</u>	<u>Total</u>
Assets			
Cash and cash equivalents	\$ 490,716	\$ 654,892	\$ 1,145,608
Investments		240,000	240,000
Assessments receivable	44,766	63,158	107,924
Allowance for doubtful accounts	(33,137)		(33,137)
Other receivables	924		924
Prepaid insurance	380,177		380,177
Prepaid expenses	22,222	7,598	29,820
Prepaid income taxes	21,839		21,839
Inventory	3,314		3,314
Fixed assets	57,322		57,322
Accumulated depreciation	(20,742)		(20,742)
Due from (to) fund	(409,573)	409,573	-
Total assets	<u>\$ 557,828</u>	<u>\$ 1,375,221</u>	<u>\$ 1,933,049</u>
Liabilities			
Accounts payable	\$ 143,736	\$ 21,134	\$ 164,870
Prepaid assessments	85,850		85,850
Deferred income	13,345	-	13,345
Deposits	10,465		10,465
Total liabilities	<u>253,396</u>	<u>21,134</u>	<u>274,530</u>
Fund balances	<u>304,432</u>	<u>1,354,087</u>	<u>1,658,519</u>
Total liabilities and fund balances	<u>\$ 557,828</u>	<u>\$ 1,375,221</u>	<u>\$ 1,933,049</u>

The accompanying notes are an integral part of the financial statements
(See Independent Auditor's Report)

Sixty-01 Association of Apartment Owners
Statement of Revenue and Expenses and Changes in Fund Balances
For the Year Ended December 31, 2018

	Operating Fund	Replacement Fund	Total
Revenues			
Owners assessments	\$ 3,444,200	\$ 300,000	\$ 3,744,200
Rental income	26,486		26,486
Insurance claim proceeds	870,341		870,341
Restaurant	97,104		97,104
Interest	371	14,375	14,746
Other member income	86,942		86,942
Total revenues	<u>4,525,444</u>	<u>314,375</u>	<u>4,839,819</u>
Expenses			
Utilities			
Electricity and gas	141,369		141,369
Water and sewer	600,106		600,106
Trash removal	80,634		80,634
Telephone	21,854		21,854
	<u>843,963</u>	<u>-</u>	<u>843,963</u>
Maintenance			
Landscape, irrigation and tree trimming	501,821	52,800	554,621
Common area repairs and maintenance	678,517	43,714	722,231
Janitorial	83,635		83,635
Patrol and security	312,218		312,218
Fire prevention	12,867		12,867
Elevator	54,570		54,570
Roof repair and maintenance	90,172		90,172
Painting		203,736	203,736
Insurance claim expenses	845,342		845,342
Sewer and drains		267,044	267,044
Asphalt		41,080	41,080
Siding		357,154	357,154
	<u>2,579,142</u>	<u>965,528</u>	<u>3,544,670</u>
Administrative			
Insurance	375,085		375,085
Management	241,000		241,000
Administrative expense	87,509		87,509
Payroll and related expenses	178,558		178,558
Legal and professional	39,793		39,793
Network Administration	44,934		44,934
Restaurant expense	94,897		94,897
Federal taxes	3,884		3,884
Bad debt expense (recoveries)	91,454		91,454
	<u>1,157,114</u>	<u>-</u>	<u>1,157,114</u>
Total expenses	<u>4,580,219</u>	<u>965,528</u>	<u>5,545,747</u>
Excess (deficit) of revenues over (under) expenses	(54,775)	(651,153)	(705,928)
Beginning fund balances	359,207	2,005,240	2,364,447
Ending fund balances	<u>\$ 304,432</u>	<u>\$ 1,354,087</u>	<u>\$ 1,658,519</u>

The accompanying notes are an integral part of the financial statements
(See Independent Auditor's Report)

Sixty-01 Association of Apartment Owners
Statement of Cash Flows
For the Year Ended December 31, 2018

	Operating Fund	Replacement Fund	Total
Excess (deficit) of revenues over (under) expenses	\$ (54,775)	\$ (651,153)	\$ (705,928)
Adjustments to reconcile excess (deficit) of revenues over (under) expenses to net cash provided (used) by operating activities			
Depreciation	(134,390)		(134,390)
Decrease (Increase) in operating assets:			
Accounts receivable	121,174	(63,158)	58,016
Insurance claim receivables	397,596		397,596
Other receivables	(924)		(924)
Prepaid insurance	(68,340)		(68,340)
Prepaid expenses	(8,738)	22,790	14,052
Prepaid income tax	(21,839)		(21,839)
Increase (decrease) in operating liabilities:			
Accounts payable	27,477	(55,551)	(28,074)
Prepaid assessments	26,491		26,491
Deposits	(3,994)		(3,994)
Inventory	612		612
Income taxes payable	(42,277)		(42,277)
Deferred income	13,345		13,345
Total adjustments	<u>306,193</u>	<u>(95,919)</u>	<u>210,274</u>
Net cash provided (used) by operating activities	<u>251,418</u>	<u>(747,072)</u>	<u>(495,654)</u>
Cash provided (used) by investing activities			
Change in investments	24,692	991,314	1,016,006
Fixed assets	133,981		133,981
Net cash provided (used) by investing activities	<u>158,673</u>	<u>991,314</u>	<u>1,149,987</u>
Cash provided (used) by financing activities			
Interfund borrowings	(113,271)	113,271	-
Net cash provided (used) by financing activities	<u>(113,271)</u>	<u>113,271</u>	<u>-</u>
Net increase (decrease) in cash and cash equivalents	296,820	357,513	654,333
Beginning cash and cash equivalents	193,896	297,379	491,275
Ending cash and cash equivalents	<u><u>490,716</u></u>	<u><u>\$ 654,892</u></u>	<u><u>\$ 1,145,608</u></u>
SUPPLEMENTAL DISCLOSURE			
Income taxes paid			\$ -
Interest paid			\$ -

The accompanying notes are an integral part of the financial statements
(See Independent Auditor's Report)

Sixty-01 Association of Apartment Owners
Notes to Financial Statements
For the Year Ended December 31, 2018

1. Organization

Sixty-01 Association of Apartment Owners (the "Association") was incorporated on September 1, 1978 as a condominium development under the laws of Washington, for the purposes of maintaining and preserving common property. The Association consists of 770 residential condominiums and is located in Redmond, Washington.

2. Summary of Significant Accounting Policies

Basis of Accounting

The Association maintains its financial records on the accrual basis of accounting, which recognizes revenues when earned and expenses when incurred.

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires the board of directors 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 significantly from those estimates.

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 property manager. Disbursements from the replacement fund generally may be made only for designated purposes.

Capital Assets and Depreciation Policy

The Association has not capitalized real and personal common area property contributed by the developer. Replacements and improvements to real property are also not capitalized; rather, they are charged to the respective fund in the period the cost is incurred. Significant personal property assets are capitalized and depreciated over their estimated lives using straight-line depreciation.

Cash and Cash Equivalents

Cash and cash equivalents include the Association's cash, checking accounts, money market funds and investments in certificates of deposit with original maturities of 90 days or less.

Investments

Investments consist of certificates of deposit and other securities and investment accounts with original maturities of more than 90 days.

Subsequent Events

Subsequent events have been evaluated through May 15, 2019, which is the date the financial statements were available to be issued.

Sixty-01 Association of Apartment Owners
Notes to Financial Statements
For the Year Ended December 31, 2018

Concentration of Credit Risk

The Association maintains bank accounts with balances that exceed FDIC federal insurance of \$250,000. The financial institution may carry private insurance, which may or may not be sufficient to reimburse for any losses. At December 31, 2018, \$221,319 was exposed to risk.

3. Assessments and Assessments Receivable

Association members are subject to monthly assessments to provide funds for the Association's operating expenses, future capital acquisitions, and major repairs and replacements. Assessments receivable represent fees due from owners. The Association's governing documents provide for various collection remedies for delinquent assessments and fees, including filing of liens on an owner's unit, foreclosing on a unit owner, and obtaining a legal judgment on an owner's other assets. Any excess operating funds are retained at the end of the fiscal year for use in future periods. After the Association has exhausted all efforts to collect delinquent accounts, the Board of Directors may elect to write off uncollectible balances.

The Association records an allowance for doubtful accounts to reflect an estimate of accounts that may not be collectible, which includes accounts receivable greater than 90 days old.

4. Future Major Repairs and Replacements

The Association's governing documents require funds to be accumulated for future major repairs and replacements. Accumulated funds are held in separate bank accounts and are generally not available for expenditures for normal operations. The board of directors conducted a reserve study to estimate the remaining useful lives and the replacement costs of the components of common property. The table included in the unaudited Supplementary Information on Future Major Repairs and Replacements is based on this study.

There were changes in the value and/or remaining useful lives of the components included in the Required Supplementary Information between the prior and current year. These changes have been approved by the Board of Directors.

The 2019 reserve study recommends a \$30,400,000 special assessment in 2019. This preliminary special assessment is for the projects factored in the next several years. The primary driver of this cost is the recladding project (siding/waterproofing replacement project) anticipated in the coming years. The Association has hired a building envelope consultant for condition assessment and scope of work and specifications development. The special assessment recommended in the reserve study is preliminary and should be adjusted based on professional consultation findings and rough order of magnitude pricing. See further special assessment related information in Note 7.

The Association is funding such major repairs and replacements over the estimated useful lives of the components based on the study's estimates of current replacement costs, considering amounts previously accumulated in the replacement fund. Actual expenditures, however, may vary from estimated amounts and the variations may be material. Therefore, amounts accumulated in the replacement fund may or may not be adequate to meet future needs. If additional funds are needed, however, the Association has the right, subject to its governing documents, to increase regular assessments or to levy special assessments, or it may delay major repairs and replacements until funds are available.

5. 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.

Sixty-01 Association of Apartment Owners
Notes to Financial Statements
For the Year Ended December 31, 2018

Under that Section, the Association is not taxed on income and the 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.

6. Related Party Transactions

The management company provides payroll services to the Association including providing contract personnel services. The Association paid \$947,142 to the management company in 2018 for this service. The Association owed \$32,457 to the management company for the service at the year-end.

7. Special Assessment/Subsequent Year Events

The Board approved and the members ratified a special assessment of \$3,509,952 payable on or before March 1, 2019. Owners had the option to pay their respective share of the special assessment in full or make 22 installment payments without interest. The special assessment was necessary to conduct the building investigation as described in Note 4, to replenish the Operating and the Replacement Funds, and to fund several major upcoming projects.

Each owner's share of the special assessment was calculated on the basis of their undivided interest in the common elements as discussed in the Declaration.

8. Insurance Claims/Subsequent Year Events

There was an insurance claim submitted in June 2016 for a building damaged by fire. Insurance claim proceeds of \$753,873 were received and all repairs were completed in the current year.

There was another insurance claim submitted in December 2017 for fire and water damages to several units. Insurance proceeds of \$502,409 after the \$25,000 deductible were received and \$514,065 repair expenses were incurred in the current year. The responsible owner reimbursed the Association for the deductible. The unexpended insurance monies have been deferred to the subsequent year. Repairs were nearly completed in 2018.

Sixty-01 Association of Apartment Owners
Supplementary Information on Future Major Repairs and Replacements
December 31, 2018
(Unaudited)

The Association's board of directors, in conjunction with a reserve study expert, conducted a reserve study dated November 6, 2018 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 on the date of the study.

The following information is based on the study and presents significant information about the components of common property.

Study Component	Estimated remaining useful lives	Estimated current replacement costs
Site / Grounds	0-16	\$ 1,198,500
Pool, Courts, and Clubhouse	0-20	1,235,550
Building Exterior	0-45	25,556,700
Building Interiors, Mid-Rise Buildings	0	450,000
Systems	0-15	6,143,350
		<u>\$ 34,584,100</u>
Replacement fund balance at December 31, 2018		<u>\$ 1,354,087</u>
<u>Other Assumptions:</u>		
Study recommended special assessment		<u>\$ 30,400,000</u>
Interest rate		<u>1%</u>
Inflation rate		<u>3%</u>

See the Balance Sheet for replacement fund cash, cash equivalents and investments balances at December 31, 2018.

Report of Internal Control

May 15, 2019

To the Board of Directors of Sixty-01 Association of Apartment Owners

Dear Board of Directors:

In planning and performing our audit of the financial statements of Sixty-01 Association of Apartment Owners as of and for the year ended December 31, 2018, in accordance with auditing standards generally accepted in the United States of America, we considered the Association's internal control over financial reporting (internal control) as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Association's internal control. Accordingly, we do not express an opinion on the effectiveness of the Association's internal control.

The Standards of Field Work

Our consideration of internal control was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control that we consider to be significant deficiencies and other deficiencies that we consider to be material weaknesses.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or a combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control. We believe that the following deficiencies constitute material weaknesses:

- ***As noted in the prior year, the Association has excess funds invested in Mutual of Omaha Bank of over \$221,000 that were not federally guaranteed under the FDIC limit as of the end of the year.***

- ***The following issues were noted with the Replacement Fund:***

- (1) One monthly insurance reserve contribution of \$31,250 was mistakenly deposited to the Replacement Fund. We recorded this as due to the Operating Fund.***

- (2) There was no proper segregation of reserve activity. Almost \$1,013,000 total reserve expenditures have been reported by the Association and approved by the Board; however, only approximately \$881,000 of reserve cash was used to pay the expenses. Total of \$132,021 reserve expenses were paid from operating cash. Reserve expenses should match cash flows. This reduced the amount due from the Operating Fund from the last year as adjusted above to \$359,573, which excludes \$50,000 November - December reserve contributions transferred in the beginning of 2019. Our understanding is that***

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the Association intends to repay this balance from the recently approved special assessment proceeds.

• As noted in the prior years, there should be independent verification of Registration (Move In/Out) Fees to ensure that all fees are charged in accordance with the Association's policy to do so. The Board should document their additional procedures in the board meeting minutes.

This communication is intended solely for the information and use of the Board of Directors and management and is not intended to be and should not be used by anyone other than these specified parties.

Newman & Associates, CPA, PC

Bellevue, Washington