

VERANO HOMEOWNERS ASSOCIATION

**FINANCIAL STATEMENTS
AND INDEPENDENT ACCOUNTANTS' REVIEW REPORT**

YEARS ENDED DECEMBER 31, 2011 AND 2010

**LEVY, ERLANGER & COMPANY
Certified Public Accountants
San Francisco, California**

VERANO HOMEOWNERS ASSOCIATION

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YEARS ENDED DECEMBER 31, 2011 AND 2010**

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LEVY, ERLANGER & COMPANY
Certified Public Accountants

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INDEPENDENT ACCOUNTANTS' REVIEW REPORT

Board Of Directors
Verano Homeowners Association
San Jose, California

We have reviewed the accompanying balance sheets of **Verano Homeowners Association** (the Association) as of December 31, 2011 and 2010 and the related statements of revenues, expenses and changes in fund balances, and the statements of cash flows, for the years then ended. A review includes primarily applying analytical procedures to management's financial data and making inquiries of Association management. A review is substantially less in scope than an audit, the objective of which is the expression of an opinion regarding the financial statements as a whole. Accordingly, we do not express such an opinion.

Management is responsible for the preparation and fair presentation of the financial statements in accordance with accounting principles generally accepted in the United States of America and for designing, implementing, and maintaining internal control relevant to the preparation and fair presentation of the financial statements.

Our responsibility is to conduct the review in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants. Those standards require us to perform procedures to obtain limited assurance that there are no material modifications that should be made to the financial statements. We believe that the results of our procedures provide a reasonable basis for our report.

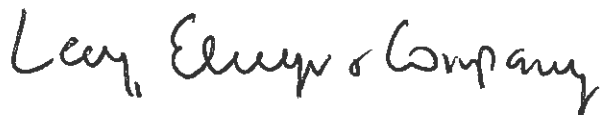
Based on our reviews, we are not aware of any material modifications that should be made to the accompanying financial statements in order for them to be in conformity with accounting principles generally accepted in the United States of America.

As further discussed in the notes to the financial statements, the Association has completed a study of its common area major components sufficient to assist the Board in planning for future major repairs and replacements. The reasonableness of the resulting replacement reserve funding plan is a function of the completeness of the major component list and the accuracy of the estimated quantity, useful and remaining lives, and replacement costs of those components.

Board Of Directors
Verano Homeowners Association
Independent Accountants' Review Report (Continued)

Funds are being accumulated in the replacement fund based on estimated future costs for repair and replacement of common area property. Actual expenditures and investment income may vary from the estimated amounts, and the variations may be material. Therefore, amounts accumulated in the replacement fund may or may not be adequate to meet all future component repair and replacement costs. The ability of the Association to fund its future requirements is dependent upon annual increases in that portion of the assessment which is allocated to the replacement fund, and/or special assessments. In the event that funds are not available when needed, the Board may, subject to the constraints of California law and the Association's governing documents, increase regular assessments, levy special assessments, and/or delay repair and replacement of common area major components until sufficient funds are available.

The supplementary information about future major repairs and replacements is not a required part of the basic financial statements but is supplementary information required by the Financial Accounting Standards Board. We have compiled the supplementary information from information that is the representation of management of **Verano Homeowners Association**, without audit or review. Accordingly, we do not express an opinion or provide any assurance on the supplementary information.



February 22, 2012

VERANO HOMEOWNERS ASSOCIATION

**BALANCE SHEETS
DECEMBER 31, 2011 AND 2010**

	<u>2011</u>			<u>2010</u>
	<u>Operations Fund</u>	<u>Replacement Fund</u>	<u>Total Funds</u>	<u>Total Funds</u>
ASSETS				
Cash and cash equivalents (Note 2)	\$ 87,601	\$ 229,976	\$ 317,577	\$ 274,464
Assessments receivable, less allowance for doubtful accounts of \$2,000 and \$10,000, respectively (Note 2)	1,077		1,077	1,661
Prepaid insurance	3,698		3,698	3,775
Prepaid income taxes	57	133	190	
Total assets	<u>\$ 92,433</u>	<u>\$ 230,109</u>	<u>\$ 322,542</u>	<u>\$ 279,900</u>
LIABILITIES				
Accounts payable	\$ 238	\$ -	\$ 238	\$ 1,156
Assessments paid in advance	3,314		3,314	3,548
Income taxes payable				96
Future major repairs and replacements (Note 3)	-	-	-	-
Total liabilities	<u>3,552</u>	<u>-</u>	<u>3,552</u>	<u>4,800</u>
COMMITMENTS (NOTE 4)	-	-	-	-
FUND BALANCE (DEFICIT)	<u>88,881</u>	<u>230,109</u>	<u>318,990</u>	<u>275,100</u>
Total liabilities and fund balance	<u>\$ 92,433</u>	<u>\$ 230,109</u>	<u>\$ 322,542</u>	<u>\$ 279,900</u>

See independent accountants' review report and accompanying notes.

VERANO HOMEOWNERS ASSOCIATION

**STATEMENTS OF REVENUES, EXPENSES
AND CHANGES IN FUND BALANCES
YEARS ENDED DECEMBER 31, 2011 AND 2010**

	<u>2011</u>			<u>2010</u>
	<u>Operations Fund</u>	<u>Replacement Fund</u>	<u>Total Funds</u>	<u>Total Funds</u>
REVENUES				
Assessments	\$ 73,656	\$ 31,320	\$ 104,976	\$ 104,976
Interest income (Note 2)	196	456	652	1,623
Late charges and other income				255
Total revenues	<u>73,852</u>	<u>31,776</u>	<u>105,628</u>	<u>106,854</u>
EXPENSES				
<u>Administration</u>				
Bad debt expense (recovery)	(8,000)	-	(8,000)	7,614
Income tax provision (Note 2)				166
Insurance	4,111		4,111	3,832
Legal and accounting	1,795		1,795	1,903
Management	11,151		11,151	10,692
Office, printing and postage	2,619		2,619	2,192
Reserve study	900		900	
	<u>12,576</u>	<u>-</u>	<u>12,576</u>	<u>26,399</u>
<u>Maintenance and operations</u>				
Landscape maintenance	24,352	-	24,352	22,674
Other maintenance and operations	45		45	1,121
	<u>24,397</u>	<u>-</u>	<u>24,397</u>	<u>23,795</u>
<u>Utilities</u>				
Gas and electricity	1,314	-	1,314	178
Water and sewer	7,509		7,509	6,932
	<u>8,823</u>	<u>-</u>	<u>8,823</u>	<u>7,110</u>

See independent accountants' review report and accompanying notes.

VERANO HOMEOWNERS ASSOCIATION

**STATEMENTS OF REVENUES, EXPENSES
AND CHANGES IN FUND BALANCES
YEARS ENDED DECEMBER 31, 2011 AND 2010**

	<u>2011</u>			<u>2010</u>
	<u>Operations Fund</u>	<u>Replacement Fund</u>	<u>Total Funds</u>	<u>Total Funds</u>
EXPENSES (CONTINUED)				
<u>Major repairs and replacements</u>				
Fences	\$ -	\$ 10,955	\$ 10,955	\$ -
Paving and concrete		4,987	4,987	
Trees and trimming				15,080
Other major repairs and replacements				6,308
	<u>-</u>	<u>15,942</u>	<u>15,942</u>	<u>21,388</u>
Total expenses	<u>45,796</u>	<u>15,942</u>	<u>61,738</u>	<u>78,692</u>
EXCESS (DEFICIENCY) OF REVENUES OVER EXPENSES	28,056	15,834	43,890	28,162
BOARD-APPROVED INTERFUND RECLASSIFICATIONS AND TRANSFERS	690	(690)	-	-
FUND BALANCE (DEFICIT), BEGINNING OF YEAR	<u>60,135</u>	<u>214,965</u>	<u>275,100</u>	<u>246,938</u>
FUND BALANCE (DEFICIT), END OF YEAR	<u>\$ 88,881</u>	<u>\$ 230,109</u>	<u>\$ 318,990</u>	<u>\$ 275,100</u>

See independent accountants' review report and accompanying notes.

VERANO HOMEOWNERS ASSOCIATION

**STATEMENTS OF CASH FLOWS
YEARS ENDED DECEMBER 31, 2011 AND 2010**

	<u>2011</u>		<u>2010</u>	
	<u>Operations Fund</u>	<u>Replacement Fund</u>	<u>Total Funds</u>	<u>Total Funds</u>
OPERATING ACTIVITIES				
Excess (deficiency) of revenues over expenses	\$ 28,056	\$ 15,834	\$ 43,890	\$ 28,162
Adjustments to reconcile excess (deficiency) of revenues over expenses to net cash provided by operating activities:				
Bad debt expense (recovery)	(8,000)	-	(8,000)	7,614
Decrease (increase) in assets:				
Assessments receivable	8,584		8,584	(6,122)
Prepaid insurance	77		77	(197)
Prepaid income taxes	(57)	(133)	(190)	977
Increase (decrease) in liabilities:				
Accounts payable	(918)		(918)	(952)
Assessments paid in advance	(234)		(234)	943
Income taxes payable	(20)	(76)	(96)	96
Total adjustments	(568)	(209)	(777)	2,359
NET CASH PROVIDED BY (USED FOR) OPERATING ACTIVITIES	27,488	15,625	43,113	30,521
INVESTING ACTIVITIES				
Net (purchase) sale of certificates of deposit	-	-	-	70,000
NET CASH PROVIDED BY (USED FOR) INVESTING ACTIVITIES	-	-	-	70,000

See independent accountants' review report and accompanying notes.

VERANO HOMEOWNERS ASSOCIATION

**STATEMENTS OF CASH FLOWS
YEARS ENDED DECEMBER 31, 2011 AND 2010**

	<u>2011</u>			<u>2010</u>
	<u>Operations Fund</u>	<u>Replacement Fund</u>	<u>Total Funds</u>	<u>Total Funds</u>
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	\$ 27,488	\$ 15,625	\$ 43,113	\$ 100,521
BOARD-APPROVED INTERFUND RECLASSIFICATIONS AND TRANSFERS	690	(690)	-	-
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	<u>59,423</u>	<u>215,041</u>	<u>274,464</u>	<u>173,943</u>
CASH AND CASH EQUIVALENTS, END OF YEAR	<u>\$ 87,601</u>	<u>\$ 229,976</u>	<u>\$ 317,577</u>	<u>\$ 274,464</u>
<u>Supplemental Disclosures</u>				
Interest paid	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>
Income taxes paid	<u>\$ 77</u>	<u>\$ 209</u>	<u>\$ 286</u>	<u>\$ (907)</u>

See independent accountants' review report and accompanying notes.

VERANO HOMEOWNERS ASSOCIATION

NOTES TO FINANCIAL STATEMENTS YEARS ENDED DECEMBER 31, 2011 AND 2010

1. THE ASSOCIATION

Verano Homeowners Association (the Association) is a common interest development located in San Jose, California which consists of 54 residential units and certain common area property. The Association was organized as a nonprofit mutual-benefit corporation in June 1988 to provide for management, maintenance and architectural control of the individual units and the common area property. The Association is governed by a member-elected Board of Directors which is responsible for enforcing provisions of the governing documents, which include covenants, conditions and restrictions (CC&Rs), by laws, and rules and regulations. Major decisions, as determined by the CC&Rs, are referred to the Association owners as a whole.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Assessments. Association members are subject to annual assessments, usually payable in equal monthly installments, to provide funds for operating expenses and major repairs and replacements. In addition to regular annual assessments, special and/or emergency assessments may be imposed by the Association's Board Of Directors, under certain circumstances without member approval. Any excess assessments at year end are retained by the Association for use in the succeeding year. Revenues and expenses and information about future major repairs and replacements are explained in greater detail in the annually-distributed pro forma operating budget (pursuant to California Civil Code Section 1365).

Assessments receivable at the balance sheet date represents the aggregate amount of assessments due from unit owners. The Association's policy is to retain a collection service and/or legal counsel and place liens on the properties of owners whose assessments are delinquent. In certain instances, foreclosure may be necessary. The collection process is explained in greater detail in the annually distributed delinquent assessment collection policy (pursuant to California Civil Code Section 1365.1). Because of these collection procedures, the Board believes that, subject to a reasonable allowance for doubtful accounts, if any, all assessments are collectible. The estimate of allowance for doubtful accounts, if any, is based, generally, on amounts past due greater than 90 to 120 days.

See independent accountants' review report.

VERANO HOMEOWNERS ASSOCIATION

NOTES TO FINANCIAL STATEMENTS YEARS ENDED DECEMBER 31, 2011 AND 2010

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Basis of presentation. The accompanying financial statements, and the Association's corporate income tax returns, have been prepared on the accrual basis of accounting, in accordance with accounting principles generally accepted in the United States of America, whereby revenues are recognized when earned and expenses are recognized when incurred.

Cash and cash equivalents. For purposes of the statement of cash flows, the Association considers all short-term investments with a maturity at date of purchase of three months or less to be cash equivalents. Cash equivalents are classified with cash in the balance sheet.

Concentrations of credit risk. Financial instruments which potentially subject the Association to concentrations of credit risk consist principally of cash, cash equivalents and investments. The Association maintains its financial instruments with what management believes to be high credit quality financial institutions and limits the amount of credit exposure to any one particular institution. Cash, cash equivalents and investments in excess of federal deposit insurance (FDIC) coverage limits as of December 31, 2011 totaled approximately \$76,000.

Estimates. The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America 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. Estimates also affect the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates, and the differences could be material.

Fund accounting. The Association's governing documents provide certain guidelines for governing its financial activities. To ensure the observance of limitations and restrictions on the use of financial resources, the Association maintains its accounts using fund accounting. Financial resources are classified for accounting and reporting purposes in two funds established according to their nature and purpose. The operations fund is used to account for the financial resources available for the general day-to-day operations of the Association. The replacement fund is used to accumulate financial resources designated for future major repairs and replacements.

See independent accountants' review report.

VERANO HOMEOWNERS ASSOCIATION

NOTES TO FINANCIAL STATEMENTS YEARS ENDED DECEMBER 31, 2011 AND 2010

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Income taxes are paid on income from sources which are not related to the nonprofit, membership purposes of the Association. Nonmembership income, less related nonmembership expenses, subject to federal and California income taxes includes interest earned on cash and cash equivalents, and investments.

For federal purposes, the Association may elect to be taxed as either a regular corporation or as a homeowners association. In the former instance, it is taxed at graduated rates from 15% to 39% on net nonmember income; in the latter case it is taxed on net nonexempt function income (which is generally similar to net nonmember income) at a flat 30% rate. California income taxes normally approximate 9% of taxable income.

Interest earned on operations and replacement funds, net of related income taxes, is retained in said respective funds.

Membership in the Association is mandatory by virtue of unit ownership.

Real and personal common property acquired by the original owners from the developer is not recognized in the Association's financial statements, in accordance with prevalent industry practice, because it is commonly owned by the individual Association members and its disposition by the Board Of Directors is restricted. Similarly, major repairs, replacements and improvements to real and personal property are not recognized.

3. FUTURE MAJOR REPAIRS AND REPLACEMENTS

The Association's governing documents, and California state law (Civil Code Section 1365), require that the Board Of Directors provide for the repair and replacement of Association common area major components. Accordingly, funds which comprise the replacement fund are not generally available for the payment of day-to-day operating expenses.

See independent accountants' review report.

VERANO HOMEOWNERS ASSOCIATION

NOTES TO FINANCIAL STATEMENTS YEARS ENDED DECEMBER 31, 2011 AND 2010

3. FUTURE MAJOR REPAIRS AND REPLACEMENTS (CONTINUED)

The Association has completed a study of its common area major components sufficient to assist the Board in planning for future major repairs and replacements. The reasonableness of the resulting reserve funding plan is a function of the completeness of the major component list, the accuracy of the estimated quantity, useful and remaining lives and current replacement costs of those components, and the reasonableness of significant funding assumptions, including but not limited to the projected major component cost increases (aka inflation) and interest earning rate(s) on replacement fund cash balances.

Funds are being accumulated in the replacement fund based on estimated future costs for repair and replacement of common area property. Actual expenditures and investment income may vary from the estimated amounts, and the variations may be material.

Therefore, amounts accumulated in the replacement fund may or may not be adequate to meet all future component repair and replacement costs. The ability of the Association to fund its future requirements is dependent upon annual increases in that portion of the assessment which is allocated to the replacement fund, and/or special assessments. In the event that funds are not available when needed, the Board may, subject to the constraints of California law and the Association's governing documents, increase regular assessments, levy special assessments, and/or delay repair and replacement of common area major components until funds are available.

Additional information about future major repairs and replacements may be found in the annually-distributed pro forma operating budget and related assessment and reserve funding disclosure summary (pursuant to California Civil Code Section 1365).

4. COMMITMENTS

The Association enters into contracts for management and/or maintenance services in the normal course of its business operations. These contracts are generally cancelable on thirty to ninety days' advance notice.

See independent accountants' review report.

VERANO HOMEOWNERS ASSOCIATION

**NOTES TO FINANCIAL STATEMENTS
YEARS ENDED DECEMBER 31, 2011 AND 2010**

5. DATE OF MANAGEMENT'S REVIEW

In preparing the financial statements, the Association has evaluated events and transactions for potential recognition or disclosure through February 22, 2012, the date that the financial statements were available to be issued.

See independent accountants' review report.

VERANO HOMEOWNERS ASSOCIATION

**SUPPLEMENTARY INFORMATION ON FUTURE
MAJOR REPAIRS AND REPLACEMENTS
DECEMBER 31, 2011
(COMPILED WITHOUT AUDIT OR REVIEW)**

The following information on common area major components was compiled by Reserve Analysis Consulting, LLC. of Sausalito, California as of **October 2011** and has served as the basis for the current estimates of replacement reserve funding:

Code #	Component Description	Year New	Useful Life	Remaining Life	Total Cost	Annual Contrib.	2011 Total Req'd in Bank
1.00	ROADS						
1.01	Asphalt Sealing	2008	5	1	\$5,200	\$1,040	\$3,120
1.02	Asphalt Repairs	2008	5	1	\$1,500	\$300	\$900
1.03	Asphalt Major Repair	1988	30	6	\$17,948	\$598	\$13,760
1.04	Asphalt Replacement	1988	60	36	\$71,792	\$1,197	\$27,520
2.00	CONCRETE & PAVERS						
2.01	Annual Repair Allowance	2011	1	0	\$1,000	\$1,000	\$0
2.02	Future Replacement Allowance	2000	15	3	\$5,000	\$333	\$3,667
3.00	SIGNAGE & FENCING						
3.01	Miscellaneous Signage Upgrade	1988	25	1	\$1,250	\$50	\$1,150
3.02	Iron Fence @ End of Verano Cul-De-Sac (w/ 2 Gates)	2011	30	29	\$10,955	\$365	\$0
4.00	ELECTRICAL						
4.01	Street Light 2 Head Fixtures	2010	20	18	\$4,201	\$210	\$210
4.02	Street Light Poles	2006	40	34	\$2,000	\$50	\$250
4.03	Street Light Poles	1988	40	16	\$4,000	\$100	\$2,300
4.04	Driveway Column Light Fixtures	1988	25	1	\$5,400	\$216	\$4,968
5.00	LANDSCAPE & IRRIGATION						
5.01	Irrigation Controllers	2008	15	11	\$1,600	\$107	\$320
5.02	Irrigation Controllers	1988	15	-9	\$3,200	\$213	\$3,200
5.03	Irrigation Equipment Replacement Allowance	2011	1	0	\$500	\$500	\$0
5.04	Backflow Prevention	1988	30	6	\$1,650	\$55	\$1,265
5.05	Tree Care	2011	1	0	\$10,000	\$10,000	\$0
5.06	Planting Enhancement	2011	1	0	\$2,000	\$2,000	\$0
6.00	PAINT ENTIRE SITE						
6.01	Paint Stucco Components	2008	10	6	\$70,200	\$7,020	\$21,060
6.02	Paint Wood/Metal Components	2008	5	1	\$43,200	\$8,640	\$25,920
6.03	Paint Iron Fence @ End of Verano Cul-De-Sac	2011	10	9	\$825	\$83	\$0

Total Value of Components: \$263,421
Annual Component Contribution: \$34,077

Total Dollars Required: \$109,610

The Association has conducted a study to estimate the useful and remaining lives and current replacement costs of common property major components. Funding requirements consider an estimated **before-tax interest rate** of **2%** on replacement fund cash balances and an annual **inflation rate** of **3%** on major component replacement costs. The replacement fund **cash** and investment balances at December 31, 2011 totaled **\$229,976**. The estimated **liability** for major repairs and replacements at this date totaled approximately **\$109,000**. The portion of **2012** regular **assessments** budgeted to be allocated to the replacement fund totals **\$32,340**.

See independent accountants' review report and accompanying notes.