

Typically, there are three types of financial statement services an accountant may provide...



- **Compilation** - This is the most basic level of service. The accountant, who does not have to be independent, will take the numbers provided and put them together in financial statement format. They may question amounts that are obviously wrong, but typically do not perform any additional analysis. The goal is to aid management in preparing financial statements in the correct format.
- **Review** - An independent Certified Public Accountant will take the numbers provided to them and put them in a financial statement format. The accountant will also ask questions of management and do some analytical testing. Reviewed financial statements are also required to include full note disclosure.
- **Audit** - An independent Certified Public Accountant will provide an opinion on the prepared financial statements as to whether they are reasonably stated. The audit will also provide for a test of the organization's internal controls and examination of documentation to verify if controls are working and also to substantiate transactions and balances. Full note disclosure is also required in audited financial statements.

An engagement that we provide for most of the associations that we work with is called an agreed upon procedures. It is exactly what it sounds like. The association and we will agree upon what procedures will be performed. We will typically do some analytical procedures as is found in audits and reviews. We often will test disbursements to substantiate expenditures. Additional procedures regarding cash and bank reconciliations are performed. Both disbursement testing and bank reconciliation procedures also provide insight as to internal control procedures. One of the procedures, although not required, will often include a compilation of the financial statements. While a compilation is the most basic level of service, the other agreed upon procedures will provide the additional analysis of amounts reported in the association books and records.

As you know, the Michigan Condominium Act now requires an audit or review to be performed annually for associations with gross receipts over \$20,000, unless opted out by the association members. Currently most of the associations that we work with are opting out of the audit or review and will continue with agreed upon procedures.

In any of the above engagements we are required to report to management if any items of fraud are discovered. The biggest cost difference is that there are specific standards and work performed that must be met in order for an engagement to be considered a review or an audit. Many of these required steps include documentation on our side that may not provide benefit to the association. However, we are still required to complete those steps to provide an audit or review that meets the standards of our profession. As an agreed upon procedures is an agreement between the association and the accountant as to specifically which procedures will be performed, there are not as many requirements set by the accounting profession as to what work must be done.

In addition to these services, we also included the preparation of the tax return. We would like to note that the taxation of home-owner's association can be a complex issue. There are several IRS revenue rulings and code sections related specifically to home-owner's associations. It is important that your tax preparer is familiar with these issues.

Please feel free to contact us if you have any questions. We look forward to working with you.

Reserve Study & the Financial Statement

A reserve study is a plan for setting aside funds for future repairs and replacement of the association's common property. It requires:

- An analysis of common property components
- The preparation of a long term range funding plan

It is recommended that the association have a formal reserve study done as it incorporates the physical analysis of common property. It also incorporates the funding goals and the reserve dues needed to properly fund the expenditures. All common property of the association should be included within the physical analysis of common property to determine what should be included within the reserve study. The reserve study will also differentiate items between capital or non-capital (also known as deferred maintenance). Some associations also included deferred maintenance account for components requiring periodic maintenance that does not occur annually.

Examples of deferred maintenance items are:

- Tree trimming
- Landscaping
- Painting & staining
- Caulking
- Termite treatment
- Cost of reserve study

For financial statement purpose these items are treated the same as capital items and are included within your reserve fund. The IRS does not allow items for deferred maintenance to be treated the same as capital items for the reserve fund, and therefore treats the dues and expenditures differently. It is recommended that the reserve fund be divided into capital and non-capital pools to distinguish between the two.

The American Institute of Certified Public Accountants requires a specific statement on the reserve fund to be included within your basic financial statements. This statement includes the estimate of current or future cost of future major repairs and replacement of all existing components including estimated amounts required, methods used to determine the cost, basis for calculations, sources used, and the dates of studies made for that purpose.

With any of our services between an audit, review, or agreed upon procedures, we provide a financial statement that includes this required statement. Associations that we have worked with like this statements as it provides a summary of future expenditures, providing more proof for the assessed dues of the reserve fund.