



OPEN MEETING

SPECIAL OPEN MEETING OF THE BOARD OF DIRECTORS OF THE THIRD LAGUNA HILLS MUTAUL A CALIFORNIA NON-PROFIT MUTUAL BENEFIT CORPORATION

**Monday, April 5, 2021 at 3:00 PM
Virtual Meeting
24351 El Toro Road**

The purpose of this meeting is to discuss and consider the results of the 2020 Audit Report prepared by KPMG as required by Article 12 of the Third bylaws dated June 17, 2014.

NOTICE AND AGENDA

1. Call Meeting to Order / Establish Quorum – Steve Parsons President
2. Approval of the Agenda
3. Open Forum (Three Minutes per Speaker)

At this time Members only may address the Board of Directors regarding items not on the agenda and within the jurisdiction of this Board of Directors. The Board reserves the right to limit the total amount of time allotted for the Open Forum. Members can attend the meeting by joining the Zoom link <https://zoom.us/j/92081839160> or by calling (949) 268-2020 or email meeting@vmsinc.org to request to speak

4. Entertain Motion to Accept the 2020 Audit Report
5. Director Comments
6. Adjournment

THIRD LAGUNA HILLS MUTUAL

Financial Statements and Supplementary Information

December 31, 2020 and 2019

(With Independent Auditors' Report Thereon)

THIRD LAGUNA HILLS MUTUAL

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Independent Auditors' Report

The Board of Directors
Third Laguna Hills Mutual:

We have audited the accompanying financial statements of Third Laguna Hills Mutual (the Mutual), which comprise the balance sheets as of December 31, 2020 and 2019, and the related statements of operations, comprehensive income, changes in members' equity, and cash flows for the years 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 U.S. generally accepted accounting principles; 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.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits 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 auditors' 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 Third Laguna Hills Mutual as of December 31, 2020 and 2019, and the results of its operations and its cash flows for the years then ended in accordance with U.S. generally accepted accounting principles.

Other Matter

U.S. generally accepted accounting principles require that the information included in schedule 1 on future major repairs and replacements be presented to supplement the financial statements. Such information, although not a part of the financial statements, is required by the Financial Accounting Standards Board who considers it to be an essential part of financial reporting for placing the 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 financial statements, and other knowledge we obtained during our audits of the 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.

(signed) KPMG LLP

Irvine, California
April xx, 2021

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Balance Sheets

December 31, 2020 and 2019

Assets	2020	2019
Cash and cash equivalents (note 3)	\$ 1,785,431	834,438
Accounts receivable and interest receivable, net of allowance for doubtful accounts of \$854,522 in 2020 and \$782,725 in 2019, respectively	172,270	406,748
Receivable from Golden Rain Foundation of Laguna Woods (note 5)	354,178	688,618
Income tax receivable (note 4)	26,005	—
Prepaid expenses	3,290,396	807,109
Total current assets	5,628,280	2,736,913
Investments (note 3)	29,206,870	30,533,117
Beneficial interest in Golden Rain Foundation of Laguna Hills Trust (note 2(h))	5,189,637	5,324,513
Equity Interest in Golden Rain Foundation of Laguna Woods (note 2(h))	39,594,122	37,749,056
Total assets	\$ 79,618,909	76,343,599
Liabilities and Members' Equity		
Liabilities:		
Accounts payable and accrued expenses	\$ 3,641,829	2,429,597
Amounts payable for accrued compensation	548,292	629,534
Assessments and charges paid in advance	759,755	659,936
Income taxes payable (note 4)	—	80,710
Total current liabilities	4,949,876	3,799,777
Total liabilities	4,949,876	3,799,777
Members' equity	74,669,033	72,543,822
Total liabilities and members' equity	\$ 79,618,909	76,343,599

See accompanying notes to financial statements.

THIRD LAGUNA HILLS MUTUAL

Statements of Operations

Years ended December 31, 2020 and 2019

	<u>2020</u>	<u>2019</u>
Revenue:		
Member assessments:		
Operating	\$ 33,526,024	32,227,670
Golden Rain Foundation of Laguna Woods restricted funds (note 5)	1,757,376	1,391,256
Restricted funds (note 3)	<u>12,935,046</u>	<u>13,459,997</u>
Total member assessments	<u>48,218,446</u>	<u>47,078,923</u>
Other revenue:		
Chargeable services revenue	401,033	1,087,533
Laundry	198,525	210,085
Investment income	443,266	665,119
Lease and resale processing fees	384,333	432,062
Income tax benefit (note 4)	25,715	—
Miscellaneous	<u>210,427</u>	<u>563,128</u>
Total other revenue	<u>1,663,299</u>	<u>2,957,927</u>
Total revenue	<u>49,881,745</u>	<u>50,036,850</u>
Expenses:		
Reimbursement to managing agent for compensation and related costs	12,367,602	12,590,828
Operating materials and supplies	1,015,170	1,375,711
Utilities and telephone	5,370,908	5,208,741
Professional fees	216,775	149,906
Legal fees	678,562	726,416
Repairs and maintenance	10,659,604	11,833,401
Insurance	2,829,407	1,512,536
Income taxes (note 4)	—	80,710
Golden Rain Foundation of Laguna Woods operating expenses	14,742,872	14,739,014
Payments to Golden Rain Foundation of Laguna Woods restricted funds (note 5)	1,757,376	1,391,256
Other	<u>307,175</u>	<u>567,089</u>
Total expenses	<u>49,945,451</u>	<u>50,175,608</u>
Net income before other changes	(63,706)	(138,758)
Other changes:		
Realized gain(loss) on available for sale investments (note 3)	41,318	(271,923)
Unrealized gain on available for sale investments	437,409	—
Unrealized gain from voting interest in Golden Rain Foundation of Laguna Woods	1,845,066	763,005
Loss from beneficial interest in Golden Rain Foundation of Laguna Hills Trust	<u>(134,876)</u>	<u>(136,229)</u>
Net income	<u>\$ 2,125,211</u>	<u>216,095</u>

See accompanying notes to financial statements.

THIRD LAGUNA HILLS MUTUAL
 Statements of Comprehensive Income
 Years ended December 31, 2020 and 2019

	<u>2020</u>	<u>2019</u>
Net income	\$ 2,125,211	216,095
Other comprehensive gain:		
Unrealized gain on available-for-sale investments arising during the year, net:		
Unrealized holding gain arising during the period	<u>—</u>	<u>567,267</u>
Comprehensive income	<u>\$ 2,125,211</u>	<u>783,362</u>

See accompanying notes to financial statements

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Statements of Changes in Members' Equity

Years ended December 31, 2020 and 2019

	Memberships		Changes	Total members' equity
	Number	Amount		
Members' equity, December 31, 2018	6,102	\$ 610,200	71,150,260	71,760,460
Net income	—	—	216,095	216,095
Unrealized gain on available-for-sale investments, net	—	—	567,267	567,267
Members' equity, December 31, 2019	6,102	610,200	71,933,622	72,543,822
Net income			2,125,211	2,125,211
Members' equity, December 31, 2020	6,102	\$ 610,200	74,058,833	74,669,033

See accompanying notes to financial statements.

THIRD LAGUNA HILLS MUTUAL

Statements of Cash Flows

Years ended December 31, 2020 and 2019

	<u>2020</u>	<u>2019</u>
Cash flows from operating activities:		
Net income	\$ 2,125,211	216,095
Adjustments to reconcile net income to net cash (used in) provided by operating activities:		
Loss from beneficial interest in Golden Rain Foundation of Laguna Hills Trust	134,876	136,229
Unrealized (gain) loss on sales of AFS investments	(437,409)	—
Amortization of investment premium and discount, net	111,066	(386,543)
Unrealized gain from voting interest in Golden Rain Foundation of Laguna Woods	(1,845,066)	(763,005)
Effect of changes in operating assets and liabilities:		
Accounts and accrued interest receivable	234,478	35,722
Prepaid expenses	(2,483,287)	(611,993)
Receivable from Golden Rain Foundation of Laguna Woods	334,440	839,043
Payable for accrued compensation	(81,242)	(16,781)
Accounts payable and accrued expenses	1,212,232	(174,658)
Member assessments paid in advance	99,819	(96,440)
Income taxes receivable	(26,005)	—
Income taxes payable	(80,710)	80,710
Net cash (used in) provided by operating activities	<u>(701,597)</u>	<u>(741,621)</u>
Cash flows from investing activities:		
Purchases of held-to-maturity investments	(13,997,717)	(21,800,527)
Maturities of held-to-maturity investments	23,850,594	19,779,105
Proceeds from payments and maturities of available-for-sale investments	4,309,546	21,739,276
Purchases of available-for-sale investments	<u>(12,509,833)</u>	<u>(21,530,913)</u>
Net cash provided by (used in) investing activities	<u>1,652,590</u>	<u>(1,813,059)</u>
Net (decrease) increase in cash and cash equivalents and restricted cash	950,993	(2,554,680)
Cash and cash equivalents and restricted cash, beginning of year	<u>834,438</u>	<u>3,389,118</u>
Cash and cash equivalents and restricted cash, end of year (note 2 (c))	<u>\$ 1,785,431</u>	<u>834,438</u>

See accompanying notes to financial statements.

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Notes to Financial Statements

December 31, 2020 and 2019

(1) Organization

(a) General

Third Laguna Hills Mutual (the Mutual), a nonprofit mutual benefit corporation, was formed to manage, operate, and maintain 6,102 condominium housing units (manors or common property) for the benefit of its members. These manors are a part of Laguna Woods Village, Laguna Woods, California (the Village), a housing development consisting of 12,736 manors and various community facilities.

The Mutual is a corporate member of Golden Rain Foundation of Laguna Woods (GRF), a nonprofit mutual benefit corporation. The individual Mutual members have a right to the use of facilities owned or held in trust by GRF, appurtenant to their membership in the Mutual. GRF, as trustee, holds title to certain community facilities in trust for the benefit of all Mutuals that are a part of the Village (the Village Mutuals).

The Mutual is a member of Village Management Services, Inc. (VMS), an affiliated California nonprofit mutual benefit corporation. VMS was formed to provide management services under contract for GRF and the Mutuals. No management fee is paid to VMS (note 5).

(b) Assessments

The Mutual receives, on a monthly basis, assessments from its members (member assessments) to conduct its operations and to fund certain reserve accounts as discussed in note 2(f). For 2020 and 2019, the members were assessed Mutual basic monthly assessments of \$652.22 and \$637.22, respectively, per manor per month, for direct and Mutual shared operating costs, Mutual reserve contributions, and GRF shared operating expenses and restricted funds. The Mutual basic monthly assessment does not include surcharges for those manors with common laundry facilities, elevators, and/or Garden Villa recreation rooms.

The total assessed to the members of the Mutual for Mutual basic costs and surcharges and GRF costs was \$48,218,446 and \$47,078,923, respectively, in 2020 and 2019.

(2) Significant Accounting Policies

(a) Basis of Presentation

The accompanying financial statements have been prepared on the accrual basis of accounting.

(b) Cash and Cash Equivalents

For purposes of reporting cash flows, the Mutual considers all highly liquid investments with an original maturity of three months or less to be cash and cash equivalents.

(c) Investments

The Mutual accounts for investments and restricted funds under the provisions of ASC Topic 320, *Investments – Debt and Equity Securities*. This statement requires the Mutual to classify and account for investments in equity securities that have readily determinable fair values, and for all debt securities, into three categories: (1) debt securities that the Mutual has the positive intent and the ability to hold to maturity are classified as held-to-maturity securities and reported at amortized cost; (2) debt and equity securities that are bought and held principally for the purpose of selling them in the near

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Notes to Financial Statements

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term are classified as trading securities and reported at fair value, with unrealized gains and losses included in earnings; and (3) debt securities not classified as held-to-maturity securities or trading securities are classified as available-for-sale securities and reported at fair value, with unrealized gains and losses excluded from earnings and reported as other comprehensive income. Equity securities including mutual funds not classified as held-to-maturity securities or trading securities are classified as available-for-sale securities and reported at fair value, with unrealized gains and losses included in earnings during the year ended December 31, 2020. Unrealized gains and losses from available-for-sale securities were included in other comprehensive income during the year ended December 31, 2019.

The Mutual restricts a portion of member assessments to finance reserves set aside as restricted funds. Disbursements from restricted funds may be made only in accordance with the purpose established. Interest income earned on restricted funds is retained within the respective fund. Additions to the funds are determined each year as outlined in the annual business plan.

(d) Fair Value Measurements

The Mutual has adopted the provisions of ASC Topic 820, *Fair Value Measurements*, for fair value measurements of financial assets and financial liabilities and for fair value measurements of nonfinancial items that are recognized or disclosed at fair value in the financial statements on a recurring basis. ASC Topic 820 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction among market participants at the measurement date. ASC Topic 820 also establishes a framework for measuring fair value and expands disclosures about fair value measurements (note 3).

(e) Property

The Mutual has adopted the provisions of ASC Topic 972, *Real Estate – Common Interest Realty Associations, Subtopic 360, Property, Plant and Equipment*, for the accounting for common real property acquired. As such, common real property directly associated with units is expensed when incurred. Common real property not directly associated with units are capitalized when the Mutual can dispose of the property, at the discretion of its board of directors or when the property is used to generate significant cash flows from members on the basis of usage or from nonmembers.

(f) Future Major Repairs and Replacements

A study was conducted by the Mutual in 2020 to estimate the remaining useful lives and current replacement costs of certain major components of common property. This study also considered future replacement costs of these certain major components based on the estimated useful lives, assuming a 3.0% inflation factor. The board of directors has a policy to plan additional fund contributions over the estimated useful lives of the components (on a current-cost basis) based on an annual analysis of the adequacy of the funds. Under the assumption that certain buildings would not be completely replaced within the next 30 years, replacement funds are not provided for those community facilities. Actual replacement costs when expended may vary from the estimated future expenditures considered in the fund analysis, and the variations may be material. If additional monies are needed, the Mutual has the right to adjust the monthly assessment, impose special assessments, or delay expenditures as appropriate.

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Notes to Financial Statements

December 31, 2020 and 2019

(g) Interests in Golden Rain Foundation of Laguna Woods and Golden Rain Foundation of Laguna Hills Trust

The Mutual reports its 47.91% interest in GRF based on the non-Trust net assets of GRF to reflect the significant influence the Mutual exercises over GRF through its voting interest in accordance with ASC Topic 323, *Investments – Equity Method and Joint Ventures*. Such interest totaled \$39,877,908 and \$37,749,056 at December 31, 2020 and 2019.

The Mutual also has a beneficial interest in Golden Rain Foundation of Laguna Hills Trust (the Trust), which holds certain community facilities in trust for the Village Mutuals. The Mutual's beneficial interest is calculated based on the Mutual's "trusteed sums," defined as the original contribution amounts as stated in the trust agreement, and totals \$5,189,637 and \$5,324,513, respectively, at December 31, 2020 and 2019.

The Third Laguna Hills Mutual's interest in Golden Rain Foundation and Golden Rain Foundation Trust consists of its respective ownership of the following:

	2020	2019
Cash and cash equivalents	\$ 2,520,519	2,731,180
Receivables	1,719,097	1,445,309
Income tax receivable	—	46,377
Other current assets	2,859,369	2,483,748
Restricted funds and investments	24,509,316	21,895,591
Property and equipment, net	59,109,271	58,814,798
Community facilities, net	10,850,965	11,185,066
Intangible assets, net	189,781	235,982
Total assets	<u>\$ 101,758,318</u>	<u>98,838,051</u>
Accounts payable and accrued liabilities	\$ 5,741,894	6,019,484
Payables to Laguna Woods Mutuals	1,333,179	2,056,698
Deferred income	471,840	613,419
Income tax payable	546,062	—
Total liabilities	<u>8,092,975</u>	<u>8,689,601</u>
Members' equity in Golden Rain Foundation of Laguna Woods	82,640,239	78,789,245
Noncontrolling interest in consolidated trust	11,025,104	11,359,205
Total equity	<u>93,665,343</u>	<u>90,148,450</u>
Total liabilities and equity	<u>\$ 101,758,318</u>	<u>98,838,051</u>
Third Laguna Hills Mutual's 47.91% interest in Golden Rain Foundation of Laguna Woods	\$ 39,594,122	37,749,056

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Notes to Financial Statements

December 31, 2020 and 2019

(h) Income Taxes

The Mutual provides for income taxes in accordance with ASC Topic 740, *Income Taxes*. ASC 740 clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements and prescribes a threshold of more likely than not for recognition of tax benefits of uncertain tax positions taken or expected to be taken in a tax return. ASC 740 also provides related guidance on measurement, derecognition, classification, interest and penalties, and disclosure. Management believes that no uncertain tax positions requiring accrual or disclosure existed at December 31, 2020 and 2019. The open years for federal and state tax assessments are 2016–2019 for federal and 2015–2019 for California.

(i) Concentration of Credit Risk

The Mutual had cash balances of \$1,412,574 and \$692,297, respectively, and restricted cash balances of \$0 and \$0, respectively, at December 31, 2020 and 2019, maintained in a commercial bank and that consist of cash on deposit. At December 31, 2020 and 2019, all noninterest-bearing deposit transaction accounts are Federal Deposit Insurance Corporation insured up to a maximum of \$250,000, per depositor, per insured bank, for each account ownership category.

The Mutual also maintained a money market fund of \$372,857 and \$142,141, respectively, at December 31, 2020 and 2019, which was Securities Investor Protection Corporation insured up to the maximum of \$500,000 per institution.

(j) Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles 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 and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

(k) Current Environment

In March 2020 the World Health Organization declared the novel coronavirus (COVID-19) a pandemic. The outbreak led to a dramatic loss of life worldwide and affected travel, commerce and financial markets globally, including the United States. The spread of COVID-19 adversely affected Mutual operations and the ability to conduct maintenance on major components as planned. Commencing March 2020, certain community and corporate facilities within the Village were closed to resident use. While some staff worked in corporate facilities adhering to social distancing programs, many employees were furloughed for a period of four months from April 2020 through July 2020. As of December 31, 2020, uncertainty remains over the progression of the virus, the availability of vaccinations, and the changing governmental directives. By the issuance of this report, Mutual operations have largely returned to normal levels.

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Notes to Financial Statements

December 31, 2020 and 2019

(3) Cash and Cash Equivalents, and Investments and Restricted Cash

The Mutual's investments and restricted cash are presented as follows on the accompanying balance sheets at December 31, 2020 and 2019:

	<u>2020</u>	<u>2019</u>
Restricted investments:		
Available for sale (at fair value):		
Index funds	\$ 25,206,976	16,569,280
Total restricted investments at fair value	<u>25,206,976</u>	<u>16,569,280</u>
Held to maturity (at amortized cost):		
U.S. Treasury notes	<u>3,919,872</u>	<u>12,277,370</u>
Total restricted investment at amortized cost	<u>3,919,872</u>	<u>12,277,370</u>
Total restricted cash and restricted investments at fair value	29,126,848	28,846,650
Unrestricted Investments:		
Held to maturity (at amortized cost):		
U.S. Treasury notes	<u>80,022</u>	<u>1,686,467</u>
Total restricted cash, restricted and unrestricted investments	<u>\$ 29,206,870</u>	<u>30,533,117</u>

The Mutual follows the provisions of ASC 820 for fair value measurements for financial assets and liabilities and nonfinancial items that are recognized at fair value in the financial statements on a recurring basis. ASC 820 establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to measurements involving significant unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are as follows:

- Level 1 inputs are quoted prices (unadjusted) in active markets for identical investments that the Mutual has the ability to access at the measurement date.
- Level 2 inputs are inputs other than quoted prices included in Level 1 that are observable for the investment, either directly or indirectly.
- Level 3 inputs are unobservable inputs for the investment.

The level in the fair value hierarchy within which a fair value measurement in its entirety falls is based on the lowest level of input that is significant to the fair value measurement.

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Notes to Financial Statements

December 31, 2020 and 2019

The Mutual's cash and cash equivalents and investments that are measured at fair value on a recurring basis as reflected on the accompanying balance sheets at December 31, 2020 and 2019 are as follows:

	2020		
	Level 1	Level 2	Total
Cash and cash equivalents	\$ 1,785,431	—	1,785,431
Investments and restricted cash:			
Available for sale:			
Index funds	25,206,976	—	25,206,976
Total investments and restricted cash	25,206,976	—	25,206,976
Total cash and cash equivalents, and investments and restricted cash	\$ 26,992,407	—	26,992,407

	2019		
	Level 1	Level 2	Total
Cash and cash equivalents	\$ 834,438	—	834,438
Investments and restricted cash:			
Available for sale:			
Index funds	16,569,280	—	16,569,280
Total investments and restricted cash	16,569,280	—	16,569,280
Total cash and cash equivalents, and investments and restricted cash	\$ 17,403,718	—	17,403,718

In November 2019 the Board of Directors approved a revised Investment Policy allowing bond holdings at investment grade ratings and directing the Mutual's Investment Manager to convert individual holdings of U.S. Treasury notes, GNMA's, and corporate bonds to a portfolio of index funds. In December 2020 the sale of previously owned holdings was executed and all proceeds were used for the immediate purchase of index funds. The valuation of the index fund portfolio used quoted prices in active markets for identical investments and are classified as Level 1 in the fair value hierarchy. Fair value of such investments totaled \$25,206,976 and \$16,569,280 at December 31, 2020 and 2019, respectively.

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Notes to Financial Statements

December 31, 2020 and 2019

Investments held to maturity comprised U.S. Treasury notes, totaling \$3,999,894 and \$13,963,837 were carried at cost at December 31, 2020 and 2019, respectively. Fair value of such investments totaled \$3,999,957 and \$13,978,194 at December 31, 2020 and 2019, respectively, and were considered Level 1 in the fair value hierarchy.

The Mutual's investments are classified as either available for sale or held to maturity and are summarized as follows:

	<u>Purchase/ amortized cost</u>	<u>Gross unrealized gains</u>	<u>Gross unrealized loss</u>	<u>Estimated fair value</u>
At December 31, 2020:				
Available for sale	\$ 24,756,027	941,075	(490,126)	25,206,976
Held to maturity	3,999,894	63	—	3,999,957
	<u>Purchase/ amortized cost</u>	<u>Gross unrealized gains</u>	<u>Gross unrealized loss</u>	<u>Estimated fair value</u>
At December 31, 2019:				
Available for sale	\$ 16,555,738	13,542	—	16,569,280
Held to maturity	13,963,837	14,357	—	13,978,194

The Mutual determines realized gains and losses based on the specific-identification method. In 2020 realized gains and realized losses were as follows in 2020 and 2019:

<u>Available for sale</u>	<u>2020</u>	<u>2019</u>
Realized gain	\$ 203,037	128,640
Realized (loss)	(161,719)	(400,563)
Realized gain (loss) on available for sale, net	<u>\$ 41,318</u>	<u>(271,923)</u>

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Notes to Financial Statements

December 31, 2020 and 2019

Restricted cash and investments consist of the following reserve funds:

	Replacement funds	Garden villa recreation room fund	Disaster fund	Unappropriated expenditures fund	Total
Balances, December 31, 2018	\$ 16,769,482	61,299	9,216,804	3,212,980	29,260,565
Member assessments	10,763,928	81,972	2,028,305	585,792	13,459,997
Net investment income and other contributions	208,992	718	111,599	37,996	359,305
Expenditures	(11,663,965)	(71,036)	(2,287,219)	(210,997)	(14,233,217)
Balances, December 31, 2019	16,078,437	72,953	9,069,489	3,625,771	28,846,650
Member assessments	11,130,048	85,698	1,133,508	585,792	12,935,046
Net investment income and other contributions	505,591	2,295	284,884	113,983	906,753
Expenditures	(9,988,044)	(71,246)	(3,502,311)	—	(13,561,601)
Balances, December 31, 2020	\$ 17,726,032	89,700	6,985,570	4,325,546	29,126,848

(a) Replacement Reserve Funds

Replacement funds were established to provide reserves for replacement of common property, roofs, elevators, and certain equipment that were originally included in the cost of individual manors purchased by the residents. Monthly member assessments for these funds are included in member assessments restricted funds in the accompanying statements of operations.

(b) Garden Villa Recreation Room Fund

This fund was established to provide funds for maintaining the Garden Villa recreation rooms. Monthly member assessments for this fund are included in member assessments-restricted funds in the accompanying statements of operations.

(c) Disaster Fund

The disaster fund was established to reserve for contingencies and emergency expenditures or catastrophic damages not covered by insurance, including insurance policy deductibles. Monthly member assessments for this fund are included in member assessments-restricted funds in the accompanying statements of operations.

(d) Unappropriated Expenditures Fund

The unappropriated expenditures fund was established to provide funds for payment of authorized expenses not specifically provided for in the annual business plan. Monthly member assessments for this fund are included in member assessments-restricted funds in the accompanying statements of operations.

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Notes to Financial Statements

December 31, 2020 and 2019

(4) Income Taxes

The Mutual is considered a homeowners' association for federal and state income tax purposes and is liable for tax on nonexempt function net income. The provision for income taxes for the years ended December 31, 2020 and 2019 consists of the following:

	2020	2019
State taxes – current	\$ 10	—
Federal taxes – current	16,285	80,710
Total taxes	<u>\$ 16,295</u>	<u>80,710</u>

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and deferred tax liabilities at December 31, 2020 and 2019 are presented below:

	2020	2019
Deferred tax assets:		
IRC Section 277 loss carryforwards	\$ 388,894	388,894
Net operating loss carryforwards	621,747	623,281
Capital loss carryforwards	68,302	79,864
Total gross deferred tax assets	1,078,943	1,092,039
Less valuation allowance	<u>(1,078,943)</u>	<u>(1,092,039)</u>
Total deferred tax assets	<u>\$ —</u>	<u>—</u>

The valuation allowance for deferred tax assets as of December 31, 2020 and 2019 was \$1,078,943 and \$1,092,039, respectively. The net change in the total valuation allowance for the years ended December 31, 2020 and 2019 was a (decrease) increase of \$(13,096) and \$76,971, respectively. Based upon the level of historical taxable income and projections for future taxable income over periods, which the deferred tax assets are deductible, management believes it is more likely than not that the Mutual will not realize the benefits of the deductible differences. As such, the Mutual recorded a full valuation allowance against the deferred tax assets at December 31, 2020 and 2019.

At December 31, 2020, the Mutual has federal and state net operating loss carryforwards of \$193,927 and \$6,572,647 available to offset future federal and state taxable income, respectively. At December 31, 2019, the Mutual has federal and state net operating loss carryforwards of \$193,927 and \$6,590,007 available to offset future federal and state taxable income, respectively. The federal and state carryforward amounts expire in varying amounts between 2022 and 2040.

Income tax expense was computed by applying the U.S. federal income tax rate of 21% for both December 31, 2020 and 2019, respectively.

THIRD LAGUNA HILLS MUTUAL

Notes to Financial Statements

December 31, 2020 and 2019

(5) Related Parties

As discussed in note 1, the Mutual is a corporate member of GRF and a member of VMS, all related entities. The accompanying financial statements include assessments to GRF for operating expenses and restricted funds as well as a receivable due from GRF for assessments collected by GRF not yet remitted to the Mutual. The accompanying financial statements also include amounts paid and owed to VMS as managing agent for compensation and related costs.

(6) Pension Plans

Village Management Services, Inc. makes contributions to two union-sponsored, multiemployer, defined-benefit pension plans (covering most union employees) in accordance with a negotiated labor contract between VMS and the labor union. In the event these plans are either terminated or VMS withdraws from the plans, VMS may be required to contribute additional amounts under the provisions of the Employee Retirement Income Security Act of 1974. Such amounts would be reimbursed by GRF and the Mutuals. However, no such termination of or withdrawal from the plans is currently contemplated.

During 2020 and 2019, VMS sponsored a 401(k) plan covering all eligible employees. Employee contributions to the plan are at the participants' discretion. In 2016, VMS made contributions into the plan for eligible nonunion employee participants. The Mutuals and GRF are not responsible for the management or ultimate funding of the 401(k) plan beyond the agreed-upon annual contributions.

Amounts contributed by VMS to these plans in 2020 and 2019, and reimbursed by the Mutual, totaled \$62,389 and \$52,322, respectively, for the defined-benefit pension plan and \$383,714 and \$364,577, respectively, for the 401(k) plan.

(7) Contingencies

The Mutual is involved in various legal matters arising in the normal course of business. In the opinion of management, the liability, if any, will not have a material effect on the Mutual's financial position.

(8) Malware Attack

The Mutual, along with Golden Rain Foundation and United Laguna Woods Mutual, were victims of a malware attack in October 2020. The criminal(s) responsible for the attack encrypted data denying users access. While the financial systems remained functional, numerous internal systems were rendered inoperable. The FBI and local law enforcement were notified and a team of professionals were contracted with to resolve the incident. At December 31, 2020 the corporations had access to the recovered data and safeguard measures had been enacted to limit the risk of future losses.

(9) Subsequent Events

Subsequent events have been evaluated through April xx, 2021, which is the date the financial statements were available to be issued.

SUPPLEMENTARY INFORMATION

Schedule 1

THIRD LAGUNA HILLS MUTUAL

Future Major Repairs and Replacements

December 31, 2020

(Unaudited)

The Mutual contracted a study in 2020 to estimate the remaining useful lives and current replacement costs of major components of common property, except for certain land improvements, buildings, and building improvements for which major repair and replacement funds are not provided, as these items are expected to last the life of the community or to be maintained from general operating and/or preventive maintenance funds. The estimates were determined from past experience and from information obtained from certain contractors.

The following table is based on the Mutual study of common property:

Major components	Estimated useful lives (in years)	Estimated remaining useful lives (in years)	Estimated current replacement costs	Estimated funding requirement as of December 31, 2020
Paved surfaces	0 to 25	0 to 24	\$ 9,164,200	4,946,628
Roofing & gutters	1 to 40	0 to 34	15,087,500	5,987,325
Building structures	0 to 20	0 to 19	10,048,500	6,351,600
Decking projects	1	0 to 5	665,000	475,000
Prior to painting & painting projects	1 to 20	0 to 9	4,808,800	2,847,285
Elevators	1 to 30	0 to 29	8,545,300	5,571,850
Garden villas	0 to 20	0 to 19	2,214,650	555,050
Lighting replacement projects	1 to 1	0	79,000	79,000
Walls, fencing & railings	1	0	253,700	253,700
Laundry facilities	1 to 20	0 to 20	387,900	215,270
Sewer lines, water lines, & electricity	0 to 1	0 to 13	1,181,600	669,600
Grounds & miscellaneous	1	0	27,000	27,000
Landscape projects	0 to 1	0 to 1	2,379,000	2,269,000
			<u>\$ 54,842,150</u>	<u>30,248,308</u>

Replacement fund balance as of December 31, 2020 (note 3) \$ 17,726,032

The Board voted to contribute \$11,130,048 to the replacement funds in 2020. The contribution is included in the 2020 member assessments at \$152.00 per manor per month. Actual replacement costs when expended may vary and the variations may be material.

Because the reserve study is a projection, the estimated lives and costs of components will likely change over time depending on a variety of factors such as (i) future inflation rates, (ii) levels of maintenance applied by future boards, unknown defects in materials that may lead to premature failures, remaining useful lives, etc. As a result, some components may experience longer lives while others will experience premature failures. Some components may cost less at the time of replacement while others may cost more. To adequately plan for future expenditures, the Board has adopted via resolution a 30-Year Funding Plan that projects contributions to and disbursements from the reserves over the next thirty years, without falling below a minimum threshold in the reserve balance.

Reserves receive monies through assessments and net interest earned on invested fund balances.

See accompanying independent auditors' report.