UNITED LAGUNA WOODS MUTUAL

Financial Statements and Supplementary Information

December 31, 2019 and 2018

(With Independent Auditors’ Report Thereon)

UNITED LAGUNA WOODS MUTUAL

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KPMG LLP
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Irvine, CA 92618-3391

Independent Auditors' Report

The Board of Directors
United Laguna Woods Mutual:

Report on the Financial Statements

We have audited the accompanying financial statements of United Laguna Woods Mutual (the Mutual), which comprise the balance sheets as of December 31, 2019 and 2018, 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 United Laguna Woods Mutual as of December 31, 2019 and 2018, and the results of its operations and its cash flows for the years then ended in accordance with U.S. generally accepted accounting principles.

KPMG

Other Matter

Required Supplementary Information

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.

KPMG LLP

Irvine, California
April 5, 2020

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Balance Sheets

December 31, 2019 and 2018

Assets	**2019**	**2018**
Cash and cash equivalents (note 3)	$ 629,027	649,392
Accounts receivable and interest receivable	675,921	791,500
Receivable from Golden Rain Foundation of Laguna Woods (note 7)	1,400,595	1,882,840
Income taxes receivable (note 4)	19,561	17,753
Prepaid expenses	718,566	129,498
Total current assets	3,443,670	3,470,983
Investments and restricted cash (note 3)	18,351,707	21,713,353
Deferred tax asset (note 4)	380,000	380,000
Property, at cost:		
Land	8,175,233	8,175,233
Buildings and improvements	83,814,372	83,814,372
Total property, at cost	91,989,605	91,989,605
Less accumulated depreciation	(83,756,191)	(83,753,128)
Property, net	8,233,414	8,236,477
Beneficial interest in Golden Rain Foundation of Laguna Hills Trust (note 2(i))	5,796,949	5,992,130
Equity interest in Golden Rain Foundation of Laguna Woods (note 2(i))	39,116,237	38,325,598
Total assets	$ 75,321,977	78,118,541
Liabilities and Members' Equity		
Liabilities:		
Accounts payable and accrued expenses	$ 1,336,442	1,293,393
Amounts payable for accrued compensation (note 7)	596,765	612,761
Assessments and charges paid in advance	819,210	918,818
Income taxes payable (note 4)	—	12,474
Deferred income	117,341	55,000
Total current liabilities	2,869,758	2,892,446
Asset retirement obligation (note 9)	1,207,814	1,128,798
Total liabilities	4,077,572	4,021,244
Members' equity	71,244,405	74,097,297
Total liabilities and members' equity	$ 75,321,977	78,118,541

See accompanying notes to financial statements.

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Statements of Operations

Years ended December 31, 2019 and 2018

		2019	2018
Revenue:			
Member assessments for:			
Operating	$	41,827,807	41,204,939
Golden Rain Foundation of Laguna Woods restricted funds (note 7)		1,441,644	1,517,520
Restricted funds (note 3)		12,367,788	11,912,532
Total member assessments		55,637,239	54,634,991
Other revenue:			
Chargeable services revenue		602,446	513,803
Laundry		253,604	271,454
Interest		440,089	391,096
Lease and resale processing fees		265,222	259,724
Collection and late fees		128,809	121,022
Deferred tax benefit (note 4)		—	380,000
Income tax benefit (note 4)		13,931	—
Miscellaneous		167,047	242,121
Total other revenue		1,871,148	2,179,220
Total revenue		57,508,387	56,814,211
Expenses:			
Reimbursement to managing agent for compensation and related costs		13,630,356	13,753,513
Operating materials and supplies		3,155,479	3,041,969
Utilities and telephone		4,126,815	4,196,751
Professional fees		149,831	174,191
Legal fees		238,961	253,208
Repairs and maintenance		10,091,965	8,012,625
Property taxes		11,375,124	10,765,612
Insurance		1,482,527	1,240,999
Golden Rain Foundation of Laguna Woods shared operating expenses		15,176,144	14,678,411
Payments to Golden Rain Foundation of Laguna Woods restricted funds (note 7)		1,441,644	1,517,520
Depreciation and amortization		3,063	3,062
Income tax provision (note 4)		—	8,833
Other		237,598	257,987
Total expenses		61,109,507	57,904,681
Net loss before other changes		(3,601,120)	(1,090,470)
Other changes:			
Accretion of asset retirement obligation		(79,017)	(73,846)
Realized loss on available for sale investments		(285,861)	—
Unrealized gain from voting interest in Golden Rain Foundation of Laguna Woods		790,640	340,089
Loss from beneficial interest in Golden Rain Foundation of Laguna Hills Trust		(195,181)	(204,953)
Net loss	$	(3,370,539)	(1,029,180)

See accompanying notes to financial statements.

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Statements of Comprehensive Income (Loss)

Years ended December 31, 2019 and 2018

		2019	2018
Net loss	$	(3,370,539)	(1,029,180)
Other comprehensive loss:			
Unrealized gain (loss) on available-for-sale investments arising during the year		517,647	(213,731)
Comprehensive loss	$	(2,852,892)	(1,242,911)

See accompanying notes to financial statements.

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Statements of Changes in Members' Equity

Years ended December 31, 2019 and 2018

	Memberships				Total members'
	Number		Amount	Changes	equity
Members' equity, December 31, 2017 (note 5)	6,323	$	3,395,803	71,944,405	75,340,208
Net loss	—		—	(1,029,180)	(1,029,180)
Unrealized losses on available-for-sale investments, net	—		—	(213,731)	(213,731)
Members' equity, December 31, 2018 (note 5)	6,323		3,395,803	70,701,494	74,097,297
Net loss	—		—	(3,370,539)	(3,370,539)
Unrealized losses on available-for-sale investments, net	—		—	517,647	517,647
Members' equity, December 31, 2019 (note 5)	6,323	$	3,395,803	67,848,602	71,244,405

See accompanying notes to financial statements.

UNITED LAGUNA WOODS MUTUAL

Statements of Cash Flows

Years ended December 31, 2019 and 2018

		2019	2018
Cash flows from operating activities:			
Net loss	$	(3,370,539)	(1,029,180)
Adjustments to reconcile net loss to net cash used in operating activities:			
Unrealized gain from voting interest in Golden Rain Foundation of Laguna Woods		(790,640)	(340,089)
Loss from beneficial interest in Golden Rain Foundation of Laguna Hills Trust		195,181	204,953
Amortization of investment premium and discount, net		(349,346)	(17,838)
Depreciation and amortization		3,063	3,062
Accretion of asset retirement obligation		79,017	73,846
Changes in operating assets and liabilities:			
Accounts and accrued interest receivable		115,579	(462,642)
Receivable from Golden Rain Foundation of Laguna Woods		482,245	227,291
Payable for accrued compensation		(15,996)	(30,173)
Income taxes receivable		(1,808)	(17,753)
Income taxes payable		(12,474)	1,853
Deferred tax asset		—	(380,000)
Prepaid expenses		(589,068)	165,675
Accounts payable and accrued expenses		43,049	24,494
Assessments and charges paid in advance		(99,608)	103,069
Deferred income		62,341	55,000
Net cash used in operating activities		(4,249,004)	(1,418,432)
Cash flows from investing activities:			
Purchases of held-to-maturity investments		(13,914,378)	(10,904,319)
Maturities of held-to-maturity investments		16,873,614	14,895,920
Proceeds from payments and maturities of available-for-sale investments		19,207,346	3,379,799
Purchases of available-for-sale investments		(18,872,361)	(3,856,569)
Net cash provided by investing activities		3,294,221	3,514,831
Net (decrease) increase in cash and cash equivalents and restricted cash		(954,783)	2,096,399
Cash and cash equivalents and restricted cash, beginning of year		3,247,052	1,150,653
Cash and cash equivalents and restricted cash, end of year (note 2 (c))	$	2,292,269	3,247,052
Supplemental disclosure of cash flow information:			
Cash paid during the year:			
Income taxes	$	3,000	10,500

See accompanying notes to financial statements.

(1) Organization

(a) General

United Laguna Woods Mutual (the Mutual), a nonprofit mutual benefit corporation, was formed to own, manage, operate, and maintain 6,323 cooperative housing units (manors or common property) for the benefit of its members. The 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 7).

(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 2019 and 2018, the members were assessed monthly member assessments of $578.52 and $568.99, respectively, per manor per month, for direct and Mutual-shared operating costs, Mutual reserve contributions, and GRF-shared operating expenses and restricted funds. The basic monthly member assessment does not include the applicable share of property taxes and property insurance related to each manor.

Total amounts assessed to the members of the Mutual for direct and Mutual-shared operating costs, Mutual reserve contributions, property tax, property insurance costs, GRF-shared operating expenses, and restricted funds were $55,637,239 and $54,634,991, respectively, in 2019 and 2018.

(2) Significant Accounting Policies

(a) Basis of Presentation

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

(b) Comprehensive Income

Accounting Standards Codification (ASC) Topic 220, *Comprehensive Income*, establishes standards for the reporting and display of comprehensive income. Comprehensive income is defined as all changes in an entity's equity except changes resulting from transactions with owners. It differs from net income in which certain items currently recorded to equity would be part of comprehensive income. Changes in accumulated other comprehensive income were as follows for 2019 and 2018:

		Unrealized gain (loss) on securities, net
Ending balance, December 31, 2017	$	(291,801)
Other comprehensive loss		(213,731)
Ending balance, December 31, 2018		(505,532)
Other comprehensive loss		517,647
Ending balance, December 31, 2019	$	12,115

(c) 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. The total balance of cash and cash equivalents at December 1, 2019 and 2018 is $629,027 and $649,392, respectively, and included $132,387 and $51,142, respectively, of money market funds.

The table below provides a reconciliation of cash, cash equivalents, and restricted cash reported on the balance sheet that sum to the total of those same amounts shown in the statement of cash flows:

		2019	2018
Cash and cash equivalents	$	629,027	649,392
Restricted cash		1,663,242	2,597,660
	$	2,292,269	3,247,052

(d) Investments and Restricted Cash

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 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

(Continued)

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, 2019.

The Mutual restricts a portion of member assessments to finance reserves set aside and reported 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.

(e) Fair Value Measurements

The Mutual has adopted the provisions of ASC Topic 820, *Fair Value Measurement*, 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. Statement 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 between 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).

(f) Future Major Repairs and Replacements

A study was contracted by the Mutual in 2019 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 that fund. Under the assumption that certain buildings would not be completely replaced within the next 30 years, replacement funds are not provided for those corporate and 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 moneys are needed, the Mutual has the right to adjust the monthly assessment, impose special assessments, or delay expenditures as appropriate.

(g) Property

The Mutual has adopted the provisions of ASC Topic 972, Real Estate - Common Interest Realty Associations, and 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 is capitalized when the Mutual can dispose of the property, at the discretion of its board of directors and retain the proceeds or when the property is used to generate significant cash flows from members on the basis of usage or from nonmembers.

Depreciation of buildings and improvements is computed on the straight-line method over an estimated useful life of 40 years.

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(h) Impairment of Long-Lived Assets and Long-Lived Assets to be Disposed of

Long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the fair value of the assets. Assets to be disposed of are reported at the lower of the carrying amount or fair value, less costs to sell. During 2019 and 2018, there were no events or changes in circumstances indicating that the carrying amount of long-lived assets may not be recoverable.

(i) Interest in Golden Rain Foundation of Laguna Woods and Golden Rain Foundation of Laguna Hills Trust

The Mutual reports its 49.65% 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 $39,116,237 and $38,325,598 at December 31, 2019 and 2018, respectively.

The United Laguna Woods 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 totaled $5,796,949 and $5,992,130 at December 31, 2019 and 2018, respectively.

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

		2019	2018
Cash and cash equivalents	$	2,731,180	4,110,259
Receivables		1,445,309	1,543,311
Income tax receivable		46,377	45,407
Other current assets		2,483,748	1,870,881
Restricted funds and investments		21,895,591	23,869,568
Property and equipment, net		58,814,798	55,538,601
Community facilities, net		11,185,066	11,522,516
Intangible assets, net		235,982	282,184
Total assets	$	98,838,051	98,782,727
Accounts payable and accrued liabilities	$	6,019,484	5,971,734
Payables to Laguna Woods Mutuals		2,056,698	3,380,132
Deferred income		613,419	537,493
Total liabilities		8,689,601	9,889,359
Members' equity in Golden Rain Foundation of Laguna Woods		78,789,245	77,196,713
Noncontrolling interest in consolidated trust		11,359,205	11,696,655
Total equity		90,148,450	88,893,368
Total liabilities and equity	$	98,838,051	98,782,727
United Laguna Woods Mutual's 49.65% interest in Golden Rain Foundation of Laguna Woods	$	39,116,237	38,325,598

(j) 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, 2019 and 2018. The open years for federal and state tax assessments are 2016–2019 for federal and 2015-2019 for California.

(k) Concentration of Credit Risk

The Mutual had cash balances of $496,640 and $598,250 and restricted cash of $1,663,242 and $2,597,660 at December 31, 2019 and 2018, respectively, maintained in a commercial bank and consisting of cash on deposit. At December 31, 2019 and 2018, 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 $132,387 and $51,142 at December 31, 2019 and 2018, that were Securities Investor Protection Corporation insured up to a maximum of $500,000, per institution.

(l) Asset Retirement Obligations

Under ASC Topic 410, *Asset Retirement Obligations*, companies must accrue for costs related to legal obligations to perform certain activities in connection with the retirement, disposal, or abandonment of assets. The obligation to perform the asset retirement activity is not conditional even though the timing or method may be conditional. The Mutual identified future asbestos abatement activities as a conditional asset retirement obligation. Asbestos abatement activities were estimated based upon historical removal costs per square foot applied to assets identified requiring asbestos abatement. ASC 410 requires that the estimate be recorded as a liability and as an increase to the recorded historical cost of the asset. The capitalized portion, if any, is depreciated over the remaining useful life of the asset. The present values of the asset retirement obligations totaled $1,207,814 and $1,128,798 utilizing a rate of 7% as of December 31, 2019 and 2018, respectively. The liability will continue to be accreted to expense until such point that the remediation costs are required (note 9).

(m) Recent Accounting Pronouncements

On January 1, 2019 the Mutual adopted ASU 2014-09 Revenue from Contracts with Customers (Topic 606), during the year ended December 31, 2019. This guidance requires an entity to recognize revenue to depict the transfer of promised goods and services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The Mutual's revenue is derived primarily from assessments billed to residents. Assessments are recognized as revenue over the course of the year in the month for which they are earned. The adoption of ASU 2014-09 did not result in a material change to the timing of when revenue is recognized.

On January 1, 2019, the Mutual adopted ASU 2016-01, Financial Instruments-Overall: *Recognition and Measurement of Financial Assets and Financial Liabilities*. This guidance addresses certain aspects of recognition, measurement, presentation, and disclosure of financial instruments including presentation of unrealized gains and losses associated with available-for-sale equity securities within the statement of operations instead of other comprehensive income. The adoption of ASU 2016-01 did not have a material impact on the Mutual's financial statements and disclosures.

On January 1, 2019, the Mutual adopted ASU No. 2016-18, Statement of Cash Flows – Restricted Cash, which requires that a statement of cash flows explain the change during the period in the total of cash, cash equivalents, and restricted cash or restricted cash equivalents. The Mutual applied a retrospective transition method to each period presented.

(n) 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 revenue and expenses during the reporting period. Actual results could differ from those estimates.

(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, 2019 and 2018:

	2019	2018
Restricted cash and cash equivalents	$ 1,663,242	2,597,660
Restricted investments:		
Available for sale (at fair value):		
Index Funds	14,695,657	—
U.S. Treasury Notes	—	6,940,965
Governmental National Mortgage Association securities (GNMAs)	—	4,238,171
Corporate bonds	—	2,969,285
Total restricted investments at fair value	14,695,657	14,148,421
Held to maturity (at amortized cost):		
U.S. Treasury Notes	1,992,808	4,967,272
Total restricted investments at amortized cost	1,992,808	4,967,272
Total restricted cash and restricted investments	$ 18,351,707	21,713,353

The Mutual follows the provisions of ASC Topic 820 for fair value measurements for financial assets and liabilities 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.

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, 2019 and 2018 are as follows:

		2019		
		Level 1	**Level 2**	**Total**
Cash and cash equivalents	$	629,027	—	629,027
Investments and restricted cash:				
Restricted cash		1,663,242	—	1,663,242
Available for sale:				
Index Funds		14,695,657	—	14,695,657
Total investments and restricted cash		16,358,899	—	16,358,899
Total cash and cash equivalents, and investments and restricted cash	$	16,987,926	—	16,987,926

		2018		
		Level 1	**Level 2**	**Total**
Cash and cash equivalents	$	649,392	—	649,392
Investments and restricted cash:				
Restricted cash		2,597,660	—	2,597,660
Available for sale:				
U.S. Treasury notes		6,940,965	—	6,940,965
GNMAs		—	4,238,171	4,238,171
Corporate bonds		—	2,969,285	2,969,285
Total investments and restricted cash		9,538,625	7,207,456	16,746,081
Total cash and cash equivalents, and investments and restricted cash	$	10,188,017	7,207,456	17,395,473

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, GNMAs, and corporate bonds to a portfolio of index funds. In December 2019 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 $14,695,657 at December 31, 2019.

Investments held to maturity comprise U.S. Treasury notes, totaling $1,992,808 and $4,967,272, respectively, and are carried at cost at December 31, 2019 and 2018. Fair value of such investments total $1,992,808 and $4,968,396 as of December 31, 2019 and 2018, respectively, and would be considered Level 2 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:

	Purchase / Amortized cost	Gross unrealized gains	Gross unrealized losses	Estimated fair value
At December 31, 2019:				
Available for sale	14,683,539	12,118	—	14,695,657
Held to maturity	1,992,808	—	—	1,992,808

		Purchase / Amortized cost	Gross unrealized gains	Gross unrealized losses	Estimated fair value
At December 31, 2018:					
Available for sale	$	14,653,489	184,315	(689,383)	14,148,421
Held to maturity		4,967,272	1,124	—	4,968,396

Due to the December 2019 conversion of individual holdings of U.S. Treasury notes, GNMAs, and corporate bonds to a Bond index mutual fund portfolio, the 2019 unrealized gain on available-for sale investment balance of $219,671 was offset by the 2018 unrealized loss on available-for-sale investment of $505,532. The result of the conversion was the Mutual had a net realized loss on available-for-sale investments of $285,861 in 2019.

The Mutual determines realized gains and losses based on the specific-identification method. In 2019 realized gains and realized losses were as follows in 2019 and 2018:

Available for sale		2019	2018
Realized gain	$	101,075	-
Realized (loss)		(386,936)	-
Realized (loss) available for sale, net	$	(285,861)	-

(Continued)

Restricted cash and investments consist of the following reserve and contingency funds:

		Replacement funds	Contingency fund	Total
Balances, December 31, 2017	$	19,285,690	3,146,840	22,432,530
Member assessments		10,850,268	1,062,264	11,912,532
Net investment income and other contributions		305,936	48,051	353,987
Expenditures		(11,389,551)	(1,596,145)	(12,985,696)
Balances, December 31, 2018		19,052,343	2,661,010	21,713,353
Member assessments		11,229,648	1,138,140	12,367,788
Net investment income and other contributions		104,125	21,257	125,382
Expenditures		(13,129,903)	(2,724,913)	(15,854,816)
Balances, December 31, 2019	$	17,256,213	1,095,494	18,351,707

(a) Replacement Reserve Funds

Replacement funds were established in amounts deemed prudent by the board of directors. Such funds are to be used for replacement of equipment and structural elements of the mutual property. Monthly member assessments for the replacement funds were included in restricted funds member assessments in the accompanying statements of operations.

(b) Contingency Fund

The contingency fund was established in the 2009 business plan as a consolidation of two other reserves, the general operating fund and the unappropriated expenditures fund. This fund is used for the repair or replacement of mutual assets damaged by uninsured or unexpected disasters in addition to providing for unanticipated significant expenditures not otherwise identified in the business plan. Monthly member assessments for the contingency fund were included in restricted funds member assessments in the accompanying statements of operations.

(4) Income Taxes

The Mutual is a cooperative housing association taxable as a regular corporation for income tax purposes. The (benefit)/provision for income taxes for the years ended December 31, 2019 and 2018 consists of the following:

		2019	2018
Federal taxes:			
Current	$	(14,930)	5,980
State taxes:			
Current		999	2,853
Total	$	(13,931)	8,833

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and deferred tax liabilities at December 31, 2019 and 2018 are presented below:

		2019	2,018
Deferred tax assets:			
IRC Section 277 loss carryforwards	$	4,395,355	4,395,356
Federal and state net operating losses		2,198,947	1,259,712
Total gross deferred tax assets		6,594,302	5,655,068
Less valuation allowance		(6,214,302)	(5,275,068)
Net deferred tax assets	$	380,000	380,000

The Mutual recognizes a deferred tax asset for the expected future tax consequences from net operating loss carryovers. The tax benefit is recorded as an asset when the benefits are more likely than not to be recognized. A valuation allowance is required to be recorded when it is more-likely-than-not that all or a portion of deferred tax assets may not be realized. A review of all available positive and negative evidence is considered, including past and future performance, the market environment in which the Mutual operates, and utilization of tax attributes in the past, length of carryforward periods, and potential utilization in the future. In prior years a full valuation allowance was assessed against the Patronage net operating loss carryovers.

The valuation allowance for deferred tax assets as of December 31, 2019 and 2018 was $6,214,302 and $5,275,068. The net change in the total valuation allowance for the years ended December 31, 2019 and 2018 was an increase (decrease) of $939,235 and ($3,525,750), respectively. Based upon the level of historical taxable income and projections for future taxable income over the periods in which the deferred tax assets are deductible, management believes it is more likely than not that the Mutual will realize some of the benefits of these deductible differences. As such, the Mutual recorded a partial valuation allowance against the deferred tax assets at December 31, 2019 and 2018, respectively.

At December 31, 2019 and 2018, the Mutual has member loss carryforwards pursuant to Internal Revenue Code Section 277 of $20,930,264 and $20,930,264, respectively, available to offset future net member income. These carryforward amounts have no expiration dates.

At December 31, 2019 and 2018, the Mutual had net operating loss carryforwards pursuant to Internal Revenue Code Section 382 of $10,471,176 and $5,998,627, respectively. These carryforwards expire in 2033 to 2035.

Income tax expense was computed by applying the U.S. federal income tax rate of 21% for both December 31, 2019 and 2018.

(5) Original Contributions to Members' Equity

The Mutual has 6,323 memberships authorized and issued, recorded at various initial capital values, ranging from $302 to $1,770 per membership. These contributions were required by the Mutual to cover the costs of acquiring its properties in excess of the funds obtained from trust deed notes, to pay the permanent finance fee, and to provide the Mutual with working capital.

(6) 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.

(7) 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.

(8) Pension Plans

Village Management Services 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 that 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 2019 and 2018, VMS sponsored a 401(k) plan covering all eligible employees. Employee contributions to the plan are at the participants' discretion. In 2019 and 2018, 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 2019 and 2018 and reimbursed by the Mutual were $376,433 and $325,638 for the defined-benefit pension plan and $51,767 and $57,623, respectively, for the 401(k) plan.

(9) Asset Retirement Obligation

The following schedule summarizes asset retirement obligation activities for the years ended December 31, 2019 and 2018:

		2019	2018
Beginning balance	$	1,128,798	1,054,952
Accretion expense		79,016	73,846
Ending balance	$	1,207,814	1,128,798

(10) Subsequent Events

Subsequent events have been evaluated through April 5, 2020, which is the date the financial statements were available to be issued.

SUPPLEMENTARY INFORMATION

UNITED LAGUNA WOODS MUTUAL

Future Major Repairs and Replacements

December 31, 2019

(Unaudited)

The Mutual contracted a study in 2019 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 operating funds. The estimates were determined from past experience and from information obtained from certain contractors.

Major components	Estimated useful lives (in years)	Estimated remaining useful lives (in years)	Estimated current replacement costs	Estimated funding requirement as of December 31, 2019
Concreate Repairs and Replacement	1	0	$ 150,000	150,000
CDS Asphalt Seal Coat	1	0	50,500	50,500
CDS Asphalt Resurface/Repairs and Replacement	25	0 to 24	6,779,350	3,767,898
Roofs – Built-Up	25	0 to 24	18,661,000	7,632,400
Roofs – Comp Shingle	40	3 to 33	12,518,000	4,293,200
Roofs – Tile	40	24 to 34	3,638,000	975,450
Infrastructure/Buildings	1 to 30	0 to 10	2,665,400	2,181,310
Carport Siding Renovation	35	12 to 22	1,412,700	736,654
Manor Components	0 to 1	0 to 10	5,384,000	3,349,000
Lighting & Electrical	1 to 20	0 to 12	1,601,000	1,229,875
Laundry Rooms	1 to 25	0 to 10	463,900	338,800
Prior to Painting	1 to 10	0 to 9	6,694,100	3,917,090
Interior & exterior Painting	1 to 10	0 to 9	16,935,500	9,537,460
Walls, Fencing, Railing & Gates	1	0	190,900	190,900
Grounds & Miscellaneous	1 to 15	0 to 13	3,212,450	2,140,333
Contingency Components	1	0	1,173,100	1,173,100
Plumbing	1	0 to 10	1,602,000	1,552,000
			$ 83,131,900	43,215,970

Replacement funds balance as of December 31, 2019 (note 3) $ 17,256,213

The Board voted to contribute $11,229,648 to the replacement funds in 2019. The contribution is included in the 2019 member assessments at $148 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 will be sufficient at the end of year to meet the Mutual's obligations for repair and/or replacement of major components during the next 30 years.

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

See accompanying independent auditors' report.