

**GOLDKLANG, CAVANAUGH & ASSOCIATES, P.C.**  
CERTIFIED PUBLIC ACCOUNTANTS

**VIRGINIA AND  
ADMINISTRATIVE OFFICES**  
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**MEMBERS OF  
AMERICAN INSTITUTE OF CPAS**

**MARYLAND OFFICE**  
1700 ROCKVILLE PIKE  
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Independent Auditor's Report

Board of Directors  
Hampshire Greens Homeowners Association, Inc.  
Silver Spring, Maryland

We have audited the accompanying Balance Sheets of Hampshire Greens Homeowners Association, Inc. as of December 31, 2006 and 2005, the related Statements of Income, Members' Equity and Cash Flows for the years then ended. These financial statements are the responsibility of the Association. 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 audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by the Association as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the statements referred to above present fairly, in all material respects, the financial positions of Hampshire Greens Homeowners Association, Inc. as of December 31, 2006 and 2005 and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The supplementary information on future repairs and replacements on page 9 is not a required part of the basic financial statements of Hampshire Greens Homeowners Association, Inc., but is supplementary information required by the American Institute of Certified Public Accountants. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

*Goldklang, Cavanaugh & Associates, P.C.*

September 10, 2007

HAMPSHIRE GREENS HOMEOWNERS ASSOCIATION, INC.

BALANCE SHEETS

DECEMBER 31, 2006 AND 2005

	<u>2006</u>	<u>2005</u>
<u>ASSETS</u>		
Cash and Cash Equivalents	\$ 110,234	\$ 97,292
Interest - Bearing Deposits	67,532	67,030
Assessments Receivable - Net	1,358	1,452
Accounts Receivable - Other	-	106
Accrued Interest	48	-
Prepaid Expenses	942	752
Utility Deposit	<u>65</u>	<u>65</u>
 Total Assets	 <u>\$ 180,179</u>	 <u>\$ 166,697</u>

LIABILITIES AND MEMBERS' EQUITY

Accounts Payable	\$ 3,974	\$ 6,063
Income Taxes Payable	541	-
Prepaid Assessments	<u>4,343</u>	<u>9,862</u>
Total Liabilities	<u>\$ 8,858</u>	<u>\$ 15,925</u>
 Initial Working Capital	 \$ -	 \$ 17,844
Replacement Reserves	121,987	44,758
Unappropriated Members' Equity	<u>49,334</u>	<u>88,170</u>
Total Members' Equity	<u>\$ 171,321</u>	<u>\$ 150,772</u>
 Total Liabilities and Members' Equity	 <u>\$ 180,179</u>	 <u>\$ 166,697</u>

See Accompanying Notes to Financial Statements

HAMPSHIRE GREENS HOMEOWNERS ASSOCIATION, INC.  
STATEMENTS OF INCOME  
FOR THE YEARS ENDED DECEMBER 31, 2006 AND 2005

	2006	2005
<u>INCOME:</u>		
Assessments	\$ 181,896	\$ 170,440
Late and Legal Fees	3,113	2,648
Interest	3,710	1,913
Bad Debt Recovery	-	5,096
Other	2,658	790
Total Income	\$ 191,377	\$ 180,887
 <u>EXPENSES:</u>		
Management	\$ 24,191	\$ 25,640
Audit and Tax Preparation	1,625	1,625
Legal	7,384	9,586
Reserve Study	2,600	-
Insurance	5,538	4,506
Social Committees	1,002	675
Postage and Printing	5,029	2,854
Administrative	3,057	3,002
Electricity	645	484
Water and Sewer	553	1,319
Trash Removal	17,613	17,100
Snow Removal	1,280	6,775
Landscaping	88,967	89,305
Common Area Maintenance	1,787	5,359
Bad Debt	348	-
Income Taxes	701	54
Total Expenses	\$ 162,320	\$ 168,284
Net Income before Contribution to Reserves	\$ 29,057	\$ 12,603
Contribution to Reserves	(7,620)	(7,620)
Net Income	\$ 21,437	\$ 4,983

See Accompanying Notes to Financial Statements

HAMPSHIRE GREENS HOMEOWNERS ASSOCIATION, INC.  
STATEMENTS OF MEMBERS' EQUITY  
FOR THE YEARS ENDED DECEMBER 31, 2006 AND 2005

	Initial Working Capital	Replacement Reserves	Unappropriated Members' Equity	Total Members' Equity
Balance as of December 31, 2004	\$ 17,844	\$ 42,939	\$ 83,187	\$ 143,970
Additions:				
Contribution to Reserves		7,620		7,620
Net Income			4,983	4,983
Deduction:				
Tennis Court		(5,801)		(5,801)
Balance as of December 31, 2005	\$ 17,844	\$ 44,758	\$ 88,170	\$ 150,772
Additions:				
Contribution to Reserves		7,620		7,620
Net Income			21,437	21,437
Inter-Equity Transfer	(17,844)	78,117	(60,273)	
Deduction:				
Park Bench and Trash Cans		(8,508)		(8,508)
Balance as of December 31, 2006	\$ -	\$ 121,987	\$ 49,334	\$ 171,321

See Accompanying Notes to Financial Statements

HAMPSHIRE GREENS HOMEOWNERS ASSOCIATION, INC.  
STATEMENTS OF CASH FLOWS  
FOR THE YEARS ENDED DECEMBER 31, 2006 AND 2005

	<u>2006</u>	<u>2005</u>
<u>CASH FLOWS FROM OPERATING ACTIVITIES:</u>		
Net Income	\$ 21,437	\$ 4,983
Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities:		
Decrease (Increase) in:		
Assessments Receivable - Net	94	(1,108)
Accounts Receivable - Other	106	194
Accrued Interest	(48)	-
Prepaid Expenses	(190)	(63)
Increase (Decrease) in:		
Accounts Payable	(2,089)	2,054
Income Taxes Payable	541	-
Prepaid Assessments	(5,519)	(10,946)
Net Cash Flows from Operating Activities	<u>\$ 14,332</u>	<u>\$ (4,886)</u>
<u>CASH FLOWS FROM INVESTING ACTIVITIES:</u>		
Received from Assessments (Reserves)	\$ 7,620	\$ 7,620
Received from Interest - Bearing Deposits	-	26,277
Disbursed for Interest - Bearing Deposits	(502)	(76,637)
Disbursed for Reserve Expenditures	(8,508)	(5,801)
Net Cash Flows From Investing Activities	<u>\$ (1,390)</u>	<u>\$ (48,541)</u>
Net Change in Cash and Cash Equivalents	\$ 12,942	\$ (53,427)
Cash and Cash Equivalents at Beginning of Year	<u>97,292</u>	<u>150,719</u>
Cash and Cash Equivalents at End of Year	<u>\$ 110,234</u>	<u>\$ 97,292</u>

SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:

Cash Paid for Income Taxes	<u>\$ 160</u>	<u>\$ 160</u>
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See Accompanying Notes to Financial Statements

HAMPSHIRE GREENS HOMEOWNERS ASSOCIATION, INC.  
NOTES TO FINANCIAL STATEMENTS  
DECEMBER 31, 2006 AND 2005

NOTE 1 - NATURE OF OPERATIONS:

The Association is organized under the laws of the State of Maryland for the purposes of maintaining and preserving the common property of the community. The Association is located in Silver Spring, Maryland and consists of 286 homes. The Association administers the operations of the community.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES:

A) Method of Accounting - The financial statements are presented on the accrual method of accounting in which revenues are recognized when earned and expenses recognized when incurred, not necessarily when received or paid.

B) Member Assessments - Association members are subject to monthly assessments to provide funds for the Association's operating expenses, future capital acquisitions, and major repairs and replacements. Assessments receivable at the balance sheet date represent fees due from homeowners. The Association's policy is to retain legal counsel and place liens on the properties of owners whose assessments are delinquent. Any excess assessments at year end are retained by the Association for use in future years. The Association utilizes the allowance method of accounting for bad debt.

C) Common Property - Real property and common areas acquired from the developer and related improvements to such property are not recorded in the Association's financial statements since the property cannot be disposed of at the discretion of the Board of Directors. Common property includes, but is not limited to, land and site improvements.

D) Estimates - The preparation of financial statements, in conformity with generally accepted accounting principles, requires management to make estimates and assumptions. Such estimates affect the reported amounts of assets and liabilities. They also affect the 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.

E) Cash Equivalents - For purposes of the statement of cash flows, the Association considers all highly liquid investments and interest-bearing deposits with an original maturity date of three months or less to be cash equivalents.

F) Reclassification - Certain amounts have been reclassified in the accompanying 2005 financial statements to conform to the 2006 presentation.

HAMPSHIRE GREENS HOMEOWNERS ASSOCIATION, INC.  
NOTES TO FINANCIAL STATEMENTS  
DECEMBER 31, 2006 AND 2005  
(CONTINUED)

NOTE 3 - REPLACEMENT RESERVES:

The Association's governing documents require that funds be accumulated for future major repairs and replacements. Accumulated funds held are generally not available for expenditures for normal operations.

The Association had a replacement reserve study conducted by an engineer during 2006 and utilizes the cash flow method of funding for replacement reserves. The table included in the Supplementary Information on Future Major Repairs and Replacements is based on this study.

The Association is funding for future major repairs and replacements over the remaining useful lives of the components based on the study's estimates of the replacement costs and considering amounts previously accumulated in the replacement reserves. Accordingly, the funding recommendation of \$7,620 (approximately \$2 per home per month) has been included in the 2006 financial statements. The Association also elected to transfer \$60,273 from unappropriated members' equity and \$17,844 from initial working capital to replacement reserves.

Funds are being accumulated in replacement reserves based on estimates. Actual expenditures may vary from the estimated future expenditures and the variations may be material; therefore, amounts accumulated in the replacement reserves may or may not be adequate to meet all future needs for major repairs and replacements. If additional funds are needed, the Board of Directors, on behalf of the Association, may increase regular assessments, pass special assessments or delay major repairs and replacements until funds are available.

As of December 31, 2006 and 2005, the Association had designated \$121,987 and \$44,758, respectively, for replacement reserves. These designated reserves were funded by cash and interest-bearing deposits.

NOTE 4 - INCOME TAXES:

For income tax purposes, the Association may elect annually to file either as an exempt homeowners association or as an association taxable as a corporation. As an exempt homeowners association, the Association's net assessment income would be exempt from income tax, but its interest income would be taxed. Electing to file as a corporation, the Association is taxed on its net income from all sources (to the extent not capitalized or deferred) at normal corporate rates after corporate exemption, subject to the limitation that operating expenses are deductible only to the extent of income from members. For 2006 and 2005, the Association's income taxes were calculated using the exempt method.

HAMPSHIRE GREENS HOMEOWNERS ASSOCIATION, INC.  
NOTES TO FINANCIAL STATEMENTS  
DECEMBER 31, 2006 AND 2005  
(CONTINUED)

NOTE 5 - INITIAL WORKING CAPITAL:

At settlement, each original purchaser is required to contribute two months assessments toward a working capital fund. The contributions provide operating funds during the Association's initial start-up period. During 2006, the Association elected to transfer \$17,844 of initial working capital to replacement reserves.

NOTE 6 - CASH AND INTEREST-BEARING DEPOSITS:

As of December 31, 2006, the Association maintained its funds in the following manner:

<u>Institution</u>	<u>Type Account</u>	<u>Cash and Cash Equivalents</u>	<u>Interest- Bearing Deposits</u>	<u>Total</u>
Sandy Spring	Checking	\$ 48,940	\$ -	\$ 48,940
Federated	Money Market	61,294		61,294
Financial Federal	Certificate of Deposit		25,030	25,030
New South	Certificate of Deposit		25,000	25,000
Chevy Chase	Certificates of Deposit (2)		17,502	17,502
		<u>\$ 110,234</u>	<u>\$ 67,532</u>	<u>\$ 177,766</u>

NOTE 7 - ASSESSMENTS RECEIVABLE - NET:

The Association utilizes the allowance method of accounting for bad debt. Individual receivables are written off as a loss when a determination is made that they are uncollectible. Under the allowance method, collection efforts may continue and recovery of amounts previously written off are recognized as income in the year of collection.

	<u>2006</u>	<u>2005</u>
Assessments Receivable	\$ 3,275	\$ 3,021
Less: Allowance for Doubtful Assessments	<u>(1,917)</u>	<u>(1,569)</u>
Assessments Receivable - Net	<u>\$ 1,358</u>	<u>\$ 1,452</u>

NOTE 8 - UTILITY DEPOSIT:

The Association maintains a deposit with PEPCO in the amount of \$65. The deposit will be refundable in 2007.



HAMPSHIRE GREENS HOMEOWNERS ASSOCIATION, INC.  
SUPPLEMENTARY INFORMATION ON FUTURE MAJOR  
REPAIRS AND REPLACEMENT  
DECEMBER 31, 2006  
(UNAUDITED)

The Association had a replacement reserve study conducted by an engineer during 2006 to estimate the remaining useful lives and the replacement costs of the components of common property. The Association utilizes on the cash flow method of funding for replacement reserves. Replacement costs were based on the estimated costs to repair or replace the common property components at the date of the study. Estimated replacement costs do not take into account the effects of inflation between the date of the study and the date the components will require repair or replacement.

The following has been extracted from the Association's replacement reserve study and presents significant information about the components of common property.

<u>Component</u>	<u>2006 Estimated Remaining Useful Life (Years)</u>	<u>2006 Estimated Replacement Cost</u>
Asphalt Pathways	3-8	\$ 40,648
Retaining Walls	2-32	8,580
Tennis Court	5-20	59,570
Tot Lots	4-16	84,962
Gazebo	12	7,500
Bench	1-8	16,000
Trash Cans	1-8	7,200
Picnic Tables	1-8	16,587

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July 9, 2007

Board of Directors  
Hampshire Greens Homeowners Association, Inc.  
Silver Spring, Maryland

Dear Board Members:

In connection with our examination of the financial statements of Hampshire Greens Homeowners Association, Inc. for the year ended December 31, 2006, we make the following comments and recommendations.

#### Small Delinquent and Prepaid Assessment Balances

As of December 31, 2006, several owner accounts had balances less than ten dollars. Additionally, several other owner balances above ten dollars have been carried forward from year to year. We recommend the receivable amounts be reviewed and, if appropriate, written off. The Association should consider turning over any prepaid balances, especially prepaid balances from previous owners to the state as unclaimed property. Maintaining accounts with such small balances can create administrative and bookkeeping problems.

#### Water and Sewer Expense

The Association has shared water and sewer expense with the Montgomery County Revenue Authority. For 2006, Montgomery County Revenue Authority did not bill the Association. Management has contacted Montgomery County Revenue Authority regarding this matter. An estimate of \$554 has been recorded as an accounts payable based on 2005 water and sewer expense.

#### Employee Dishonesty Policy

We recommend the Association continue to review its insurance policies annually to ensure adequate coverage. The Association should maintain crime coverage that equals or exceeds the total of its accounts. It should be structured to include a defalcation or misappropriation committed by a Board member or the management company, including principals. As of December 31, 2006, the Association maintained employee dishonesty coverage of \$50,000, which did not fully cover the Association's cash and interest-bearing deposits of \$177,766. We recommend the Association obtain coverage to include its funds and the parties listed above.

#### Income Taxes

For 2006, we recommend the Association file using the exempt method.

We shall be pleased to discuss our comments and recommendations in greater detail and we are always available to give advice on any financial matter. Please do not hesitate to contact us if there are any questions regarding proper accounting procedures or the implementation of our suggested changes.

Very truly yours,

  
GOLDKLANG, CAVANAUGH & ASSOCIATES, P.C.

(This letter is intended solely for the use of management and the Board of Directors.)

**GOLDKLANG, CAVANAUGH & ASSOCIATES, P.C.**  
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July 9, 2007

Board of Directors  
Hampshire Greens Homeowners Association, Inc.  
Silver Spring, Maryland

Dear Board Members:

In planning and performing our audit of the financial statements of Hampshire Greens Homeowners Association, Inc. as of December 31, 2006 and for the year then ended, in accordance with auditing standards generally accepted in the United States of America, we considered the Association's internal control over financial reporting (internal control) as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Association's internal control. Accordingly, we do not express an opinion on the effectiveness of the Association's internal control.

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

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

Modified Accrual Basis

The Association's books are maintained on a modified accrual basis of accounting throughout the year. We have proposed several adjustments to present the financial statements on the accrual basis of accounting.

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

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

Very truly yours,

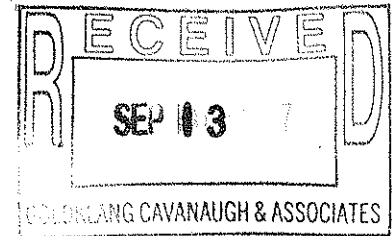
A handwritten signature in cursive script that reads "Goldklang, Cavanaugh & Associates, P.C.".

GOLDKLANG, CAVANAUGH & ASSOCIATES, P.C.

# Hampshire Greens Homeowners Association, Inc.

Date SEP 13 2007

GOLDKLANG, CAVANAUGH & ASSOCIATES, P.C.  
1801 Robert Fulton Drive, Suite 200  
Reston, Virginia 20191



Dear Auditors:

We are providing this letter in connection with your audits of the financial statements of **Hampshire Greens Homeowners Association, Inc.** as of **December 31, 2006 and 2005**, and for the years then ended, for the purpose of expressing an opinion as to whether the financial statements present fairly, in all material respects, the financial position, and results of operations and cash flows, in conformity with accounting principles generally accepted in the United States of America. We confirm that we are responsible for the fair presentation in the financial statements of financial position, results of operations, and cash flows in conformity with accounting principles generally accepted in the United States of America. We are also responsible for adopting sound accounting policies, establishing and maintaining internal control, and preventing and detecting fraud.

We confirm, to the best of our knowledge and belief, the following representations made to you during your audits:

1. The financial statements referred to above are fairly presented in conformity with accounting principles generally accepted in the United States of America. Because of our limited expertise with generally accepted accounting principles, including financial statement disclosure, we have engaged you to advise us in fulfilling this responsibility.
2. We are responsible for the fair presentation of the supplemental information accompanying the financial statements about future major repairs and replacements.
3. We have made available to you all –
  - A) Financial records and related data.
  - B) Minutes of meetings of the Board of Directors.
4. There have been no communications from regulatory agencies concerning noncompliance with, or deficiencies in, financial reporting practices.
5. There are no material transactions that have not been properly recorded in accounting records underlying the financial statements.
6. We are in agreement with the adjusting journal entries you have recommended, and they have been posted to the Association's accounts, if appropriate.
7. We acknowledge our responsibility for the design and implementation of programs and controls to prevent and detect fraud.
8. We have no knowledge of any fraud or suspected fraud affecting the Association involving:
  - A) management,
  - B) employees who have significant roles in internal control, or

(51)

- C) others where the fraud could have a material effect on the financial statements.
9. We have no knowledge of any allegations of fraud or suspected fraud affecting the Association received in communications from employees, former employees, owners, regulators, or others.
  10. The Association has no undisclosed plans or intentions that may materially affect the carrying value or classification of assets and liabilities.
  11. The following have been properly recorded or disclosed in the financial statements –
    - A) Related party transactions and related accounts receivable or payable, including sales, purchases, loans, transfers, leasing arrangement, and guarantees.
    - B) Guarantees, whether written or oral, under which the Association is contingently liable.
  12. There are no estimates that may be subject to a material change in the near term that have not been properly disclosed in the financial statements. We understand that near term means the period within one year of the date of the financial statements. In addition, we have no knowledge of concentrations existing at the date of the financial statements that make the Association vulnerable to the risk of severe impact that have not been properly disclosed in the financial statements. We understand that concentrations include individual or group concentrations of sources of labor, services, suppliers or lenders. We further understand that severe impact means a significantly financially disruptive effect on the normal functioning of the Association.
  13. There are no -
    - A) Violations or possible violations of laws or regulations whose effects should be considered for disclosure in the financial statements or as a basis for recording a loss contingency.
    - B) Pending or threatened litigation, claims or unasserted claims that are required to be accrued or disclosed in the financial statements in accordance with Statement of Financial Accounting Standards No. 5, and we have not consulted a lawyer concerning litigation or claims.
    - C) Other liabilities or gain or loss contingencies that are required to be accrued or disclosed by Statement of Financial Accounting Standards No. 5.
  14. The Association has satisfactory title to all owned assets, and there are no liens or encumbrances on such assets nor has any asset been pledged, except as made known to you and disclosed in the notes to the financial statements.
  15. We have complied with all aspects of contractual agreements that would have a material effect on the financial statements in the event of noncompliance.
  16. The board of directors is collecting funds for future major repairs and replacements in conformity with the Association's policy to fund for those needs based on a study for the replacement reserve supplemental information conducted in 2006. The board of directors believes the funds will adequately provide for future major repairs and replacements.
  17. The Association's allocation of expenses against exempt and nonexempt function income conforms to IRS rules, which require that the allocation be made "on a reasonable basis."
  18. We understand that the Association is responsible for the choice of income tax filing method and the consequences thereof.

19. We have reviewed the transactions affecting replacement reserves (including inter-equity transfers). We are in agreement with them and they are properly authorized and approved.
20. Based on the advice of an insurance professional, insurance coverage is considered adequate for any anticipated property damage losses or liability claims.
21. Assessments receivable recorded in the financial statements represent valid claims against debtors for assessments or other charges arising on or before the balance sheet date and have been reduced to their estimated realizable value.
22. If we intend to print a portion of your report (not in its entirety), we will notify you in advance, and you will have the opportunity to review such printed material before its issuance.
23. We have disclosed to you all material events, if any, that would require adjustments to, or disclosure in, the financial statements. In addition, we represent that no other material events have occurred since you completed your audit fieldwork on May 15, 2007 and through the date of this letter. Examples of material events include, but are not limited to, contracts for replacement reserve expenditures, losses due to a fire, changes in ongoing litigation or new litigation and approval of special assessments. Material events that have occurred are:

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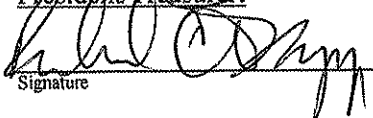
**Hampshire Greens Homeowners Association, Inc.**  
**December 31, 2006 and 2005**

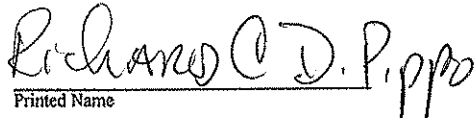
Management Representative:

  
 Signature

  
 Printed Name

President/Treasurer:

  
 Signature

  
 Printed Name

