HOA Accounting Cheat Sheet

For Basic Financial Statements

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HOA Accounting Cheat Sheet for Basic Financial Statements

Accounting in a homeowners association is an important, but often tedious task and usually something that Board members don't all jump up at once to help oversee. But, whether you like it or not, as a Board member you have the responsibility of understanding what the numbers mean to help guide the financial course of the Association.

When it comes to the budget HOA accounting can feel cumbersome to understand because you look at the financial statement and only see a mess of numbers. It can also seem like an overwhelming task because you just don't have a lot of accounting knowledge. When you hear the word "budget" you start to glaze over, intimidated by the conversation that follows. ***We understand that not everyone is a numbers person that has the head knowledge about HOA accounting, so we've put together a quick at-a-glance list of important terms you'll hear relating to the financial statement.*** *Take a moment to educate yourself and you won't have to worry about missing out on the conversation anymore.*

Financial Statements Can Be Prepared in 3 Different Ways:

1. Cash Method

A cash accounting method is simple: money in money out. Similar to your checking account system, it tracks when cash is received and when cash is paid out. When a deposit is made it's recorded as income. When a check is written it's recorded as an expense. The cash method is easy to understand and prepare, however it's not the ideal method to use because it doesn't pay attention to unpaid bills or uncollected HOA fees.

2. Accrual Method

An Accrual HOA accounting method is more accurate and required by the Davis-Stirling Act. It tracks all transactions in the month in which income is earned and the expense is incurred, regardless of whether the money has been received or the expense paid out. Any income, like HOA Fees, is recorded when it's due instead of when it's received. Expenses are recorded when they are performed. For example, if the Association purchased and installed a new piece of exercise equipment for the fitness center on March 31st, then it's added to the financial statement in March, even if it wasn't paid for until April.

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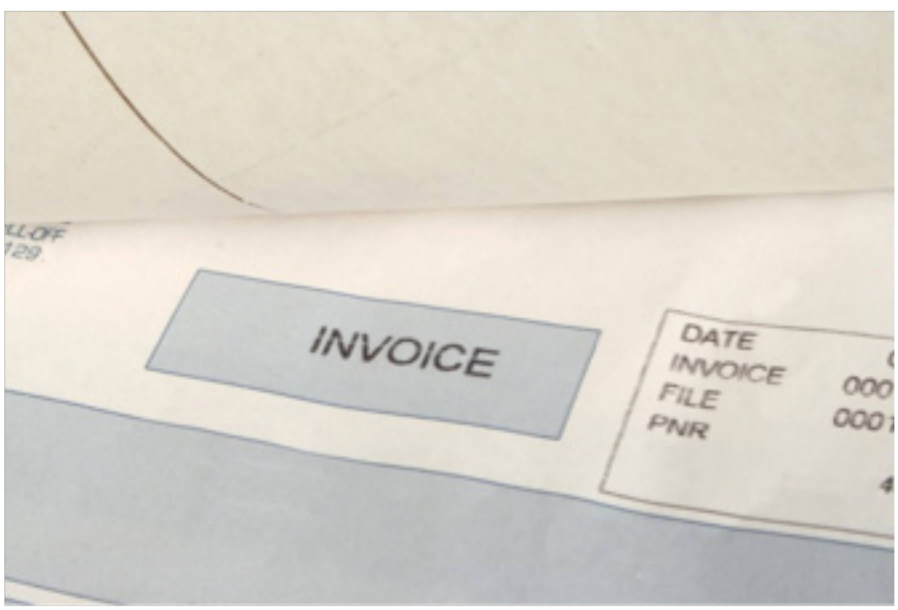
3. Modified Accrual Method

This is the most common HOA accounting method used during the year, with full accrual required at yearend. A modified accrual method is a combination of the cash and accrual methods. Some of the transactions made are recorded using the cash method, but some are also recorded using the accrual method. For example, any fees or fines that homeowners owe the Association are recorded when they are billed out (the accrual method). Expenses like regular landscape maintenance or pool cleaning, could be recorded when they are paid (the cash method), if not included in the open Accounts Payable at the end of the month in which the expense was actually incurred. The timing to close the interim monthly financial statements usually does not allow for waiting for late invoicing by vendors. Although a modified accrual method is less complex, a downfall is that it doesn't always accurately match all the income and expenses in the interim fiscal month being evaluated, thus distorting the true financial position of the entity.



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Financial Statements include two Basic Reports:

1. Balance Sheet

The balance sheet is like an accounting snapshot of the Association's financial status as of a certain date. It's made up of assets, liabilities and equity/fund balances. Fund Accounting required by the Davis-Stirling Act requires the segregation of the Operating Fund and the Reserve Fund for Major Repairs & Replacements.

2. Statement of Income and Expenses

The statement of income and expenses shows transactions for a certain period of time, like the month, quarter or yearly total. This statement closes at the end of each year fiscal year and then starts again with the new fiscal year. Again, Fund Accounting required by the Davis-Stirling Act requires the segregation of the Operating Fund and the Reserve Fund for Major Repairs & Replacements.

Financial Statements Will Refer To These Common Terms:

Assessments – The fees or dues charged to homeowners in the Association that are used for maintaining, preserving and managing the Association.

Assets – These are what the Association owns. They may show on the financial statement as cash, receivables in the form of fees and fines, prepayments, etc.; or they may show as capital goods like buildings, vehicles, or equipment the Association uses.

Chart of Accounts – This is the group of accounts used to segregate assets, liabilities, equity, income and expenses into categories to see easily see where money is owned, owed, coming in and how it's being spent.

Liabilities – These are what the Association owes, such as accounts payable, services or taxes. They aren't always included on the interim monthly or quarterly financial statements, but will appear as expenses on the yearly statement.

Operating Fund – This is the segregated fund used for the Association's day to day operations.

Reserve Fund – This is the segregated fund used for future major replacements and repairs of the common areas in the Association. The Reserve Fund Balance line item on the balance sheet usually indicates the amount the HOA has saved and earmarked for future expenditures.

Reserve Allocation – The amount of the assessment fees that is budgeted to put into the Reserve Fund.

Retained Earnings – This is the portion of equity or fund balances representing the cumulative earnings (excess of income over expenses) from prior years still held in the HOA.

Remember, it's always important to review the governing documents of your Association and State laws, especially when it comes to HOA accounting.

Whether you're a new Board member who is just beginning to understand the HOA accounting process, or a seasoned Board member who usually tunes out during discussions about the financial statement, we hope this information will help you become fully engaged in the financial decisions that are made for your Association.

Contact us today to see how we can help you and provide the professional resources your HOA accounting needs.

If your Board is in need of management assistance, The Hignell Companies currently manages over 40 associations and helps them with all of their accounting and reporting needs. With dedicated professionals at your side and over 30 years' experience working with boards and their members, you will sleep better at night knowing your accounting and reporting is correct and up to date.

Call us at (530) 419-6032

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