

Goldklang & Group[®]

CPAs, P.C.

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Associate Principals

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Sheila M. Lewis, CPA

Management Letter

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.

July 23, 2019

Board of Directors
Prosperity Heights Homeowners Association, Inc.

Dear Board Members:

In planning and performing our audit of the financial statements of Prosperity Heights Homeowners Association, Inc. as of June 30, 2018 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 auditing procedures that are appropriate in the circumstances 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.

However, during our audit, we became aware of matters that are opportunities for strengthening internal controls and improving operating efficiency. This letter summarizes our comments and suggestions regarding those matters.

Association Specific Comments

Financial Analysis

Associations budget their income evenly over a twelve-month period. When assessments become delinquent, cash flow problems develop and the Association may have problems paying its monthly expenses. Assessments receivable at a level of 3% or less of annual assessments indicates good collection procedures and has a positive impact on cash flow, whereas a balance of more than 3% of annual assessments suggests the Association may have future cash flow problems. As of June 30, 2018, the Association's assessments receivable balance of \$8,176 (before deducting the allowance for doubtful assessments of \$420) was equal to 9% of annual assessments. We recommend the Association continue to aggressively pursue all delinquent accounts.

As of June 30, 2018, the Association had a surplus of \$51,967 in unappropriated members' equity (excess operating funds). This represents 59% of annual assessments. We recommend the Association maintain excess operating funds at a level of 10% to 20% of annual assessments. Any funds in excess of 20% may be transferred to replacement reserves.

The designated replacement reserves of \$32,065 as of June 30, 2018 were funded by cash and interest-bearing deposits.

Year End

The Association's legal documents designated the operating year of the Association as the calendar year and empowered the Board to change the year end via a resolution. For 2018, the Association filed its tax returns on a calendar year basis. It appears that the Association used both a fiscal year end and a calendar year end for its budget. We performed the audit on a fiscal year end basis. We recommend the Association consider choosing either a fiscal or calendar year so that the tax returns, budgets, and audit(s) are consistent.

Filing of 1099 Forms

The Association should file a 1099 Form as required by the IRS for any individual paid more than \$600 for services in each calendar year. From July 2018 through December 2018, the Association paid \$650 for labor for mulching, but we did not see a 1099-Misc in the Association's records. We recommend the Association comply with 1099 filing requirements.

Contracts

The Association's landscaping and trash contracts are outdated. We recommend the Association obtain new contracts with the vendors that detail the terms of service, monthly fee, and annual price increases.

Authorized Signers

The Association appears to have only one authorized signer on its bank accounts. We recommend the Association consider adding a second authorized signer on its bank accounts.

Industry Standard Comments

Insurance

We recommend the Association meet with its insurance agent at least annually to discuss insurance coverage. The Association should make sure the insurance policies provide the necessary and appropriate protection. In addition to all of the standard coverage that is usually recommended, the Association should maintain appropriate crime and directors & officers (D&O) coverage. At a minimum, the Association should maintain crime coverage that equals or exceeds the total of its funds or as required by state law. It should be structured to include a defalcation or misappropriation committed by a Board member, an employee of the Association, or employees of the management company, including principals.

Investment Policy

The Association should have a conservative investment policy, which is structured around three elements, in order of importance 1) safety, 2) liquidity and 3) yield. Because safety and liquidity are

of prime importance to any association, we recommend investments be limited to instruments of the federal government, which are backed by its full faith and credit, and money market accounts and certificates of deposit at insured institutions.

Periodically, the Association should monitor its accounts for FDIC and SIPC coverage. The FDIC insurance limit is \$250,000 per financial institution. Cash and securities held at a SIPC member brokerage firm are insured by the SIPC for up to \$500,000, which includes \$250,000 limit for cash. The Association should also periodically check the ratings for all financial institutions used by the Association.

Monitoring Activities

The Board of Directors is an integral part of the Association's internal controls. Each month the individual board members should be performing monitoring activities. When performed routinely, these monitoring activities strengthen the Association's internal controls and are essential to ensuring the financial security of the Association's resources.

The Board of Directors should obtain and read the monthly financial statements as prepared and presented by management. At a minimum, the financial statements should include a balance sheet, income statement with budget to actual comparisons, a check register, a general ledger, and bank statements with reconciliations. Variances and unusual transactions should be discussed with management and resolved in a timely manner.

The Board of Directors should consider periodically reviewing randomly selected copies of paid invoices to ensure that the appropriate level of approval has occurred and that the approval is appropriately documented. The Board of Directors should also consider selecting invoices from vendors not recognized or not used on a regular basis.

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 Group CPAs, P.C.

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Communication with Those Charged with Governance under AU-C §260

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.

July 23, 2019

Board of Directors
Prosperity Heights Homeowners Association, Inc.

Dear Board Members:

We have audited the financial statements of Prosperity Heights Homeowners Association, Inc. as of June 30, 2018 and for the year then ended and have issued our report thereon. Professional standards require that we provide you with information about our responsibilities under generally accepted auditing standards, as well as certain information related to the planned scope and timing of our audit. We have communicated such information in our engagement letter. Professional standards also require that we communicate to you the following information related to our audit.

Our Responsibility under U.S. Generally Accepted Auditing Standards

As stated in our engagement letter, our responsibility, as described by professional standards, is to express an opinion about whether the financial statements prepared by management with your oversight are fairly presented, in all material respects, in conformity with U.S. generally accepted accounting principles. Our audit of the financial statements does not relieve you or management of your responsibilities.

Our responsibility for the supplementary information required by the Financial Accounting Standards Board, as described by professional standards, is to apply certain limited procedures to the information about management's methods of preparing the information; however, we will not express an opinion or any assurance on the information.

Planned Scope and Timing of the Audit

An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements; therefore, our audit will involve judgment about the number of transactions to be examined and the areas to be tested.

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Our audit will include obtaining an understanding of the Association and its environment, including internal control, sufficient to assess the risks of material misstatement of the financial statements and to design the nature, timing, and extent of further audit procedures. Material misstatements may result from (1) errors, (2) fraudulent financial reporting, (3) misappropriation of assets, or (4) violations of laws or governmental regulations that are attributable to the Association or to acts by management or employees acting on behalf of the Association. We will generally communicate our significant findings at the conclusion of the audit. However, some matters could be communicated sooner, particularly if significant difficulties are encountered during the audit where assistance is needed to overcome the difficulties or if the difficulties may lead to a modified opinion. We will also communicate any internal control related matters that are required to be communicated under professional standards.

Significant Audit Findings

Qualitative Aspects of Accounting Practices

Management is responsible for the selection and use of appropriate accounting policies. The significant accounting policies used by the Association are described in Note 2 to the financial statements. No new accounting policies were adopted and the application of existing policies was not changed during the year. We noted no transactions entered into by the Association during the year for which there is a lack of authoritative guidance or consensus. All significant transactions have been recognized in the financial statements in the proper period.

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. There were no significant accounting estimates for the year under audit.

Certain financial statement disclosures are particularly sensitive because of their significance to financial statement users. There were no significant disclosures to the financial statements for the year under audit.

The financial statement disclosures are neutral, consistent, and clear.

Difficulties Encountered in Performing the Audit

We encountered no significant difficulties in dealing with management in performing and completing our audit.

Corrected and Uncorrected Misstatements

Professional standards require us to accumulate all misstatements identified during the audit, other than those that are clearly trivial, and communicate them to the appropriate level of management. The adjusting journal entries have been provided to the Association and will be posted to the Association's accounts, if appropriate. The journal entries are material, either individually or in the aggregate, to the financial statements.

Disagreements with Management

For purposes of this letter, a disagreement with management is a financial accounting, reporting, or auditing matter, whether or not resolved to our satisfaction, that could be significant to the financial statements or the auditor's report. We are pleased to report that no such disagreements arose during the course of our audit.

Management Representations

We have requested certain representations from management that are included in the management representation letter.

Management Consultations with Other Independent Accountants

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to the Association's financial statements or a determination of the type of auditor's opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

Other Audit Findings or Issues

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as the Association's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

Required Supplementary Information

With respect to the supplementary information required by the Financial Accounting Standards Board, we applied certain limited procedures to the information, including inquiring of management about their methods of preparing the information; comparing the information for consistency with management's responses to the foregoing inquiries, the basic financial statements, and other knowledge obtained during the audit of the basic financial statements; and obtaining certain representations from management, including about whether the required supplementary information is measured and presented in accordance with prescribed guidelines.

Very truly yours,

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Communication of Significant Deficiencies and/or Material Weaknesses under AU-C §265

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July 23, 2019

Board of Directors
Prosperity Heights Homeowners Association, Inc.

Dear Board Members:

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Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and, therefore, material weaknesses or significant deficiencies may exist that were not identified. In addition, because of inherent limitations in internal control, including the possibility of management override of controls, misstatements due to error or fraud may occur and not be detected by such controls. However, as discussed below, we identified certain deficiencies in internal control that we consider to be material weaknesses or other deficiencies that we consider to be significant deficiencies.

A deficiency in internal control 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 and correct, misstatements on a timely basis. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. A material weakness is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the Association's financial statements will not be prevented, or detected and corrected, on a timely basis. We consider the following deficiencies in the Association's internal control to be material weaknesses or significant deficiencies:

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Segregation of Duties

The Association has a limited number of individuals performing the accounting function. This prevents the Association from segregating all accounting functions. The absence of adequate segregation of duties is considered a material weakness because there is a risk that intentional fraud or unintentional errors could occur and go undetected.

Modified Cash Basis of Accounting Used and Adjusting Journal Entries

The Association's accounting records are maintained on the modified cash basis of accounting throughout the year. We have proposed several material adjustments to present the financial statements on the accrual basis of accounting. In addition, we proposed an adjustment to reclassify the replacement reserve balance. The absence of controls over preparing the financial statements on the accrual basis of accounting, which is in accordance with U.S. GAAP, is considered a material weakness because there is a reasonable possibility that a material misstatement of the financial statements could occur and not be prevented, or detected and corrected, by the Association's internal control.

Very truly yours,

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