

May 23, 2006

Richmond, Neiley, Sprouse & Murphy, LLC
P.O. Box 280
Frisco, CO 80443
ATTN: Mark Richmond

Dear Mr. Richmond:

Common Interest Realty Associations ("CIRA") financial statements prepared in accordance with Generally Accepted Accounting Principles ("GAAP") include the following minimum criteria:

1. The use of the accrual basis of accounting. By definition this includes recording revenues when they are earned, rather than received, and expenses when they are incurred, rather than paid. For example, prepaid assessments, accounts payable, and accounts receivable should be recorded.
2. Full presentation of financial statements:
 - a. A balance sheet
 - b. A statement of revenues and expenses
 - c. A statement of changes in fund balances
 - d. A statement of cash flows
 - e. Notes to the financial statements
3. Notes to the financial statements should include the following:
 - a. The CIRA's legal form, areas it controls, and the number of units.
 - b. Common property.
 - c. Services and subsidies provided by the developer.
 - d. The CIRA's income tax filing status and its liability for income taxes.
 - e. The proposed use for funds collected in special assessments.
 - f. The number of units owned by the developer.
 - g. Credits from taxing authorities that will be phased out in future reporting periods.
 - h. Assessments that were used for purposes other than those for which they were designed.
 - i. Funding for future major repairs and replacements.

CIRA's with more complex transactions such as commercial operations, exclusive ownership to certain assets such as a manager's unit, and timeshare operations with unit inventories require further knowledge of GAAP than listed above.

While not required under GAAP, the American Institute of Certified Public Accountants ("AICPA") requires disclosure and presentation of Estimates of current or future costs of future major repairs and replacements of all existing components, such as roofs, including estimated amounts required, methods used to determine the costs, the basis for calculations, sources used, and the dates of the studies. Included in the presentation should also be amounts of funds accumulated for each component to the extent designated by the board.

For your information, please find enclosed a copy of a letter outlining important tax reminders related to Major Repairs and Replacement Funds.

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We've also enclosed a memo describing the various levels of financial statement services:
Compilation, Review, and Audit.

We hope this letter is helpful. Please call if you have any questions.

Sincerely,

Jolene Reddell, CPA
Stuhr and Associates, LLC

DATE

Board members:

We would like to make you aware of your responsibilities with regard to the tax return for XYZ Association ("Association") for the year ended _____. In doing so, we request that you review the following observations and comments:

1. When an Association maintains and funds reserve funds for capital projects, major maintenance, repairs and replacements, it is important that the Board conduct whatever study is necessary to identify the components and funding amounts of each. All Replacement Fund transactions should be documented in the Association's budget and minutes.
2. For reserve income not to be considered taxable income to the Association per Internal Revenue Service ("IRS") rulings, the following conditions must be met:
 - A. Separate bank accounts should be established for each reserve fund and a portion of revenues of the Association should be earmarked or budgeted to the reserves.
 - B. The reserve assessment income must be earmarked for specific major improvements and replacements.
 - C. Reserve income cannot be co-mingled with operating funds.
 - D. Deposits of reserve income to reserve bank accounts must be made in a timely manner. We would suggest allocating funds and depositing them at least monthly.
 - E. The budget must clearly delineate between member (operating) activities and capital reserve and/or replacement fund activities.
 - F. The replacement fund (reserve) study should agree to and support the budget. While the budget supports the current year's capital reserve income, the reserve study supports the purpose for which the reserve income is being recorded over the long term.
 - G. Minutes of the meetings of the Board of Directors should document adoption of the reserve study and budget and authorize expenditures of funds for specific capital purposes.
3. Capital assessments, when accounted for as outlined above, are considered an automatic increase in the capital basis of each member. Invoices and/or statements to members should delineate capital and operating assessments.
4. At the annual meeting of the Association, the membership should approve a resolution to apply excess membership income over membership expenses for the year ended _____ against subsequent year's assessments. The adoption of this resolution should be recorded in the minutes, signed and retained in the Association's corporate records. A sample resolution has been enclosed for your convenience.

5. When auditing associations, the IRS will specifically look at the reserves and allocation of expenses to non-membership income (e.g. interest income and other non-member income). Documentation to support allocations of expenses to non-membership income should be retained.

In order to manage the Association's liability regarding Federal and State taxes, the Company must adhere to the IRS Code and Revenue Rulings specifically dealing with homeowner associations. It is important that all decisions regarding management, revenue allocations, budgets, etc., be well documented and all minutes and resolutions adopted by the Board be approved.

We will be happy to discuss any of the above and answer any questions you may have.

Sincerely,

Stuhr and Associates, LLC

RESOLUTION OF THE XYZ ASSOCIATION

RE: EXCESS INCOME APPLIED TO THE FOLLOWING YEAR'S ASSESSMENTS
REVENUE RULING 70-604

WHEREAS, XYZ Association is a Colorado corporation duly organized and existing under the laws of the State of Colorado;

and

WHEREAS, the members desire that the corporation shall act in full accordance with the rulings and regulations of the Internal Revenue Service;

NOW, THEREFORE, the members hereby adopt the following resolution by and on behalf of XYZ Association:

RESOLVED, that any excess of membership income over membership expenses for the year ended _____, shall be applied against the subsequent tax year member assessments as provided by IRS Revenue Ruling 70-604.

The resolution is adopted and made part of the minutes of the meeting of _____

BY: _____
President

ATTESTED: _____
Secretary

Following are the definitions of compilations, reviews and audits:

- *Compilations.* Presenting in the form of financial statements in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants, information that is the representation of management (owners) without undertaking to express any assurance on the financial statements.
- *Reviews.* Performing inquiry and analytical procedures that provide the accountant with a reasonable basis for expressing limited assurance that there are no material modifications that should be made to the statements in order for them to be in conformity with U.S. generally accepted accounting principles or, if applicable, with an other comprehensive basis of accounting.
- *Audits.* The objective of an audit is the expression of an opinion about whether the financial statements are fairly presented, in all material respects, in conformity with U.S. generally accepted accounting principles. An audit includes performing procedures that include tests of documentary evidence supporting the transactions recorded in the accounts and direct confirmation of cash, investments, and certain other assets and liabilities with correspondence with selected owners, creditors, legal counsel, and financial institutions. An audit also includes obtaining an understanding of internal control sufficient to plan the audit and to determine the nature, timing, and extent of audit procedures to be performed.

The differences between the three types of engagements can be summarized by the increasing levels of assurance provided by the accountant that the financial statements are fairly presented for the users of the financial statements.

Often an Association's bylaws or other governing documents require an audit. Effective January 1, 2006, Colorado Senate Bill 05-100 may require an audit or review performed every other year. Consult your lawyer as to specific matters of compliance with this law.