Grand Pacific Palisades
Owners Association, Inc.

5805 Armada Drive, Carlsbad, CA 92008

Financial Statements

December 31, 2015

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Independent Auditor's Report

To the Board of Directors and Owners
Grand Pacific Palisades Owners Association, Inc.
Carlsbad, California

Report on the Financial Statements
We have audited the accompanying financial statements of Grand Pacific Palisades Owners Association, Inc. (the Association), which comprise the statement of assets, liabilities and fund balance as of December 31, 2015; the related statement of revenues, expenses and changes in fund balance (deficit), and cash flows for the year then ended; and the related notes to the financial statements (collectively, 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 accounting principles generally accepted in the United States of America; 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.

Auditor's Responsibility
Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit 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 auditor's 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 Grand Pacific Palisades Owners Association, Inc. as of December 31, 2015 and the changes in its fund balance and cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Report on Supplementary Information
Accounting principles generally accepted in the United States of America require that the supplementary information on future major repairs and replacements on page 7 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Financial Accounting Standards Board, which considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic or historical context. Such information is the responsibility of the Association's management. 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 basic financial statements and other knowledge we obtained during our audit of the basic 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.

RSM US LLP

San Francisco, California
June 14, 2016

GRAND PACIFIC PALISADES
OWNERS ASSOCIATION, INC.

Statement of Assets, Liabilities and Fund Balance

December 31, 2015

	Operating Fund	Replacement Fund	Total
Assets			
Cash	$ 3,579,154	$ 237,958	$ 3,817,112
Assessments and other receivables, net	5,703,511	986,189	6,689,700
Prepaid expenses	157,216	-	157,216
Due from operating fund	-	295,251	295,251
Total assets	$9,439,881	$1,519,398	$10,959,279
Liabilities and Fund Balance			
Accounts payable and accrued liabilities	$ 807,659	$ 16,916	$ 824,575
Due to related parties, net	613,289	-	613,289
Due to replacement fund	295,251	-	295,251
Deferred assessments	7,426,955	1,468,953	8,895,908
Total liabilities	9,143,154	1,485,869	10,629,023
Fund balance	296,727	33,529	330,256
Total liabilities and fund balance	$9,439,881	$1,519,398	$10,959,279

See notes to the financial statements

GRAND PACIFIC PALISADES
OWNERS ASSOCIATION, INC.

Statement of Revenues, Expenses and Changes in Fund Balance (Deficit)

Year Ended December 31, 2015

	Operating Fund	Replacement Fund	Total
Revenues:			
Assessments	$ 7,198,296	$ 1,207,358	$ 8,405,654
Interest	2,421	421	2,842
Room revenue and other income	1,067,586	-	1,067,586
Total revenues	**8,268,303**	**1,207,779**	**9,476,082**
Expenses:			
Front office	674,439	-	674,439
Housekeeping	1,933,330	-	1,933,330
Owner relations and guest activities	339,705	-	339,705
Administration and sales	844,805	16,519	861,324
Repairs, replacements and maintenance	971,905	1,156,482	2,128,387
Telephone and utilities	757,997	-	757,997
Fixed expenses	1,064,777	-	1,064,777
Property tax and insurance	1,055,252	-	1,055,252
Uncollectible assessments, net	329,394	46,445	375,839
Provision for income taxes	800	-	800
Total expenses	**7,972,404**	**1,219,446**	**9,191,850**
Excess (deficiency) of revenues over expenses	**295,899**	**(11,667)**	**284,232**
Fund balance (deficit), beginning of year	150,828	(104,804)	46,024
Board-approved transfer	(150,000)	150,000	-
Fund balance, end of year	$ 296,727	$ 33,529	$ 330,256

See notes to the financial statements

GRAND PACIFIC PALISADES
OWNERS ASSOCIATION, INC.

Statement of Cash Flows

Year Ended December 31, 2015

	Operating Fund	Replacement Fund	Total
Cash flows from operating activities:			
Excess (deficiency) of revenues over expenses	$ 295,899	$ (11,667)	$ 284,232
Adjustments to reconcile excess (deficiency) of revenues over expenses to net cash provided by (used in) operating activities:			
Uncollectible assessments, net	329,394	46,445	375,839
(Increase) decrease in operating assets:			
Assessments and other receivables, net	(522,895)	(232,153)	(755,048)
Prepaid expenses	13,777	-	13,777
Due from operating fund	-	(53,797)	(53,797)
Increase (decrease) in operating liabilities:			
Accounts payable and accrued liabilities	55,550	(122,355)	(66,805)
Due to related parties, net	318,813	-	318,813
Due to replacement fund	53,797	-	53,797
Deferred assessments	195,540	278,622	474,162
Net cash provided by (used in) operating activities	**739,875**	**(94,905)**	**644,970**
Net cash flows from financing activities:			
Board-approved transfer	(150,000)	150,000	-
Net increase in cash	**589,875**	**55,095**	**644,970**
Cash, beginning of year	2,989,279	182,863	3,172,142
Cash, end of year	$ 3,579,154	$ 237,958	$ 3,817,112
Supplemental disclosure of cash flow information:			
Cash paid during the year for income taxes			$ 800

See notes to the financial statements

Notes to the Financial Statements

Note 1. Nature of Association and Significant Accounting Policies

Association and membership: Grand Pacific Palisades Owners Association, Inc. (the Association) was incorporated on December 21, 1998, as a California nonprofit mutual benefit corporation, with the specific and primary purpose of promoting the interests and welfare of the owners of vacation intervals situated in the project known as Grand Pacific Palisades in Carlsbad, California. The Association is comprised of Class A memberships for annual owners, Class B memberships for biennial owners, Class C memberships for vacation intervals still owned by the project's developer, and Class D memberships for units used as a facility and/or amenity within the project. Annual memberships are entitled to two votes, and biennial memberships are entitled to one vote. Class D members are entitled to 102 votes for each facility/amenity owned. Vacation interval sales commenced in February 2000.

In accordance with the Association's bylaws, each vacation interval owner is subject to basic, special and personal charge assessments by the Association.

A summary of significant accounting policies is as follows:

Basis of accounting: The financial statements of the Association have been prepared on the accrual basis of accounting. Accordingly, all significant receivables, revenues and gains are recognized when earned, and expenses, liabilities and losses are recognized when incurred.

Fund accounting: The Association uses fund accounting, which requires that funds, such as the operating fund and replacement fund, be classified separately for accounting and reporting purposes. Disbursements from the operating and replacement funds are generally at the discretion of the Board of Directors (the Board) and the Association's management. Disbursements from the replacement fund generally may be made only for designated purposes.

Concentration of credit risk: The Association maintains its cash in bank accounts and money market accounts that exceed the federally insured limit of $250,000. The Association has not experienced any losses in such accounts. Management believes the Association is not exposed to significant credit risk relating to cash.

Assessments and deferred assessments: For the year ended December 31, 2015, each annual vacation membership owner was generally assessed $1,253 for a Penthouse unit, $1,063 for a three-bedroom unit, $934 for a two-bedroom unit and $889 for a one-bedroom unit, inclusive of the replacement fund assessment. Biennial vacation membership assessments are one-half of the annual membership assessment amount. Under this program, units within the unit type originally purchased can be used once every two years.

For the year ending December 31, 2016, the annual assessment of $1,341 (Penthouse), $1,143 (three bedrooms, $999 (two bedrooms) and $950 (one bedroom), inclusive of the replacement fund assessment, is included in deferred assessments until earned.

The Association's policy is to bill the annual assessments in advance and recognized them as revenue on a pro rata basis over the period covered by the billing. As of December 31, 2015, the Association has billed in advance $8,715,692 of the 2016 assessment and collected $2,891,252. Deferred assessments include year 2016 amounts billed but not collected of $5,824,440 at December 31, 2015.

Allowance for doubtful accounts: Assessments receivable at December 31, 2015 consist principally of advance assessment billings for the year ending December 31, 2016. Accordingly an allowance for doubtful accounts has not been established as of December 31, 2015.

All assessments are due and payable January 1 after the interval owner is billed. Interest, at rates determined by the Board, is charged on delinquent assessments. The Association may suspend rights and privileges of interval owners with delinquent assessments as defined in the bylaws. The Association's policy is to write off all assessment receivables not collected by December 31 of the year in which the assessment pertains. Subsequent collection is recognized as bad debt recovery in the year received, which is netted with the uncollectible assessments on the statement of revenues, expenses and changes in fund balance (deficit).

Property and equipment: Ownership of the commonly owned assets is vested directly and indirectly in the interval owners, and those assets are not titled in the Association's name. As a result, commonly owned assets are not presented in the Association's statement of assets, liabilities and fund balance. Expenses incurred for the repair and replacement of commonly owned assets are reported as expenses in the replacement fund on the statement of revenues, expenses and changes in fund balance (deficit).

Replacement fund assessments: The Association has designated certain amounts as replacement funds to provide for the payment of future repair and rehabilitation expenditures, as specifically approved by the Association's Board of Directors. The Association's replacement fund program is subject to a reserve analysis study. The most recent study conducted on June 23, 2015 was prepared by Association Reserves San Diego, LLC, who specializes in the preparation of reserve studies. The preparation of the reserve analysis is based upon certain assumptions in regards to existing reserve fund balances, inflation and investment rate factors, the estimated life span and the current cost of the reserve items. Furthermore, there will usually be differences between the projected and actual results, because events and circumstances frequently do not occur as expected, and those differences may be material.

Based on the study and the estimates contained in the underlying report, the Association's management believes that the existing replacement funding program together with the future business plan is adequate to meet future repair and rehabilitation expenditures. Should such funds not be adequate, or if additional funds are needed, the Association has the right, subject to certain limitations, to increase the annual assessments, pass special assessments or delay the expenditures until funds are available.

Presentation of certain taxes: The Association collects various taxes, generally occupancy taxes, and remits these amounts to applicable taxing authorities. The Association's accounting policy is to exclude these taxes from revenues and expenses.

Accounting estimates: The preparation of financial statements in accordance with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported as assets, liabilities, revenues, expenses and related disclosures. Actual results could differ from these estimates.

Subsequent events: Management has assessed subsequent events through June 14, 2016, the date on which the financial statements were available to be issued.

Note 2. Related Parties

Management agreement: The Association is operated under a management agreement with a professional property management company, Grand Pacific Resort Services, L.P. (GPRS), an affiliate of the developer. The Association's management budget is within guidelines established by the California Bureau of Real Estate, which regulates common interest developments. Management fees under this agreement were $736,504 for the year ended December 31, 2015, of which $620,426 is allocated as fixed expenses under the operating fund and $116,078 is allocated as repairs, replacements and maintenance under the replacement fund on the statement of revenues, expenses and changes in fund balance (deficit).

In addition, the Association shall compensate GPRS and Advanced Financial Corporation (AFC), an affiliate of the developer, for other services provided, including but not limited to assessments billing and collection, accounting and computer services, file and reservation system maintenance, owner relations service, and Board of Directors and members meetings coordination. The Association also reimburses GPRS for any out-of-pocket expenses paid. At December 31, 2015, the Association owed GPRS and AFC and other related parties $199,363 for services provided, including $154,887 of fees billed to interval owners included in assessments and other receivables, which will be collected by the Association on behalf of AFC. At December 31, 2015, the Association incurred $377,382 in expense for these services, which has been allocated to administration and sales, fixed expenses and owner relations and guest services in the operating fund on the statement of revenue, expenses and changes in fund balance (deficit).

Developer subsidy: In accordance with the limited subsidy agreement between the Association and the project's developer, Grand Pacific Palisades, L.P., the developer has agreed, subject to certain limitations, to pay the Association for the excess of operating expenses over revenues. Upon termination of the agreement, the developer will become responsible for the assessments pertaining to unpurchased vacation plans. During 2015 in accordance with the limited subsidy agreement, the developer informed the Association that all 6,569 ownership intervals have been conveyed for first sale and has elected to terminate the subsidy agreement. The Board of Directors consented to the termination of the limited subsidy agreement.

Cost-sharing agreement: The Association has entered into a cost-sharing agreement with Grand Pacific Palisades Hotel, an affiliate of the developer, to share common operating costs. These expenses shall be shared between the Association and the Hotel based on the burden each places on the property, as measured by such factors as the number of rooms, square footage of rooms, occupancy rates and occupants per unit. At December 31, 2015, generally the allocation percentages for the Association and the Hotel were 80 percent and 20 percent, respectively. Under the cost-sharing agreement, the Association owed the Hotel $413,926 at December 31, 2015.

Unit week inventory: The Association, developer and Advanced Commercial Corporation (ACC), a company affiliated with the developer, entered into various agreements regarding unpurchased vacation intervals. The developer and ACC will bear the cost of foreclosing, deeding back, marketing and reselling the unpurchased vacation intervals. The Association will not receive the net proceeds from the sale, but is responsible for property taxes on unpurchased vacation intervals. The developer will not be responsible for assessments on unpurchased vacation intervals.

Inventory management agreement: The Association entered into an inventory management agreement with GPRS. Under this agreement, GPRS will use its centralized management of resort interval inventory to maximize owner use of the property, ensure quality outbound exchanges for owners who wish to vacation elsewhere. The Association agrees to permit GPRS to manage, allocate and control resort room inventory and to use all room inventory that is not occupied. In exchange, GPRS guarantees the Association will receive the transient room revenue it has budgeted. The Association recognized $672,900 in guaranteed room revenue for the year ended December 31, 2015.

Note 3. Income Taxes

For federal tax purposes, the Association is taxed under Internal Revenue Code Section 528 as an exempt organization. The Association is taxed on its non-exempt income less expenses directly connected with the production of the non-exempt income. Exempt function income is not subject to tax. Income tax is calculated at 32 percent of taxable income.

For state tax purposes, the Association is organized as a non-exempt membership organization and is taxed on its excess nonmember income (principally interest and usage by nonmembers) at the normal corporate tax rates.

Federal and state income taxes for 2015 totaled $0 and $800, respectively.

Uncertain tax positions: The Association identifies and evaluates all uncertain tax positions and believes that positions taken are more likely than not to be sustained upon examination for all open tax years. The Association's tax returns are subject to examination by federal taxing authorities for a period of three years from the date they are filed and a period of four years for California taxing authorities.

Note 4. Operating Lease

Effective March 15, 1999, the Association has leased telecommunication equipment from GPRS. The Association has also granted GPRS the exclusive rights to provide local and long distance services and operator-assisted services. The term of the lease is 10 years and is automatically renewable for two additional five-year terms, unless terminated in accordance with the lease agreement. The Association pays approximately $5,863 per month (subject to annual cost of living increases) for the leased equipment and remits user charges in accordance with the agreement. Telephone expense of $111,813 for the year ended December 31, 2015 included operating lease payments and charges incurred with long distance carriers.

Note 5. Contingencies

Periodically, the Association may become involved in litigation in the normal course of business. The Association believes that the result of any potential litigation will not have a material effect on the Association's financial condition..

Supplementary Information on Future Major Repairs and Replacements (Unaudited)

Association Reserves San Diego, LLC conducted an updated site visit study on June 23, 2015 to estimate the remaining useful lives and the replacement costs of the components of common property subject to future repairs and replacements. Estimated current replacement costs have been based on the average best and worst case estimates using Association cost history, database industry history, vendor history and national industry cost estimation guides. The estimated current replacement costs have not been revised since that date and 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, or the costs incurred since the date of the study. During 2015 the Association conducted repairs and replacements totaling $1,040,404.

The following table is based on the site visit study conducted on March 9, 2015 and presents a condensed summary of information about the items of property. Recommended funding requirements are based on the assumptions that the inflation rate and interest rate are 3 percent and 1 percent, respectively.

	2015	
Components	Estimated Remaining Life in Years	Estimated Current Replacement Costs
Building exterior	1-30	$ 1,655,500
Common interiors	8-20	177,250
Mechanical	3-20	614,300
Unit interiors	1-24	11,939,500
Shared, general common areas	4-30	1,417,050
Shared, mechanical	8-25	719,590
Shares, recreation	3-30	924,470
Total		**$17,447,660**