

Financial Statements with Supplementary
Information and Independent Auditors' Report

Daniel Island Park Association, Inc.

As of December 31, 2017 and December 31, 2016

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VANCE FLOUHOUSE & GARGES, PLLC
Certified Public Accountants and Consultants

Independent Auditors' Report

To the Board of Directors of
Daniel Island Park Association, Inc.:

We have audited the accompanying financial statements of Daniel Island Park Association, Inc., which comprise the balance sheet as of December 31, 2017 and 2016, and the related statements of revenues, expenses, and changes in fund balance and cash flows for the years then ended, and the related notes to 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 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 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 Daniel Island Park Association, Inc. as of December 31, 2017, and the results of its operations and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Report on Summarized Comparative Information

We have previously audited the Association's December 31, 2016 financial statements, and our report dated September 13, 2017 expressed an unmodified opinion on those financial statements. In our opinion, the summarized comparative information presented herein as of and for the year ended December 31, 2016, is consistent, in all material respects, with the audited financial statements from which it has been derived.

Disclaimer of Opinion on Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the supplementary information on future major repairs and replacements as listed in the table of contents 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. 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.

Vance Flournoy & Dejes PLLC

Charlotte, North Carolina
August 14, 2018

Balance Sheet

December 31, 2017

| | <u>Operating Fund</u> | <u>Replacement Fund</u> | <u>Total 2017</u> | <u>Summarized 2016</u> |
|---|----------------------------|-----------------------------|----------------------------|----------------------------|
| Assets | | | | |
| Current assets: | | | | |
| Cash and cash equivalents | \$ 735,784 | \$ 38,433 | \$ 774,217 | \$ 511,998 |
| Cash escrow - construction deposits | 764,104 | - | 764,104 | 951,640 |
| Investments | - | 387,793 | 387,793 | 341,938 |
| Accounts receivable (net) | 4,325 | - | 4,325 | 1,851 |
| Interfund due from (due to) | 17,209 | (17,209) | - | - |
| Prepaid expenses | 5,905 | - | 5,905 | 10,293 |
| Total current assets | <u>1,527,327</u> | <u>409,017</u> | <u>1,936,344</u> | <u>1,817,720</u> |
| Furniture and equipment, net of accumulated depreciation | <u>3,844</u> | <u>-</u> | <u>3,844</u> | <u>3,348</u> |
| Total assets | <u><u>\$ 1,531,171</u></u> | <u><u>\$ 409,017</u></u> | <u><u>\$ 1,940,188</u></u> | <u><u>\$ 1,821,068</u></u> |
| Liabilities and fund balances | | | | |
| Current liabilities: | | | | |
| Accounts payable and accrued expenses | \$ 5,223 | \$ - | \$ 5,223 | \$ 46,926 |
| Due to related parties | 473 | - | 473 | 176 |
| Prepaid assessments | 529,041 | - | 529,041 | 351,304 |
| Construction deposits | 763,235 | - | 763,235 | 950,066 |
| Taxes payable | 224 | - | 224 | - |
| Total current liabilities | <u>1,298,196</u> | <u>-</u> | <u>1,298,196</u> | <u>1,348,472</u> |
| Fund balances | <u>232,975</u> | <u>409,017</u> | <u>641,992</u> | <u>472,596</u> |
| Total Liabilities and fund balances | <u><u>\$ 1,531,171</u></u> | <u><u>\$ 409,017</u></u> | <u><u>\$ 1,940,188</u></u> | <u><u>\$ 1,821,068</u></u> |

The accompanying notes are an integral part of these financial statements.

Statement of Revenues, Expenses, and Changes in Fund Balances

Year Ended December 31, 2017

| | Operating Fund | Replacement Fund | Total 2017 | Summarized 2016 |
|--|-------------------|---------------------|-------------------|--------------------|
| Revenues: | | | | |
| Property owner assessments | \$ 906,613 | \$ 20,000 | \$ 926,613 | \$ 866,839 |
| Capitalization assessments | 35,188 | - | 35,188 | 17,374 |
| Lot maintenance assessments | 40,580 | - | 40,580 | 35,533 |
| Finance charges | 2,785 | - | 2,785 | 2,839 |
| Interest and dividend income | 1,364 | 9,726 | 11,090 | 7,757 |
| Realized gains (losses) on investments | - | 1,634 | 1,634 | (3,241) |
| Unrealized gains (losses) on investments | - | 20,003 | 20,003 | 14,616 |
| Other income | 143,680 | - | 143,680 | 28,758 |
| Total revenues | <u>1,130,210</u> | <u>51,363</u> | <u>1,181,573</u> | <u>970,475</u> |
| Expenses: | | | | |
| Amenity expenses | 11,021 | - | 11,021 | 6,888 |
| Bad debt expense | 2,602 | - | 2,602 | 3,805 |
| Grounds maintenance | 74,653 | - | 74,653 | 44,408 |
| Insurance | 14,816 | - | 14,816 | 11,278 |
| Landscape maintenance | 438,078 | - | 438,078 | 423,782 |
| Mailbox cost | 21,126 | - | 21,126 | 20,098 |
| Professional fees | - | 2,607 | 2,607 | 3,369 |
| Professional services | 21,631 | - | 21,631 | 13,828 |
| Repairs and replacements | - | 7,227 | 7,227 | 2,983 |
| Shared cost contribution | 353,345 | - | 353,345 | 321,008 |
| Utilities - common area | 45,189 | - | 45,189 | 51,155 |
| Depreciation | 836 | - | 836 | 752 |
| Other expenses | 19,046 | - | 19,046 | 3,632 |
| | <u>1,002,343</u> | <u>9,834</u> | <u>1,012,177</u> | <u>906,986</u> |
| Revenues over expenses | 127,867 | 41,529 | 169,396 | 63,489 |
| Fund balances, beginning of year | 105,108 | 367,488 | 472,596 | 409,107 |
| Fund balances, end of year | <u>\$ 232,975</u> | <u>\$ 409,017</u> | <u>\$ 641,992</u> | <u>\$ 472,596</u> |

The accompanying notes are an integral part of these financial statements.

Statement of Cash Flows

Year Ended December 31, 2017

| | Operating Fund | Replacement Fund | Total 2017 | Summarized 2016 |
|---|----------------------------|-------------------------|----------------------------|----------------------------|
| Cash flows from operating activities: | | | | |
| Revenues over expenses | \$ 127,867 | \$ 41,529 | \$ 169,396 | \$ 63,489 |
| Adjustments to reconcile revenues over expenses to net cash provided by (used in) operating activities: | | | | |
| Unrealized (gains) losses on investments | - | (20,003) | (20,003) | (14,616) |
| Depreciation | 836 | - | 836 | 752 |
| Changes in operating assets and liabilities: | | | | |
| Accounts receivable | (2,474) | - | (2,474) | 1,829 |
| Income tax refunds receivable | - | - | - | - |
| Due from related parties | - | - | - | 2,544 |
| Prepaid expenses | 4,388 | - | 4,388 | (5,598) |
| Due to/from between funds fund | (19,244) | 19,244 | - | - |
| Accounts payable | (41,703) | - | (41,703) | 46,443 |
| Due to related parties | 297 | - | 297 | (918) |
| Prepaid assessments | 177,737 | - | 177,737 | (57,291) |
| Taxes payable | 224 | - | 224 | - |
| Construction deposits | (186,831) | - | (186,831) | (65,959) |
| Net cash provided by (used in) operating activities | <u>61,097</u> | <u>40,770</u> | <u>101,867</u> | <u>(29,325)</u> |
| Cash flows from investing activities: | | | | |
| Purchase of property and equipment | (1,332) | - | (1,332) | (4,100) |
| Sale of investments | - | 30,000 | 30,000 | 52,795 |
| Purchase of investments | - | (55,852) | (55,852) | (106,932) |
| Net cash used in investing activities | <u>(1,332)</u> | <u>(25,852)</u> | <u>(27,184)</u> | <u>(58,237)</u> |
| Cash flows from financing activities: | | | | |
| Transfers between funds | - | - | - | - |
| Net cash provided by (used in) financing activities | <u>-</u> | <u>-</u> | <u>-</u> | <u>-</u> |
| Increase (decrease) in cash and equivalents | 59,765 | 14,918 | 74,683 | (87,562) |
| Cash and cash equivalents, beginning of year | <u>1,440,123</u> | <u>23,515</u> | <u>1,463,638</u> | 1,551,200 |
| Cash and cash equivalents, end of year | <u><u>\$ 1,499,888</u></u> | <u><u>\$ 38,433</u></u> | <u><u>\$ 1,538,321</u></u> | <u><u>\$ 1,463,638</u></u> |
| Supplemental disclosures of cash flow information: | | | | |
| Cash paid for income taxes | <u>25</u> | <u>-</u> | <u>25</u> | <u>506</u> |

The accompanying notes are an integral part of these financial statements.

Notes to Financial Statements

December 31, 2017

1. Organization

Daniel Island Park Association, Inc. (the Association) was formed as a home owners' association to maintain and preserve the common property of the development. The development consists of 966 developed units and lots located on Daniel Island in Charleston, South Carolina of which 939 have been sold. At completion, the development is expected to encompass approximately 1,014 homes. The common property consists of land, playgrounds, parks, bridges, bike trails, ponds, boat landing, sea wall, sidewalks, green belts and other infrastructure improvements.

2. Summary of Significant Accounting Policies

Fund Accounting

The Association uses fund accounting which reports activity within the operating and replacement funds separately for accounting and financial reporting purposes. Fund accounting is helpful in segregating amounts which have been designated for special use. The Associations funds are as follows:

Operating Fund - This fund is used to account for the general operations of the Association.

Replacement Fund - This fund is used to accumulate financial resources designated for future major repairs and replacements.

Cash and Cash Equivalents

Cash and cash equivalents include cash and highly liquid investments that are readily convertible into cash and have a maturity of three months or less when purchased.

Member Assessments

Association members are subject to annual assessments to provide funds for operating expenses, future capital acquisitions, and major repairs and replacements. The annual budget and member assessments are determined and approved by the board of directors. Any excess operating funds remaining at the end of the operating year are retained for use in future operating periods.

The Association's policy is to place liens on the properties of homeowners whose assessments are delinquent more than 105 days. The Association performs ongoing evaluations of its accounts receivable and establishes an allowance for doubtful accounts based upon factors surrounding the collection of specific receivables. Accounts are charged against the allowance account as management deems them uncollectible. The allowance for doubtful accounts was approximately \$4,000 and \$8,000 at December 31, 2017 and December 31, 2016, respectively.

Investments

Investments consist of mutual funds that hold corporate equity stocks and bonds, electronic transfer funds and corporate and government bonds. The Association has adopted *ASC 958-320 Not-for-Profit Entities: Investments-Debt and Equity Securities*. Under *ASC 958-320*, investments in marketable securities with readily determinable fair values are reported at their fair values in the balance sheets. Unrealized gains and losses are included in the change in net assets.

Fair Value Measurements

The Association has estimated the fair value of its financial instruments using available market information and other valuation methodologies in accordance with *ASC 820 Fair Value Measurements and Disclosures*. Accordingly, the estimates presented are not necessarily indicative of the amount that the organization could realize in a current market exchange. Determinations of fair value are based on subjective data and significant judgment relating to timing of payments, collections, and the amount to be realized. Different market assumptions and/or estimation methodologies might have a material effect on the estimated fair value amounts.

Property and Equipment

In accordance with industry standards and because its disposition by the Association's board is unlikely, common real property acquired from or donated by the developer is not recognized on the Association's financial statements. Property and equipment acquired by the Association are capitalized and recorded at cost. Replacements and improvements to common property are expensed as incurred.

Property and equipment consisted solely of equipment at December 31, 2017 and are depreciated over their estimated useful lives ranging from 5 to 7 years using the straight line and accelerated depreciation methods. Depreciation expense was \$836 and \$752 for the year ended December 31, 2017 and December 31, 2016, respectively.

Advertising

The Association expenses all advertising and promotion costs in the period the expense is incurred.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and 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.

Taxes

The Association presents all tax expense and any related interest and penalties as one line on the financial statements.

Subsequent Events

The Association has evaluated subsequent events through August 14, 2018, the date the financial statements were available to be issued.

3. Federal and State Taxes

The Association has elected to file its income tax returns as a homeowners' association in accordance with the Internal Revenue Service Code §528 under which the Association may exclude from taxation exempt function income, which generally consists of revenue from uniform assessments to owners. The Association's investment and other nonexempt income are subject to tax. Income tax expense for the year ended December 31, 2017 and December 31, 2016 was \$249 and \$22, respectively.

4. Investments

Investments at December 31, 2017 and December 31, 2016 are summarized as follows:

| | Cost | Unrealized Gains (Losses) | Fair Value |
|---|-------------------|---------------------------------|-------------------|
| <u>2017</u> | | | |
| Mutual Funds | \$ 50,049 | \$ 20,299 | \$ 70,348 |
| Corporate and government bonds | 130,006 | 1,102 | 131,108 |
| Corporate stock and electronic transfer funds | 170,274 | 16,063 | 186,337 |
| | <u>\$ 350,329</u> | <u>\$ 37,464</u> | <u>\$ 387,793</u> |
| <u>2016</u> | | | |
| Mutual Funds | \$ 50,049 | \$ 14,860 | \$ 64,909 |
| Corporate and government bonds | 149,139 | 421 | 149,560 |
| Electronic transfer funds | 125,519 | 1,950 | 127,469 |
| | <u>\$ 324,707</u> | <u>\$ 17,231</u> | <u>\$ 341,938</u> |

5. Fair Value Measures

FASB Accounting Standards Codification ("ASC") 820 provides the framework for measuring fair value. That framework provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (level 1 measurement) and the lowest priority to unobservable inputs (level 3 measurements). The three levels of the fair value hierarchy under ASC 820 are described as follows:

Level 1: Quoted market prices for identical assets or liabilities in active markets that the Plan has the ability to access.

Level 2: Inputs and information other than quoted prices within Level 1 that are observable for the asset or liability, either directly or indirectly.

Level 3: Unobservable inputs for the asset or liability. Unobservable inputs should be used to measure the fair value to the extent that observable inputs are not available.

The asset or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques used need to maximize the use of observable inputs and minimize the use of unobservable inputs.

Following is a description of the valuation methodologies used for assets measured at fair value. There have been no changes in the methodologies used at December 31, 2017.

Mutual funds, corporate stock, and electronic transfer funds: Valued at the quoted net asset value of shares held by the Plan at year end.

Corporate and government bonds: Valued using pricing models maximizing the use of observable inputs for similar securities. This includes basing value on yields currently available on comparable securities of issuers with similar credit ratings.

The preceding methods described may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, although management believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

The following table sets forth by level, within the fair value hierarchy, the Plan's assets at fair value as of December 31, 2017 and December 31, 2016:

| | <u>Fair Value</u> | <u>Level 1</u> | <u>Level 2</u> | <u>Level 3</u> |
|---|-------------------|-------------------|-------------------|----------------|
| <u>2017</u> | | | | |
| Mutual Funds | \$ 70,348 | \$ 70,348 | \$ - | \$ - |
| Corporate and government bonds | 131,108 | - | 131,108 | - |
| Corporate stock and electronic transfer funds | 186,337 | 186,337 | - | - |
| | <u>\$ 387,793</u> | <u>\$ 256,685</u> | <u>\$ 131,108</u> | <u>\$ -</u> |
| <u>2016</u> | | | | |
| Mutual Funds | \$ 64,909 | \$ 64,909 | \$ - | \$ - |
| Corporate and government bonds | 149,560 | - | 149,560 | - |
| Electronic transfer funds | 127,469 | 127,469 | - | - |
| | <u>\$ 341,938</u> | <u>\$ 192,378</u> | <u>\$ 149,560</u> | <u>\$ -</u> |

6. Concentrations

Daniel Island is located in the coastal region of South Carolina, a popular vacation destination area. The members of the Association include those purchasing property for personal residential use as well as for investment or commercial/rental purposes. The Association is exposed to risks associated with conditions affecting the weather, economy, and real estate and tourism industries for the geographic region. Severe fluctuations in the above variables could have a negative effect on revenues and expenses.

The Association maintains cash deposits with major banks, which may exceed federally insured limits. The Association periodically assesses the financial condition of the institutions and believes the risk of loss to be remote.

One vendor provides all landscaping services for the Association. In the years 2017 and 2016, landscaping expenses were about 44% and 47% of total expenses paid by the association, respectively.

7. Commitments

The Association has various contracts with vendors that provide landscaping services; these contracts auto renew on an annual basis. The contracted payments due during 2018 are \$329,580.

8. Related Party Transactions

The Developer may, but has no obligation to make subsidies to the Association. For the years ended December 31, 2017 and December 31, 2016, the Developer made no subsidy payments to the Association. Daniel Island Company, an entity related to the developer, provides certain administrative and accounting functions to the Association at no charge.

Certain common property maintenance expenses and costs of community-wide services beneficial to the area are shared between the Association, Daniel Island Park Association, Inc. and Daniel Island Town Association, Inc. (together, the "DI Associations"), each a related party located Daniel Island. The boards of directors of the DI Associations establish the method for sharing the costs. For the year ended December 31, 2017, the Association incurred shared cost expenses of \$353,345. The Association had payables to Daniel Island Town Association, Inc. of \$473 at December 31, 2017.

9. Future Major Repairs and Replacements

The Association's governing documents require funds to be accumulated for future major repairs and replacements. Funds are being accumulated in the replacement fund based on estimated future costs for repairs and replacements of common property components and estimates of when the repairs and replacements will be needed. Accumulated replacement funds are retained in bank accounts separate from operating amounts and are generally not available for operating expenditures.

The estimates of both anticipated costs and timing of expenditures are subject to review and revision based on circumstances as they occur. Actual expenditures and investment income may vary from the estimated amounts, the variations may be material and amounts accumulated in the replacement fund may not be adequate to meet all future needs for major repairs and replacements. If additional funds are needed, the Association has the right to increase regular assessments, pass special assessments or delay replacements until funds are available.

Supplementary Information

Supplementary Information on Future Major Repairs and Replacements (Unaudited)

December 31, 2017

The following table is derived from a reserve study conducted for Daniel Island Park Association, Inc. in 2017 and presents significant information regarding the components of future repairs and replacements of common property. Estimated replacement costs are based on the component's original cost, where available and do not take into account the effects of inflation between the date of the study and the date that the components will require replacement.

| <u>Component/Area</u> | <u>Estimated Replacement Cost (Total)</u> | <u>Replacement Fund Balance</u> | <u>Estimated Remaining Useful Life (Years)</u> |
|------------------------|---|-------------------------------------|--|
| Great Oak Park | \$ 221,050 | | 0-15 |
| Grove Park | 14,150 | | 0-9 |
| Beckon Park | 11,850 | | 1 |
| Balfour Park | 28,300 | | 2-7 |
| Cattle Trough Park | 10,450 | | 6-12 |
| Butterfly Pond | 177,000 | | 2-17 |
| Ralston grove | 30,000 | | 19 |
| Ithecaw creek fountain | 11,000 | | 2 |
| Ralston cemetery | 9,000 | | 15 |
| Saucy jack streetscape | 26,000 | | 0-12 |
| Fish tale | 17,500 | | 19 |
| Miscellaneous | <u>96,600</u> | | 0-12 |
| Total | <u>\$ 652,900</u> | <u>\$ 409,017</u> | |

See independent auditors' report.