

**KIAWAH ISLAND
COMMUNITY ASSOCIATION, INC.**

KIAWAH ISLAND, SOUTH CAROLINA

AUDITED FINANCIAL STATEMENTS

DECEMBER 31, 2018 AND 2017

KIAWAH ISLAND COMMUNITY ASSOCIATION, INC.

INDEPENDENT AUDITORS' REPORT

AND

AUDITED FINANCIAL STATEMENTS

DECEMBER 31, 2018 AND 2017

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Mike Feldman – Treasurer
Rajan Govindan
Lynn Morgenstern
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Independent Auditors' Report

February 25, 2019

The Board of Directors
Kiawah Island Community Association, Inc.
Kiawah Island, South Carolina

We have audited the accompanying financial statements of Kiawah Island Community Association, Inc. (the "Association"), which comprise the balance sheets as of December 31, 2018 and 2017, and the related statements of revenues, expenses and changes in fund balance, comprehensive income 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.

Auditors' 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 audits 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 auditors' 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 Kiawah Island Community Association, Inc. as of December 31, 2018 and 2017, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

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 on page 23 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, who 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 audits 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.

Johnson & Co., P.A.

KIAWAH ISLAND COMMUNITY ASSOCIATION, INC.

BALANCE SHEETS

AS OF DECEMBER 31, 2018 AND 2017

	<u>2018</u>	<u>2017</u>
CURRENT ASSETS		
Cash - undesignated	\$ 2,908,394	\$ 6,997,266
Accounts receivable (less allowance for doubtful accounts of \$6,415 and \$21,500, respectively)	100,153	87,487
Accounts receivable - other	325	28,637
Royalty receivable	41,200	37,500
Prepaid expenses	<u>198,848</u>	<u>170,133</u>
Total current assets	3,248,920	7,321,023
 NON-CURRENT ASSETS		
Property and equipment, at cost (less accumulated depreciation of \$2,462,723 and \$2,292,302, respectively)	3,194,826	3,182,493
 DESIGNATED ASSETS		
Cash - designated	607,307	2,244,384
Investments - designated	6,979,911	4,867,151
Accrued interest receivable - designated	<u>32,713</u>	<u>35,328</u>
Total designated assets	<u>7,619,931</u>	<u>7,146,863</u>
 TOTAL ASSETS	 <u>\$ 14,063,677</u>	 <u>\$ 17,650,379</u>

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

KIAWAH ISLAND COMMUNITY ASSOCIATION, INC.

BALANCE SHEETS

AS OF DECEMBER 31, 2018 AND 2017

	<u>2018</u>	<u>2017</u>
CURRENT LIABILITIES		
Accounts payable	\$ 202,764	\$ 1,286,696
Accrued payroll and payroll taxes/withholdings	136,633	100,646
Accrued annual leave	311,362	281,849
Deferred revenue - prepaid assessments	303,141	62,290
Accrued expenses	515,691	18,931
Deferred revenue - royalty income	50,156	50,156
Mortgage payable	58,682	56,471
Deposits held	<u>40,619</u>	<u>28,263</u>
Total current liabilities	1,619,048	1,885,302
NONCURRENT LIABILITIES		
Deferred revenue - royalty income	351,095	401,251
Mortgage payable	<u>1,397,440</u>	<u>1,456,122</u>
Total noncurrent liabilities	<u>1,748,535</u>	<u>1,857,373</u>
Total liabilities	<u>3,367,583</u>	<u>3,742,675</u>
FUND BALANCES		
Accumulated excess of revenues over expenses (undesignated)	4,210,996	7,797,828
Accumulated excess of revenues over expenses (designated)	6,824,370	6,151,300
Accumulated other comprehensive income (loss)	<u>(339,272)</u>	<u>(41,424)</u>
Total fund balances	<u>10,696,094</u>	<u>13,907,704</u>
TOTAL LIABILITIES AND FUND BALANCES	<u>\$ 14,063,677</u>	<u>\$ 17,650,379</u>

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

KIAWAH ISLAND COMMUNITY ASSOCIATION, INC.
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN FUND BALANCES
FOR THE YEAR ENDED DECEMBER 31, 2018

	UNDESIGNATED					DESIGNATED			
	Total	General Operations Fund	Recreation Center Fund	Vanderhorst Gate Fund	Personal and Real Property Fund	Major Repair and Replacements Fund (MR&R)	Vanderhorst Gate Fund	Preserve Fence Fund	Landscape Capital Improvements
REVENUES									
Assessments	\$ 9,898,160	\$ 7,686,044	\$ 621,609	\$ 197,113	\$ -	\$ 1,364,176	\$ -	\$ 29,218	\$ -
Late charges	23,493	20,607	1,776	1,110	-	-	-	-	-
Investment income	200,077	27,651	1,285	7,130	28,821	135,083	-	107	-
Royalty income	258,416	258,416	-	-	-	-	-	-	-
Other income	580,977	266,466	314,511	-	-	-	-	-	-
Initiation fees	88,510	-	88,510	-	-	-	-	-	-
Contribution to reserve	1,738,296	-	-	-	-	1,738,296	-	-	-
Vehicle access fee revenue	1,686,315	1,186,311	-	-	-	500,004	-	-	-
GROSS REVENUES	14,474,244	9,445,495	1,027,691	205,353	28,821	3,737,559	-	29,325	-
EXPENSES AND OTHER GAINS/LOSSES									
General and administrative	2,487,750	2,483,569	-	-	4,181	-	-	-	-
Land management	2,305,183	2,305,183	-	-	-	-	-	-	-
Lakes management	253,362	253,362	-	-	-	-	-	-	-
General maintenance	652,132	646,466	-	-	5,666	-	-	-	-
Security - main gate	1,677,769	1,677,769	-	-	-	-	-	-	-
Mechanic's shop	267,468	267,468	-	-	-	-	-	-	-
Livability	286,011	286,011	-	-	-	-	-	-	-
Sandcastle operations	1,494,509	-	1,465,957	-	28,552	-	-	-	-
Security - second gate	200,181	-	-	200,181	-	-	-	-	-
Depreciation	404,430	-	-	-	404,430	-	-	-	-
Loss (gain) on sale of property and equipment	(601)	(3,841)	3,240	-	-	-	-	-	-
Loss (gain) on sale of investments	-	-	-	-	-	-	-	-	-
Major repairs and replacements	7,083,172	-	-	-	-	7,083,172	-	-	-
Landscape improvements	276,640	-	-	-	-	-	-	33,010	243,630
TOTAL EXPENSES AND OTHER GAINS/LOSSES	17,388,006	7,915,987	1,469,197	200,181	442,829	7,083,172	-	33,010	243,630
EXCESS (DEFICIT) REVENUES OVER EXPENSES	(2,913,762)	1,529,508	(441,506)	5,172	(414,008)	(3,345,613)	-	(3,685)	(243,630)
ACCUMULATED EXCESS - January 1, 2018	13,949,128	2,968,424	33,129	-	4,796,275	5,775,574	361,502	14,224	-
Transfer to/from other funds	-	(3,657,717)	408,377	-	(1,016,658)	4,022,368	-	-	243,630
ACCUMULATED EXCESS - December 31, 2018	\$ 11,035,366	\$ 840,215	\$ -	\$ 5,172	\$ 3,365,609	\$ 6,452,329	\$ 361,502	\$ 10,539	\$ -

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

KIAWAH ISLAND COMMUNITY ASSOCIATION, INC.
STATEMENT OF COMPREHENSIVE INCOME
FOR THE YEAR ENDED DECEMBER 31, 2018

	<u>UNDESIGNATED</u>					<u>DESIGNATED</u>			
	<u>Total</u>	<u>General Operations Fund</u>	<u>Recreation Center Fund</u>	<u>Vanderhorst Gate Fund</u>	<u>Personal and Real Property Fund</u>	<u>Major Repair and Replacements Fund (MR&R)</u>	<u>Vanderhorst Gate Fund</u>	<u>Preserve Fence Fund</u>	<u>Landscape Capital Improvements</u>
EXCESS (DEFICIT) REVENUES OVER EXPENSES	\$ (2,913,762)	\$ 1,529,508	\$ (441,506)	\$ 5,172	\$ (414,008)	\$ (3,345,613)	\$ -	\$ (3,685)	\$ (243,630)
<u>OTHER COMPREHENSIVE INCOME</u>									
Unrealized gain (loss) on investments	(297,848)	-	-	-	(57,664)	(234,745)	(5,439)	-	-
COMPREHENSIVE INCOME (LOSS)	\$ (3,211,610)	\$ 1,529,508	\$ (441,506)	\$ 5,172	\$ (471,672)	\$ (3,580,358)	\$ (5,439)	\$ (3,685)	\$ (243,630)

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

KIAWAH ISLAND COMMUNITY ASSOCIATION, INC.
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN FUND BALANCES
FOR THE YEAR ENDED DECEMBER 31, 2017

	UNDESIGNATED					DESIGNATED			
	Total	General Operations Fund	Recreation Center Fund	Vanderhorst Gate Fund	Personal and Real Property Fund	Major Repair and Replacements Fund (MR&R)	Vanderhorst Gate Fund	Preserve Fence Fund	Landscape Capital Improvements
REVENUES									
Assessments	\$ 10,799,573	\$ 8,632,018	\$ 586,411	\$ 200,773	\$ -	\$ 1,357,241	\$ -	\$ 23,130	\$ -
Late charges	27,697	26,496	994	176	-	-	-	31	-
Investment income	153,963	24,708	1,159	1,451	4,938	121,661	-	46	-
Royalty income	228,606	228,606	-	-	-	-	-	-	-
Other income	661,029	364,651	296,378	-	-	-	-	-	-
Initiation fees	76,820	-	76,820	-	-	-	-	-	-
Contribution to reserve	1,480,684	-	-	-	-	1,480,684	-	-	-
Vehicle access fees	1,567,808	1,067,804	-	-	-	500,004	-	-	-
GROSS REVENUES	14,996,180	10,344,283	961,762	202,400	4,938	3,459,590	-	23,207	-
EXPENSES AND OTHER GAINS AND LOSSES									
General and administrative	3,012,019	3,012,019	-	-	-	-	-	-	-
Land management	2,661,886	2,661,886	-	-	-	-	-	-	-
Lakes management	391,305	378,245	-	-	13,060	-	-	-	-
General maintenance	595,567	595,567	-	-	-	-	-	-	-
Security - main gate	1,541,004	1,495,595	-	-	45,409	-	-	-	-
Mechanic's shop	244,674	244,674	-	-	-	-	-	-	-
Livability	264,773	257,824	-	-	6,949	-	-	-	-
Sandcastle operations	1,214,890	-	1,214,890	-	-	-	-	-	-
Security - second gate	215,425	-	-	215,425	-	-	-	-	-
Depreciation	400,420	-	-	-	400,420	-	-	-	-
Loss (gain) on sale of property and equipment	(24,813)	(26,213)	1,400	-	-	-	-	-	-
Loss (gain) on sale of investments	2,868	-	-	-	-	2,868	-	-	-
Major repairs and replacements	5,533,915	-	-	-	-	5,533,915	-	-	-
Landscape improvements	303,264	-	-	-	-	-	-	23,368	279,896
TOTAL EXPENSES AND OTHER GAINS/LOSSES	16,357,197	8,619,597	1,216,290	215,425	465,838	5,536,783	-	23,368	279,896
EXCESS (DEFICIT) REVENUES OVER EXPENSES	(1,361,017)	1,724,686	(254,528)	(13,025)	(460,900)	(2,077,193)	-	(161)	(279,896)
ACCUMULATED EXCESS - January 1, 2017	15,310,145	3,335,504	79,536	-	4,802,804	6,716,406	374,527	1,368	-
Transfer to/from other funds	-	(2,091,766)	208,121	13,025	454,371	1,136,361	(13,025)	13,017	279,896
ACCUMULATED EXCESS - December 31, 2017	\$ 13,949,128	\$ 2,968,424	\$ 33,129	\$ -	\$ 4,796,275	\$ 5,775,574	\$ 361,502	\$ 14,224	\$ -

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

KIAWAH ISLAND COMMUNITY ASSOCIATION, INC.
STATEMENT OF COMPREHENSIVE INCOME
FOR THE YEAR ENDED DECEMBER 31, 2017

	<u>UNDESIGNATED</u>					<u>DESIGNATED</u>			
	<u>Total</u>	<u>General Operations Fund</u>	<u>Recreation Center Fund</u>	<u>Vanderhorst Gate Fund</u>	<u>Personal and Real Property Fund</u>	<u>Major Repair and Replacements Fund (MR&R)</u>	<u>Vanderhorst Gate Fund</u>	<u>Preserve Fence Fund</u>	<u>Landscape Capital Improvements</u>
EXCESS (DEFICIT) REVENUES OVER EXPENSES	\$ (1,361,017)	\$ 1,724,686	\$ (254,528)	\$ (13,025)	\$ (460,900)	\$ (2,077,193)	\$ -	\$ (161)	\$ (279,896)
OTHER COMPREHENSIVE INCOME									
Unrealized gain (loss) on investments	\$ (29,386)	-	-	-	-	\$ (29,386)	-	-	-
COMPREHENSIVE INCOME (LOSS)	<u>\$ (1,390,403)</u>	<u>\$ 1,724,686</u>	<u>\$ (254,528)</u>	<u>\$ (13,025)</u>	<u>\$ (460,900)</u>	<u>\$ (2,106,579)</u>	<u>\$ -</u>	<u>\$ (161)</u>	<u>\$ (279,896)</u>

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

KIAWAH ISLAND COMMUNITY ASSOCIATION, INC.

STATEMENTS OF CASH FLOWS

FOR THE YEARS ENDED DECEMBER 31, 2018 AND 2017

	2018	2017
CASH FLOWS FROM OPERATING ACTIVITIES		
Excess (deficit) revenues over expenses	\$ (2,913,762)	\$ (1,361,017)
Adjustments to reconcile excess (deficit) revenues over expenses to net cash flow provided by (used in) operating activities:		
Depreciation	404,430	400,420
Provision for losses on receivables	(15,085)	(13,500)
Loss (gain) on sale of property and equipment	(601)	(24,813)
Amortization of bond premiums and discounts	39,696	50,510
(Increase) decrease in:		
Accounts receivable	2,422	1,124,441
Accounts receivable - other	28,312	466
Royalty receivable	(3,700)	-
Accrued interest on investments	2,615	(2,695)
Prepaid expenses	(28,715)	114,374
Increase (decrease) in:		
Accounts payable	(1,083,932)	864,665
Accrued payroll and payroll taxes/withholdings	35,987	9,744
Accrued annual leave	29,513	1,181
Prepaid assessments	240,851	32,406
Accrued expenses	496,760	(161,671)
Deferred revenue - royalty income	(50,156)	(50,156)
Deposits held	12,356	16,626
	(2,803,009)	1,000,981
NET CASH FLOWS PROVIDED BY (USED IN) OPERATING ACTIVITIES		
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of property and equipment	(425,437)	(327,215)
Proceeds from sale of property and equipment	9,276	38,500
Purchase of investments	(3,058,338)	(1,310,644)
Proceeds from maturities of debt securities	608,030	900,686
	608,030	900,686

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

KIAWAH ISLAND COMMUNITY ASSOCIATION, INC.

STATEMENTS OF CASH FLOWS

FOR THE YEARS ENDED DECEMBER 31, 2018 AND 2017

	<u>2018</u>	<u>2017</u>
NET CASH FLOWS PROVIDED BY (USED IN)		
INVESTING ACTIVITIES	<u>(2,866,469)</u>	<u>(698,673)</u>
CASH FLOWS FROM FINANCING ACTIVITIES		
Principal payments on mortgage	<u>(56,471)</u>	<u>(53,686)</u>
NET CASH FLOWS PROVIDED BY (USED IN)		
INVESTING ACTIVITIES	<u>(56,471)</u>	<u>(53,686)</u>
NET INCREASE (DECREASE) IN CASH	(5,725,949)	248,622
CASH AND CASH EQUIVALENTS, beginning of year	<u>9,241,650</u>	<u>8,993,028</u>
CASH AND CASH EQUIVALENTS, end of year	<u>\$ 3,515,701</u>	<u>\$ 9,241,650</u>
<u>CASH SUMMARY</u>		
Undesignated	\$ 2,908,394	\$ 6,997,266
Designated	<u>607,307</u>	<u>2,244,384</u>
TOTALS	<u>\$ 3,515,701</u>	<u>\$ 9,241,650</u>
<u>SUPPLEMENTAL INFORMATION</u>		
Amount of Interest Paid	<u>\$ 55,106</u>	<u>\$ 59,405</u>

SUPPLEMENTAL DISCLOSURES OF NON-CASH TRANSACTIONS

The Association records its investments that are classified as available-for-sale at their fair market value. In accordance with this method of reporting investments, the Association recorded unrealized gains (losses) of (\$297,848) and (\$29,386) in 2018 and 2017, respectively.

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

KIAWAH ISLAND COMMUNITY ASSOCIATION, INC.
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2018 AND 2017

Note 1 – Nature of Organization

Kiawah Island Community Association, Inc. (the Association) is a non-profit, non-stock, corporate property owners' association whose Declaration of Covenants and Restrictions of the Kiawah Island Community Association, Inc. were adopted December 21, 1977. On July 8, 2010, the Internal Revenue Service approved the Association's application to be treated as a tax-exempt entity. The Association's primary purpose is to maintain the common areas and provide various services for property owners of Kiawah Island Community Association, Inc.

The Association is geographically located on Kiawah Island which is approximately 10,000 acres in size and lies within a coastal region 21 miles south of Charleston, South Carolina. The Association consists of approximately 4,298 residential properties, of which approximately 86.78% are improved, 62 commercial properties and various common areas including roads, lakes and lagoons, recreational facilities, pathways, nature trails and various other forms of infrastructure. The Association occupies the majority of the total area of Kiawah Island, SC and the number of properties within the Association is the largest of all total properties located on Kiawah Island.

Note 2 – Summary of Significant Accounting Policies

Accounting Method

The Association uses the accrual method of accounting whereby revenues are recognized when earned and expenses when incurred.

Fund Basis of Accounting

To ensure observance of limitations and restrictions on the use of financial resources, the Association maintains its accounts using fund accounting for reporting purposes. Disbursements from the operating fund are for operating costs and are generally at the discretion of the board of directors and Association management. Disbursements from reserve funds may only be utilized in accordance with the established purposes for accumulation. Replacement disbursements are comprised of building repairs, pavement resurfacing, infrastructure replacements and other similar repairs or additions. Financial resources are classified for accounting and reporting purposes in the following funds which are established according to their nature and purpose:

- General Operations Fund - used to account for financial resources available for the general daily operations of the Association.
- Recreation Center Fund - provides funds for operations of the recreation community center activities.
- Personal and Real Property Fund - accounts for capitalized property and accumulates funds designated for replacement of capital assets.
- Preserve Fence Fund - accounts for future repairs and maintenance of the split rail fence and for other extraordinary land management costs in the Preserve neighborhood.

KIAWAH ISLAND COMMUNITY ASSOCIATION, INC.
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2018 AND 2017

Note 2 – Summary of Significant Accounting Policies (continued)

Fund Basis of Accounting (continued)

- Vanderhorst Gate Fund - provides funds for the operations of a second security gate.
- Major Repair and Replacements Fund and Landscape Capital Improvements Fund - used to accumulate funds designated for future major repairs and replacements of existing facilities and equipment, board-approved capital projects, major landscape repairs and replacements and ongoing landscape capital projects.

Cash Equivalents

For purpose of the statement of cash flows, the association considers all highly liquid debt instruments purchased with a maturity of three months or less to be cash equivalents. This includes any operating bank accounts, interest-bearing money market funds and deposit accounts.

Allowance for Doubtful Accounts

Assessments are considered delinquent after thirty days of nonpayment and a late fee of 1.5% of the unpaid balance is charged monthly. The Association's policy is to retain legal counsel and place liens on the properties of those members whose assessments are 120 days or more delinquent. The Association provides an allowance for doubtful accounts equal to the estimated uncollectible portion of assessments receivable. The amount calculated is based on the balance of outstanding assessments receivable on properties in foreclosure at the end of the year and its prior history of assessments deemed uncollectible. As of December 31, 2018 and 2017, the Association's allowance for doubtful accounts was \$6,415 and \$21,500, respectively, and bad debt expense (recovery) totaled \$2,895 and (\$9,489) for 2018 and 2017, respectively.

Property and Equipment

Property and equipment, with both an estimated useful life of more than one year and a cost of more than \$2,500 when purchased, are accounted for on the balance sheet at their original cost amount. Depreciation is provided using the straight-line method of calculation over the estimated useful lives of the respective assets. Maintenance and repair costs are charged to expenses as incurred; major renovations and improvements are capitalized.

The Association owns significant amounts of real property and improvements as follows: common areas and rights of way, roadways, leisure trails and lakes. These properties are being conveyed periodically to the Association for the consideration of \$1 under an agreement with the developer or conveyed by means of a 99-year lease agreement. These common properties are real property directly associated with the individual ownership of member properties and dedicated for the use of the entire community. They cannot be sold and thus have no fair market value other than that related to their intended use. In conformity with industry practice, such assets are not accounted for in the financial statements of the Association. The Association is responsible for the upkeep, repair, maintenance and improvement of these assets. Replacements and improvements to the common area assets are expensed as incurred.

KIAWAH ISLAND COMMUNITY ASSOCIATION, INC.
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2018 AND 2017

Note 2 – Summary of Significant Accounting Policies (continued)

Investment Securities

As of December 31, 2018 and 2017 investments held by the company consists of both debt and equity securities which, in accordance with Accounting Standards Codification (ASC) 320-10, *Accounting for Certain Investments in Debt and Equity Securities*, are classified into the following categories: (a) *trading*, (b) *available-for-sale*, and (c) *held-to-maturity*. While not precluded from being categorized as *trading* or *held-to-maturity*, as of December 31, 2018 investment securities owned by the Association are classified as *available-for-sale*.

Securities considered to be available-for-sale are recorded at fair value with unrealized holding gains and losses being excluded from earnings and instead are reported as a separate component of accumulated other comprehensive income. Realized gains and losses, which result from the actual sale of securities, are determined on a specific-identification basis.

Investments are considered impaired when the associated fair value has declined below the investment's adjusted cost basis. If an impairment is determined to be *other-than-temporary*, the cost basis of the investment is adjusted/decreased to the current fair value and the impairment loss is charged against earnings at that time. To determine whether an impairment is *other-than-temporary*, the Association 1) considers whether it has both the ability and intent to hold the investment until a subsequent market price recovery and 2) examines whether any evidence that indicates the cost of the investment may be recoverable outweighs any indications to the contrary. During this assessment, the following factors are examined: reasons for the impairment, the severity and possible duration of the impairment, any change in value subsequent to year-end, forecasted performance of the investee and the general market condition in the geographic area or industry in which the investee operates. Because the Association has both the intent and ability to hold securities until a market price recovery or maturity, investment securities at December 31, 2018 are not considered to be *other-than-temporarily* impaired. There were no impairments recognized by the Association during the years ended December 31, 2018 and December 31, 2017.

Fair Value Measurements

The Association applies generally accepted accounting principles (GAAP) for fair value measurements of financial assets which, on a recurring basis, are recognized or disclosed at fair value in the financial statements. GAAP defines fair value as either the price on the measurement date that would either be (a) received to sell an asset or (b) paid to transfer a liability in an orderly transaction between market participants. GAAP also establishes a framework for measuring fair value and expands disclosures about fair value measurements. See Note 7 for further information.

Contribution to Reserve Fees

Those who purchase applicable property within the Association pay, at closing, a fee in the amount of 0.50% of the gross purchase price of the property. Amounts collected from these transactions are designated for major repairs and replacements and landscape capital improvements.

KIAWAH ISLAND COMMUNITY ASSOCIATION, INC.
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2018 AND 2017

Note 2 – Summary of Significant Accounting Policies (continued)

Uninsured Cash Balance

The Association maintains a portion of its cash balances at several banks and invests the balance in money market funds. Cash balances are insured through the Federal Deposit Insurance Corporation (FDIC) for a maximum of \$250,000 at each bank in which the Association has funds invested. This coverage, however, does not protect against losses from any change in the market value of investments. As of December 31, 2018, the Association's uninsured balances totaled \$2,487,421. The Association manages this risk by depositing with reputable financial institutions and believes there is no significant possibility of loss with respect to these deposits.

Assessments

To provide funds for the Association's operating expenses, members are subject to annual assessments. Amounts assessed for unimproved and improved properties (for type A residential) ranged between \$913 to \$1,922 and \$910 to \$1,915 for 2018 and 2017, respectively. In addition, the board approved a supplemental annual assessment in 2018 and 2017 of \$150 for unimproved and \$300 for improved properties. This assessment is designated by the board to provide revenue for the reserve fund for infrastructure repair and replacement. In October 2017, the board approved an additional supplemental annual assessment of \$113 for unimproved and \$225 for improved properties, and totaling \$1,018,516, to help fund the ongoing clean-up and necessary repairs following Tropical Storm Irma which brought winds and flooding to South Carolina on September 11, 2017. These storm assessments were not designated for scheduled major repairs and replacements; accordingly, they are reported as a part of general operations fund assessments on the statement of revenues, expenses, and changes in fund balance. However, funds were transferred from the operating fund to designated MRR funds to the extent that those designated funds incurred expenses related to the storms. The annual budgets and member's assessments are determined by the Board of Directors, within the restrictions imposed by the governing documents. The Association retains excess funds at the end of the operating year, if any, for use in future periods.

Vehicle Access Fee Revenue

The Association charges an access fee to commercial entities that need to enter the Association for business purposes. The amount of the fee charged is determined annually by the board of directors and revenues from these fees consist of both annual and daily passes purchased by businesses. Fees are accumulated in the general operations fund to provide amounts for future road and drainage repairs and replacements. Total fee revenues for 2018 and 2017 were \$1,686,315 and \$1,567,808, respectively. During 2018 and 2017, \$500,004 of these fees were designated by the board for future major repairs and replacements.

Date of Management's Review

In preparing the financial statements, the Association has evaluated events and transactions for potential recognition or disclosure through February 25, 2019, the date that the financial statements were available to be issued.

KIAWAH ISLAND COMMUNITY ASSOCIATION, INC.
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2018 AND 2017

Note 2 – Summary of Significant Accounting Policies (continued)

Deferred Revenue – Prepaid Assessments

Prepaid assessment deferred revenues consist of assessment amounts applicable for the 2019 operating cycle but received from members prior to December 31, 2018. In the year in which they are received, deferred revenues are recorded on the balance sheet as a liability and then subsequently, in the year in which it is earned, reclassified to a revenue account on the *Statement of Revenues, Expenses and Changes in Fund Balance*. Deferred revenues related to prepaid assessments totaled \$303,141 and \$62,290 for the years ended December 31, 2018 and 2017, respectively.

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 asset 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.

Note 3 – Comprehensive Income

The Association complies with the provisions of ASC 220, *Comprehensive Income*, which establishes rules for the reporting and presentation of comprehensive income and its components. Accounting principles generally require that recognized revenues, expenses, gains and losses be included in net income. However, certain changes in assets and liabilities, including unrealized gains and losses on available-for-sale securities, are reported as a separate component of the equity section of the balance sheet and, along with net income, are components of comprehensive income. The components and changes of other comprehensive income for 2018 and 2017 are as follows:

	<u>2018</u>	<u>2017</u>
Unrealized gains (losses) on available-for-sale securities	\$ (297,848)	\$ (29,386)
Total other comprehensive income (loss)	<u>\$ (297,848)</u>	<u>\$ (29,386)</u>
	<u>2018</u>	<u>2017</u>
Accumulated other comprehensive income (loss), beginning balance	\$ (41,424)	\$ (12,038)
Change during the year	<u>(297,848)</u>	<u>(29,386)</u>
Accumulated other comprehensive income (loss), ending balance	<u>\$ (339,272)</u>	<u>\$ (41,424)</u>

KIAWAH ISLAND COMMUNITY ASSOCIATION, INC.
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2018 AND 2017

Note 4 – Property and Equipment

Depreciation expense for the years ended December 31, 2018 and 2017 was \$404,430 and \$400,420, respectively. Major classifications of property and equipment and their respective useful lives as of December 31 are as follows:

Description	Estimated Lives	2018	2017
Land	non-depreciable	\$ 440,253	\$ 440,253
Buildings and improvements	5-40 yrs.	2,530,342	2,531,828
Furniture and equipment	3-15 yrs.	1,864,846	1,671,486
Vehicles and trailers	5-10 yrs.	822,108	831,228
		<u>5,657,549</u>	<u>5,474,795</u>
Less: accumulated depreciation		<u>(2,462,723)</u>	<u>(2,292,302)</u>
Total property and equipment, net		<u>\$ 3,194,826</u>	<u>\$ 3,182,493</u>

Note 5 – Future Major Repairs and Replacements

The Association's governing documents provide for the levying of an annual general-purpose assessment which, in addition to providing funds for general operations of the Association, also provide for the repair and maintenance of the common areas. Accumulated funds, which aggregate \$6,824,370 and \$6,151,300 as of December 31, 2018 and 2017, respectively, are maintained in separate accounts and are not available for general operating purposes.

An independent review of future expected infrastructure repair and replacement costs was conducted by an independent third-party consultant and their findings were compiled into a reserve study document issued on December 17, 2018. There may be variances between the expenditure amounts the reserve study estimates and the actual costs incurred and those variations may be material. Over the last five-year period, expenditures for major repairs and maintenance have averaged \$4,570,454. To aid with funding for these future expected costs, the Association annually allocates a portion of assessment revenues to reserve funds. Over the last five-year period, these amounts have averaged \$1,538,389. In addition, to further fund these expenditures, in 2018 and 2017 the board approved a supplemental annual assessment totaling \$1,364,176 and \$1,357,241, respectively and also designated \$500,004 of vehicle access fee revenue to the reserve fund in both 2018 and 2017 as well. It is possible that amounts accumulated in the major repair and replacement funds and annual sources of revenue may not be adequate to meet all future needs for major repairs and replacements. This, in turn, may require the Association to consider alternate sources of revenue to ensure continued funding of necessary repair and replacement projects. In order to accomplish this, the Association has the right to (1) increase, up to the maximum amount set forth in the covenants, annual assessments; (2) levy special assessments, subject to member approval; (3) transfer funds from operations; or (4) delay repairs and replacements until funds are available.

KIAWAH ISLAND COMMUNITY ASSOCIATION, INC.
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2018 AND 2017

Note 6 – Investments

Maturities of debt securities classified as available-for-sale were as follows at December 31, 2018:

<u>Available for sale:</u>	<u>Cost</u>	<u>Fair Value</u>
Due before one year	\$ 1,168,399	\$ 1,185,892
Due one through five years	<u>3,890,878</u>	<u>3,786,756</u>
Totals	<u>\$ 5,059,277</u>	<u>\$ 4,972,648</u>

Proceeds from maturities of debt securities and from the sale of investment securities classified as available-for-sale were \$1,594,901 in 2018 and \$900,686 in 2017; gross realized gains in 2018 and 2017 were \$-0- and \$2,868, respectively.

The cost, gross unrealized holding gains, gross unrealized holding losses and fair value of available-for-sale investment securities by major security type and class of security as of December 31, 2018 and 2017 are as follows:

Description	Cost	Gross Unrealized Holding Gains/(Losses)	Fair value
		December 31, 2018	
Certificates of deposit	\$ 1,250,000	\$ (15,290)	\$ 1,234,710
Corporate bonds	3,242,945	(92,885)	3,150,060
U.S. Treasury investments	566,331	21,552	587,883
Mutual funds	<u>2,259,907</u>	<u>(252,649)</u>	<u>2,007,258</u>
Totals	<u>\$ 7,319,183</u>	<u>\$ (339,272)</u>	<u>\$ 6,979,911</u>
		December 31, 2017	
Certificates of deposit	\$ 450,000	\$ 2,798	\$ 452,798
Corporate bonds	3,871,046	(43,045)	\$ 3,828,001
U.S. Treasury investments	<u>587,529</u>	<u>(1,177)</u>	<u>586,352</u>
Totals	<u>\$ 4,908,575</u>	<u>\$ (41,424)</u>	<u>\$ 4,867,151</u>

KIAWAH ISLAND COMMUNITY ASSOCIATION, INC.
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2018 AND 2017

Note 7 – Fair Value Measurements

The Association applies GAAP for fair value measurements of financial assets that are recognized or disclosed at fair value in the financial statements on a recurring basis. GAAP establishes 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 measurements) and the lowest priority to measurements involving significant unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are as follows:

- Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the Association has the ability to access at the measurement date.
- Level 2 inputs are inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly.
- Level 3 inputs are unobservable inputs for the asset or liability.

The level in the fair value hierarchy within which a fair measurement in its entirety falls is based on the lowest level input that is significant to the fair value measurement in its entirety. The following tables present assets that are measured at fair value on a recurring basis at December 31, 2018 and 2017:

Fair Value Measurements at Reporting Date Using:

Total at December 31, 2018	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
<u>\$ 6,979,911</u>	<u>\$ 6,979,911</u>	<u>\$ -</u>	<u>\$ -</u>

Fair Value Measurements at Reporting Date Using:

Total at December 31, 2017	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
<u>\$ 4,867,151</u>	<u>\$ 4,867,151</u>	<u>\$ -</u>	<u>\$ -</u>

KIAWAH ISLAND COMMUNITY ASSOCIATION, INC.
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2018 AND 2017

Note 8 – Deferred Royalty Income

On December 30, 2014, the Association entered into an agreement with Comcast of Georgia/South Carolina II, LLC (Comcast), to allow Comcast use of easements within the association to install and maintain broadband services on Kiawah Island and to allow exclusive use of the Association's name in marketing materials. The term of this agreement is twelve years, with automatic one-month renewal periods thereafter until either party terminates the agreement. Comcast paid the Association an initial payment of \$802,500, based upon the number of residential units, which was due within 90 days of execution of the contract. An additional per unit payment will be due for any additional units added in the future.

The Association engaged a consulting firm to help negotiate and secure the Comcast agreements described above. The terms of the agreement with the consultant specify that the Association will pay the consultant a commission equal to 25% of all monies received from Comcast throughout the life of the contract.

At December 31, 2014, the initial fee was recorded, net of the related commission, as deferred income and as a royalty receivable in the amount of \$601,875. The deferred income is being amortized over the twelve-year term of the contract. As of December 31, 2018 and 2017, the balance of the deferred revenue totaled \$401,251 and \$451,407, respectively, and the net related royalty income was \$67,656 and \$62,094 for 2018 and 2017, respectively.

In addition to the per unit fee described above, the Association also entered into a concurrent twelve-year agreement with Comcast whereby the Association will receive a percentage, varying from 0% to 9%, of the broadband service revenue that Comcast receives from the Association's members based upon the overall number of Association residential units that subscribe to Comcast's services. This will be calculated and paid on a quarterly basis. A related 25% commission will be paid on these amounts. The net amount of this royalty income for 2018 and 2017 totaled \$190,760 and \$166,513, respectively.

Note 9 – Mortgage Payable

In October 2016, the Association entered into a mortgage in the amount of \$1,575,000 to finance the purchase of the building that houses its administrative offices. The mortgage bore interest at a rate of 3.8% and is payable in one hundred and nineteen principal and interest monthly payments of \$9,424 with a final payment of \$946,597 due on October 19, 2026. In January 2018, the interest rate of the loan was reduced to 3.65% which lowered monthly payments to \$9,298 and reduced the final payment, which remains due on October 19, 2026, to \$942,390. The mortgage is secured by the building, the Association's personal property and any rental/lease income associated with the building. The mortgage also requires the Association to maintain the banking account it holds with the mortgage holder and gives the mortgage holder a right of offset against any cash or investment accounts held at the mortgage holder in the event of default.

KIAWAH ISLAND COMMUNITY ASSOCIATION, INC.
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2018 AND 2017

Note 9 – Mortgage Payable (continued)

As of December 31, 2018 and 2017, the balance of the mortgage was \$1,456,122 and \$1,512,593, respectively. Interest costs paid totaled \$55,106 and \$59,405 during 2018 and 2017, respectively. Mortgage debt service requirements to maturity are as follows:

Year Ending <u>December 31,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2019	58,682	52,896	111,578
2020	60,746	50,831	111,577
2021	63,177	48,400	111,577
2022	65,555	46,022	111,577
2023	68,023	43,555	111,578
2024-2026	<u>1,139,939</u>	<u>109,287</u>	<u>1,249,226</u>
Total	<u><u>1,456,122</u></u>	<u><u>350,991</u></u>	<u><u>1,807,113</u></u>

The Association was leasing a portion of the building to the former owner until the earlier of eighteen months or forty-five days after the former owner receives a certificate of occupancy on their new building. During this term, rent was fixed at \$7,656 plus a percentage of certain operating costs. In August 2017 the former tenant vacated the property and the agreement concluded. During the year ended December 31, 2017, the Association received rent revenues in the amount of \$78,762.

Note 10 – Line of Credit

The Association has a line of credit that carries a variable interest rate equal to LIBOR plus 2.00%. The line is secured by a right of offset against bank and investment accounts the Association maintains with the lender. The total amount of credit available from the line of credit to the Association is \$2,500,000 and the current maturity date is August 4, 2019. The Association took no draws against the line during the years ended December 31, 2018 and 2017 and accordingly had no outstanding balances due.

Note 11 – Federal and State Income Taxes

In December 2008, the Association filed an exemption application (Form 1024 – Application for Recognition of Exemption Under Section 501(a)) with the Internal Revenue Service to be recognized as a social welfare organization under Internal Revenue Code section 501(c)(4). In July 2010 the application was approved and as a result, with exception of income derived from unrelated business activities, the Association is exempt from federal and state income taxes.

KIAWAH ISLAND COMMUNITY ASSOCIATION, INC.
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2018 AND 2017

Note 11 – Federal and State Income Taxes (continued)

Management has determined the Association does not have any uncertain tax positions that materially impact the financial statements or related disclosures. Since tax matters are subject to some degree of uncertainty, there can be no assurance the Association’s tax returns will not be challenged by taxing authorities and that the Organization will not be subject to tax, penalties and interest as result of those challenges. The Organization’s tax returns remain open for examination by government authorities for three years subsequent their original filing.

Note 12 – Retirement Plan

The Association maintains a defined contribution retirement plan, which allows eligible employees meeting minimum age and service requirements to make contributions by salary reduction pursuant to Section 401(k) of the Internal Revenue Code. Total deferrals in any plan year may not exceed the dollar limit, which is determined by law.

The Association will match the employee’s contribution at a rate of 80% on the first 5% of the employee’s gross wages. The Association’s cost for this benefit was \$106,031 and \$91,276 for the years ended December 31, 2018 and 2017, respectively.

Note 13 – Operating Leases

The Association maintains various operating leases for operating, fitness, and office equipment. The future annual lease payments required under these operating leases are as follows:

<u>For year ending December 31,</u>	
2019	\$ 128,428
2020	95,850
2021	44,430
2022	33,542
2023	<u>1,766</u>
Total	<u>\$ 304,016</u>

Rent and usage expense associated with lease payments in 2018 and 2017 was \$166,724 and \$139,641, respectively.

KIAWAH ISLAND COMMUNITY ASSOCIATION, INC.
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2018 AND 2017

Note 14 – Related Party Transactions

Kiawah Resort Associates (KRA), the developer, held one seat on the Association's board of directors for the years covered in these financial statements. Additionally, KRA owned 105 and 107 properties during 2018 and 2017, respectively, of which 82 are lots in inventory, 15 are un-subdivided and 8 are commercial for 2018. Assessments paid by KRA, including storm supplemental special assessments, for this inventory was \$257,732 and \$274,506 in 2018 and 2017, respectively. As of December 31, 2018 and 2017, \$-0- was owed to the Association by the developer, respectively.

Note 15 – Concentrations

Kiawah Island is geographically located in the coastal region of South Carolina and is a popular vacation and recreational destination. The members of the Association include those both purchasing a home for personal residential use as well as for investment and commercial/rental purposes. Although the Association's members are not all necessarily from a concentrated geographical area, the Association and its members are exposed to risks associated with conditions affecting the economy, real estate, tourism and weather for its geographical area.

Note 16 – Commitments

As of December 31, 2018, the Association had committed to several contracts that commenced in 2018 but were not completed by December 31, 2018. As of December 31, 2018, the remaining outstanding amount on these contracts totaled \$134,438 and is expected to be completed and expensed in 2019.

KIAWAH ISLAND COMMUNITY ASSOCIATION, INC.
FUTURE MAJOR REPAIRS AND REPLACEMENTS (UNAUDITED)
FOR THE YEAR ENDING DECEMBER 31, 2018

The Association engaged Design Management Associates to estimate the remaining useful lives and replacement costs of the components of common property. The latest reserve study was issued on December 17, 2018. All of the estimates were based on future estimated replacement costs. Replacement costs were based on the estimated costs to repair or replace common property components at the date of the study. Estimated current replacement costs have not been revised since December 2018 and do not take into account the effects of inflation between the date of the study and the date that the components will require repair or replacement. The following information is based on the study, and presents significant information about the components of common property.

Component	Estimated Replacement Lives	Estimated Replacement Costs	Fund Balance as of December 31, 2018
Street repair, resurfacing	1-50 years	\$ 15,429,148	
Off-road drainage system	1-36 years	16,896,195	
Buildings and structures:			
Security gate house #1	1-25 years	149,262	
Maintenance facility	1-36 years	909,615	
Sandcastle recreation center	1-40 years	4,665,796	
Administrative building	1-49 years	1,645,054	
Boardwalks	1-40 years	2,480,332	
Walking bridges	1-38 years	2,200,929	
Roadway bridges	1-29 years	9,766,851	
Observation towers	1-25 years	295,632	
Revetments/bulkheads	1-18 years	937,194	
Docks	1-29 years	481,129	
Rhetts' Bluff facility	1-28 years	722,724	
Canoe/Boat launch & pavilion	1-21 years	314,827	
Irrigation	1-10 years	116,385	
Signage	1-40 years	1,783,894	
Railings	1-32 years	188,520	
Total		58,983,487	\$ 6,452,329
Security gate house - second gate	1-24 years	64,365	361,502
Preserve split rail fence	1-25 years	238,645	10,539
Totals		<u>\$ 59,286,497</u>	<u>\$ 6,824,370</u>

Actual expenditures may vary from the estimated future expenditures and the variations may be material.