

**KIAWAH ISLAND
COMMUNITY ASSOCIATION, INC.**

KIAWAH ISLAND, SOUTH CAROLINA

AUDITED FINANCIAL STATEMENTS

DECEMBER 31, 2017 AND 2016

KIAWAH ISLAND COMMUNITY ASSOCIATION, INC.

INDEPENDENT AUDITORS' REPORT

AND

AUDITED FINANCIAL STATEMENTS

DECEMBER 31, 2017 AND 2016

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DIRECTORS

Dave Singer – Chair
Lynn Morgenstern – Vice Chair
Ben Cheatham – Treasurer
Rajan Govindan
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Independent Auditors' Report

February 16, 2018

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, 2017 and 2016, 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, 2017 and 2016, 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 24 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.

Robinson Hunt & Co., P.A.

KIAWAH ISLAND COMMUNITY ASSOCIATION, INC.

BALANCE SHEETS

AS OF DECEMBER 31, 2017 AND 2016

	<u>2017</u>	<u>2016</u>
CURRENT ASSETS		
Cash - undesignated	\$ 6,997,266	\$ 6,180,096
Accounts receivable (less allowance for doubtful accounts of \$21,500 and \$35,000, respectively)	87,487	1,198,428
Accounts receivable - other	28,637	29,103
Royalty receivable	37,500	37,500
Prepaid expenses	<u>170,133</u>	<u>284,507</u>
Total current assets	7,321,023	7,729,634
NON-CURRENT ASSETS		
Property and equipment, at cost (less accumulated depreciation of \$2,292,302 and \$2,135,484, respectively)	3,182,493	3,269,384
DESIGNATED ASSETS		
Cash - designated	2,244,384	2,812,932
Investments - designated	4,867,151	4,537,090
Accrued interest receivable - designated	<u>35,328</u>	<u>32,633</u>
Total designated assets	<u>7,146,863</u>	<u>7,382,655</u>
TOTAL ASSETS	<u>\$ 17,650,379</u>	<u>\$ 18,381,673</u>

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

KIAWAH ISLAND COMMUNITY ASSOCIATION, INC.

BALANCE SHEETS

AS OF DECEMBER 31, 2017 AND 2016

	<u>2017</u>	<u>2016</u>
CURRENT LIABILITIES		
Accounts payable	\$ 1,286,696	\$ 422,031
Accrued payroll and payroll taxes/withholdings	100,646	90,902
Accrued annual leave	281,849	280,668
Prepaid assessments	62,290	29,884
Accrued expenses	18,931	180,602
Deferred revenue - royalty income, current	50,156	50,156
Mortgage payable - current	56,471	53,689
Deposits held	28,263	11,637
Total current liabilities	<u>1,885,302</u>	<u>1,119,569</u>
NONCURRENT LIABILITIES		
Deferred revenue - royalty income	401,251	451,407
Mortgage payable - noncurrent	1,456,122	1,512,590
Total noncurrent liabilities	<u>1,857,373</u>	<u>1,963,997</u>
Total liabilities	<u>3,742,675</u>	<u>3,083,566</u>
FUND BALANCES		
Accumulated excess of revenues over expenses (undesignated)	7,797,828	8,217,844
Accumulated excess of revenues over expenses (designated)	6,151,300	7,092,301
Accumulated other comprehensive income (loss)	(41,424)	(12,038)
Total fund balances	<u>13,907,704</u>	<u>15,298,107</u>
TOTAL LIABILITIES AND FUND BALANCES	<u>\$ 17,650,379</u>	<u>\$ 18,381,673</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, 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/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

	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
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)	\$ (1,390,403)	\$ 1,724,686	\$ (254,528)	\$ (13,025)	\$ (460,900)	\$ (2,106,579)	\$ -	\$ (161)	\$ (279,896)

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, 2016

	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	\$ 10,445,228	\$ 8,334,100	\$ 553,900	\$ 193,319	\$ -	\$ 1,347,784	\$ -	\$ 16,125	\$ -
Late charges	35,231	29,736	4,311	1,100	-	-	-	84	-
Investment income	146,288	32,518	3,043	1,985	-	108,687	-	55	-
Royalty income	216,805	216,805	-	-	-	-	-	-	-
Other income	639,998	340,185	299,813	-	-	-	-	-	-
Initiation fees	47,700	-	47,700	-	-	-	-	-	-
Contribution to reserve	1,446,658	-	-	-	-	1,446,658	-	-	-
Vehicle access fees	1,153,930	1,153,930	-	-	-	-	-	-	-
GROSS REVENUES	14,131,838	10,107,274	908,767	196,404	-	2,903,129	-	16,264	-
EXPENSES AND OTHER GAINS/LOSSES									
General and administrative	2,758,055	2,758,055	-	-	-	-	-	-	-
Land management	2,188,604	2,188,604	-	-	-	-	-	-	-
Lakes management	232,947	232,947	-	-	-	-	-	-	-
General maintenance	517,697	517,697	-	-	-	-	-	-	-
Security - main gate	1,331,078	1,331,078	-	-	-	-	-	-	-
Mechanic's shop	249,455	249,455	-	-	-	-	-	-	-
Livability	244,671	244,671	-	-	-	-	-	-	-
Sandcastle operations	1,164,117	-	1,164,117	-	-	-	-	-	-
Security - second gate	225,916	-	-	225,916	-	-	-	-	-
Depreciation	321,805	-	-	-	321,805	-	-	-	-
Loss (gain) on sale of property and equipment	(19,211)	(19,211)	-	-	-	-	-	-	-
Loss (gain) on sale of investments	-	-	-	-	-	-	-	-	-
Major repairs and replacements	3,412,316	-	-	-	-	3,412,316	-	-	-
Landscape improvements	292,635	-	-	-	-	-	-	22,732	269,903
TOTAL EXPENSES AND OTHER GAINS/LOSSES	12,920,085	7,503,296	1,164,117	225,916	321,805	3,412,316	-	22,732	269,903
EXCESS (DEFICIT) REVENUES OVER EXPENSES	1,211,753	2,603,978	(255,350)	(29,512)	(321,805)	(509,187)	-	(6,468)	(269,903)
ACCUMULATED EXCESS - January 1, 2016 (as previously reported)	17,706,350	3,975,022	403,092	-	5,390,890	7,523,626	405,884	7,836	-
Adjustment to reverse capitalization of common property assets	(3,607,958)	-	-	-	(3,607,958)	-	-	-	-
ADJUSTED ACCUMULATED EXCESS - January 1, 2016 (as restated)	14,098,392	3,975,022	403,092	-	1,782,932	7,523,626	405,884	7,836	-
Transfer to/from other funds	-	(1,469,705)	(66,627)	29,512	1,536,332	(269,903)	(29,512)	-	269,903
Transfer of fixed assets	-	(1,773,791)	(1,579)	-	1,805,345	(28,130)	(1,845)	-	-
ACCUMULATED EXCESS - December 31, 2016	\$ 15,310,145	\$ 3,335,504	\$ 79,536	\$ -	\$ 4,802,804	\$ 6,716,406	\$ 374,527	\$ 1,368	\$ -

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, 2016

	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
EXCESS (DEFICIT) REVENUES OVER EXPENSES	\$ 1,211,753	\$ 2,603,978	\$ (255,350)	\$ (29,512)	\$ (321,805)	\$ (509,187)	\$ -	\$ (6,468)	\$ (269,903)
OTHER COMPREHENSIVE INCOME									
Unrealized gain/(loss) on investments	(31,460)	-	-	-	-	(31,460)	-	-	-
COMPREHENSIVE INCOME (LOSS)	\$ 1,180,293	\$ 2,603,978	\$ (255,350)	\$ (29,512)	\$ (321,805)	\$ (540,647)	\$ -	\$ (6,468)	\$ (269,903)

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, 2017 AND 2016

	2017	2016
CASH FLOWS FROM OPERATING ACTIVITIES		
Excess (deficit) revenues over expenses	\$ (1,361,017)	\$ 1,211,753
Adjustments to reconcile excess (deficit) revenues over expenses to net cash flow provided by (used in) operating activities:		
Depreciation	400,420	321,805
Provision for losses on receivables	(13,500)	(5,000)
Loss (gain) on sale of property and equipment	(24,813)	(19,211)
Amortization of bond premiums and discounts	50,510	56,661
(Increase) decrease in:		
Accounts receivable	1,124,441	(1,081,823)
Accounts receivable - other	466	(208)
Accrued interest on investments	(2,695)	(4,456)
Prepaid expenses	114,374	(71,680)
Increase (decrease) in:		
Accounts payable	864,665	242,913
Accrued payroll and payroll taxes/withholdings	9,744	23,103
Accrued annual leave	1,181	18,017
Prepaid assessments	32,406	16,126
Accrued expenses	(161,671)	179,448
Deferred revenue - royalty income	(50,156)	(50,156)
Deposits held	16,626	(29,928)
NET CASH FLOWS PROVIDED BY (USED IN) OPERATING ACTIVITIES	1,000,981	807,364
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of property and equipment	(327,215)	(1,808,258)
Proceeds from sale of property and equipment	38,500	19,211
Purchase of investments	(1,310,644)	(1,703,842)
Proceeds from sale of investments	900,686	1,053,947

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, 2017 AND 2016

	<u>2017</u>	<u>2016</u>
NET CASH FLOWS PROVIDED BY (USED IN)		
INVESTING ACTIVITIES	<u>(698,673)</u>	<u>(2,438,942)</u>
CASH FLOWS FROM FINANCING ACTIVITIES		
Principal payments on mortgage	(53,686)	(8,721)
Proceeds from mortgage loan	<u>-</u>	<u>1,575,000</u>
NET CASH FLOWS PROVIDED BY (USED IN)		
INVESTING ACTIVITIES	<u>(53,686)</u>	<u>1,566,279</u>
NET INCREASE (DECREASE) IN CASH	248,622	(65,299)
CASH AND CASH EQUIVALENTS, beginning of year	<u>8,993,028</u>	<u>9,058,327</u>
CASH AND CASH EQUIVALENTS, end of year	<u>\$ 9,241,650</u>	<u>\$ 8,993,028</u>
<u>CASH SUMMARY</u>		
Undesignated	\$ 6,997,266	\$ 6,180,096
Designated	<u>2,244,384</u>	<u>2,812,932</u>
	<u>\$ 9,241,650</u>	<u>\$ 8,993,028</u>
<u>SUPPLEMENTAL INFORMATION</u>		
Amount of Interest Paid	<u>\$ 59,405</u>	<u>\$ 10,127</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 (\$29,386) and (\$31,460) in 2017 and 2016, respectively.

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

KIAWAH ISLAND COMMUNITY ASSOCIATION, INC.
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2017 AND 2016

NOTE 1 – NATURE OF ORGANIZATION

Kiawah Island Community Association, Inc. (the “Association”) is a non-profit, non-stock, corporate homeowners' association. On July 8, 2010, the IRS approved the Association’s application to be treated as a tax-exempt entity. The membership consists of most property owners on Kiawah Island, South Carolina. The "Declaration of Covenants and Restrictions of the Kiawah Island Community Association, Inc." was adopted December 21, 1977. Kiawah Island is located 21 miles south of Charleston, South Carolina. The island consists of approximately 10,000 acres. There are approximately 4,265 residential properties, of which approximately 85.83% are improved. In addition, there are 62 commercial properties.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Accounting Method

The Association uses the accrual method of accounting. Revenues, which consist primarily of property assessments, are recognized when earned. Expenses are recognized when incurred.

The Association uses fund accounting, which requires that funds, such as operating funds, property funds, and funds designated for future major repair and replacement costs, be classified separately for accounting and reporting purposes. The disbursements from the operating fund are generally at the discretion of the Board of Directors and management for operating expenses. The disbursements from the reserve funds may only be utilized in accordance with the established purposes for accumulation. These replacement disbursements are comprised of building repairs, pavement resurfacing, and other infrastructure replacements, repairs or additions.

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. Financial resources are classified for accounting and reporting purposes in the following funds established according to their nature and purpose:

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

KIAWAH ISLAND COMMUNITY ASSOCIATION, INC.
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2017 AND 2016

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Fund Basis of Accounting (continued)

- Major Repair and Replacements Fund and Landscape Capital Improvements Fund - These funds are used to accumulate funds designated for future major repairs and replacements of existing facilities and equipment plus capital projects approved by the Board, and for the major landscape repairs and replacements plus the 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 and interest bearing money market funds and deposit accounts.

Allowance for Doubtful Accounts

Assessments are considered delinquent after thirty days and a late fee of 1.5% is charged each month on the unpaid balance. 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 which is based on the balance of outstanding assessments receivable on properties in foreclosure at the end of the year and its prior history of writing off uncollectible assessments. At December 31, 2017 and 2016, the Association's allowance for doubtful accounts was \$21,500 and \$35,000, respectively, and bad debt expense (recovery) totaled (\$9,489) and \$32,406 for 2017 and 2016, respectively.

Property and Equipment

Property and equipment, with a useful life in excess of one year and costing more than \$2,500 when purchased, are recorded at cost. Depreciation is provided on the straight-line method over the estimated useful lives of the respective assets. Maintenance and repairs are charged to expense 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 separately and thus have no fair market value other than related to their intended use. Such assets are not recognized 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, 2017 AND 2016

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Investment Securities

Investment securities at December 31, 2017 and 2016 consist of debt securities. Debt securities are classified in one of three categories: trading, available for sale, or held to maturity. While not precluded from trading or held to maturity investments, all of the Association's investment securities are classified as available-for-sale at December 31, 2017 and 2016.

Available-for-sale securities are recorded at fair value. Unrealized holding gains and losses on available-for-sale securities are excluded from earnings and are reported as a separate component of accumulated other comprehensive income until realized. Realized gains and losses from the sale of available-for-sale securities are determined on a specific-identification basis.

A decline in the market value of any available-for-sale security below cost that is deemed to be other-than-temporary results in an impairment to reduce the carrying amount to fair value. The impairment is charged to earnings and a new cost basis for the security is established. To determine whether an impairment is other-than-temporary, the Association considers whether it has the ability and intent to hold the investment until a market price recovery and considers whether evidence indicating the cost of the investment is recoverable outweighs evidence to the contrary. Evidence considered in this assessment includes the reasons for the impairment, the severity and duration of the impairment, changes 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 the intent and the ability to hold these securities until a market price recovery or maturity, investment securities at December 31, 2017 and 2016 are not other than temporarily impaired. No impairments were recognized by the Association during the years ended December 31, 2017 and 2016.

Fair Value Measurements

The Association applies generally accepted accounting principles (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 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. GAAP also establishes a framework for measuring fair value and expands disclosures about fair value measurements (Note 7).

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 by the FDIC up to \$250,000 at each bank through December 31, 2017. This coverage, however, does not protect against losses from any change in the market value of investments. The Association's uninsured balances totaled \$7,846,717 at December 31, 2017.

KIAWAH ISLAND COMMUNITY ASSOCIATION, INC.
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2017 AND 2016

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Assessments

Association members are subject to annual assessments to provide funds for the Association's operating expenses. Annual assessments for unimproved and improved properties (for type A residential) ranged between \$910 to \$1,915 and \$866 to \$1,828 for 2017 and 2016, respectively. In addition, the board approved a supplemental annual assessment in 2017 and 2016 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 December 2016, the board approved an additional supplemental annual assessment of \$125 for unimproved and \$250 for improved properties, and totaling \$1,127,317, to help fund the ongoing clean-up and necessary repairs following Hurricane Matthew which moved up the coast of South Carolina on October 7, 2016 as a category 2 storm. 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 Fees

The Association charges a vehicle access fee to commercial entities doing business on the island. The fee is determined annually by the Board of Directors and consists of annual business passes and daily trip fees. Fees are accumulated in the general operations fund to fund road and drainage repairs and replacements. Total fees for 2017 and 2016 were \$1,567,808 and \$1,153,930, respectively. During 2017, \$500,004 were designated by the Board for future major repairs and replacements.

Contribution to Reserve Fees

A contribution to reserve fee in the amount of 0.50% of the gross purchase price of real estate transfers of subject property is collected at closing from the buyer. This fee is designated for major repairs and replacements and landscape capital improvements.

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.

KIAWAH ISLAND COMMUNITY ASSOCIATION, INC.
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2017 AND 2016

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Reclassifications

Certain accounts and amounts in the December 31, 2016 financial statements have been reclassified to conform with the December 31, 2017 presentation.

Date of Management’s Review

In preparing the financial statements, the Association has evaluated events and transactions for potential recognition or disclosure through February 16, 2018, the date that the financial statements were available to be issued.

NOTE 3 – COMPREHENSIVE INCOME

The Association complies with the provisions of FASB ASC 220, *Comprehensive Income*, which establishes rules for the reporting and presentation of comprehensive income and its components. Accounting principles generally require that recognized revenue, expense, gains and losses be included in net income. However, certain changes in assets and liabilities, such as unrealized gain and loss on available-for-sale securities, are reported as a separate component of the equity section of the balance sheet, such items, along with net income, are components of comprehensive income. The components of other comprehensive income for 2017 and 2016 are as follows:

	2017	2016
Unrealized gains (losses) on available-for-sale securities	\$ (29,386)	\$ (31,460)
Other comprehensive income (loss)	\$ (29,386)	\$ (31,460)

Changes in accumulated other comprehensive income are as follows:

	2017	2016
Accumulated other comprehensive income (loss), beginning balance	\$ (12,038)	\$ 19,422
Change during the year	(29,386)	(31,460)
Accumulated other comprehensive income (loss), ending balance	\$ (41,424)	\$ (12,038)

NOTE 4 - PROPERTY AND EQUIPMENT

The 2016 numbers in this footnote have been restated to incorporate the effects of the prior period adjustment which is described more fully in Note 17 to these financials statements. Depreciation expense for the years ended December 31, 2017 and 2016 was \$400,420 and \$321,805, respectively.

KIAWAH ISLAND COMMUNITY ASSOCIATION, INC.
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2017 AND 2016

NOTE 4 - PROPERTY AND EQUIPMENT (continued)

Major classifications of property and equipment and their respective useful lives at December 31 are as follows:

Description	Estimated Lives	2017	2016
Land	non-depreciable	\$ 440,253	\$ 440,253
Buildings and improvements	5-40 yrs.	2,531,828	2,558,112
Furniture and equipment	3-15 yrs.	1,671,486	1,620,775
Vehicles and trailers	5-10 yrs.	831,228	785,728
		<u>5,474,795</u>	<u>5,404,868</u>
Less: accumulated depreciation		<u>(2,292,302)</u>	<u>(2,135,484)</u>
		<u>\$ 3,182,493</u>	<u>\$ 3,269,384</u>

NOTE 5 – FUTURE MAJOR REPAIRS AND REPLACEMENTS

The Association's governing documents provide for the levying of the annual general purpose assessment which, in addition to providing funds for general operations of the Association, also provides for the repair and maintenance of the common properties, e.g., roads, bridges, lakes, drainage systems, etc. Accumulated funds, which aggregate \$6,151,300 and \$7,092,301 at December 31, 2017 and 2016, respectively, are held in separate accounts and are not available for general operating purposes.

An independent review of expected infrastructure repair and replacement costs was conducted by an outside consultant and the latest reserve study was issued on December 2, 2017. Actual expenditures may vary from the estimated future expenditures and the variations may be material. Over the last five year period, expenditures for major repairs and maintenance have averaged \$3,393,028. The Association receives contribution to reserve fees each year to help fund these expenditures. Over the last five year period, these fees have averaged \$1,493,417. In 2017 and 2016, the board approved a supplemental annual assessment to further help fund these expenditures which amounted to \$1,357,241 and \$1,347,784, respectively. Additionally, during 2017 the board designated \$500,004 of vehicle access fees to further help fund these expenditures. It is possible, however, that amounts accumulated in the major repair and replacement funds, plus the annual sources of revenue, may not be adequate to meet all the future needs for major repairs and replacements and that the Association may need to consider alternate sources of revenue to ensure continued funding of necessary repair and replacement projects. The Association has the right to increase annual assessments up to the maximum amount set forth in the covenants; levy special assessments, subject to member approval; transfer funds from operations; or delay repairs and replacements until funds are available.

KIAWAH ISLAND COMMUNITY ASSOCIATION, INC.
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2017 AND 2016

NOTE 6 – INVESTMENTS

Maturities of debt securities classified as available-for-sale were as follows at December 31, 2017:

Available for sale:	<u>Cost</u>	<u>Fair Value</u>
Due before one year	\$ 608,030	\$ 607,959
Due after one year through five years	3,599,782	3,559,060
Due after five years through ten years	<u>700,763</u>	<u>700,132</u>
	<u>\$ 4,908,575</u>	<u>\$ 4,867,151</u>

Proceeds from the sale of investment securities classified as available for sale were \$900,686 in 2017 and \$1,053,947 in 2016; gross realized gains in 2017 and 2016 were \$2,868 and \$-0-, 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, 2017 and 2016 are as follows:

	<u>Cost</u>	<u>Gross unrealized holding gains/(losses)</u>	<u>Fair value</u>
	<u>December 31, 2017</u>		
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>
	<u>\$ 4,908,575</u>	<u>\$ (41,424)</u>	<u>\$ 4,867,151</u>
	<u>December 31, 2016</u>		
Certificates of deposit	\$ 450,000	\$ 5,346	\$ 455,346
Corporate bonds	3,521,257	(34,031)	\$ 3,487,226
U.S. Treasury investments	<u>577,871</u>	<u>16,647</u>	<u>594,518</u>
	<u>\$ 4,549,128</u>	<u>\$ (12,038)</u>	<u>\$ 4,537,090</u>

KIAWAH ISLAND COMMUNITY ASSOCIATION, INC.
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2017 AND 2016

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, 2017 and 2016:

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)
\$ 4,867,151	\$ 4,867,151	\$ -	\$ -

Fair Value Measurements at Reporting Date Using:			
Total at December 31, 2016	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
\$ 4,537,090	\$ 4,537,090	\$ -	\$ -

KIAWAH ISLAND COMMUNITY ASSOCIATION, INC.
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2017 AND 2016

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. At December 31, 2017 and 2016, the balance of the deferred revenue totaled \$451,407 and \$501,563, respectively, and the net related royalty income was \$62,094 and \$57,156 for 2017 and 2016, 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 2017 and 2016 totaled \$166,513 and \$159,649, respectively.

NOTE 9 – MORTGAGE PAYABLE

In October 2016, the Association took out 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, 2017 AND 2016

NOTE 9 – MORTGAGE PAYABLE (continued)

At December 31, 2017 and 2016, the balance of the mortgage was \$1,512,593 and \$1,566,279, respectively, and interest paid totaled \$59,405 and \$10,127 during 2017 and 2016, respectively.

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. The former owner moved out in August 2017 and the agreement concluded. During the year ended December 31, 2017 and 2016, the Association received rents in the amount of \$78,762 and \$26,127, respectively.

Mortgage debt service requirements to maturity are as follows:

Year ending December 31,	Principal	Interest	Total
2018	\$ 56,484	\$ 55,219	\$ 111,703
2019	58,682	52,895	111,577
2020	60,746	50,831	111,577
2021	63,177	48,400	111,577
2022	65,555	46,022	111,577
2023 - 2026	1,207,949	152,842	1,360,791
Total	<u>\$ 1,512,593</u>	<u>\$ 406,209</u>	<u>\$ 1,918,802</u>

NOTE 10 – LINE OF CREDIT

The Association has one 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 the line of credit available for the Association is \$2,500,000 and the current maturity date is February 5, 2019. The Association has made no draws on this line and accordingly had no outstanding balances at December 31, 2017 and 2016.

KIAWAH ISLAND COMMUNITY ASSOCIATION, INC.
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2017 AND 2016

NOTE 11 – FEDERAL AND STATE INCOME TAXES

During December 2008, the Association filed an exemption application (Form 1024 – Application for Recognition of Exemption Under Section 501(a)) with the IRS to be recognized as a social welfare organization under Internal Revenue Code section 501(c)(4). The application was approved on July 8, 2010.

The Association is exempt from federal income taxes under Section 501(c)(4) of the Internal Revenue Code, except on income derived from unrelated business activities. The Association believes that it has appropriate support for any tax positions taken, and as such, does not have any uncertain tax positions that are material to the financial statements. The Association’s tax returns are subject to examination by the IRS, generally for three years after 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 70% on the first 5% of the employee’s gross wages. The Association's expense was \$91,276 and \$89,127 for the years ended December 31, 2017 and 2016, 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>	
2018	\$ 146,746
2019	117,396
2020	84,764
2021	33,462
2022	24,297
Thereafter	<u>-</u>
Total minimum lease payments	<u>\$ 406,665</u>

Rent and usage expense associated with lease payments in 2017 and 2016 was \$139,641 and \$204,641, respectively.

KIAWAH ISLAND COMMUNITY ASSOCIATION, INC.
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2017 AND 2016

NOTE 14 - RELATED PARTY TRANSACTIONS

Kiawah Resort Associates (KRA), the developer, held one seat on the Association's board for the years covered in these financial statements. Additionally, KRA owned 107 and 144 properties during 2017 and 2016, respectively, of which 86 are lots in inventory, 13 are unsubdivided and 8 are commercial for 2017. Assessments paid by KRA, including storm supplemental special assessments, for this inventory was \$274,506 and \$284,527 in 2017 and 2016, respectively. At December 31, 2017 and 2016, \$-0- and \$33,271 was owed to the Association, respectively.

NOTE 15 – CONCENTRATIONS

Kiawah Island is a coastal community located on the upper-part of the southeastern coast of the United States and is a vacation destination for thousands of people each year. The members of the Association include persons purchasing a home for personal residential use as well as those purchasing homes and land for investment and commercial/rental purposes. Although the Association's members, and those vacationing on Kiawah Island, are not necessarily from a concentrated geographical area, the Association is exposed to risks associated with conditions affecting the economy, real estate, tourism and weather for its geographical area.

NOTE 16 – COMMITMENTS

At December 31, 2017, the Association had one major repairs and replacement contract that commenced in 2017 but had not been completed by December 31, 2017. The total amount of the contract was \$4,516,635. Management estimated that \$90,469 of the total contract amount was attributable to work performed during 2017 and is included as major repairs and replacements on the statement of revenues, expenses and changes in fund balance. The remaining amount outstanding totaled \$4,426,166 and is expected to be completed and expensed in 2018.

NOTE 17 – PRIOR PERIOD ADJUSTMENT

During 2017, the Association elected to adjust its property and equipment reporting to a manner that is more consistent with prevalent industry practice. As such, a number of assets previously included on the balance sheet as property and equipment including the Sandcastle recreation facility and pool, the main gate buildings, the bathroom facility at the property owners' boat launch area, sewer system components, and various building and land improvements related to these areas, have been removed from the books as a prior period adjustment. The Association believes that these items belong to the property owners collectively, not the Association, as the Association would not be able to sell them without a vote of the membership.

KIAWAH ISLAND COMMUNITY ASSOCIATION, INC.
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2017 AND 2016

NOTE 17 – PRIOR PERIOD ADJUSTMENT

At January 1, 2016, the cost of these items totaled \$6,096,737 and accumulated depreciation amounted to \$2,488,779 which results in a net adjustment to beginning net assets of \$3,607,958. Accordingly, beginning net assets have been restated by this amount from the \$17,706,350 previously reported to the restated amount of \$14,098,392 shown on the 2016 statement of revenues, expenses, and changes in fund balance. Additionally, depreciation of \$172,805 was taken on these assets in 2016, and, accordingly, that depreciation was removed from these statements which reduced 2016 depreciation from the \$494,610 previously reported to \$321,805. That depreciation removal is the only adjustment to the previously reported excess revenues over expenses which was changed from \$1,038,948 to \$1,211,753. The only effect on the previously issued 2016 balance sheet was a reduction to property and equipment, net from \$6,704,537 to \$3,239,384 and to accumulated excess of revenues over expenses (undesignated) fund balance from \$11,652,997 to \$8,217,844. The amount of these reductions is \$3,435,153 which is the net adjustment of \$3,607,958 noted above less the depreciation removed on those assets of \$172,805.

During the process of evaluating its property and equipment, the Association also made some transfers between property and equipment categories and reassessed the value of land reported on the administrative building purchase that occurred in late 2016. These adjustments did not have a material financial statement effect on the financial statements. The updated classifications and effects of the prior period adjustments are reflected in Note 4 to the financial statements.

KIAWAH ISLAND COMMUNITY ASSOCIATION, INC.
FUTURE MAJOR REPAIRS AND REPLACEMENTS (UNAUDITED)
FOR THE YEAR ENDING DECEMBER 31, 2017

The Association engaged Design Management Associates to estimate the remaining useful lives and replacement costs of the components of common property except for the preserve split rail fence. The latest reserve study was issued on December 2, 2017. The preserve split rail fence was not included in the most recent study and is based on management's internal estimate. 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 2017 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 December 31, 2017
Street repair, resurfacing	1-28 years	\$ 15,407,879	
Off-road drainage system	1-33 years	16,704,757	
Buildings and structures:			
Security gate house #1	1-25 years	135,961	
Maintenance facility	1-37 years	915,690	
Sandcastle recreation center	1-39 years	3,021,704	
Administrative building	1-50 years	1,355,659	
Boardwalks	1-39 years	1,869,997	
Walking bridges	1-39 years	1,644,042	
Roadway bridges	1-30 years	8,674,702	
Observation towers	1-26 years	294,856	
Revetments/bulkheads	1-18 years	934,794	
Docks	1-26 years	255,877	
Rhetts' Bluff facility	1-28 years	617,183	
Canoe/Boat launch & pavilion	1-30 years	347,238	
Irrigation	1-10 years	109,999	
Signage	1-40 years	1,739,534	
Railings	1-34 years	183,794	
		\$ 54,213,666	\$ 5,775,574
Security gate house - second gate	1-28 years	58,227	361,502
Preserve split rail fence	1-30 years	211,462	14,224
Totals		\$ 54,483,355	\$ 6,151,300

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

See accompanying independent accountants' audit report.