

Bald Head Association

Bald Head Island, North Carolina

FINANCIAL STATEMENTS AND REPORT OF INDEPENDENT
CERTIFIED PUBLIC ACCOUNTANT

For the Year Ended December 31, 2016

Bald Head Association
CONTENTS
For the Year Ended December 31, 2016

	Page
REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANT	3
FINANCIAL STATEMENTS	
BALANCE SHEET	4
REVENUES, EXPENSES AND CHANGES IN FUND BALANCE	5
STATEMENT OF CASH FLOWS	6
NOTES TO FINANCIAL STATEMENTS	7 - 11
SUPPLEMENTARY INFORMATION ON FUTURE MAJOR REPAIRS AND REPLACEMENTS	12



JASON C. KELLER, CPA, PLLC

REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANT

Board of Directors, Bald Head Association
Bald Head Island, NC

We have audited the accompanying financial statements of Bald Head Association which comprise the balance sheet as of December 31, 2016, and the related statements of revenues, expenses and changes in fund balance and cash flows for the year then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Bald Head Island Association as of December 31, 2016, and the results of its operations and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Disclaimer of Opinion on Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the information on future major repairs and replacements on page 12 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 audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance

Report on Summarized Comparative Information

We have previously audited the Bald Head Association's 2015 financial statements, and we expressed an unmodified audit opinion on those audited financial statements in our report dated October 13, 2016. In our opinion, the summarized comparative information presented herein as of and for the year ended December 31, 2015, is consistent, in all material respects, with the audited financial statements from which it has been derived.

Jason C Keller CPA PLLC

Wilmington, NC
September 15, 2017

Bald Head Association
Balance Sheet
December 31, 2016

	2016			2015
	Operating Fund	Repairs & Replacement Fund	Total	Total (for comparative purposes only)
Assets:				
Current assets:				
Cash and cash equivalents	\$ 72,132	\$ 137,439	\$ 209,571	\$ 189,018
Assessments receivable net of \$12,750 allowance in 2016 and \$8,535 in 2015	19,709	-	19,709	18,490
Accounts receivable net of \$29,100 allowance in 2016 and 2015	11,229	-	11,229	14,715
Prepaid expenses	1,119	-	1,119	266
Total current assets	<u>104,189</u>	<u>137,439</u>	<u>241,628</u>	<u>222,489</u>
Land - Battery 4 creek lot	651,801	-	651,801	-
Fixed assets, net of accumulated depreciation of \$486,279 in 2016 and \$447,774 in 2015	642,926	-	642,926	674,011
Loan fees, net of accumulated amortization of \$3,565 in 2016 and \$3,211 in 2015	-	-	-	354
TOTAL ASSETS	<u><u>\$ 1,398,916</u></u>	<u><u>\$ 137,439</u></u>	<u><u>\$ 1,536,355</u></u>	<u><u>\$ 896,854</u></u>
Liabilities and Fund Balance:				
Current liabilities:				
Accounts payable	\$ 35,379	\$ -	\$ 35,379	\$ 29,128
Accrued interest payable	4,343	-	4,343	-
Deferred revenue	5,500	-	5,500	7,920
Security bonds and deposits	36,500	-	36,500	35,500
Income taxes payable	97,143	-	97,143	-
Line of Credit	3,543	-	3,543	-
Mortgage payable - Assoc. Center (current)	-	-	-	13,500
Total current liabilities	<u>182,408</u>	<u>-</u>	<u>182,408</u>	<u>86,048</u>
Mortgage payable - Battery 4	202,731	-	202,731	-
Mortgage payable - Assoc. Center (less current portion)	-	-	-	76,459
TOTAL LIABILITIES	<u>385,139</u>	<u>-</u>	<u>385,139</u>	<u>162,507</u>
Fund Balance				
Undesignated	(78,219)	-	(78,219)	52,060
Investment in fixed assets net of related debt	1,091,996	-	1,091,996	584,052
Repairs & replacement fund balance	-	137,439	137,439	98,235
TOTAL FUND BALANCE	<u>1,013,777</u>	<u>137,439</u>	<u>1,151,216</u>	<u>734,347</u>
TOTAL LIABILITIES AND FUND BALANCE	<u><u>\$ 1,398,916</u></u>	<u><u>\$ 137,439</u></u>	<u><u>\$ 1,536,355</u></u>	<u><u>\$ 896,854</u></u>

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

Bald Head Association
Statements of Revenues and Expenses and Changes in Fund Balance
for the Year Ended December 31,2016

	2016			2015
	Operating Fund	Repairs & Replacement Fund	Total	Total (for comparative purposes only)
Revenues:				
Member assessments	\$ 330,462	\$ 39,178	\$ 369,640	\$ 366,375
Special assessments	240,450	-	240,450	-
Association center fees	7,795	-	7,795	7,800
Architectural review committee	38,400	-	38,400	43,400
ARC contracting revenue	45,998	-	45,998	45,996
Penalties and interest	1,285	-	1,285	3,013
Interest income	85	26	111	65
Gain on sale of assets	282,355	-	282,355	-
Island report advertising	31,933	-	31,933	31,365
Boat park annual leases	16,333	-	16,333	15,500
Garden plot annual leases	3,250	-	3,250	2,696
Other income	497	-	497	2,004
TOTAL REVENUES	998,843	39,204	1,038,047	518,214
Expenses:				
Operating and administrative expenses:				
Wages	170,765	-	170,765	159,862
Health insurance expense	37,119	-	37,119	42,652
Payroll taxes	13,682	-	13,682	12,722
Pension plan	3,412	-	3,412	3,815
Other employee benefits	3,475	-	3,475	4,034
Transportation	13,653	-	13,653	13,596
Payroll processing fee	2,952	-	2,952	2,205
Computer expense	4,543	-	4,543	7,038
Other administrative	15,384	-	15,384	7,336
Bank charges	1,265	-	1,265	1,155
Bad debt	5,595	-	5,595	5,039
Equipment lease	2,344	-	2,344	2,458
Assessment expense	1,911	-	1,911	804
Office supplies	3,121	-	3,121	2,679
Office postage	5,368	-	5,368	1,196
Communications media expense	5,973	-	5,973	3,360
Consulting	3,579	-	3,579	1,927
Miscellaneous	476	-	476	40
Amortization	354	-	354	510
Income Taxes	97,143	-	97,143	-
Total operating and admin. exp.	392,114	-	392,114	272,428
Depreciation	40,055	-	40,055	37,439
Association Center				
Repairs and maintenance	29,040	-	29,040	26,816
Utilities	16,131	-	16,131	15,886
Interest expense	17,072	-	17,072	4,636
Taxes - property	15,419	-	15,419	15,418
Association Center building insurance	14,459	-	14,459	12,950
Miscellaneous association center expenses	136	-	136	775
Total association center	92,257	-	92,257	76,481
Other service areas				
Committees	2,431	-	2,431	2,423
Island report	39,118	-	39,118	33,482
Boat park	3,336	-	3,336	1,529
Insurance	13,294	-	13,294	12,278
Audit and accounting	5,700	-	5,700	12,024
Legal	31,873	-	31,873	6,686
	95,752	-	95,752	68,422
TOTAL EXPENSES	620,178	-	620,178	454,770
Revenues over expenses	378,665	39,204	417,869	63,444
Fund Balances:				
Beginning Fund Balance	636,112	98,235	734,347	670,903
Prior period adjustment	(1,000)	-	(1,000)	-
Ending Fund Balance	<u>\$ 1,013,777</u>	<u>\$ 137,439</u>	<u>\$ 1,152,216</u>	<u>\$ 734,347</u>

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

Bald Head Association
Statement of Cash Flows
for the Year Ended December 31, 2016

	2016			2015
	Operating Fund	Repairs & Replacement Fund	Total	Total (for comparative purposes only)
Cash flows from Operating Activities:				
Revenues over(under) expenses	\$ 378,665	\$ 39,204	\$ 417,869	\$ 63,444
Adjustments to reconcile revenues over(under) expenses to net cash provided (used) by operating activities				
Depreciation and amortization	40,409	-	40,409	37,949
Bad debt expense	5,595	-	5,595	5,039
Prior period adjustment	(1,000)	-	(1,000)	-
Loss on sale of recorded assets	53	-	53	-
(Increase) decrease in:				
Assessments receivable	(6,814)	-	(6,814)	8,591
Accounts receivable	3,486	-	3,486	(6,556)
Prepays	(853)	-	(853)	639
Increase (decrease) in:				
Accounts payable	6,251	-	6,251	4,866
Payroll liabilities	-	-	-	(365)
Accrued interest payable	4,343	-	-	-
Deferred revenue	(2,420)	-	(2,420)	(417)
Security bonds and deposits	1,000	-	1,000	16,594
Income taxes payable	97,143	-	97,143	-
Net Cash provided (used) by Operating Activities	525,858	39,204	565,062	129,784
Cash flows from Investing Activities:				
Proceeds from the sale of recorded assets	1,000	-	1,000	-
Purchase of fixed assets	(661,824)	-	(661,824)	(66,072)
Net Cash provided (used) by Investing Activities	(660,824)	-	(660,824)	(66,072)
Cash flows from Financing Activities:				
Borrowings on line of credit	53,402	-	53,402	-
Payments on line of credit	(49,859)	-	(49,859)	-
Borrowings secured by real estate - Battery 4	585,630	-	585,630	-
Mortgage principal payments - Battery 4	(382,899)	-	(382,899)	-
Mortgage principal payments - Assoc. Center	(89,959)	-	(89,959)	(17,505)
Net Cash provided (used) by Financing Activities	116,315	-	116,315	(17,505)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(18,651)	39,204	20,553	46,207
CASH AND CASH EQUIVALENTS - BEGINNING OF YEAR	90,783	98,235	189,018	142,811
CASH AND CASH EQUIVALENTS - END OF YEAR	<u>\$ 72,132</u>	<u>\$ 137,439</u>	<u>\$ 209,571</u>	<u>\$ 189,018</u>

Supplemental information:

Interest paid in 2016: \$12,729

Income taxes paid in 2016: \$0

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

Bald Head Association
NOTES TO FINANCIAL STATEMENTS
For the Year Ended December 31, 2016

NOTE 1: NATURE OF THE ORGANIZATION

Bald Head Association, Bald Head Island, North Carolina is a homeowners association incorporated as a non-profit corporation in the State of North Carolina in April 1982. The primary purpose of the Association is to provide for beautification, maintenance, preservation, and architectural control of the exterior of the single family homes, multi-family units and non-residential areas, the residence lots, assessable properties and the common areas within certain tracts subject to the Amended and Restated Declaration of Covenants, Conditions and Restrictions for Bald Head Island, Stage I and amendments thereto applicable to the Property and recorded in the Office of the Register of Deeds of Brunswick County, North Carolina.

NOTE 2: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Member Assessments and Receivables

Property owners are subject to annual assessments to provide funds for the Association's operating expenses and special assessments for capital improvements. Assessment receivables are stated at the amount management expects to collect from outstanding balances. Management provides for probable uncollectible amounts through a provision for bad debt expense and an adjustment to a valuation allowance based on its assessment of the current status of individual accounts. The Association's by-laws provide for its board of directors to enforce liens on the property whose assessments are thirty days or more delinquent or to bring an action of law against the owner. Balances that are still outstanding after management has used reasonable collection efforts are written off through a charge to the valuation allowance and a credit to accounts receivable. Total write offs to the valuation allowance was \$604 for the year ended December 31, 2016. The valuation allowance for uncollectible assessment receivables is \$12,750 at December 31, 2016.

Voluntary Memberships

Bald Head Island property owners who have not had their homes annexed into the Association's domain can still become "voluntary" members of the Association. The "voluntary" membership allows the members to receive the monthly newsletter, attain member rates on the Association's building rental, and have access to common areas. The "voluntary" members are not subject to the Association's building guidelines, and can revoke their membership at any time.

Cash and Cash Equivalents

For the purposes of the statement of cash flows, the Association considers all highly liquid investments with original maturities of six months or less to be cash equivalents.

Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

Bald Head Association
NOTES TO FINANCIAL STATEMENTS
For the Year Ended December 31, 2016

NOTE 2: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Property, Equipment and Depreciation

Common property reported within the Association's financial statement such as the Association Center building and personal property acquired by the Association is capitalized at cost. All capitalized property and equipment is depreciated using the straight line method over the estimated useful life of the asset. Depreciation expense totaled \$40,055 for the year ended December 31, 2016.

Real property and common areas acquired from the developer and related improvements to such property are not recorded in the Association's financial statement because those properties were transferred to the Association at the final basis in the hands of the developer, which was zero. The real property and common areas that are not recorded in the Association's financial statements include certain right-of-ways, buffer zones, and green belts.

Real property obtained after December 31, 2015 has been capitalized at cost and includes 1.3 acres of land referred to as Battery 4 Creek Lot.

Fund Accounting

The Association uses fund accounting, which requires that funds, such as operating funds and funds designated for future major repairs and replacements, to be classified separately for accounting and reporting purposes. Disbursements from the operating fund are generally at the discretion of management or the board of directors. Disbursements from the repairs and replacement fund generally may be made only for designated purposes.

The Association management has made the following designations of fund balance:

Undesignated - portion of total fund balance available for future budgetary appropriations.

Investments in Fixed Assets, net of Related Debt – portion of fund balance not considered available for future budgetary appropriations as it is generated by the undepreciated value of fixed assets previously purchased, net of related debt.

Repairs and Replacement Fund Balance - portion of the total fund balance that has been designated in the budget to fund future major repairs and replacements.

NOTE 3: FUTURE MAJOR REPAIRS AND REPLACEMENTS

The Association's governing body has determined that funds should be accumulated for future major repairs and replacements. Accumulated funds are to be placed in a separate savings account and generally are not available for expenditures for normal operations.

The Board of Directors conducted a study in March 2013 in order to estimate the remaining useful lives and the replacement costs of the components of common property. The table included in the unaudited supplementary information on Future Major Repairs and Replacements is based on the study.

The board is funding for major repairs and replacements over the remaining useful lives of the components based on the study's estimates of current replacement costs and considering amounts previously accumulated in the replacement fund. Accordingly, the funding requirement of \$19,658 based on full funding plan, has been included in the 2017 budget.

Bald Head Association
NOTES TO FINANCIAL STATEMENTS
For the Year Ended December 31, 2016

NOTE 3: FUTURE MAJOR REPAIRS AND REPLACEMENTS (continued)

Funds are being accumulated in the replacement fund based on estimates of future needs for repairs and replacements of common property components. Actual expenditures may vary from the estimated future expenditures, and the variations may be material. Therefore, amounts accumulated in the fund balance designated for future major repairs and replacements may not be adequate to meet all future needs. If additional funds are needed, the Association has the right to increase regular assessments, levy special assessments (membership approval may be needed depending on the amount), or delay major repairs and replacements until funds are available. The effect on future assessments has not been determined at this time.

Current year activity in the Repairs and Replacements Fund is as follows:

Balance 1/1/2016	\$ 98,235
Current year additions from assessments	39,178
Current year interest	26
Balance 12/31/16	<u>\$ 137,439</u>

NOTE 4: ACCOUNTS RECEIVABLE

Accounts receivable consisted of the following at December 31, 2016.

Covenant Violation Fines	\$ 29,100
Stage II ARC fees	3,833
Island Report Advertising	2,993
Association Center Fees	2,814
Late Assessment Penalties & Finance Charges	1,589
Less: Allowance for doubtful accounts	<u>(29,100)</u>
	<u>\$ 11,229</u>

While the Association intends to aggressively pursue all amounts owed an allowance for doubtful accounts of \$29,100 has been recorded for the possibility of uncollectible accounts receivable.

NOTE 5: PROPERTY AND EQUIPMENT

Property and equipment are recorded at cost and consist of the following at December 31, 2016:

Land – Battery 4 creek lot	\$ 651,801
Buildings	861,883
Improvements	115,783
Furniture and fixtures	30,299
Equipment	112,667
Software and website	<u>8,573</u>
	1,781,006
Less accumulated depreciation	<u>(486,279)</u>
	<u>\$ 1,294,727</u>

Bald Head Association
NOTES TO FINANCIAL STATEMENTS
For the Year Ended December 31, 2016

NOTE 6: DEFERRED REVENUE

Deferred revenue consists of advanced payments of assessments and fees for future periods and totaled \$5,500 on December 31, 2016.

NOTE 7: DEPOSITS

The Association requires a \$500 repair and cleaning deposit to be made in order for the rental use of its Association Center building. Inspection of the building after use is made, and the deposit is returned if the building is in satisfactory condition. As of December 31, 2016, \$2,500 in deposits are being held by the Association.

The Association also requires construction deposits to ensure construction is completed within the two year mandated time frame. The deposit is returned at the completion of construction if there are no violations. As of December 31, 2016, \$34,000 in construction deposits are being held by the Association.

NOTE 8: LINE OF CREDIT

The Association has an existing line-of-credit with a local financial institution in the amount of \$100,000. As of December 31, 2016, \$3,543 was outstanding on the line. Interest accrues on the line at the bank's prime rate and is due monthly. The line of credit expires September 24, 2017.

NOTE 9: MORTGAGE PAYABLE – ASSOCIATION CENTER

The mortgage payable secured by the Association Center was completely paid off during the year ended December 31, 2016.

NOTE 10: MORTGAGE PAYABLE – BATTERY 4

Mortgage payable consists of a 4.25% fixed rate note payable to Bald Head Island Limited, LLC. The note is collateralized by Association real property.

The note terms call for 3 annual payments of \$212,033 beginning in February 2017. However, as of December 31, 2016 the Association has made principal payments that satisfy the amounts due in 2017 and 2018.

Remaining principal maturities of the mortgage note are as follows:

<u>Year Ending December 31st</u>	
2019	\$ <u>202,731</u>

Interest expense related to the above mortgage totaled \$13,848 for the year ended December 31, 2016.

NOTE 11: UNINSURED CASH BALANCES

The Association maintains its cash balances at BB&T located in Southport, North Carolina. Accounts are secured by the Federal Deposit Insurance Corporation up to \$250,000. Uninsured balances are \$0 at December 31, 2016.

Bald Head Association
NOTES TO FINANCIAL STATEMENTS
For the Year Ended December 31, 2016

NOTE 12: INCOME TAXES

For the year ended December 31, 2016, the Association is ineligible to file a Form 1120-H under Internal Revenue Code Section 528 due to regulations regarding non-exempt income such as capital gains on the sale of assets. The Association will file a Form 1120 as a corporation and pay taxes at regular corporate income tax rates on the net of taxable income minus deductions for eligible expenses. Income tax expense for the year ended December 31, 2016 is \$95,611. Tax returns remain subject to examination by taxing authorities for a period of 3 years. At December 31, 2016 tax returns for calendar years 2013, 2014 and 2015 remain “open” to possible examination.

NOTE 13: CLAIMS AND JUDGEMENTS

At December 31, 2016, there is an open judgment entered by the Superior Court against an owner of property within Bald Head Island Stage I for refusal to pay assessment fees and architectural review committee fines. The Association is pursuing collection vigorously but no amounts have been received as of the audit report date.

NOTE 14: COMPARATIVE INFORMATION

The financial statements include certain prior-year summarized comparative information in total but not by net asset class. Such information does not include sufficient detail to constitute a presentation in conformity with generally accepted accounting principles. Accordingly, such information should be read in conjunction with the Association’s financial statements for the year ended December 31, 2015, from which the summarized information was derived. Certain prior year revenue and/or expense accounts may have been consolidated or expanded in order to better conform with current year presentation.

NOTE 15: SPECIAL ASSESSMENT

The Association issued a special assessment to property owners for the year ended December 31, 2016 in anticipation of acquiring real property. The property was acquired on February 12, 2016.

NOTE 16: PRIOR PERIOD ADJUSTMENT

Prior period adjustments for the year ended December 31, 2016 consist of the following:

Unrestricted Fund Balance was adjusted (\$1,000) to reflect an adjustment to Security Bonds and Deposits liability.

NOTE 17: SUBSEQUENT EVENTS

On March 29, 2017, Bald Head Association membership voted to approve a merger with Stage II Association. The merger is scheduled to take place January 2, 2018.

Excluding the above mentioned merger vote, the Association did not have any subsequent events through September 15, 2017 requiring recording or disclosure in the financial statements for the year ended December 31, 2016. September 15, 2017 is the approximate date the financial statements were available to be issued.

Bald Head Association
Supplementary Information on Future Major Repairs and Replacements
December 31, 2016
(UNAUDITED)

In March, 2013 the board of directors conducted a study to estimate the remaining useful lives and the replacement cost of the components of the building and equipment. The estimates were obtained from a licensed contractor who inspected the property.

The balance of the Future Major Repairs and Replacements Fund at December 31, 2016 has not been designated by the Board of Directors for specific components of common property.

The following table is based on that study and presents significant information about the components of the building and equipment.

Components	Estimated Remaining Useful Lives (Years)	Estimated Current Replacement Costs	Ending Fund Balance
Shingle roof	9-12	\$ 25,000	
Exterior painting	2-4	22,000	
Exterior trim/siding	14-17	125,000	
Wood walkways	14-17	45,000	
Hardwood/VCT floor	9-15	27,000	
Carpet	0-2	5,000	
Appliances	0-9	8,000	
Plumbing fixtures (16)	14-22	8,000	
HVAC (6)	0-14	54,000	
Light fixtures	3-13	5,000	
Total		\$ 324,000	\$ 137,439