

**ASSOCIATION OF APARTMENT OWNERS OF  
THE BAY CLUB AT WAIKOLOA BEACH RESORT  
WAIKOLOA, HAWAII  
FINANCIAL STATEMENTS  
YEAR ENDED DECEMBER 31, 2010**



**Myers, Brettholtz & Company, PA**

**CERTIFIED PUBLIC ACCOUNTANTS & BUSINESS CONSULTANTS**

12671 Whitehall Drive, Fort Myers, Florida 33907-3626  
239.939.5775 · 800.749.8270 · Fax: 239.939.3032 · e-mail: [mbcopa@mbcopa.com](mailto:mbcopa@mbcopa.com)

**THE EXCEPTION TO THE RULE**

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## INDEPENDENT AUDITOR'S REPORT

The Board of Directors  
Association of Apartment Owners of the Bay Club at Waikoloa Beach Resort  
Waikoloa, Hawaii

We have audited the accompanying balance sheet of Association of Apartment Owners of the Bay Club at Waikoloa Beach Resort, as of December 31, 2010, and the related statements of revenues, expenses and changes in fund balances and cash flows for the year then ended. These financial statements are the responsibility of the Association's management. 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 of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Association of Apartment Owners of the Bay Club at Waikoloa Beach Resort, as of December 31, 2010, 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.

Our audit was made for the purpose of forming an opinion on the basic financial statements taken as a whole. The accompanying supplementary information on future major repairs and replacements is required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted primarily of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it. The schedule of operating fund revenues and expenses - budget to actual is presented for the purpose of additional analysis and is not a required part of the basic financial statements. Such information, except for the portion marked "unaudited," on which we express no opinion, has been subjected to the auditing procedures applied during the audit of the basic financial statements and, in our opinion, the information is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

MYERS, BRETT HOLTZ & COMPANY, PA  
Fort Myers, Florida  
April 8, 2011

ASSOCIATION OF APARTMENT OWNERS OF THE BAY CLUB  
 AT WAIKOLOA BEACH RESORT  
 BALANCE SHEET  
 DECEMBER 31, 2010

	FUNDS		
	Operating	Replacement	Total
<b>ASSETS</b>			
Cash and cash equivalents	\$ 613,257	\$ 90,534	\$ 703,791
Investments	-	275,055	275,055
Accounts receivable - members	27,064	-	27,064
Prepaid insurance	113,325	-	113,325
<b>Total assets</b>	<b>\$ 753,646</b>	<b>\$ 365,589</b>	<b>\$ 1,119,235</b>
<b>LIABILITIES AND FUND BALANCES</b>			
<b>LIABILITIES</b>			
Accounts payable and accrued expenses	\$ 192,901	\$ 40,861	\$ 233,762
Income taxes payable	3,455	-	3,455
Assessments received in advance	5,437	-	5,437
<b>Total liabilities</b>	<b>201,793</b>	<b>40,861</b>	<b>242,654</b>
<b>FUND BALANCES</b>	<b>551,853</b>	<b>324,728</b>	<b>876,581</b>
<b>Total liabilities and fund balances</b>	<b>\$ 753,646</b>	<b>\$ 365,589</b>	<b>\$ 1,119,235</b>

Read Independent Auditor's Report.  
 The accompanying notes are an integral  
 part of the financial statements.

ASSOCIATION OF APARTMENT OWNERS OF THE BAY CLUB  
 AT WAIKOLOA BEACH RESORT  
 STATEMENT OF REVENUES, EXPENSES AND CHANGES IN FUND BALANCES  
 FOR THE YEAR ENDED DECEMBER 31, 2010

	FUNDS		
	Operating	Replacement	Total
REVENUES			
Maintenance fees	\$ 2,247,690	\$ 240,270	\$ 2,487,960
Interest and dividends	-	44,223	44,223
Other	151,372	-	151,372
Gain on sales of investments	-	4,627	4,627
 Total revenues	 <u>2,399,062</u>	 <u>289,120</u>	 <u>2,688,182</u>
EXPENSES			
Administrative	509,235	-	509,235
Security	88,778	-	88,778
Common area	927,936	-	927,936
Utilities	628,730	-	628,730
Other	9,510	-	9,510
Replacement	-	1,433,491	1,433,491
 Total expenses	 <u>2,164,189</u>	 <u>1,433,491</u>	 <u>3,597,680</u>
 Excess (deficiency) of revenues over expenses	 234,873	 (1,144,371)	 (909,498)
FUND BALANCES - January 1, 2010	<u>316,980</u>	<u>1,469,099</u>	<u>1,786,079</u>
FUND BALANCES - December 31, 2010	<u>\$ 551,853</u>	<u>\$ 324,728</u>	<u>\$ 876,581</u>

Read Independent Auditor's Report.  
 The accompanying notes are an integral  
 part of the financial statements.

ASSOCIATION OF APARTMENT OWNERS OF THE BAY CLUB  
 AT WAIKOLOA BEACH RESORT  
 STATEMENT OF CASH FLOWS  
 FOR THE YEAR ENDED DECEMBER 31, 2010

	FUNDS		
	Operating	Replacement	Total
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>			
Maintenance fees collected	\$ 2,226,095	\$ 240,270	\$ 2,466,365
Interest and dividends received	-	44,324	44,324
Other revenue received	151,372	-	151,372
Cash paid for expenditures	(2,197,211)	(1,398,145)	(3,595,356)
Cash paid for income taxes	(9,100)	-	(9,100)
Net cash provided (used) by operating activities	171,156	(1,113,551)	(942,395)
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>			
Sales of investments	-	1,109,761	1,109,761
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>			
Interfund reimbursement	(1)	1	-
Net increase (decrease) in cash	171,155	(3,789)	167,366
<b>CASH AND CASH EQUIVALENTS -</b>			
January 1, 2010	442,102	94,323	536,425
<b>CASH AND CASH EQUIVALENTS -</b>			
December 31, 2010	<u>\$ 613,257</u>	<u>\$ 90,534</u>	<u>\$ 703,791</u>

	FUNDS		
	Operating	Replacement	Total
<b>RECONCILIATION OF EXCESS (DEFICIENCY) OF REVENUES OVER EXPENSES TO NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES</b>			
Excess (deficiency) of revenues over expenses	\$ 234,873	\$ (1,144,371)	\$ (909,498)
Adjustments to reconcile excess (deficiency) of revenues over expenses to net cash provided (used) by operating activities:			
Gain on sales of investments	-	(4,627)	(4,627)
Changes in:			
Accounts receivable - members	(22,694)	-	(22,694)
Accounts receivable - other	1,780	-	1,780
Interest receivable	-	101	101
Prepaid insurance	18,847	-	18,847
Accounts payable and accrued expenses	(49,056)	35,346	(13,710)
Income taxes payable	(5,645)	-	(5,645)
Due to BCVOA	(8,048)	-	(8,048)
Assessments received in advance	1,099	-	1,099
Total adjustments	(63,717)	30,820	(32,897)
Net cash provided (used) by operating activities	\$ 171,156	\$ (1,113,551)	\$ (942,395)

Read Independent Auditor's Report.  
The accompanying notes are an integral  
part of the financial statements.

ASSOCIATION OF APARTMENT OWNERS OF THE BAY CLUB  
AT WAIKOLOA BEACH RESORT  
NOTES TO FINANCIAL STATEMENTS  
DECEMBER 31, 2010

**NOTE 1 - THE ASSOCIATION**

Association of Apartment Owners of the Bay Club at Waikoloa Beach Resort (the “Association”) was incorporated on June 20, 1995, under the laws of Hawaii as a nonprofit, non-stock corporation to operate and manage the Bay Club at Waikoloa Beach Resort (the “Condominium”). The Condominium consists of 172 units located in Waikoloa Beach, Hawaii, of which 167 units are operated as an 8,517 interval unit-week timeshare association. The Association is responsible for roof replacement, building painting, pavement resurfacing, and capital improvements for the 172 units. The owners of all units and unit-weeks in the Condominium are the only members.

Nikken Corporation (the “Developer”), a Hawaii corporation, is the developer of the Condominium. As of December 31, 2010, the Developer owned 81 unit-weeks.

**NOTE 2 - DATE OF MANAGEMENT’S REVIEW**

In preparing the financial statements, the Association has evaluated events and transactions for potential recognition or disclosure through April 8, 2011, the date that the financial statements were available to be issued.

**NOTE 3 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

Fund Accounting

The Association prepares its financial statements on the accrual basis and presents them as separate funds based on its different funding policies for operations and major repairs and replacements.

The operating fund reflects the operating portion of the annual assessments billed to the unit-week owners and monthly assessments billed to the unit owners to meet the various day-to-day expenditures incurred in the administration and operation of the Condominium and its recreational facilities.

The replacement fund is composed of the portion of the annual and monthly assessments designated in the budget to fund future major repairs and replacements, as further described in Note 7.

Investments

The Association classifies its debt securities into held-to-maturity or available-for-sale categories. Debt securities are classified as held-to-maturity when the Association has the positive intent and ability to hold the securities to maturity. Debt securities for which the Association does not have the intent or ability to hold to maturity are classified as available-for-sale. Held-to-maturity securities are recorded at amortized cost. Available-for-sale securities are carried at fair market value, with the unrealized gains and losses, net of tax, included in the determination of other comprehensive income and reported as a separate component of fund balance.

The fair value of substantially all debt securities is determined by the broker using a third party source. Gains or losses on securities sold are based on the specific identification method.

ASSOCIATION OF APARTMENT OWNERS OF THE BAY CLUB  
AT WAIKOLOA BEACH RESORT  
NOTES TO FINANCIAL STATEMENTS  
DECEMBER 31, 2010

**NOTE 3 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

Accounts Receivable

Accounts receivable related to the five whole ownership units, are generally considered delinquent when they are one day past due. Association management has reviewed accounts receivable outstanding as of December 31, 2010 and considers them to be fully collectible. Based on this and the Association's prior history of insignificant bad debts on accounts receivable, no allowance for uncollectible accounts is considered necessary. Expense is recognized during the period in which a specific account is determined to be uncollectible. The Association has not incurred any bad debt expense for the year ended December 31, 2010.

Common Property

The Association is responsible to preserve and maintain the common property of the Condominium. Ownership of the commonly owned assets is vested directly or indirectly in the unit and unit-week owners, those assets are not titled in the Association's name and disposition of those assets by the Board of Directors (the "Board") is restricted. As a result, commonly owned assets are not presented in the Association's financial statements. Common property not capitalized consists of a pool, sidewalks, roadways, parking areas and landscaped areas.

Income Taxes

Management has analyzed its various federal and state filing positions and believes that the Association's income tax filing positions and deductions are well documented, supported and contain no uncertain tax positions. Additionally, management believes that no accruals for tax liabilities, interest or penalties are required. Therefore, no reserves for uncertain income tax positions have been recorded. Further, no interest or penalties have been included since no reserves were recorded. When applicable, such interest and penalties will be reported as income tax expense. The years 2007 through 2010 remain open to examination under federal statute and applicable state statute limitations.

The Association has elected to be taxed as a homeowners' association, in accordance with Internal Revenue Code Section 528. Under that Section, the Association is not taxed on uniform assessments to members and other income received from Association members solely as a function of their membership in the Association. The Association is taxed at a federal rate of 32% on its investment income and other non-exempt function income, less allocable expenses. There are no temporary differences between the financial reporting and tax reporting with respect to the non-exempt function income; therefore, no deferred tax provision has been recorded. The Association incurred an income tax liability of \$3,455 for the year ended December 31, 2010.

Fair Value of Financial Instruments

Substantially all of the Association's assets and liabilities, excluding prepaid insurance and assessments received in advance, are considered financial instruments. These assets and liabilities are reflected at fair value, or at carrying amounts that approximate fair value because of the short maturity of the instrument. Investments are valued based on the classification as further described in the investment policy above.

ASSOCIATION OF APARTMENT OWNERS OF THE BAY CLUB  
AT WAIKOLOA BEACH RESORT  
NOTES TO FINANCIAL STATEMENTS  
DECEMBER 31, 2010

**NOTE 3 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

Revenue Recognition

Maintenance fees revenue is recognized monthly in the amount of the membership assessment allocation specified for current period operations, based on the annual budget adopted by the Board. Each unit and unit-week owner is an Association member and a proportionate amount of the maintenance fees is assessed for each unit and unit-week.

Maintenance fees for the unit-weeks are billed and collected through The Bay Club Vacation Owners Association ("BCVOA"). The fees are then transferred to the Association on a monthly basis. In addition, certain costs are allocated between the Association and BCVOA. As of December 31, 2010, no amount was due to BCVOA. Maintenance fees assessments invoiced from BCVOA were \$2,402,319 for the year ended December 31, 2010.

Cash Flows

For purposes of the statement of cash flows, the Association considers all highly liquid debt instruments purchased with an original maturity of three months or less to be cash equivalents.

The Association made cash payments of \$9,100 for income taxes and no cash payments for interest during the year ended December 31, 2010.

Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the financial statements and the reported amount of revenues and expenses during the reporting period. Actual results could differ from those estimates.

**NOTE 4 - CONCENTRATION OF CREDIT RISK**

The Association maintains cash balances at two financial institutions. Accounts at each institution are insured by the Federal Deposit Insurance Corporation ("FDIC"). The balances were fully insured as of December 31, 2010, based on the bank statement balances, less the FDIC insurance. Cash equivalents totaling \$30,452 as of December 31, 2010, are not insured by the FDIC. These non-insured FDIC funds are maintained in money market mutual funds invested in U.S. Government obligations.

ASSOCIATION OF APARTMENT OWNERS OF THE BAY CLUB  
 AT WAIKOLOA BEACH RESORT  
 NOTES TO FINANCIAL STATEMENTS  
 DECEMBER 31, 2010

**NOTE 5 - INVESTMENTS**

The Association invests idle cash balances in debt securities. The amortized historical cost, aggregate fair value, and gross unrealized holding losses, summarized by major security type, as of December 31, 2010, consisted of:

<u>Replacement Fund</u>	<u>Amortized Historical Cost</u>	<u>Aggregate Fair Value</u>	<u>Gross Unrealized Holding Losses</u>
Held-to-maturity			
Municipal bonds	\$ 275,055	\$ 259,378	\$ (15,677)

Future maturities of debt securities held as of December 31, 2010, consist of:

<u>Maturities</u>	<u>Amortized Historical Cost</u>	<u>Aggregate Fair Value</u>	<u>Unrealized Holding Losses</u>
Less than 1 year	\$ 275,055	\$ 259,378	\$ (15,677)

**NOTE 6 - ASSESSMENTS RECEIVED IN ADVANCE**

Assessments received in advance consisted of 2011 maintenance fees for units received by the Association prior to January 1, 2011.

**NOTE 7 - REPLACEMENT FUND**

The Association's replacement fund is utilized to accumulate funds for future major repairs and replacements, by an allocation of the maintenance fees assessment charged to each unit and unit-week owner, and specifically designated for the fund in the annual budget. Deductions from the fund are recorded as costs, as incurred, which are determined by the Board, to meet the objective for which the fund was established.

The following is a table of the current year's activity in the replacement fund, by component:

<u>Components</u>	<u>Balance January 1, 2010</u>	<u>Additions to Fund</u>	<u>Charges to Fund</u>	<u>Intrafund Transfer</u>	<u>Balance December 31, 2010</u>
Roof	\$ 752,979	\$ 113,931	\$ 92,731	\$ (719,238)	\$ 54,941
Painting	363,223	40,386	517,662	149,485	35,432
Paving	98,117	23,125	9,376	(98,327)	13,539
Capital improvements	254,780	111,678	813,722	668,080	220,816
	<u>\$ 1,469,099</u>	<u>\$ 289,120</u>	<u>\$ 1,433,491</u>	<u>\$ -</u>	<u>\$ 324,728</u>

ASSOCIATION OF APARTMENT OWNERS OF THE BAY CLUB  
AT WAIKOLOA BEACH RESORT  
NOTES TO FINANCIAL STATEMENTS  
DECEMBER 31, 2010

**NOTE 7 - REPLACEMENT FUND (Continued)**

Additions to fund include \$44,223 of interest and dividends and gain on sales of investments of \$4,627. The Association's policy for allocating the replacement fund's investment income is based on the same percentage each components beginning fund balance bears to the total beginning fund balance. During the year ended December 31, 2010, the Board approved a transfer among the components of the replacement fund.

During the year ended December 31, 2010, the Association funded for major repairs and replacements over the estimated useful lives of the components, based on an independent reserve consulting firm's estimates of current replacement costs.

The 2011 proposed budgeted funding is \$270,304, as shown in the unaudited supplementary information. The components' actual replacement costs, useful lives, and investment income may vary from the estimated amounts and the variation may be material. Therefore, the Association's replacement fund may not be adequate to meet all future needs for major repairs and replacements. If additional funds are needed, the Association has the right, subject to the Board's approval, to increase regular assessments, pass special assessments, transfer among components, or delay major repairs and replacements until funds are available.

**NOTE 8 - OPERATING LEASE**

Although no written agreement has been signed the Association leases the activities desk to Hilton Grand Vacations Company, LLC's ("HGVC") marketing department, to market HGVC's Kohala Vacation Suites. The lease requires monthly payments of \$6,050 with an annual increase of 10% thereafter until the agreement expires. Rental income received for the year ended December 31, 2010 was \$72,600 and is included in other revenue.

**NOTE 9 - COMMITMENTS**

The Association currently has a one-year management agreement ending in June 2011, with HGVC. HGVC provides on-site management and maintenance services and off-site administrative and accounting services. The contract automatically renews for successive one-year periods unless HGVC or the Association determines not to renew the agreement and gives appropriate notice of that determination.

Although no written agreement has been signed, the Association allows BCVOA to conduct certain operations in the designated common elements of the Association. BCVOA pays a monthly fee of \$6,552 together with Hawaii general excise tax. For the year ended December 31, 2010, fees amounted to \$78,624 and are included in other revenue.

**SUPPLEMENTARY INFORMATION**

ASSOCIATION OF APARTMENT OWNERS OF THE BAY CLUB  
 AT WAIKOLOA BEACH RESORT  
 SUPPLEMENTARY INFORMATION ON  
 FUTURE MAJOR REPAIRS AND REPLACEMENTS  
 DECEMBER 31, 2010  
 (Unaudited)

A study was performed by an independent appraiser during 2009, to estimate the remaining useful lives and replacement costs of the components of common property. The estimates were based on future estimated replacement costs. The following table presents significant information about the components of common property. Amounts are based on normal operation and without the effect of potential catastrophic occurrences.

Components	Average Estimated Useful Lives	Average Estimated Remaining Useful Lives	Estimated Current Replacement Costs	2011 Proposed Budgeted Funding
Roof	20.00 years	10.38 years	\$ 1,545,000	\$ 45,284
Capital improvements	11.71 years	6.55 years	2,426,725	109,034
Painting	10.00 years	5.40 years	787,412	107,862
Pavement	18.33 years	9.33 years	313,520	8,124
			<u>\$ 5,072,657</u>	<u>\$ 270,304</u>

Estimated current replacement costs are based on the assumption that the rate of investment income earned on replacement funds will be 3% and the rate of inflation 4%.

ASSOCIATION OF APARTMENT OWNERS OF THE BAY CLUB  
 AT WAIKOLOA BEACH RESORT  
 SCHEDULE OF OPERATING FUND REVENUES AND EXPENSES -  
 BUDGET TO ACTUAL  
 FOR THE YEAR ENDED DECEMBER 31, 2010

	Budget <i>(Unaudited)</i>	Actual	Variance Favorable (Unfavorable)
<b>REVENUES</b>			
Maintenance fees	\$ 2,247,689	\$ 2,247,690	\$ 1
Other	151,224	151,372	148
Total operating fund revenues	<u>2,398,913</u>	<u>2,399,062</u>	<u>149</u>
<b>EXPENSES</b>			
<b>ADMINISTRATIVE</b>			
Annual audit	10,100	8,110	1,990
Management salaries and wages	90,034	77,006	13,028
Other administrative	144,633	109,310	35,323
General insurance	320,721	310,153	10,568
Financial services and data processing	2,856	2,856	-
Management fee	1,800	1,800	-
Total administrative	<u>570,144</u>	<u>509,235</u>	<u>60,909</u>
<b>SECURITY</b>			
Security payroll and related supplies	16,662	25,018	(8,356)
Security contract	54,000	63,760	(9,760)
Total security	<u>70,662</u>	<u>88,778</u>	<u>(18,116)</u>
<b>COMMON AREA</b>			
Common area payroll and related supplies	847,282	698,267	149,015
Grounds and landscaping	122,775	132,087	(9,312)
Pool and spa equipment and supplies	19,200	16,939	2,261
Building and equipment contracts	30,350	23,200	7,150
Elevator and fire system contracts	46,900	41,837	5,063
Automotive repair and supplies	14,300	15,606	(1,306)
Total common area	<u>1,080,807</u>	<u>927,936</u>	<u>152,871</u>
<b>UTILITIES</b>			
Electric	236,000	175,950	60,050
Water, sewer and gas	246,000	258,850	(12,850)
Waste disposal	78,000	83,287	(5,287)
Telephone	31,080	31,917	(837)
Cable television	78,000	78,726	(726)
Total utilities	<u>669,080</u>	<u>628,730</u>	<u>40,350</u>

	Budget <i>(Unaudited)</i>	Actual	Variance Favorable (Unfavorable)
OTHER			
Income taxes	2,220	3,455	(1,235)
Hawaii general excise tax	6,000	6,055	(55)
Total other	<u>8,220</u>	<u>9,510</u>	<u>(1,290)</u>
 Total operating fund expenses	 <u>2,398,913</u>	 <u>2,164,189</u>	 <u>234,724</u>
 Excess of revenues over expenses	 <u>\$ -</u>	 <u>\$ 234,873</u>	 <u>\$ 234,873</u>