

**LAKE ROYALE PROPERTY  
OWNERS ASSOCIATION, INC.**

**FINANCIAL STATEMENTS**

**BUNN, NORTH CAROLINA**

**YEAR ENDED MARCH 31, 2009**

## CONTENTS

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	Page (s)
Independent Auditors' Report	3
FINANCIAL STATEMENTS	
Balance Sheet	4
Statement of Revenues and Expenses	5
Statement of Changes in Members' Equity	6
Statement of Cash Flows	7
Notes to Financial Statements	8

PETWAY  
MILLS &  
PEARSON, PA

Board of Directors  
Lake Royale Property Owners Association, Inc.  
Bunn, North Carolina

CERTIFIED PUBLIC ACCOUNTANTS

C. Briggs Petway, Jr.  
Roger G. Mills  
Phyllis M. Pearson

We have audited the accompanying balance sheet of Lake Royale Property Owners Association, Inc., as of March 31, 2009 and the related statements of revenues, expenses, and changes in members' equity and cash flows for the year then ended. These financial statements are the responsibility of Lake Royale Property Owners Association, Inc.'s management. Our responsibility is to express an opinion on these financial statements based on our audit.

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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 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.

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In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Lake Royale Property Owners Association, Inc., as of March 31, 2009, and the changes in members' equity and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The reserve study information in Note 7 is not a required part of the basic financial statements, and we did not audit and do not express an opinion on it. The American Institute of Certified Public Accountants has determined that supplementary information about future major repairs and replacements of common property is required to supplement, but not required to be a part of, the basic financial statements. The Association has not presented this supplementary information.

*Memberships:*

North Carolina  
Association of  
Certified Public  
Accountants

Our audit was performed for the purpose of forming an opinion on the basic financial statements taken as a whole. We have not applied procedures to determine whether the funds designated for future major repairs and replacements are adequate to meet such future costs because that determination is outside the scope of our audit.

American Institute  
of Certified Public  
Accountants

Petway Mills & Pearson, PA

PETWAY MILLS & PEARSON, PA  
Certified Public Accountants  
Zebulon, North Carolina

Medical Group  
Management  
Association

July 13, 2009

**LAKE ROYALE PROPERTY OWNERS ASSOCIATION, INC.**  
**BALANCE SHEET**  
**MARCH 31, 2009**

**Assets**

<b>Current assets</b>		\$ 808,699
Cash - undesignated		1,064,353
Cash - designated		575,232
Dues and fees receivable, net of allowance for uncollectible accounts		20,561
Prepaid expenses		35,383
Prepaid income taxes		544,751
Land inventory		<u>3,048,979</u>
<b>Total current assets</b>		<u>3,048,979</u>
<b>Fixed assets</b>		<u>3,013,746</u>
Property and equipment, net of accumulated depreciation		<u>3,013,746</u>
<b>Total fixed assets</b>		<u>3,013,746</u>
<b>Total assets</b>		<u><u>\$ 6,062,725</u></u>

**Liabilities and Members' Equity**

<b>Current liabilities</b>		\$ 880,950
Dues received in advance		57,540
Accounts payable and accrued expenses		30,671
Wages payable		26,102
Accrued leave		1,842
Security deposits		20,232
Deferred revenue		149,516
Current portion of note payable		<u>1,166,853</u>
<b>Total current liabilities</b>		<u>1,166,853</u>
<b>Long-term liabilities</b>		<u>500,565</u>
Note payable		<u>500,565</u>
<b>Total long-term liabilities</b>		<u>500,565</u>
<b>Total liabilities</b>		<u>1,667,418</u>
<b>Members' equity</b>		164,324
Contributed capital		3,166,630
Undesignated		693,854
Designated for future major repairs and replacements		200,000
Designated for emergency disaster fund		170,499
Designated for road repairs		<u>4,395,307</u>
<b>Total members' equity</b>		<u>4,395,307</u>
<b>Total liabilities and members' equity</b>		<u><u>\$ 6,062,725</u></u>

See Accompanying Notes to Financial Statements.

LAKE ROYALE PROPERTY OWNERS ASSOCIATION, INC.  
STATEMENT OF REVENUES AND EXPENSES  
YEAR ENDED MARCH 31, 2009

<b>Operating revenues</b>	
Member dues - operations	\$ 1,515,148
Member dues - repairs and replacements	844,101
User fees	64,106
Other fees	388,297
Rental income - office	30,263
Other income	3,903
<b>Total operating revenues</b>	<u>2,845,818</u>
<b>Operating expenses</b>	
Salaries and wages	852,295
Payroll taxes	71,782
Employee benefits	165,119
Contracted services	179,919
Contracted labor	6,935
Depreciation	280,389
Insurance	67,362
Operating supplies	98,397
Utilities	131,971
Repairs and maintenance	90,005
Professional fees	55,803
Taxes and licenses	3,349
Vehicle expense	48,006
Communications	28,239
Postage and printing	35,536
Staff development and training	11,030
Board meeting expense	11,094
Special Projects	14,449
Other operating expenses	14,073
<b>Total operating expenses</b>	<u>2,165,753</u>
<b>Net operating income (loss)</b>	<u>680,065</u>
<b>Foreclosure Income</b>	
Land income	344,890
Foreclosure billed income	156,793
Received land foreclosure income	491,885
<b>Total foreclosure income</b>	<u>993,568</u>
<b>Cost of foreclosures</b>	
Cost of land inventory sold	560,090
Land sales expense	38,370
Foreclosure property taxes	41,173
Foreclosure legal fees	222,794
Uncollectible accounts - foreclosures	83,806
Miscellaneous foreclosure expenses	4,458
<b>Total cost of foreclosures</b>	<u>950,691</u>
<b>Gain on foreclosures</b>	<u>42,877</u>
<b>Other Income (Expenses)</b>	
Interest income	34,051
Uncollectible accounts	(797,946)
Loss on disposal of fixed assets	(69)
Penalties and Interest	(4,405)
Interest expense	(46,296)
Income tax expense	(76,684)
<b>Total other income (expenses)</b>	<u>(891,349)</u>
<b>Deficit of revenues over expenses</b>	<u>\$ (168,407)</u>

See Accompanying Notes to Financial Statements.

LAKE ROYALE PROPERTY OWNERS ASSOCIATION, INC.  
STATEMENT OF CHANGES IN MEMBERS' EQUITY  
YEAR ENDED MARCH 31, 2009

	Total	Undesignated	Designated for Future Repairs	Designated for Emergency Disaster	Designated for Road Repairs
<b>Members' equity - April 1, 2008</b>	\$ 4,399,390	\$ 3,545,508	\$ 653,435	\$ 200,447	\$ -
Deficit of revenues over expenses	(168,407)	(168,407)	-	-	
Allocated to future repairs and replacements:					
Dues Collected	-	(844,101)	844,101	-	-
Major repairs/replacements:					
Land	-	6,039	(6,039)	-	-
Buildings	-	5,296	(5,296)	-	-
Furniture and equipment	-	64,254	(64,254)	-	-
Vehicles	-	31,326	(31,326)	-	-
Improvements	-	11,463	(11,463)	-	-
Principal paid on road loan	-	204,001	(204,001)	-	-
Transfer to (from) undesignated equity	-	311,251	(481,303)	(447)	170,499
<b>Members' equity - March 31, 2009</b>	4,230,983	<u>\$ 3,166,630</u>	<u>\$ 693,854</u>	<u>\$ 200,000</u>	<u>\$ 170,499</u>
<b>Add contributed capital</b>	<u>164,324</u>				
<b>Total members' equity - March 31, 2009</b>	<u>\$ 4,395,307</u>				

See Accompanying Notes to Financial Statements.

**LAKE ROYALE PROPERTY OWNERS ASSOCIATION, INC.**  
**STATEMENT OF CASH FLOWS**  
**YEAR ENDED MARCH 31, 2009**

<b>Cash flows from operating activities</b>	<b>\$ (168,407)</b>
Deficit of revenues over expenses	
Adjustments to reconcile deficit of revenues over expenses to net cash provided by operating activities:	
Depreciation	280,389
Noncash adjustments	(3,109)
Loss on sale of assets	69
(Gain) on lot foreclosures	(42,877)
(Increase) decrease in:	
Dues and fees receivable	341,017
Prepaid expense	(938)
Prepaid income taxes	(35,383)
Increase (decrease) in:	
Dues received in advance	31,275
Accounts payable and accrued expenses	(34,446)
Wages payable	823
Accrued leave	1,903
Security deposits	373
Deferred revenue	7,806
Total adjustments	<u>546,902</u>
<b>Net cash provided by operating activities</b>	<u>378,495</u>
<b>Cash flows from investing activities</b>	111,081
Proceeds from sale of property	
Capital expenditures	<u>(118,378)</u>
<b>Net cash used by investing activities</b>	<u>(7,297)</u>
<b>Cash flows from financing activities</b>	(204,001)
Principal payments on long-term debt	<u>(204,001)</u>
<b>Net cash used in financing activities</b>	<u>(204,001)</u>
<b>Net increase in cash and cash equivalents</b>	167,197
<b>Cash and cash equivalents, beginning of year</b>	<u>1,705,855</u>
<b>Cash and cash equivalents, end of year</b>	<u><u>\$ 1,873,052</u></u>
<b>Summary of Cash Accounts</b>	
Cash - undesignated	\$ 808,699
Cash - designated	1,064,353
<b>Total cash</b>	<u><u>\$ 1,873,052</u></u>

See Accompanying Notes to Financial Statements.

**LAKE ROYALE PROPERTY OWNERS ASSOCIATION, INC.**  
**NOTES TO FINANCIAL STATEMENTS**  
**MARCH 31, 2009**

**NOTE 1 – NATURE OF ORGANIZATION**

Lake Royale Property Owners Association, Inc. (Association) located in Bunn, North Carolina was incorporated in January 1972 as a non-stock corporation in the State of North Carolina. The Association is responsible for the operation and maintenance of the common property within the development, which surrounds a 345-acre lake and consists of entrance gates, comfort centers, pool, miniature golf course and roads. There are approximately 4,700 current property owners. The majority of the owners permanently reside in North Carolina; however, there are some located throughout the United States and abroad.

**NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**Basis of Accounting** - The accompanying financial statements have been prepared on the accrual basis of accounting.

**Dues and Fees Receivable** – Association members are subject to annual dues to provide funds for the Association's operating expenses, future capital acquisitions and major repairs and replacements. Dues and fees receivable at the balance sheet date represent the annual assessments and other fees including late charges, lien fees, etc. due from property owners. The Association's policy is to retain legal counsel and place liens on members' property and proceed with foreclosures as warranted when dues are delinquent. Uncollectible accounts were estimated at \$2,118,692 as of March 31, 2009.

**Income Tax Status** – The Association is taxed as a regular corporation. As a regular corporation, membership income is exempt from taxation if certain elections are made, and the Association is taxed only on its nonmembership income, such as interest earnings and rental income, at regular federal and State corporate rates. Exempt function income, which consists primarily of member assessments, is not taxable.

**Property and Equipment** – Buildings, furniture, equipment, vehicles, and improvements are recorded at cost. If an expenditure results in an asset having an estimated useful life which extends substantially beyond the year of acquisition, the expenditure is capitalized and depreciated or amortized over the estimated useful life of the asset. Depreciation is calculated by the straight-line method over the useful lives of the assets as follows:

Buildings	30 years
Furniture and Equipment	5-15 years
Vehicles	5-7 years
Improvements	10-30 years

Maintenance and repairs are charged to expense as incurred. Property contributed to the Association by the developer is recorded at estimated fair value at the date of contribution.

**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.

**Cash and Cash Equivalents** – The Association considers all cash and other highly liquid assets with maturities of three months or less at the date of acquisition to be "cash and cash equivalents."

**LAKE ROYALE PROPERTY OWNERS ASSOCIATION, INC.**  
**NOTES TO FINANCIAL STATEMENTS**  
**MARCH 31, 2009**

**NOTE 3 – PROPERTY AND EQUIPMENT**

Property and equipment consists of the following at March 31, 2009:

Land	\$ 36,363
Greenways	123,130
Buildings	528,060
Furniture and Equipment	387,958
Vehicles	168,364
Improvements	<u>4,122,539</u>
	5,366,414
Less Accumulated Depreciation	<u>(2,352,668)</u>
	<u><u>\$ 3,013,746</u></u>

**NOTE 4 – REAL ESTATE ACQUIRED**

The Association acquired the titles to various lots during the year through legal proceedings due to abandonment or foreclosure. These lots have been recorded at their fair value with a gain or loss recognized on the difference between the fair value of the property received and the delinquent assessments and related fees. Management has utilized property tax valuation to establish fair value.

**NOTE 5 – CONCENTRATION OF CREDIT RISK FOR CASH HELD IN BANK**

The Association maintains its cash balances in four financial institutions. The balances are insured by the Federal Deposit Insurance Corporation up to \$250,000. As of March 31, 2009, the Association's uninsured cash balances were \$897,250, \$2,248 and \$1,606. The Association does not believe that it is exposed to any significant credit risk on uninsured amounts.

**NOTE 6 – CONTRIBUTED CAPITAL**

Contributed capital consists of the estimated fair value of certain land and buildings transferred from National American Companies (NACO) to the Association at no cost during the 1993-1994 fiscal year.

**NOTE 7 – FUTURE MAJOR REPAIRS AND REPLACEMENTS**

The Association's governing documents require the Association to provide for future major repairs and replacements of common property, including the roads, pool and clubhouse.

During 2007, the Association hired a firm to perform a reserve study. The Association will contribute funds to its replacement fund based on this study. Actual expenditures, however, may vary from the estimated amounts and the variations may be material. Therefore, amounts accumulated in the reserve fund may not be adequate to meet future needs. The Association is not required to accumulate funds for estimated future repairs and replacements; however, if additional funds are needed, the Association has the right, subject to member approval, to increase regular assessments, to levy special assessments, or it may delay major repairs and replacements until funds are available.

During the current fiscal year, the Association continued with its program to accumulate funds for future repairs and replacements. Of dues collected during the year, 18.4% of current dues collections and 100% of all prior years' dues collections were transferred to funds designated for future repairs and replacements. The cash available at March 31, 2009 designated for future major repairs and replacements is \$1,064,353 and is included in the balance sheet line item titled "Cash - designated." The change in net equity is shown on the statement of changes in members' equity.

**LAKE ROYALE PROPERTY OWNERS ASSOCIATION, INC.  
NOTES TO FINANCIAL STATEMENTS  
MARCH 31, 2009**

**NOTE 8 – SECURITY DEPOSIT LIABILITY**

Security deposits are received on camping rentals and business rentals. These deposits are refundable and as such are recorded as a liability by the Association. Outstanding security deposits held by the Association as of March 31, 2009 are \$1,842.

**NOTE 9 – OPERATING LEASES**

The Association leases office space to various organizations. The leases operate on an annual basis indefinitely until the Association gives the tenant thirty days notice to vacate the premises or the tenant gives the Association thirty days notice of its intention to vacate the premises. The total revenue received during the year from office space leases was \$30,263.

**NOTE 10 – DEFERRED REVENUE**

In prior years, the Association received funds from the North Carolina Division of Emergency Management to be used in establishing a Community Emergency Response Team (CERT). In addition to these grant funds, donations were also received for this purpose. As of March 31, 2009, there remains a balance of \$100 not yet spent and is included in "Deferred Revenue" on the balance sheet.

The Association also holds funds for several of its committees conducting projects during the year until needed. The total of these funds included in "Deferred revenue" at March 31, 2009 is \$20,132.

**NOTE 11 – NOTE PAYABLE**

Note payable consists of the following at March 31, 2009:

Note to bank with annual principal payments of \$149,516 and interest payments due monthly with final payment of all unpaid principal and interest due January 2014, interest at 6.5%, secured by assessments	<u>\$ 650,081</u>
Total Note Payable	<u><u>\$ 650,081</u></u>

Aggregate maturities of the note payable are as follows:

Year ended March 31	
2010	\$ 149,516
2011	149,516
2012	149,516
2013	149,516
2014	<u>52,017</u>
	<u><u>\$ 650,081</u></u>

**LAKE ROYALE PROPERTY OWNERS ASSOCIATION, INC.**  
**NOTES TO FINANCIAL STATEMENTS**  
**MARCH 31, 2009**

**NOTE 12 – CASH AND CASH EQUIVALENTS**

Cash and cash equivalents consist of the following:

Cash - undesignated	<u>\$ 808,699</u>
Cash - designated for future major repairs and replacements	693,854
Cash - designated for emergency disaster fund	200,000
Cash - designated for road repairs	<u>170,499</u>
	<u>1,064,353</u>
Total cash and cash equivalents	<u><u>\$ 1,873,052</u></u>

**NOTE 13 – SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION**

Cash paid during the year for:

Interest expense	<u>\$ 46,296</u>
Income taxes paid	<u>\$ 76,684</u>

Schedule of Non - cash Investing and Financing Transactions

Fair value of lots acquired by abandonment/foreclosure	
Delinquent dues and fees satisfied due to abandonment/foreclosure	<u>\$ 491,885</u>

**NOTE 14 – RETIREMENT PLAN**

The Association maintains a SIMPLE IRA retirement plan for eligible employees. For those employees contributing a portion of their earning into the plan, the Association matched the employee deferral on a dollar-for-dollar basis up to 3% of allowed compensation. For the year ended March 31, 2009, retirement expense was \$18,058.

**NOTE 15 – MARKET CONCENTRATIONS**

The majority of the Association's members reside in Bunn, North Carolina and within the Lake Royale Development.

**NOTE 16 – COMMITMENTS**

On January 12, 2009, the Association entered into a contract with H.G. Reynolds Company, Inc. to perform dam and spillway repairs which will approximate \$241,117. Repairs have not been started as of March 31, 2009.

On November 7, 2008, the Association entered into a contract with Progress Energy for surge protection services. The rental amount for the protection is \$6.36 per month, and the initial term of service is 24 months. The Association is obligated to pay \$76 and \$45 during the years ended March 31, 2010 and 2011 under this contract.

**NOTE 17 – FAIR VALUE OF FINANCIAL INSTRUMENTS**

The following methods and assumptions were used by the Association in estimating the fair value of its financial instruments:

Accounts Receivable – The carrying amount reported in the balance sheet approximates fair value due to the short-term nature of the receivables.

**LAKE ROYALE PROPERTY OWNERS ASSOCIATION, INC.**  
**NOTES TO FINANCIAL STATEMENTS**  
**MARCH 31, 2009**

Note Payable – The carrying amount reported in the balance sheet approximates fair value because the Association can obtain similar loans at the same terms with other parties.

	Carrying Amount	Fair Value
Accounts Receivable	\$ 575,232	\$ 575,232
Note Payable	\$ 650,081	\$ 650,081