

Financial Statements

**Desert Breezes Resort
Timeshare Owners Association**

**For the Year Ended
October 31, 2017**

Desert Breezes Resort Timeshare Owners Association

Contents

October 31, 2017

(Summarized Totals for October 31, 2016)

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Report of Independent Auditor

Board of Directors
Desert Breezes Resort
Timeshare Owners Association
Palm Desert, California

We have audited the accompanying financial statements of Desert Breezes Resort Timeshare Owners Association which comprise the balance sheet as of October 31, 2017, and the related statements of income, expenses, changes in fund balances, cash flows, and other operating income and expenses 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 Desert Breezes Resort Timeshare Owners Association as of October 31, 2017, and the results of its operations and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Board of Directors
Desert Breezes Resort
Timeshare Owners Association
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Report on Supplementary Information

Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The supplemental information on Future Major Repairs and Replacements on Page 12, which is the responsibility of the Association's management, is presented for purposes of additional analysis and is not a required part of the financial statements. Such information has not been subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we do not express an opinion or provide any assurance on it.

Other Matter

The prior year summarized comparative information has been derived from the Association's October 31, 2016 financial statements and, in our report dated January 12, 2017, we expressed an unqualified opinion on those financial statements.

FITZGERALD & ASSOCIATES, INC. CPAs

Redlands, California
December 20, 2017

**Desert Breezes Resort
Timeshare Owners Association**

**Balance Sheet
October 31, 2017**

(Summarized Totals for October 31, 2016)

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	<u>Operating Fund</u>	<u>Replacement Fund</u>	<u>Capital Fund</u>	<u>2017 Total</u>	<u>2016 Total</u>
Assets					
Cash, including interest-bearing deposits	\$ 1,520,586	\$ 440,491	\$ -	\$ 1,961,077	\$ 2,135,707
Accounts receivable, net (Note 4)	46,828	-	-	46,828	46,497
Interest receivable	3,753	-	-	3,753	2,455
Interval inventory	53,569	-	-	53,569	53,569
Prepaid expenses (Note 5)	91,959	-	-	91,959	59,687
Property and equipment, net (Note 7)	-	-	100,000	100,000	100,000
Total assets	<u>\$ 1,716,695</u>	<u>\$ 440,491</u>	<u>\$ 100,000</u>	<u>\$ 2,257,186</u>	<u>\$ 2,397,915</u>
Liabilities and Fund Balances					
Accounts payable	\$ 42,878	\$ -	\$ -	\$ 42,878	\$ 163,885
Accrued expenses (Note 6)	32,179	-	-	32,179	35,704
Due to related association	6,252	-	-	6,252	7,065
Prepaid assessments	1,183,260	-	-	1,183,260	1,081,839
Total liabilities	<u>1,264,569</u>	<u>-</u>	<u>-</u>	<u>1,264,569</u>	<u>1,288,493</u>
Fund balances	<u>452,126</u>	<u>440,491</u>	<u>100,000</u>	<u>992,617</u>	<u>1,109,422</u>
Total liabilities and fund balances	<u>\$ 1,716,695</u>	<u>\$ 440,491</u>	<u>\$ 100,000</u>	<u>\$ 2,257,186</u>	<u>\$ 2,397,915</u>

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

**Desert Breezes Resort
Timeshare Owners Association**

**Statement of Revenue, Expenses, and Changes in Fund Balances
For the Year Ended October 31, 2017
(Summarized Totals for October 31, 2016)**

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	<u>Operating Fund</u>	<u>Replacement Fund</u>	<u>Capital Fund</u>	<u>2017 Total</u>	<u>2016 Total</u>
Revenue					
Member assessments	\$ 2,327,118	\$ 218,891	\$ -	\$ 2,546,009	\$ 2,489,532
Interest income	8,682	970	-	9,652	8,322
Rental income	379,983	-	-	379,983	348,901
Bonus time	67,436	-	-	67,436	62,596
Other income (Schedule)	118,181	-	-	118,181	111,120
Total revenue	<u>2,901,400</u>	<u>219,861</u>	<u>-</u>	<u>3,121,261</u>	<u>3,020,471</u>
Expenses					
Bad debt expense	424,137	-	-	424,137	372,062
Front desk	254,628	-	-	254,628	226,522
General maintenance	535,993	-	-	535,993	565,199
General and administrative (Schedule)	676,320	-	-	676,320	662,942
Housekeeping	664,604	-	-	664,604	645,496
Income taxes	17,005	-	-	17,005	29,110
Repairs and replacements	-	374,453	-	374,453	224,507
Utilities	290,926	-	-	290,926	294,415
Total expenses	<u>2,863,613</u>	<u>374,453</u>	<u>-</u>	<u>3,238,066</u>	<u>3,020,253</u>
Excess revenue (expenses)	37,787	(154,592)	-	(116,805)	218
Fund balance, beginning	415,590	593,832	100,000	1,109,422	1,109,204
Fund transfers	(1,251)	1,251	-	-	-
Fund balance, ending	<u>\$ 452,126</u>	<u>\$ 440,491</u>	<u>\$ 100,000</u>	<u>\$ 992,617</u>	<u>\$ 1,109,422</u>

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

**Desert Breezes Resort
Timeshare Owners Association**

**Statement of Cash Flows
For the Year Ended October 31, 2017
(Summarized Totals for October 31, 2016)**

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	<u>Operating Fund</u>	<u>Replacement Fund</u>	<u>Capital Fund</u>	<u>2017 Total</u>	<u>2016 Total</u>
Cash Flows From Operating Activities					
Excess revenue (expenses)	\$ 37,787	\$ (154,592)	\$ -	\$ (116,805)	\$ 218
Adjustments to reconcile excess of revenues over expenses to net cash provided by operating activities:					
Changes in:					
Accounts receivable	(331)	-	-	(331)	(12,584)
Interest receivable	(1,298)	-	-	(1,298)	(954)
Interval deposit	-	-	-	-	44,145
Interval inventory	-	-	-	-	(53,569)
Prepaid expenses	(32,272)	-	-	(32,272)	4,778
Accounts payable	(119,757)	(1,250)	-	(121,007)	68,218
Accrued expenses	(3,525)	-	-	(3,525)	(4,455)
Due to related association	(813)	-	-	(813)	3,295
Prepaid assessments	101,421	-	-	101,421	(130,974)
Net cash provided (used) by operating activities	<u>(18,788)</u>	<u>(155,842)</u>	<u>-</u>	<u>(174,630)</u>	<u>(81,882)</u>
Cash Flows From Financing Activities					
Interfund transfers	(150,000)	150,000			
Fund transfers	(1,251)	1,251	-	-	-
Net cash provided (used) by financing activities	<u>(151,251)</u>	<u>151,251</u>	<u>-</u>	<u>-</u>	<u>-</u>
Net increase (decrease) in cash	(170,039)	(4,591)	-	(174,630)	(81,882)
Cash, beginning of year	<u>1,690,625</u>	<u>445,082</u>	<u>-</u>	<u>2,135,707</u>	<u>2,217,589</u>
Cash, end of year	<u>\$ 1,520,586</u>	<u>\$ 440,491</u>	<u>\$ -</u>	<u>\$ 1,961,077</u>	<u>\$ 2,135,707</u>

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

**Desert Breezes Resort
Timeshare Owners Association**

**Statement of Other Operating Income and Expenses
For the Year Ended October 31, 2017
(Summarized Totals for October 31, 2016)**

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	<u>2017</u> <u>Total</u>	<u>2016</u> <u>Total</u>
Other Income		
Breezes time	\$ 13,658	\$ 13,763
Cleaning	4,123	4,364
Golf	8,792	12,308
Late fee income	17,962	38,037
Resort fees	57,481	25,306
Wi-Fi revenue	-	2,512
Other income	16,165	14,830
	<u>\$ 118,181</u>	<u>\$ 111,120</u>
General and Administrative		
Bank charges	\$ 45,480	\$ 31,528
Golf membership	8,543	11,226
Insurance	85,069	85,732
Legal and professional fees	12,900	9,642
Management fees	222,854	218,484
Master association dues	107,992	96,672
Property taxes	41,417	31,204
Payroll and related	111,081	97,054
Taxes and licenses	7,726	11,138
Wi-Fi expenses	3,540	20,535
Other general and administrative	29,718	49,727
	<u>\$ 676,320</u>	<u>\$ 662,942</u>

The accompanying notes are an integral part of these financial statements

Desert Breezes Resort Timeshare Owners Association

Notes to Financial Statements October 31, 2017 (Summarized Totals for October 31, 2016)

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1. Organization and Other Matters

Desert Breezes Resort Timeshare Owners Association was organized as a corporation in August 1984. The Association is responsible for the maintenance and operation of the common areas of 76 condominium units, representing 3,876 timeshare intervals, located in Palm Desert, California. The Association is a sub-association of the Desert Breezes Master Association.

2. Significant Accounting Policies

Comparative Information

The financial statements include certain 2016 comparative information. With respect to the balance sheet, the statement of revenue, expenses, and changes in fund balances, the statement of cash flows, and the statement of other operating income and expenses, such prior year information is not presented by fund. Accordingly, such information should be read in conjunction with the Association's financial statement for the year ended October 31, 2016 from which the summarized information was derived.

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. These estimates and assumptions affect the reported amounts of assets and liabilities at the reporting date and revenues and expenses during the reporting period. Actual results could differ from those estimates.

Fund Accounting

The Association's governing documents provide guidelines for managing its financial activities. To ensure compliance with limitations and restrictions on the use of financial resources, the Association maintains its records using fund accounting. They classify transactions for accounting and reporting purposes in funds established according to their nature and purpose.

Operating Fund - This fund is used to account for the financial resources available for the general operations of the Association.

Replacement Fund - This fund is used to account for financial resources designated for future major repairs and replacements.

Capital Fund - This fund is used to account for capital assets purchased by the Association and the related depreciation expense over the life of the asset.

Desert Breezes Resort Timeshare Owners Association

Notes to Financial Statements October 31, 2017 (Summarized Totals for October 31, 2016)

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2. Significant Accounting Policies (concluded)

Cash and Cash Equivalents

For financial statement purposes, the Association considers all highly liquid investments purchased with a maturity of three months or less to be cash equivalents.

Major Repairs and Replacements

Members pay a portion of their Association dues for reserve expenses, generally major repairs and replacements. The Association deposits these funds in separate interest-bearing bank accounts. See Note 8 for a further discussion of reserves.

Member Assessments

Members are subject to annual assessments to provide funds for operating expenses, future major repairs and replacements and capital asset acquisitions. The annual budget and assessments of owners are determined by the board of directors and are approved by the owners. Assessments receivable at the reporting date represent amounts due from members.

The Association's policy is to accrue interest on all amounts due, including delinquent assessments, reasonable collection costs and late charges commencing 30 days after assessments become due. Interest and related charges are recorded as income when billed to the owner. See Note 4 for details on accounts receivable. The Association's policies permit various collection remedies for delinquent assessments, principally the cancellation of the membership.

Property and Equipment

The costs of real property and the related improvements to such property in which the Association has title to are not presented as depreciable assets in the Association's financial statements as their disposition is restricted. The Association capitalizes personal property to which it has title at cost and depreciates them using the straight-line method over useful lives ranging from five to ten years. See Note 7 for additional information on property and equipment.

Interval Inventory

Interval inventory is valued at the lower of cost or market using the average cost method.

Prepaid Assessments

Prepaid assessments consist of members' annual assessments received in advance. The Association recognizes these amounts as income when they are earned in the subsequent year.

Desert Breezes Resort Timeshare Owners Association

Notes to Financial Statements October 31, 2017 (Summarized Totals for October 31, 2016)

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3. Income Taxes

Timeshare associations may elect to be taxed as regular corporations or as timeshare associations. The Association elected to be taxed as a timeshare association in accordance with Internal Revenue Code Section 528 for the year ending October 31, 2017 and 2016. Under that Section, the Association is not taxed on assessments to members and other income received from association members solely as a function of their membership in the Association.

The Association is taxed for federal purposes at the rate of 32% and taxed for state purposes at a rate of 8.84% on its nonexempt function income such as interest.

4. Accounts Receivable

Accounts receivable at the reporting dates consist of the following amounts:

	<u>2017</u>	<u>2016</u>
Member assessments	\$2,109,541	\$1,625,067
Due from Trading Places International-rentals	46,828	46,497
Allowance for doubtful accounts	<u>(2,109,541)</u>	<u>(1,625,067)</u>
Accounts receivable, net	<u>\$46,828</u>	<u>\$46,497</u>

5. Prepaid Expenses

Prepaid expenses at the reporting dates consist of the following amounts:

	<u>2017</u>	<u>2016</u>
Insurance	\$49,356	\$38,454
Income taxes	12,225	850
Other prepaid expenses	<u>30,378</u>	<u>20,383</u>
Total prepaid expenses	<u>\$91,959</u>	<u>\$59,687</u>

6. Accrued Expenses

Accrued expenses at the reporting dates consist of the following amounts:

	<u>2017</u>	<u>2016</u>
Sales and use tax	\$843	\$1,425
Accrued payroll and related costs	<u>31,336</u>	<u>34,279</u>
Total accrued expenses	<u>\$32,179</u>	<u>\$35,704</u>

Desert Breezes Resort Timeshare Owners Association

Notes to Financial Statements October 31, 2017 (Summarized Totals for October 31, 2016)

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7. Property and Equipment

Property and equipment at the reporting dates consist of the following amounts:

	<u>2017</u>	<u>2016</u>
Vehicles	\$16,252	\$16,252
Clubhouse building	229,659	229,659
Land	<u>100,000</u>	<u>100,000</u>
Total property and equipment	345,911	345,911
Less accumulated depreciation	<u>(245,911)</u>	<u>(245,911)</u>
Property and equipment-net	<u>\$100,000</u>	<u>\$100,000</u>

8. Future Major Repairs and Replacements

The Association's governing documents require that funds be accumulated for future major repairs and replacements. Accumulated funds are held in separate savings accounts and are generally not available for expenditures for normal operations.

Association Reserves, Inc. conducted a study in November 2016 to estimate the remaining useful lives and the replacement costs of the components of common property. The estimates were based on future estimated replacement costs. Fund requirements consider an annual inflation rate of 3 percent and interest of 1 percent, net of taxes, on amounts funded for future repairs and replacements. The table included in the unaudited supplementary information on Future Major Repairs and Replacements is based on the study. See the supplemental information presented on page 12 for additional details.

The board of directors decided to fund 87 percent of the amount recommended by the study for the year ended October 31, 2017. Accordingly, \$218,891 was included in the October 31, 2017 budget. For that reason, and because actual expenditures may vary from estimated future expenditures and the variations may be material, amounts accumulated in the 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 membership approval, to increase regular assessments, pass special assessments, or delay major repairs and replacements until funds are available.

Desert Breezes Resort Timeshare Owners Association

Notes to Financial Statements October 31, 2017 (Summarized Totals for October 31, 2016)

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9. Supplemental Cash Flow Information

Cash flows from operating activities included state and federal income tax payments of \$28,380 in 2017 and \$27,472 in 2016.

10. Commitments and Contingencies

The Association amended its management agreement with Trading Places International (TPI) beginning November 1, 2017 through December 31, 2022. The agreement increases the professional management fee for the fiscal year beginning November 1, 2017 with increases of 2% for each of the subsequent four years. The contract automatically renews for successive additional five-year terms unless terminated earlier by majority of the board members within a ninety-day window before the expiration of the current term. TPI will provide administrative, financial, and accounting services for the Association.

11. Subsequent Events

Management has evaluated subsequent events through December 20, 2017, the date which the financial statements were available for issue. Management has determined there are no subsequent events that require recognition or disclosure in these financial statements.

Supplemental Information

**Desert Breezes Resort
Timeshare Owners Association**

**Supplemental Information on Future Major
Repairs and Replacements
October 31, 2017 (Unaudited)**

Association Reserves, Inc., conducted a study in November of 2016 to estimate the remaining useful lives and replacement costs of the components of common property. The estimates were based on future estimated replacement costs. Funding requirements consider an annual inflation rate of 3% and interest of 1%, net of taxes, on amounts funded for future major repairs and replacements.

The following table is based on the study and presents significant information about the components of common property.

Component	Estimated Remaining Useful Life (Years)	Estimated November 2016 Replacement Cost	Estimated 2018 Funding Requirement	Reserve Expenditures For the Year Ended 10/31/17	Replacement Fund Cash 10/31/17
Unit building exteriors	0-19	\$ 1,462,400	\$ 52,888	\$ -	\$ 718,159
Unit building interiors	0-24	3,127,950	182,669	(305,302)	1,536,081
Clubhouse exterior	1-16	100,525	4,830	-	49,366
Clubhouse interior	0-13	159,250	11,826	-	78,205
Laundry facilities	0-4	47,600	3,019	-	23,376
Pools and spas	0-27	151,350	12,928	(16,265)	74,325
General common areas	0-29	840,750	23,570	(52,886)	412,877
Cash deficit		-	-	-	(2,451,898)
Totals		\$ 5,889,825	\$ 291,730	\$ (374,453)	\$ 440,491

See auditors' report.