

THE NEW PROPERTY OWNERS ASSOCIATION OF NEWPORT, INC.  
AND SUBSIDIARY

FINANCIAL STATEMENTS

For the Years Ended December 31, 2016 and 2015

Ken Skrabanek, CPA  
P.O. Box 1246  
Crosby, Texas 77532

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AND SUBSIDIARY  
FINANCIAL STATEMENTS  
For the Years Ended December 31, 2016 and 2015

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## Independent Auditor's Report

To the Board of Directors  
The New Property Owners Association of Newport, Inc.  
Crosby, Texas

### Report on the Financial Statements

I have audited the accompanying financial statements of The New Property Owners Association of Newport, Inc. And Subsidiary, which comprise the consolidating balance sheet as of December 31, 2016 and 2015, and the related consolidating statements of revenues and expenses and changes in fund balances/retained earnings, and the consolidated statements of cash flows for the years then ended, and the 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

My responsibility is to express an opinion on these financial statements based on my audit. I conducted my audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that I plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of 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



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effectiveness of the entity's internal control. Accordingly, I express no such opinion. An audit also includes evaluation of significant estimates made by management, as well as evaluating the overall presentation of the financial statements.

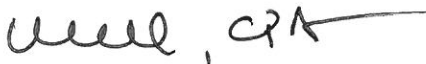
I believe the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

## Opinion

In my opinion, the financial statements referred to above present fairly, in all material respects, the financial position of The New Property Owners Association of Newport, Inc. And Subsidiary as of December 31, 2016 and 2015, and its revenues and expenses, and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

## Other Matter

The supplementary information on future repairs and replacements on page 13 is not a required part of the basic financial statements, but is supplementary information required by accounting principles generally accepted in the United States of America. I have applied certain limited procedures, which consisted primarily of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, I did not audit the information and express no opinion on it.

A handwritten signature in dark ink, appearing to read 'Ken Skrabanek', followed by a horizontal line.

Ken Skrabanek, CPA  
Crosby, Texas  
May 16, 2017

## December 31, 2016 and 2015

	2016				2015			
	The New Property Owners Association of Newport, Inc.	Stonebridge at Newport, Inc.	Eliminations	Consolidated Total	The New Property Owners Association of Newport, Inc.	Stonebridge at Newport, Inc.	Eliminations	Consolidated Total
<b>ASSETS</b>								
Cash	\$258,962	\$4,486	\$-	\$263,448	\$951,081	\$-	\$-	\$951,081
Certificate of deposits	235,723	-	-	235,723	24,098	-	-	24,098
Assessments receivable, net	791,359	-	-	791,359	637,087	-	-	637,087
Inventory	-	10,000	-	10,000	-	-	-	-
Prepaid expenses	29,942	-	-	29,942	47,776	-	-	47,776
Investment in Stonebridge at Newport, Inc.	87,247	-	(87,247)	-	-	-	-	-
Advances to Stonebridge at Newport, Inc.	706,910	-	(706,910)	-	-	-	-	-
Due from related party	-	-	-	-	87,247	-	-	87,247
Due from Newport Golf Partners	-	-	-	-	55,375	-	-	55,375
Utility deposit	-	2,351	-	2,351	-	-	-	-
Property and equipment, net	484,319	2,138,723	-	2,623,042	423,887	-	-	423,887
<b>Total Assets</b>	<b>\$2,594,462</b>	<b>\$2,155,560</b>	<b>(\$794,157)</b>	<b>\$3,955,865</b>	<b>\$2,226,551</b>	<b>\$-</b>	<b>\$-</b>	<b>\$2,226,551</b>
<b>LIABILITIES AND FUND BALANCE</b>								
<b>Liabilities</b>								
Accounts payable/accrued expenses	\$84,305	58,334	\$-	142,639	82,594	\$-	\$-	\$82,594
Prepaid assessments	297,728	-	-	297,728	247,282	-	-	247,282
Advances from Newport	-	706,910	(706,910)	-	-	-	-	0
Notes payable	180,410	1,736,103	-	1,916,513	196,018	-	-	196,018
Capital lease obligation	-	232,898	-	232,898	-	-	-	-
<b>Total Liabilities</b>	<b>562,443</b>	<b>2,734,245</b>	<b>(706,910)</b>	<b>2,589,778</b>	<b>525,894</b>	<b>-</b>	<b>-</b>	<b>525,894</b>
Fund balances/stockholder's equity	2,032,019	(578,685)	(87,247)	1,366,087	1,700,657	-	-	1,700,657
<b>Total Liabilities and Fund Balances</b>	<b>\$2,594,462</b>	<b>\$2,155,560</b>	<b>(\$794,157)</b>	<b>\$3,955,865</b>	<b>\$2,226,551</b>	<b>\$-</b>	<b>\$-</b>	<b>\$2,226,551</b>

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

**THE NEW PROPERTY OWNERS ASSOCIATION OF NEWPORT, INC. AND SUBSIDIARY**  
**CONSOLIDATING STATEMENT OF REVENUES AND EXPENSES**  
**AND CHANGES IN FUND BALANCES/RETAINED EARNINGS**  
For the Years Ended December 31, 2016 and 2015

	2016			2015				
	The New Property Owners Association of Newport, Inc.	Stonebridge at Newport, Inc.	Eliminations	Consolidated Total	The New Property Owners Association of Newport, Inc.	Stonebridge at Newport, Inc.	Eliminations	Consolidated Total
REVENUES								
Homeowner assessments	\$1,712,704	\$-	\$-	\$1,712,704	\$1,660,320	\$-	\$-	\$1,660,320
Late charges and other	453,727	18,770	-	472,497	397,814	-	-	397,814
Event revenues	-	229,386	-	229,386	-	-	-	-
Galley Grill	-	154,768	-	154,768	-	-	-	-
Golf operations	-	320,894	-	320,894	-	-	-	-
Total Revenues	2,166,431	723,818	-	2,890,249	2,058,134	-	-	2,058,134
COST OF SALES								
Events	-	65,753	-	65,753	-	-	-	-
Galley Grill	-	109,258	-	109,258	-	-	-	-
Golf operations	-	204,856	-	204,856	-	-	-	-
Total Cost of Sales	-	379,867	-	379,867	-	-	-	-
NET BEFORE OTHER EXPENSES	2,166,431	343,951	-	2,510,382	2,058,134	-	-	2,058,134
ADMINISTRATIVE AND OTHER EXPENSES								
Sheriff contract/patrol services	291,799	-	-	291,799	296,342	-	-	296,342
Other contract services	32,082	-	-	32,082	25,108	-	-	25,108
Utilities	285,706	64,119	-	329,825	329,825	-	-	254,271
Grounds maintenance	286,945	15,508	-	302,453	240,137	-	-	240,137
Pool operations	99,448	-	-	99,448	70,930	-	-	70,930
Major repairs and maintenance	131,425	-	-	131,425	132,125	-	-	132,125
General maintenance and repairs	108,071	65,010	-	173,081	139,618	-	-	139,618
Insurance and taxes	72,148	88,536	-	160,684	57,882	-	-	57,882
Newsletter/community events	56,355	-	-	56,355	54,716	-	-	54,716
Other administrative costs	94,743	123,062	-	217,805	88,096	-	-	88,096
Interest expense	9,554	91,764	-	101,318	15,581	-	-	15,581
Depreciation expense	34,569	37,504	-	72,073	39,862	-	-	39,862
Payroll costs	352,224	524,380	-	876,604	358,474	-	-	358,474
Total Expenses	1,835,069	1,009,883	-	2,844,952	1,773,142	-	-	1,773,142
Revenues Over (Under) Expenses	331,362	(665,932)	-	(334,570)	284,992	-	-	284,992
Fund Balance/Retained earnings, beginning of year	1,700,657	-	-	1,700,657	1,415,665	-	-	1,415,665
Fund Balance/Retained earnings, end of year	\$2,032,019	(665,932)	\$-	\$1,366,087	\$1,700,657	\$-	\$-	\$1,700,657

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

**THE NEW PROPERTY OWNERS ASSOCIATION OF NEWPORT, INC.  
AND SUBSIDIARY  
CONSOLIDATED STATEMENT OF CASH FLOWS  
For the Years Ended December 31, 2016 and 2015**

	<u>2016</u>	<u>2015</u>
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Revenues over (under) expenses	(334,570)	284,992
Adjustments to reconcile to net cash provided by operating activities:		
Depreciation expense	72,073	39,862
(Increase) decrease in assets:		
Certificates of deposit	(1,625)	(48)
Assessments receivable	(154,272)	60,737
Prepaid expenses and other	5,483	(1,288)
Due from related party	87,247	(87,247)
Due from Newport Golf Partners	55,375	(55,375)
Increase (decrease in liabilities)		
Accounts payable	60,045	21,742
Prepaid assessments	50,446	(2,266)
<b>NET CASH PROVIDED BY (USED FOR) OPERATING ACTIVITIES</b>	<u>(159,798)</u>	<u>261,109</u>
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Proceeds from note payable	2,000,000	-
Principal payments on note payable	(279,505)	(95,891)
Proceeds from capital lease obligation	269,451	-
Principal payments on capital lease	(36,553)	-
<b>NET CASH PROVIDED BY (USED FOR) FINANCING ACTIVITIES</b>	<u>1,953,393</u>	<u>(95,891)</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Purchase of property and equipment	(2,271,228)	(28,772)
Purchase of certificate of deposit	(210,000)	-
<b>NET CASH PROVIDED BY (USED FOR) FINANCING ACTIVITIES</b>	<u>(2,481,228)</u>	<u>(28,772)</u>
<b>NET INCREASE (DECREASE) IN CASH</b>	(687,633)	136,446
<b>CASH, BEGINNING OF YEAR</b>	<u>951,081</u>	<u>814,635</u>
<b>CASH, END OF YEAR</b>	<u><u>263,448</u></u>	<u><u>951,081</u></u>
<b>SUPPLEMENTAL DISCLOSURES:</b>		
Income taxes paid	<u>\$-</u>	<u>\$-</u>
Interest paid	<u>\$101,318</u>	<u>\$15,581</u>

THE NEW PROPERTY OWNERS ASSOCIATION OF NEWPORT, INC.  
NOTES TO FINANCIAL STATEMENTS  
December 31, 2016 and 2015

Note 1 - Nature of Organization

The New Property Owners Association of Newport, Inc. (the "Association") was incorporated as a Texas non-profit corporation in 1996 to provide for the operation and maintenance of the common property of Newport, a residential subdivision located in Crosby, Texas. On December 4, 2015, the Association formed and acquired all of the outstanding shares of stock of Stonebridge at Newport, Inc. ("Stonebridge"). Collectively, the Association and Stonebridge are referred to as the Company.

Note 2 - Summary of Significant Accounting Policies

This summary of significant accounting policies of the Association is presented to assist in understanding the Association's financial statements. The financial statements and notes are the representation of the Association's management, who is responsible for their integrity and objectivity. These accounting policies conform to generally accepted accounting principles and have been consistently applied in the preparation of the financial statements.

Principles of Consolidation

The accompanying financial statements include the accounts of the Association and its wholly-owned subsidiary. All significant intercompany transactions and balances have been eliminated in consolidation.

Basis of Accounting

The accompanying financial statements have been prepared on the accrual basis of accounting. Under this method, revenues are recognized when earned and expenses are recognized when incurred.

Member Assessments

Association members are subject to assessments to provide funds for the Association's operating expenses, future capital acquisitions, and major repairs and replacements. Members have the option of paying their assessments on a yearly basis or on a monthly basis. Any excess assessments at year end are retained by the Association for use in future years. Liens can be attached on the properties of homeowners whose assessments are in arrears.



THE NEW PROPERTY OWNERS ASSOCIATION OF NEWPORT, INC.  
NOTES TO FINANCIAL STATEMENTS  
December 31, 2016 and 2015

Summary of Significant Accounting Policies (Continued)

Event and Golf Revenues

Stonebridge engages in operating a golf course, sponsoring events (such as weddings) and providing food and beverage to patrons. Revenues from such activities are recorded as the related activities are provided. Event deposits, which are nonrefundable are recorded as revenue as received. Golf memberships paid in advance are deferred and recognized as revenue over the term of the membership.

Property and Equipment

Real property and common areas acquired from the developer and related improvements to such property are not recorded in the Association's financial statements in accordance with accepted accounting practices for homeowners associations. The Association capitalizes significant personal property it acquires.

Income Taxes

The Association is exempt from federal income taxes under Section 501(c)(4) of the Internal Revenue Code. Stonebridge is a "C" corporation and is a taxable entity under applicable sections of the Internal Revenue Code. At December 31, 2016, Stonebridge had a net operating loss for federal income tax purposes in the amount of \$665,933.

Estimates

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

Statement of Cash Flows

For purposes of the statement of cash flows, the Company considers investments with a maturity of three months or less to be cash equivalents.

THE NEW PROPERTY OWNERS ASSOCIATION OF NEWPORT, INC.  
NOTES TO FINANCIAL STATEMENTS  
December 31, 2016 and 2015

Note 3 - Concentrations

The Company maintains cash accounts and certificates of deposit, which at times, may exceed federally insured limits. The Company has not experienced any losses from maintaining cash accounts in excess of federally insured limits. Management believes it is not exposed to any significant credit risk on its cash accounts.

Note 4 - Management

Effective November 1, 2010, the Association became fully self-managed.

Note 5 - Allowance for Doubtful Accounts

The Association has provided an allowance for accounts which are considered doubtful of collection. This allowance is based on several factors, including consideration of the statute of limitations for collection of assessments from members, historical information on the collection of assessments in the succeeding years after they are billed to members, and the nature of amounts included in such assessments (such as legal fees, finance charges, etc.). Since becoming self-managed, the Association has experienced increased collection rates, and believes such trends will continue in the future. At December 31, 2016, an allowance of \$397,396 has been established for accounts which are considered doubtful of collection.

Note 6 - Future Major Repairs and Replacements

The Association conducted an internal study to determine the remaining useful lives or replacement costs of the components of common property. The study was based on the past history of major repairs and replacements, and management's knowledge of needed repairs and replacements needed. The results of the study are presented on page 13.

At December 31, 2016, the Association did not have a separate bank or other account designated as a reserve account. Actual expenditures accumulated for future major repairs and replacements may be greater than funds accumulated for those purposes. When major repairs and replacement funds are needed, the Association has the right to increase regular assessments or pass special assessments, or may delay such replacements until funds are available.

THE NEW PROPERTY OWNERS ASSOCIATION OF NEWPORT, INC.  
NOTES TO FINANCIAL STATEMENTS  
December 31, 2016 and 2015

Note 7 - Stonebridge Purchase

In January, 2016 Stonebridge purchased all the real, personal and intangible property related to the Newport Golf Club and Conference Center. Such property included an eighteen hole golf course, the pro shop, conference center, and country club, and all furniture and fixtures related thereto. The purchase price was \$1,400,000. Subsequent to the purchase, the Association and Stonebridge made significant improvements to the golf course, the country club building, and acquired new equipment for the maintenance of the golf course.

Note 8 - Note Payable

In connection with the purchase discussed at Note 7 above, Stonebridge borrowed an amount of \$2,000,000 from a local bank. The proceeds were used to pay off an existing loan of the Association, complete the purchase, and provide working capital to fund necessary equipment purchases and building improvements. In addition, a portion of the funds were used to fund deficit operations of the golf course and country club. A portion of the loan equivalent to the outstanding balance of the Association loan was allocated to the Association. The balance of the loan was allocated to Stonebridge. The loan is repayable in monthly installments of \$15,891, including interest at the rate of 5%. The loan is payable in sixty monthly installments, with a final payment due and payable on February 22, 2021. The loan is secured by substantially all of the assets of Stonebridge and by certain property and assessments of the Association.

Required principal installments on the note described above, based on the contractual required monthly payments, are as follows:

<u>Year</u>	<u>Amount</u>
2017	\$ 97,074
2018	102,041
2019	107,262
2020	112,749
2021	1,497,387

THE NEW PROPERTY OWNERS ASSOCIATION OF NEWPORT, INC.  
NOTES TO FINANCIAL STATEMENTS  
December 31, 2016 and 2015

Note 9- Capital Lease Obligation

In order to finance the acquisition of certain golf course maintenance equipment, Stonebridge entered into a capital lease obligation with a finance company. The lease contains a bargain purchase option at the end of the lease term. The capitalized cost of the associated equipment was \$269,452. The lease is due in sixty monthly installments of \$5,040, which includes interest at an implicit rate of 4.6%.

Required principal installments on the capital lease are as follows:

<u>Year</u>	<u>Amount</u>
2017	\$ 50,753
2018	53,157
2019	55,674
2020	58,311
2021	15,003

Note 10 - Property and Equipment

Property and equipment consists of the following:

<u>Description</u>	<u>2016</u>	<u>2015</u>
Land	\$ 836,000	\$ -
Buildings and improvements	1,514,488	575,638
Other equipment	<u>634,140</u>	<u>137,762</u>
Total	2,984,628	713,400
Less-Accumulated depreciation	<u>361,586</u>	<u>289,513</u>
Net property and equipment	\$ <u>2,623,042</u>	\$ <u>423,887</u>

Depreciation expenses amounted to \$72,073 and \$39,862 for the years ended December 31, 2016 and 2015.

THE NEW PROPERTY OWNERS ASSOCIATION OF NEWPORT, INC.  
NOTES TO FINANCIAL STATEMENTS  
December 31, 2016 and 2015

Note 11 - Fair Value of Financial Instruments

The Company's financial instruments consist of cash and cash equivalents, certificates of deposits, accounts receivable, accounts payable and accrued expenses, prepaid assessments, and notes payable. The recorded values of these financial instruments approximate their fair value based on their short term nature.

Note 12 - Date of Management's Review

Subsequent events were evaluated through May 16, 2017, which is the date the financial statements were available to be issued.

Note 13- Litigation Matters

Since 1996, Lakewood Development Corporation ("Lakewood") has owned the property from the end of South Diamondhead Blvd. to both the San Jacinto River and Lake Houston. The Association has maintained and operated parks at both sites since 1972. In the deed conveying the property to Lakewood, the grantor reserved an access easement to these park sites and to the storage and stables in favor of Newport property owners.

Lakewood is now challenging the rights of Newport owners to the facilities located on property owned by Lakewood. The Association intends to vigorously defend its rights, and management of the Association believes it has adequate defenses to defend this matter.

**SUPPLEMENTARY INFORMATION**

THE NEW PROPERTY OWNERS ASSOCIATION OF NEWPORT, INC.  
SUPPLEMENTARY INFORMATION ON FUTURE  
MAJOR REPAIRS AND REPLACEMENTS (UNAUDITED)  
December 31, 2016

In 2015, the Association conducted an internal study to estimate the remaining useful lives and the estimated costs of future major repairs and replacements. Replacement costs were based on the estimated costs to repair or replace the common property at the date of the study. The total estimated current replacement costs do not take into account the effects of inflation.

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

<u>Component</u>	<u>Expected Replacement Year</u>	<u>Replacement Cost</u>
Replaster pool	2018	\$ 40,150
Reseal pool deck	2018	15,000
Replace tennis court decks	2019	70,000
Replace perimeter fencing	2021-2024	80,000
Replace lake bulkhead	2017-2018	40,000
Replace bulkheads-ponds	2020	<u>35,000</u>
Total		\$ <u>280,000</u>

The accompanying notes are an integral part of the financial statements