



**JOLLY HARBOUR HOMEOWNERS
ASSOCIATION**

COMMUNITY CHARGES

August 23, 2001



Chartered Accountants

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Our ref: CS/sc

By Fax: 268 560 5525

August 23, 2001

Dear Mr. Guenther;

Re: Community Charges

Further to our letter dated April 02, 2001, we write to advise that we have completed our work as outlined in respect of community charges during the period January 1 to December 31, 2000 as disclosed by Caribbean Developments Antigua Limited (CDAL) to Jolly Harbour Homeowners Association. This letter sets out the scope of our engagement, our findings and conclusions.

Terms of Reference

Outlined below are the terms of reference for this engagement.

1. Advise of any legal basis in Antigua for charging community costs.
2. Review the accounting system used for capturing and recording community costs.
3. Review the nature of community costs charges and advise on their applicability.
4. Ascertain to what extent community costs are based on actual charges incurred.
5. Review the basis of apportionment of costs and comment thereon.
6. Ascertain whether the correct total number of villas and lots are used for purposes of allocation of costs.



KPMG, a partnership registered under the law of Antigua and Barbuda, is a member of KPMG International, a Swiss association.

Cleveland S. Seaforth (Resident)
Jeffrey W. Gellineau
Irving Burrowes
Michael A. Edghill
Carol L. Nicholls

James M. Payne
Frank V. Myers
Reuben John
Brian Glasgow
Brenda Pope (Principal)

7. Meet with the Management of Caribbean Developments (Antigua) Limited and their Accountants in order to facilitate the conduct of our exercise.
8. Prepare a report detailing our findings in respect of the abovementioned matters.

2. Review of Accounting System:

The company uses computerised accounting software for the recording and processing of transactions. The use of the accounting software allows for the recording of all transactions under specific account codes.

However, based on the account structure used, there is no differentiation made between costs which should be borne by the company and those which should be recharged to homeowners. All costs pertaining to any item of expenditure are recorded into the specific expenditure account and as such costs to be charged to homeowners cannot be specifically identified by the account structure or cost centres.

At the end of the financial year, all community charges are allocated between the company and homeowners on a pre-determined allocation basis.

In the processing and recording of transactions, individual invoices are reviewed and charges are identified. Depending on the nature of services or product acquired, some charges may not be coded to those accounts which are related to community charges.

3. Nature of Community Costs Charges:

- **Gardeners' Salaries**

Salaries used in the computation of community charges for gardeners' include only the payroll costs associated with the ground staff.

A review of the employment contracts revealed that groundsmen are responsible for cleaning the gardens and surrounding areas, watering of plants, spraying of plants to control insects and the removal of debris from the commercial centre and other properties.

- **Security -Patrols Inc.**

Security costs used in the calculation of community charges include all security charges from Patrols Inc and Guardian Security except those costs for the boatyard. Security costs included in community charges arises as a result of guards stationed at the following:

- Shopping Area
- Golf Course
- Sewage Plant

Our review of a sample of invoices indicated that two (2) invoices in the amount of \$ 2,052 relating to the boatyard were inadvertently included in community charges and billed to the homeowners.

The security costs incurred included charges from both Patrols Inc. and Guardian Security even though the account is described as Security-Patrols Inc.

- **Security Salaries**

This item of expenditure relates to the services of a Security Manager who was needed to oversee the guards from the two (2) security companies.

The costs included in this account represents both actual costs paid for a period of six (6) month and six (6) months of estimated charges. Effective July 2000, the services of the Security Manager was terminated and the function was then provided by Jolly Beach Resorts.

However, in April 2001, Jolly Beach billed a total cost of \$ 9,460 for services between the period July to December 2000. However, because Caribbean Developments (Antigua) Limited continued to reflect a monthly charge of \$6,353 for the period July to December 2000, the cost for these services was overcharged by approximately \$ 28,655.

- **Landscaping**

Landscaping costs relate to all materials and gardening supplies such as flower pots, fertilizers, grafting tape, hedge trimmers and water cans.

Upon receipt of invoices, all costs not pertaining to landscaping are excluded and the remained recorded as community charges. However, in our review, we found costs amounting to \$2,620 which were not related to landscaping but included in these costs.

- **Sewage**

The costs in respect of these charges arises principally from a contract with Linde Limited for operative and preventative maintenance of all plant functions as well as ensuring the quality of the effluent discharge from the plant.

The sewage treatment plant at Jolly Harbour collects sewage waste and drainage water from both Jolly Beach Resort and Jolly Harbour. The waste and water collected from the drainage pipes located in these areas (including the kitchen, laundry, rooms and bathrooms) are channeled via underground pipelines, to the sewage treatment plant for treatment and reuse by Jolly Harbour. The treated water (or "gray water" as it is commonly referred to) is used by Jolly Harbour mainly for maintaining the lawn at the golf course on a daily basis. The sewage by product is treated and allowed to settle and dry and is then used as fertilizer for the plants maintained at the nursery.

- **Garbage Removal**

Garbage removal costs relate to charges associated with the cleaning and collection of garbage from the Jolly Harbour area. The transactions included mainly related to amounts invoiced by Environmental Garbage and Leroy Trucking for the collection and removal of garbage.

Environmental Garbage is normally responsible for the collection of domestic waste while Leroy Trucking collects non domestic waste products which are produced outside of the villa community.

- **Equipment Rental**

Equipment rental is related to costs associated with the rental of heavy duty equipment such as backhoes and excavators. It also includes trucking costs which relates to the transportation of materials such as stone, cement, sand, lumber and steel to Jolly Harbour. CDAL also rented its main office computers for a period of thirteen (13) months which were also included in these costs.

- **Uniforms**

Uniform costs relate to the purchase of uniforms for the CDAL's ground staff and administrative members of staff. Charges to this account were supported by invoices.

- **Vehicle Fuel**

The charges for vehicle fuel relate to fuel taken at the Marina/boatyard at Jolly Harbour for all of the company's vehicles.

Each driver of the company's vehicles signs an invoice for the fuel which is received for each vehicle. Costs are incurred in respect of the villa community as vehicles are used for transportation of maintenance and ground staff, transporting maintenance supplies, plants and general supplies.

- **Utilities**

This item of costs represents an estimate of costs incurred for community lighting and water costs for gardening at the villa community.

The charge was made after the company reviewed its recoveries for utilities for the 1999 financial year. Recoveries from villa owners amounted to \$ 889,320 or just above fifty (50%) percent of the total electricity charges at Jolly Harbour

Management is of the view that the recoveries were too low given the magnitude of business conducted outside the administrative and CDAL operated areas of Jolly Harbour, signifying that there was a need to increase the allocated amount for general utilities.

- **General Maintenance**

General maintenance is comprised of six (6) categories of expenditure as follows:



Maintenance - Infrastructure	\$ 695,445
Inventory - Cost of Sales	855,859
Maintenance - Barge	65,153
Furniture Villas	155,916
Cleaning supplies	4,309
Merchandise - Cost of Sales	<u>16,129</u>
	<u>\$ 1,792,811</u>

- **Maintenance - Infrastructure**

With the exception of infrastructure maintenance at the beach and commercial centre, all other infrastructure activities undertaken at Jolly Harbour are included in these costs.

The main items of expenditure included:

- √ Purchase of construction piles
- √ Repair of high voltage cable faults
- √ Salaries and wages for maintenance subcontractors.

In our review of invoices, it was difficult to ascertain infrastructure costs as it relates specifically to the villa community as there is no distinction made on the invoices. Based on our discussions with management, it was revealed that infrastructure charges included as it related to the villa community comprise of maintenance of the seawall, maintaining the exterior portion of the villas and work carried out on commercial areas.

- **Inventory - Cost of Sales**

Inventory - cost of sales represents costs in respect of materials and supplies including furniture, fuel, paint, electrical and plumbing supplies.

At the end of every year, a physical stock count is done and an adjustment made to the company's accounts to reflect the actual stock value. As at October 31, 2000, the company reduced the value of its inventory by approximately \$ 203,000 after having made provisions of \$50,000 per month to reflect monthly usage.

In addition, the company was advised by its external auditors to make a provision of \$200,000 to reflect the write down of obsolete stock.

The rationale represented by CDAL for including cost of sales in general maintenance is that items from the warehouse are used in general maintenance in the Jolly Harbour Development.

- **Barge Maintenance**

The barge, which is a small vessel with a crane, is used in the execution of a variety of activities such as boat lifting, piling and power washing of patios.

The costs incurred is mainly comprised of expenditure for spare parts for the barge.

- **Furniture-Villas**

These costs relate to an audit adjustment which was advised by the company's auditors to write off furniture which has been considered obsolete as they were damaged during a hurricane.

- **Cleaning Supplies & Merchandise Cost of Sales**

All of these costs are related to golf expenditure and should not be reflected as community charges. Management has acknowledged that these costs should be excluded.

4. **Basis of Community Charges:**

Community charges are based on actual charges incurred during the company's financial year. However, at the end of the financial year, accruals are made for those items of expenditure which have been incurred but invoices may not have been received at the time of closure of the company's accounts.

Based on our review of the individual accounts in those instances where accruals have been made, they have been found to be reasonable in the context of the amount of expenditure incurred in that account.

During the twelve (12) month period ended December 31, 2000, the company changed its financial year end from December 31 to October 31. As a consequence, actual expenditure incurred by the company was for a ten (10) month period only. In order to charge homeowners community charges on the basis of costs incurred for a period of one (1) year the actual costs for the ten (10) month period were projected for a twelve (12) month period.

Based on our review, the average monthly costs for the ten (10) month period was determined and extrapolated for twelve (12) months. These calculations were tested and found to be correct.

5. Basis of Apportionment of Costs

- **Gardeners' Salaries**

The allocation of seventy six (76%) percent has been used by CDAL and is based on the number of gardeners who work at the villas and common areas in relation to the total number of gardeners.

Based on a review of the allocation of ground staff, we computed an allocation percentage of seventy seven (77%) percent. However, we are not in agreement with the 501 division factor which has been used to determine the per unit costs of community charges as it relates to ground staff as it has been acknowledged that a groundsman resources has been used on substantial work done on and around lots.

- **Security -Patrols Inc.**

The allocation of security charges was tested on a sample basis by the calculation of the proportion of security hours associated with the Villas and common areas in relation to the total number of security hours billed.

In our review of the percentage allocation, security costs for the following areas were excluded from the computation.

- Jolly Beach Main Gate
- Golf Course

- Shopping Centre
- Sewage Plant

Based on our assessment, the sixty (60%) percent allocation basis used by Caribbean Developments (Antigua) Limited in its calculation of community charges appear reasonable.

- **Security Salaries**

The allocation of one hundred (100%) percent of these costs do not appear to be justified because the service of overseeing the security guards related to all locations including the boatyard, shopping centre, golf course and parking lot.

A more equitable basis would be to allocate these costs in the same proportion to the security charges in respect of Patrol Inc. and Guardian Security i.e. sixty (60%) percent.

- **Landscaping**

The allocation of ninety (90%) percent of landscaping costs to community charges is based on the level of estimated landscaping activity carried out at the villas in relation to the total landscaping activity.

- **Sewage**

CDAL has used a ninety (90%) percent allocation basis for sewage maintenance charges to the villa community. This allocation is based on the proportionate amount of sewage usage at the villas in relation to total sewage usage at Jolly Harbour.

The basis of allocation is questionable because the charges billed by the service provider are related to the treatment of water, the end of product of which is used to provide water on a daily basis to maintain the lawn and golf course. However, no portion of the savings resulting from the use of treated water is used to reduce the charges to villa owners.

In addition, Jolly Beach Hotel is charged monthly by CDAL for having its sewage and waste channeled through the treatment plant. A charge of seventy five (75) cents per head count is billed to the hotel for this service.

In view of the above, the charges to the villa owners should be reduced by the savings resulting from the use of treated water and by an allocated portion of amount charged to Jolly Beach. Alternately, a lower percentage basis for the allocation of the charges should be adopted.

- **Garbage Removal**

CDAL's allocation of garbage removal costs of eighty three (83%) percent is based on the estimated amount of garbage collected at the villa community in relation to hotel garbage collected at Jolly Harbour.

An analysis of garbage collection was done in relation to domestic and non domestic waste products on the basis that Leroy's Trucking collected the non domestic garbage which is usually produced outside the villa community, whilst Environmental Garbage mainly collected domestic waste from the villa community and surrounding areas.

Based on the assumption as outlined above, the eighty three (83%) percent allocation basis for garbage removal is considered reasonable.

- **Equipment Rental**

CDAL's allocation basis for equipment rental of 60.3% is based on the estimated amount of equipment rental costs which relates to the hire of equipment in relation to total usage at Jolly Harbour.

The basis of allocation of equipment rental charges was in respect of rental costs related solely to the rental of backhoes and other heavy duty equipment, despite the fact that the total rental costs included computer rental charges and other recurring costs relating to the trucking of construction materials and supplies to the golf course and other areas of Jolly Harbour.

It was not possible to test the basis of allocation for this item of expenditure because invoices did not provide a breakdown of the expenditure incurred.

- **Uniforms**

The allocation of fifty (50%) percent of the costs incurred is based on the amount of uniforms used by staff working on the villas, compared to the total numbers of uniform used.

- **Vehicle Fuel**

The allocation of fifty (50%) percent is based on the number of vehicles used by employees in performing their daily tasks at the villa community in relation to the total company vehicles used by employees at Jolly Harbour.

- **General Maintenance**

- **Maintenance Infrastructure**

An allocation of twenty (20%) percent has been used by CDAL and is based on the estimated amount of general maintenance at the villa community in relation to total general maintenance at Jolly Harbour. Management has represented that because of the current system used to record these charges, whereby all infrastructure costs are captured in this account, a minimal allocation basis of twenty (20%) percent has been established.

Based on the present method of capturing costs, it is not possible to comment on whether this basis is appropriate.

- **Inventory - Cost of Sales**

An allocation of twenty (20%) percent is used on the basis of the estimated amount of general maintenance for the villa community in relation to the general maintenance at Jolly Harbour.

It is not possible to ascertain whether this basis of allocation is justified.

- **Maintenance-Barge**

Same basis of allocation for all other items of general maintenance.

6. Number of Villas and Lots

The division factor (501) used by CDAL in the calculation of community charges includes all villas at the Jolly Harbour Development, including staff villas and the villas located in the administrative building as follows:

Unsold/Rental Villas	320
Sold Villas	<u>181</u>
	<u>501</u>

Only the villas have been included in the calculation of community charges. Yet discussions with CDAL's management revealed that community charges are not solely collected from villa owners, but are also collected from lot owners who have had any sort of construction activities carried out on their lot. As a result, although a 501 division factor representing total number of villas is used in determining the per unit community charge, community charges are collected from villa owners, and lot owners, who were not included in the division factor.

The effect of this approach is that the company recovers from owners an amount greater than the total community charges incurred.

The division factor used by CDAL should represent the total units which will be billed for community charges. This in effect would produce a lower community charge per unit.

7. Proposed Community Charges

Caribbean Development Antigua Limited has issued a proposal in May 2001 with reference to amendments to the calculation and allocation of community charges.

The new proposal explains the rationale underlying the allocation of costs pertaining to the community charges. It also provides a more equitable distribution basis as in addition to villas, lots would also be included in the division factor for community charges. Since the services provided to lots and villas are basically identical with the exception of painting, CDAL in its new proposal has made an adjustment for the charges between the villas and the plot owners to account for villa painting expenses, which is a cost applicable solely to villa owners.

The commercial centre tenants have been levied a fifteen (15%) percent surcharge in relation to community charges. KPMG in its review of the community charges however noted that these amounts recovered were not deducted from the total costs allocated to the community.

However, in the May 2001 proposal, provision has been made whereby amounts recovered from commercial centre tenants would be credited against community charges.

It must be noted that included in the new proposal are additional charges to be included in the calculation of community charges. These include the following:

- Sixty (60%) percent allocation of the General Manager and the General Manager secretary's salaries;
- Twenty five (25%) percent allocation of the Financial Controller and Accounting staff salaries;
- Thirty (30%) percent of the other administrative expenses including telephone, faxes, office expenses, computer maintenance and consulting charges;
- One hundred (100%) percent of audit fees relating to external auditors reporting separately on community charges;
- Thirty one (31%) percent of workmen's compensation insurance will also be included in the calculation of community charges.

KPMG in its analysis on the sewage account noted that ninety (90%) percent of the sewage maintenance charges are allocated to the villa community, and the account did not reflect the portion of the costs recovered from billings to Jolly Harbour. KPMG was of the opinion that the allocated percentage to the villa owners should be decreased or the amounts recovered from Jolly Harbour be charged against the account. It was however noted in the amended proposal that the villa community will be charged at an allocated rate of fifty (50%) percent instead of the currently established rate of ninety (90%) percent.

The groundstaff salaries and landscaping expenses allocation basis will be increased from seventy six (76%) percent and ninety (90%) percent respectively, to a one hundred (100%) percent allocation basis for both charges; while there will be a decrease in the garbage removal allocation basis from eighty three (83%) percent to fifty (50%) percent.

General maintenance includes maintenance of electrical lines and transformers, seawall, water and drainage pipes, painting of common area walls, roads and villa exteriors and the maintenance of the property infrastructure and administration block. General maintenance in the new proposal increased from twenty (20%) percent to thirty three (33%) percent. Vehicle fuel remained constant at fifty (50%) percent, while there was a decrease in uniform allocation from fifty (50%) percent to thirty one (31%) percent.

Overall, with the new proposal in effect, community charges would be significantly higher, especially given the fact that the General Manager and his secretary's salaries, the Financial Controller and the Accounting staff salaries would be incorporated in the calculation of community charges at an allocated rate of sixty (60%) percent. A summary of the current and proposed allocation percentages is as follows:

	<u>CDAL Current Percentage</u>	<u>KPMG Findings</u>	<u>CDAL Proposed Percentage</u>
Gardeners' Salaries	76%	77%	100%
Security	60%	60%	70%
Landscaping	90%	77%	100%
Sewage	90%		50%
Garbage removal	83%	83%	50%
General maintenance	20%		33%
Equipment rental	60.3%		40%
Vehicle fuel	50%		50%
Uniforms	50%		31%
Utilities	100%		20%
General Manager's salary	-		60%
General Manager's Secretary's salary	-		60%
Financial Controller's salary	-		25%
Accounting staff salaries	-		25%
Other administrative expenses	-		30%
Audit fees	-		100%
Workmen's compensation insurance	-		31%

In general, the determination of the basis of allocation in several instances appears to be arbitrary rather than based on an indepth analysis of the particular circumstances relating to the area of activity. The following areas may be worthy of more indepth analysis:

- General maintenance
- Garden's salaries and landscaping expenses
- Equipment rental
- Uniforms
- General Manager's, Financial Controller's and Accounting Staff salaries
- Other Administrative expenses

8. Utility Charges:

Water and electricity are provided to Jolly Harbour via the Antigua Public Utilities Authority (APUA). APUA levies a charge of approximately \$0.69 per unit on electricity consumed, while a charge of \$0.50 is levied per gallon on water consumed by the Development.

The homeowners are invoiced on a monthly basis by CDAL for their consumption of water and electrical units based on readings obtained from the installed meters. The present reading (or the reading at the end of the month) is deducted from the previous reading (reading at the end of the previous month) to ascertain the units of water and electricity consumed during the period.

The consumed units are multiplied by a standard rate of \$0.77 and \$0.55 levied for electricity and water respectively by the CDAL. These rates used by CDAL are ten percent (10%) higher than the average rates levied by APUA of \$0.67 and \$0.05 respectively. KPMG inquired of the Management of CDAL (representative - David Watt) about the difference in the rates charged by APUA and that levied by CDAL. It was represented by Mr. Watt that the infrastructure in place at Jolly Harbour to facilitate the provision of electricity and water was provided and paid for by CDAL (not APUA). As such, CDAL levies an additional ten (10%) percent charge on the standard APUA rates to subsidise a portion of the infrastructure costs incurred by CDAL. The cost of the infrastructure was treated as a capital asset in CDAL's accounts and was not previously included in the community charges expense account.

In November of the 2000 financial year, APUA increased its electricity per unit charges from approximately \$0.67 per unit to an average of \$0.77 per unit. As such, effective January 2001, CDAL has increased its charges from \$0.77 per kWh unit to \$0.85 per unit, representing the increase \$0.77 charge plus the 10% markup levied by CDAL.

KPMG inquired of personnel at the APUA Head Office of the basic standard rates levied by it on its customers during the 2000 calendar year. It was represented that for water, the charge was \$50 per 1000 gallons of water consumed or \$0.50 per gallon, while for electricity there is a split charge of \$0.40 per unit for fuel variation costs and a \$0.27 electricity charge per unit, giving a total of approximately \$0.67 per unit consumed. As such, KPMG is satisfied that the basic rates used by CDAL to arrive at the electricity and water charges are reasonable.

In fact, the average cost for electricity during the period August 2000 to July 2001, based on the methodology used by CDAL was \$0.84 whilst the average cost charged to homeowners was \$0.81.

Conclusion:

Based on our review and findings in respect of the year ended December 31, 2000, we list below recommendations which should be considered for adoption:

1. Accounting System:

Separate cost centres should be established so as to facilitate the capture of community related charges which as far as practical should not be mixed with non-community charges.

This process will reduce the possibility of errors resulting from the processing of charges and places the emphasis on the need for the identification of community charges which should be charged to homeowners.

2. Invoicing:

As far as possible, suppliers of goods and services should be requested to invoice separately for community and non related community charges. This approach would have the effect of reducing the possibility of errors in the analysis and allocation of invoiced amounts from third parties.

This recommendation arises from the fact that during our review, we noted that in a sample test, there were allocation errors in the processing of invoices which resulted in overcharges to home owners in the following areas:

- Security
- Landscaping
- Maintenance

3. Work Orders:

A system of work orders should be followed at all times which would serve as the basis for work to be carried in respect of homeowners. Work orders would then be matched to respective invoices before invoices are approved for processing and charged to respective community charge accounts.

4. **Allocation Factor:**

In the year under review, an allocation factor of five hundred and one (501) representing all villas was used as the basis of the allocation of community charges. However, community charges were in fact recovered from both villa owners and lot owners who had any sort of construction activity carried on their lots.

The allocation factor used should accurately reflect the number of owners billed for community charges including both lot and villa owners thereby preventing an over charge to one (1) group of owners.

5. **Credit for Recoveries:**

In instances where there are recoveries in respect of amounts charged as community charges, such recoveries should be credited against community charges thereby reducing the final charge to villa and lot owners.

In particular, recoveries from commercial tenants in respect of general upkeep and maintenance and sewage recoveries from third parties should be credited to community charges where the respective expense has been incurred.

6. **Percentage Allocation:**

Based on a review of the existing and proposed percentage allocations, there appears to be no substantial underlying rationale or basis which could be reviewed to ascertain the reasonableness of the allocations.

For each class of expenditure, the basis of determination of allocation percentages should be clearly identified and documented in order that their reasonableness could be assessed otherwise it gives the impression that percentage allocations have been arbitrarily determined.



Chartered Accountants
Antigua and Barbuda

August 23, 2001