Lakewood
PROPERTY OWNERS ASSOCIATION

TRANSPARENCY SERIES: Lakewood Oaks Country Club
Presented by the Lakewood Property Owners Association
General Manager Mark Reid
Published: March 26, 2024

History: The Lease of Clubhouse Space to the LPOA (Tenant) from the LHC (Landlord)

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Introduction

It has been 18 years since the acquisition of the Lakewood Oaks Golf Course by the Lakewood Holding Company (LHC), which is controlled by the Lakewood Property Owners Association (LPOA).

Of those years, the LPOA has been a lease-paying tenant of the Lakewood Oaks Golf Course for 13 years (2011-2024).

In recent months, residents have expressed an interest in advocating that the lease arrangement between the LHC and LPOA is equitable for both parties.

After 18 years of management by staff and financial advisors, we can confidently confirm for our members that during the last six years, financial managers have indeed generated a financial structure between the LPOA and LHC where both parties are finally paying their fair share for the shared usage of the Lakewood Oaks Clubhouse.

Stakeholders should know that even though the LPOA has always had a favorable lease arrangement with the LHC (or no-fee lease agreement), it has not always been a fair arrangement for the LHC. The LHC had to shoulder the costs of the LPOA for six years (2010-2016) before the financial arrangement finally became equitable in 2017.

This report will document the shifts in operations over the last 18 years, the history of the LHC/LPOA lease agreement, and will demonstrate why the lease arrangement between the LHC and LPOA is now highly equitable for both parties.

The History of Clubhouses in Lakewood

Built by developers after 1973, the LPOA had two clubhouses that they owned: the Cove Clubhouse (1973-2016) and the Bayview Clubhouse (1970s-2010). These clubhouses were used for decades to meet a wide variety of needs agreed to by the community, including staff offices, food and beverage services, special events, meeting space, club space, and more.

The LPOA paid expenses for both Clubhouse facilities, including operations and maintenance, for the duration of their lifecycle. **LPOA operating expenses for both clubhouses (circa 2006) were roughly**:

- Cove Clubhouse - $165,000/yr
- Bayview Clubhouse - $$83,000/yr
- Total combined: $248,000/yr, which equals $381,750 after inflation.

At the end of the life cycle of both clubhouses in 2010 and 2016, the LPOA lost these facilities that they relied on to meet the needs of the community. However, ever since those buildings were removed, the LPOA has had <u>NO</u> expenses for their Clubhouse operation and maintenance line items, since they no longer own any Clubhouses.

<u>**By contrast, the Lakewood Holding Company has owned the Lakewood Oaks Country Club Clubhouse since 2007. The Lakewood Holding Company pays ALL expenses associated with the Clubhouse as well as all taxes, insurance and mortgage principal and interest.**</u>

The LPOA is now a lease-paying tenant who benefits from the Oaks Clubhouse by using it for all the functions that used to be fulfilled through the Cove and Bayview Clubhouses.

(2007) History of Food & Beverage Services and Fees

For about 40 years, there were two restaurant locations in Lakewood: the Golf Course restaurant and the Cove Clubhouse Restaurant (Lake Drive).

Prior to the Golf Course acquisition in 2007, only Golf Course equity members had been allowed to have access to the restaurant and banquet space at the Oaks Clubhouse, (except for one year of a trial period), and the equity members paid a quarterly Food & Beverage fee of $100.

However, with the acquisition in 2007, the LPOA wanted all 2400 residents to have unlimited access to the restaurant and the clubhouse.

The LPOA was unable (and unwilling) to charge a Food & Beverage fee to all 2400 residents for access, so they granted automatic free Social Memberships to all residents in 2008. As Social Members of the club, all residents were granted access to the restaurant, the club, and were provided 6 opportunities for tee times each year without having to pay Golf Membership dues. This Social Membership status still applies today.

The LPOA then removed the Food & Beverage fee from the 265 golfers, in order to prevent an imbalance in the financial burden of the original golf course members.

Therefore, when the LPOA closed the Cove Restaurant in 2008, it relocated all Food and Beverage services to the Lakewood Oaks Clubhouse, where they fulfilled the promise of offering free access to all 2400 members.

<u>However, when the LPOA restaurant moved from the Cove to the Clubhouse, the LPOA opted to transfer these Food and Beverage costs onto the books of the newly formed LHC. This cost savings to the LPOA was approximately $165,000 in 2008, ($237,822 factored up by inflation in 2024). Inversely, the LHC budget incurred this burden on behalf of the residents, from 2008-2011.</u>

Many residents were disappointed to lose the Cove Restaurant, but the overall strategy of acquiring the Clubhouse allowed for cost benefits in a variety of places, and this was a significant savings for the LPOA.

The merging of these two restaurants in 2008 was an enormous financial benefit to LPOA, but was not actually beneficial to LHC.

These unbalanced LPOA savings ended eventually when the LPOA took the amenity back onto their books in 2011, relieving the 265 LHC golf members of the burden of all Food and Beverage costs on behalf of the 2400 residents.

<u>From 2011 - 2024, the LPOA has managed Food and Beverage operations for the Argyle and the St. Andrews Pub, full banquet service for events, and pool Snack Bars. The Food and Beverage department is now running at a current cost of $105,000 per year in 2024, far less than the $165,000 ($237,822/inflation) that was common at the Cove Clubhouse.</u>

(2010) LPOA Demolishes their Records Storage and Offices at the Bayview Clubhouse.

The Bayview Clubhouse was a cheaply built structure by the developer in the late 70s, originally intended to be a private clubhouse for the residents of the Lakewood Bay Parcel.

During the 80s, when the Lakewood Bay Parcel refused to make payments towards the operation and maintenance of the building, the LPOA took it over and moved the administrative offices out of the Cove Clubhouse and into the Bayview Clubhouse (1998).

During the Golf Course acquisition time frame in 2007, the LPOA was also faced with many repairs to the Bayview Clubhouse. Imminent repairs included replacing the roof, deck and siding, and also addressing the fact that the second floor access up a narrow set of stairs was not conducive to accessibility for members who were handicapped or senior with limited mobility.

Keep in mind, there had been no significant Reserve Funds built up during the first 40 years of Lakewood, so there were no funds available to renovate or replace the Bayview Clubhouse. Strategic Reserve Funding would not begin in Lakewood until 2015.

Soon after the LPOA moved into the Lakewood Oaks Clubhouse in 2010, the LPOA demolished the Bayview Clubhouse but left the Bayview pool and the pool equipment room and bathroom for those who wanted a quiet pool experience.

(2010) Using the Lakewood Oaks Clubhouse for LPOA needs

During the acquisition of the Golf Course, there were a variety of financial analysis reports from accounting professionals about the impacts of acquiring the Oaks Clubhouse. Based on professional projections and reasonable business principles, it became apparent that it was operationally most efficient to have both the LPOA and LHC staff operating out of one location, and also sharing office equipment like the postage machine, copiers, etc.

<u>This also created an opportunity for savings in the option to hire just one General Manager to manage both entities, with an office right on site, whereas before there had been two GMs in two different office locations. (EAGL management had been hired for the first 2 years, but they managed remotely out of Texas).</u>

In 2010, the LPOA elected to move into the Lakewood Oaks Country Club Clubhouse as a Tenant in order to provide office space for their employees and to take over operations for providing a social / food and beverage amenity for their members.

The first arm's length transaction for use of the LHC Clubhouse by the LPOA was documented in a lease. For the first five years of the lease (2010-2015), the Lease Fair Market Value (FMV) rate was held to a very low rate.

Both parties agreed to lease the upper floor only for 11,500 sq. ft. at the base rate of $10.50 per square feet, for a total annual payment of $120.750.00. The Board agreed to hold this rate for three years. No CAMS / Taxes / Insurance or Trash or other factors of a NNN (triple net) lease are factored into this lease.

With the lease set at a very low end of the FMV, the professional auditor made the LPOA and LHC state that improvements paid for by the tenant (LPOA) were warranted and required.

This low 2010 rate was established to accommodate the LPOA, who still had the expenses of the Cove Clubhouse event space. Even though the restaurant had closed in 2008, it still housed a few Community Services Staff and a small fitness equipment area in the basement.

It was also used by the social Bridge Groups and LPOA members who rented it for their self-service banquet events and meetings.

Ultimately during these first five years of tenancy, and finally ending at the end of 2016, the Lakewood Holding Company carried a large load of the operating costs generated by the LPOA at the Lakewood Oaks Clubhouse. They carried costs not only through the Food and Beverage fees they had been covering, but also through the intentionally low lease costs for office space.

(2010) The Lack of Reserve Funding

The LPOA was fortunate to have access to the Lakewood Oaks Clubhouse in 2010, because there had been no significant reserve funds built up in the 80s and 90s that would have allowed them to construct a new facility of their own, to replace the Cove or the Bayview Clubhouses.

During the first 40 years of Lakewood, there were 22 different years when dues were not increased, meaning that dues fell behind inflation, along with the lack of reserve funding. This is important because it is estimated that approximately $2 million dollars was left uncollected during this time, which could have been allocated towards a new clubhouse or other facility.

Nevertheless, the LPOA did finally establish a significant Reserve Fund program in 2015, as a part of Program 2020. Those funds continue to grow today as the LPOA responsibly prepares for 30-40 years of scheduled maintenance projections, based on professional Reserve Studies.

LPOA Reserve Funds have been funded at various amounts per year since 2015, and are funded out of the LIP Budget (the Lakewood Improvement Budget).

(2016) LPOA Demolishes the Cove Clubhouse

In 2016 the LPOA was faced with limited use of the Cove Clubhouse, impractical floor space design, lack of ADA compliance, and extensive mold. Based on the 2014 inspection report (Midwest Commercial Building Inspections Inc), followed up by $1,301,297 of deferred maintenance that had moved to critical status (as determined by Barstow Construction Inc.), the LPOA was facing insurmountable expenses with the impending repairs required for the Cove Clubhouse.

The building was also upside down in equity, even though it underwent an $800k renovation in 2008.

The LPOA elected to demolish the Cove Clubhouse in its entirety and build a low maintenance pavilion in its place.

This move saved the LPOA all of the operating, insurance and maintenance costs associated with this 1973 building. This decision was part of Program 2020, designed through the collaboration of the Finance Committee, Facilities Committee, and Board, who had all worked together to create the 5 year plan.

The operational savings in 2015 by demolishing the Cove Clubhouse were:

- $106,125 per year ($138,949.30/inflation)
- $1,301,297 of impending required repairs to the siding, roof and interior spaces.

(2015) LPOA leases space for the LPOA Community Services Personnel and the Maintenance Manager

When the Cove Clubhouse came down, it caused a need for additional space for a few Maintenance and Community Services staff.

In November of 2015, the LPOA signed a lease with Kansas City Development Corporation for 1,498 square feet. This was for the office space on Lakewood Boulevard, now known as the Community Services building.

The price per square foot for the first year was $12 plus CAMS / Taxes / Insurance and Trash for an additional $3.80 per sq. ft. for a total of $15.80.

<u>Keep in mind that the LPOA was only paying $10.50 per square foot and no CAMS / Taxes / Insurance and Trash for their lease in a Country Club facility during this period. By comparison, the LPOA/LHC was much lower than FMV, and was acting as a burden to the LHC.</u>

(2017) LPOA and LHC Agree on the first true market value lease that is fair to both companies

After the demolition of their second clubhouse, it was finally time for the LPOA to pick up their fair share of expenses for their use of the Lakewood Oaks Clubhouse that they had been using since 2008, including leasehold improvements.

Keep in mind that by 2017, the Cove Clubhouse operating expense had been costing the LPOA $106,125 for just 6,300 square feet of usable space ($134,356/ inflation). **This was a rate of $16.84 per sq ft.**

Also, the lease for the Community Services office was costing $24,429 annually for $1,498 square feet. **This was a rate of $16.30 per square foot.**

Therefore, beginning in January of 2017 the LPOA increased their lease to accurately reflect the square feet of the building they were using and began paying a price much closer to actual fair market value. This lease arrangement continues to this very day.

A hybrid triple net lease was set up beginning Jan 2017, where the LPOA would pay for the 18,589 sq.ft. they were using at a price per square foot rate of $16.43 per square foot.

It was time for the LPOA to cover expenses, and to end the golf members having to subsidize the LPOAs operating costs.

(2017) The Lease is annually revised by Bureau of Labor Statistics CPI.

After the new hybrid NNN lease was adopted for fiscal year 2017, each subsequent year was flat or simply increased solely by the published rate of inflation shown in the US Bureau of Labor Statistics Consumer Price Index.

- Beginning annual price in 2017 $305,508
- Adjusted price in 2018 $305,508
- Adjusted price in 2019 $314,673
- Adjusted price in 2020 $320,970
- Adjusted price in 2021 $327,384
- Adjusted price in 2022 $339,487
- Adjusted price in 2023 $368,000
- Adjusted price in 2024 $360,082* 1

*Note 1: this price decline was due to an adjustment in square footage of floor space used on the lower level against the recommendations of Staff.

Lakewood Oaks Lease FAQs

Q: The LPOA owns the Clubhouse, why do we have to pay to use it?

A: The LPOA assigned all of the property and physical assets of the Lakewood Oaks Country Club to the Lakewood Holding Company. **THE LAKEWOOD HOLDING COMPANY OWNS THE CLUBHOUSE, NOT THE LPOA**. The Lakewood Holding Company pays all the bills, taxes, insurance and mortgage principal and interest. LPOA pays none of this.

Note: we all “OWN” homes and we don’t get to use them for free. We still have to pay the utilities, taxes, insurance and mortgage. If we don’t own it and live in it, we are either a renter who reimburses the Landlord with a rent payment (and then pays the utilities themselves), or we are squatters who live there illegally.

Also, the LPOA /LHC Board is required to make choices that are equally beneficial to both parties. Giving away 83% of space of the Clubhouse to a tenant for free or reduced costs would not be beneficial to the LHC. Based on a variety of variables, doing this may also cost them their tax exempt status.

Q: What is the impact of the LHC Lease on LPOA Dues

Although there are many misconceptions that dues increases over the last 15 years has been attributed to the Golf Course lease, it's simply not true. The LHC Lease today is comparable to what had always been budgeted for operations for the two previous clubhouses when factored up by inflation.

Again, when the old Clubhouses were fully operational with staff offices and food and beverage services, their original operational expenses equaled about:

- 2006 | Cove - $165,000, Bayview - $83,000, about 10,600 sq ft
- Totalling $248,000 per year, ($381,750/inflation)
- By comparison, the current LHC/LPOA lease is just $360,082, for 17,497 sq ft.

This means the LPOA is paying almost $20,000 less per year now for almost 7000 more sq ft, than we were in 2006.

The trend in increased dues in the last several years has actually been largely due to:

Reserve Funding:

1) Funding the Reserve Funds that had been missing prior to 2015, at variable amounts leading up to the current level of funding of $955,000 in 2024, which includes $320,000 of debt P&I and $250,000 in accelerated debt reduction payments. This comes from the LIP Budget.

Debt Paydown:

1) Payments of of $320,134 in annual debt burden, through May 2025

2) Debt includes what was incurred in 2015 under Program 2020, when LPOA had to replace the Cove Pavilion, East Lake Pool, and East Lake Marina electrical renovations, all at the same time (without an existing reserve fund).

3) Paying down the 2020 investment of the brand new slips at both marinas, with an additional 78 additional boat slips. This investment has generated an increase in annual boat slip revenue.

4) Most new projects for the last several years have been on hold until this debt has been completed; only the most important maintenance projects have been completed

The Appeals Court Ruling in Davis et al vs LPOA:

The ruling in 2018 initiated a change in the process that had been used for the previous 46 years by the LPOA for formulating dues increases. The new dues formula instructions provided by the court in 2018 has had an impact on the way our dues are formulated each year, resulting in less flexibility for the LPOA to fulfill their annual fiduciary duty. This topic will be covered under separate cover.

Note: The debt balloons in May 2025, and the Finance Committee recommends that we pay off the note in full, in order to relieve the LPOA of this $320,134/annual debt burden.

<u>This Debt payoff in May 2025 is triggering the need for strategic decisions about how to move forward intentionally once the burden of the $320,134 annual expense has been lifted. The 2024 Strategic Vision Ad Hoc Committee is tasked with providing guidance on next steps, based on community feedback.</u>

Q. Didn't the LPOA pay $3,100,000 when they bought the Golf Course?

A: In 2007, the LPOA Board agreed to a total price of $3,100,000 to acquire the assets of the former Lakewood Oaks Golf Club, Ltd II. (Note: At the time, the estimated replacement cost for the assets were valued at $8.8million.)

However, the LPOA has never paid towards the golf course loan. Additionally, the dues of the LPOA were not increased or impacted by the acquisition. The LPOA had a small amount of reserves saved in 2007 without earmarks, and used these reserves to invest in the LHC.

<u>The LPOA has not paid even $1 of the mortgage for the assets they assigned to the Lakewood Holding Company</u>. The LHC has paid all mortgage payments directly, since the beginning of the loan.

Summary of Promissory Note Content:

When the LPOA assigned the assets to the Lakewood Holding Company upon acquisition, the LPOA loaned the LHC $586,746 cash (essentially a 20% equity down payment), so that the LHC could purchase the equity shares held by the members of the former Lakewood Oaks Golf Club Ltd. II.

After the LHC received the $586,746 from LPOA to pay off the member equity, the balance of the $3,100,000 acquisition price was reduced to $2,513,253 (80%). This portion was paid out to U.S. Bank (to the Equity Members) by a loan taken out by the Lakewood Holding Company through Bank of Lee's Summit. The LHC loan was backed by the LPOA, but did not cost the LPOA money.

(In very loose terms, you could consider the 80% loan as being acquired by the LHC but co-signed by the LPOA. If the LHC dissolved or was unable to pay the loan, the LPOA has backed the loan and would be responsible. This relationship still applies today.).

During the first 2 years of the acquisition, the LPOA did end up providing additional operating cash infusions of $376,369, and increased the promissory note accordingly, which stands at $963,115 currently.

As of 2024, the LHC only has about $850,000 left of the $2,513,253 bank loan to pay off, while the facility was valued at $10.3m replacement cost in 2017.

18 years of Boards and Advisors have operated with the strategy that it is in the best interest of both entities that the bank loan get paid off first, which will balloon in Dec 2024. It is likely that after the LHC pays off their bank loan, they may then prioritize reimbursing the LPOA for some of the cash advances from early in the acquisition process. This would be done strategically so as not to negatively impact the equity stake held by the LPOA.

To find additional details about the equity loans LPOA provided to LHC during 2007-2008, please read "The History of the Investment Promissory Note issued by the LPOA (Lender) to the LHC (Borrower)", under the Members Only Login.

Annually, the only funding that goes from the LPOA to the LHC is the lease line item, out of the LPOA Operating Budget, Administrative Department. Again, this lease payment is comparable to the Operations and Maintenance costs of the previous two clubhouses that LPOA owned.

Q: Why do we have to have a fair market value lease? Why can't we just charge a couple of bucks per square foot and save the LPOA some money?

A: The LPOA files its IRS taxes as an 1120h Homeowners Association. The Lakewood Holding Company is a 501c7 not for profit. The LPOA CAN NOT own stock in the Lakewood Holding Company.

The LPOA CAN NOT pull money out of the LHC. The LPOA CAN NOT misuse the Lakewood Holding Company, which the LPOA controls, and steal services from the Lakewood Holding company. Therefore, an arm's length transaction must be in place (Lease) and priced at fair market value (current lease rate).

Q: How much space does the LPOA use in the Clubhouse?

The Clubhouse spans 21,153 sq ft, with the LPOA utilizing 17,497 sq ft, representing 83% of the space, while the Golf Course uses 17%.

The LPOA uses the facility for the following:

- Staff offices for LPOA
- 2 Food & Beverage services that are operated by LPOA and available to all 2400 residents
- Banquet Hall for resident rentals and for special events sponsored by the LPOA, all year round
- Meeting space for monthly Board meetings and Annual meetings, all year round
- The August Room which is available for committee meetings, clubs, pilates, yoga, girl scouts, and a line item of $30k worth of No-Fee Use meeting space on behalf of residents

The Golf Course uses the indoor space for:

- Pro Shop on the lower floor
- Staff offices
- Men's and Women's lockers
- *They use the Augusta room and/or Banquet Hall space for Monday tournaments during golf season, but they pay fees to the LPOA for use of these rooms.

The total annual cost to operate the clubhouse is approximately $510,000, paid by the LHC. The LPOA pays $360k annually to the LHC for the lease of their space. The LPOA covers only 70% of the operating costs but utilizes 83% of the building.

In Conclusion

There has been an enormous amount of advocacy the last few years for the importance of establishing an equitable financial relationship between the LHC and LPOA.

However, contrary to some public discourse, the financial relationship between the two is now finally at its most equitable. The truth is that it is actually more accurate that the LHC spent many years in an unfavorable financial position while they absorbed costs incurred by the LPOA, and now the LPOA has adjusted course. .

We believe that this equitable relationship that we've maintained since 2017 ensures that we are operating most efficiently for both companies, thereby guaranteeing their successful operations for many years to come. The success of these companies is ultimately what protects the home values for generations, and we are proud to be fulfilling the mission.

Attachments:

- Board motion from 2010 issuance of first lease.
- Fiscal Year 2010 Lease (Covers 2010, 2011 and 2012)
- Fiscal Year 2013 Lease (Covers 2013,2014 and 2015)
- Fiscal Year 2016 Lease
- 2016 KC Development Corp Lease
- Fiscal Year 2017 Lease
- Fiscal Year 2018 Lease
- Fiscal Year 2019 Lease
- Fiscal Year 2020 Lease
- Fiscal Year 2021 Lease
- Fiscal Year 2022 Lease
- Fiscal Year 2023 Lease
- Fiscal Year 2024 Lease