Regency Affiliates, Inc. and Subsidiaries

Consolidated Financial Statements

December 31, 2017 and 2016

Regency Affiliates, Inc. and Subsidiaries

Index to the Consolidated Financial Statements

ACCOUNTANTS + ADVISORS

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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors and Stockholders
of Regency Affiliates, Inc. and Subsidiaries

We have audited the accompanying consolidated financial statements of Regency Affiliates, Inc. and Subsidiaries (the "Company"), which comprise the consolidated balance sheets as of December 31, 2017 and 2016, and the related consolidated statements of income, changes in equity, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Consolidated Financial Statements
Management is responsible for the preparation and fair presentation of these consolidated 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 consolidated 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 consolidated financial statements based on our audits. We conducted our audits 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 consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated 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 consolidated 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 consolidated 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 consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Regency Affiliates, Inc. and Subsidiaries as of December 31, 2016 and 2015, and the consolidated results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Rosenberg Rich Baker Berman, P.A.

Somerset, New Jersey
July 17, 2018

Regency Affiliates, Inc. and Subsidiaries
Consolidated Balance Sheets
December 31, 2017 and 2016

	2017	2016
Assets		
Current Assets:		
Cash and cash equivalents	$ 5,255,732	$ 5,044,512
Restricted cash	339,002	289,469
Prepaid expenses	421,693	386,640
Prepaid insurance	90,600	105,100
Prepaid income taxes	231,409	67,392
Rent receivable	20,700	4,119
Inventory	-	5,741
Total current assets	6,359,136	5,902,973
Real Estate		
Self-storage properties	35,087,576	35,078,359
Less accumulated depreciation	(1,325,507)	(548,565)
Property, plant and equipment, net	25,127	22,933
Investment in partnerships/LLC	39,723,401	36,689,891
Prepaid insurance, net of current portion	377,200	467,800
Other assets	204,360	204,360
Total assets	$ 80,451,293	$ 77,817,751
Liabilities and Shareholders' Equity		
Current Liabilities:		
Accounts payable and accrued expenses	$ 321,283	$ 199,061
Deferred revenue	145,683	142,285
Deferred rent	81,081	79,192
Income tax payable	233,722	12,000
Dividends payable	299,457	291,467
Tenant security deposits	8,244	9,296
Total current liabilities	1,089,470	733,301
Non-current Liabilities:		
Mortgage note payable, net	25,144,791	25,132,167
Total liabilities	26,234,261	25,865,468
Commitments and contingencies		
Shareholders' Equity		
Serial preferred stock, par value $0.10; 2,000,000 shares authorized; no shares issued and outstanding	-	-
Common stock, par value $0.01; 8,000,000 shares authorized; 4,791,308 and 4,778,144 shares issued and outstanding, as of December, 2017 and 2016, respectively	47,913	47,781
Additional paid-in capital	14,016,916	13,978,408
Retained earnings	40,113,418	37,839,563
Total shareholders' equity	54,178,247	51,865,752
Noncontrolling interest	38,785	86,531
Total equity	54,217,032	51,952,283
Total liabilities and shareholders' equity	$ 80,451,293	$ 77,817,751

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

Regency Affiliates, Inc. and Subsidiaries
Consolidated Statements of Income

	Years Ended Decemberr 31, 2017	2016
Revenue		
Rental	$ 3,116,251	$ 2,190,622
Insurance, late fees and other income	292,382	146,332
Retail	-	4,770
Total revenue	3,408,633	2,341,724
Operating expenses:		
Self-storage cost of operations	1,418,599	864,232
Self-storage depreciation expense	776,942	548,565
General and administrative expenses	1,912,800	2,140,887
Total operating expenses	4,108,341	3,553,684
Loss from operations	(699,708)	(1,211,960)
Other (income) expense:		
Acquisition costs	-	1,298,494
Income from equity investment in partnerships/LLC	(6,128,915)	(7,289,347)
License agreement income	(106,989)	(54,522)
Interest income	(6,196)	(2,610)
Interest expense	1,275,958	880,049
Amortization of debt discount	12,624	8,417
Total other (income) expense	(4,953,518)	(5,159,519)
Net income before income taxes	4,253,810	3,947,559
Income tax expense	813,203	860,090
Net income	3,440,607	3,087,469
Net loss attributable to noncontrolling interest	(15,096)	(251,584)
Net income allocated to shareholders	$ 3,455,703	$ 3,339,053

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

Regency Affiliates, Inc. and Subsidiaries
Consolidated Statements of Changes in Equity
For the Years Ended December 31, 2017 and 2016

	Preferred Stock		Common Stock		Additional Paid-In Capital	Retained Earnings	Shareholders' Equity	Noncontrolling Interest	Total Equity
	Shares	Amount	Shares	Amount					
Balance at January 1, 2016	-	$ -	3,678,559	$ 36,786	$ 5,057,196	$ 35,581,506	$ 40,675,488	$ -	$ 40,675,488
Cashless exercise of common stock options	-	-	20,952	209	(209)	-	-	-	-
Common stock issued through private placement offering	-	-	1,078,633	10,786	8,887,936	-	8,898,722	-	8,898,722
Noncontrolling interest expense	-	-	-	-	-	-	-	350,000	350,000
Stock options compensation expense	-	-	-	-	33,485	-	33,485		33,485
Dividend paid to noncontrolling interest	-	-	-	-	-		-	(11,885)	(11,885)
Cash dividends paid	-	-	-	-	-	(789,529)	(789,529)	-	(789,529)
Cash dividends declared	-	-	-	-	-	(291,467)	(291,467)	-	(291,467)
Net income (loss)	-	-	-	-	-	3,339,053	3,339,053	(251,584)	3,087,469
Balance at December 31, 2016	-	$ -	4,778,144	$ 47,781	$ 13,978,408	$ 37,839,563	$ 51,865,752	$ 86,531	$ 51,952,283
Cashless exercise of common stock options	-	-	13,164	132	(132)	-	-	-	-
Stock options compensation expense	-	-	-	-	38,640	-	38,640	-	38,640
Dividend paid to noncontrolling interest	-	-	-	-	-	-	-	(32,650)	(32,650)
Cash dividends paid	-	-	-	-	-	(882,391)	(882,391)	-	(882,391)
Cash dividends declared	-	-	-	-	-	(299,457)	(299,457)	-	(299,457)
Net income (loss)	-	-	-	-	-	3,455,703	3,455,703	(15,096)	3,440,607
Balance at December 31, 2017	-	$ -	4,791,308	$ 47,913	$ 14,016,916	$ 40,113,418	$ 54,178,247	$ 38,785	$ 54,217,032

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

Regency Affiliates, Inc. and Subsidiaries
Consolidated Statements of Cash Flows

	Years Ended December 31, 2017	Years Ended December 31, 2016
Cash Flows From Operating Activities		
Net Income	$ 3,440,607	$ 3,087,469
Adjustments to reconcile net income to net cash used in operating activities:		
Non-cash expenses		
Depreciation and amortization	781,280	551,171
Income from equity investment in partnerships/LLCs	(6,128,915)	(7,289,347)
Stock based compensation	38,640	33,485
Amortization of debt discount	12,624	8,417
Bad debt expense	-	21,000
Changes in operating assets and liabilities		
Prepaid expenses	(35,053)	(307,906)
Prepaid insurance	105,100	(540,400)
Prepaid income taxes	(164,017)	132,177
Rent receivable	(16,581)	(5,619)
Inventory	5,741	(2,073)
Other assets	-	(182,731)
Accounts payable and accrued expenses	122,222	8,735
Deferred revenue	3,398	142,285
Deferred rent	1,889	79,192
Income tax payable	221,722	(53,021)
Tenant security deposits	(1,052)	(1,000)
Total adjustments	(5,053,002)	(7,405,635)
Net cash used in operating activities	(1,612,395)	(4,318,166)
Cash Flows From Investing Activities		
Acquisition of SSCP, net of cash acquired and acquisition expenses	-	(9,750,000)
Distributions of earnings from partnerships/LLC	3,095,405	3,050,000
Purchase of property and equipment	(15,749)	(40,127)
Additional deposits to restricted cash	(49,533)	(289,469)
Net cash provided by (used in) investing activities	3,030,123	(7,029,596)
Cash Flows From Financing Activities		
Dividends paid to common shareholders	(1,173,858)	(1,005,644)
Dividends paid to noncontrolling shareholder	(32,650)	(11,885)
Proceeds from comon stock private placement offering	-	8,898,722
Cash paid for debt financing fee	-	(126,250)
Contribution from non-controlling interest	-	350,000
Net cash (used in) provided by financing activities	(1,206,508)	8,104,943
Net increase (decrease) in cash and cash equivalents	211,220	(3,242,819)
Cash and cash equivalents - beginning	5,044,512	8,287,331
Cash and cash equivalents - ending	$ 5,255,732	$ 5,044,512
Supplemental Disclosures of Cash Flow Information		
Cash paid during the period for:		
Interest	$ 1,276,234	$ 777,320
Income taxes	$ 755,498	$ 1,045,288
Non-cash investing and financing activities:		
Common stock dividends declared	$ 299,457	$ 291,467
Cashless exercise of common stock	$ 132	$ 209

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

Note 1. Summary of Significant Accounting Policies

Basis of Presentation

The financial statements are presented on an accrual basis in accordance with U.S. generally accepted accounting principles ("U.S. GAAP") as defined in the Financial Accounting Standards Board Accounting Standards Codification (the "Codification").

Nature of Operations

Regency Affiliates, Inc. ("Regency" or "the Company") invests in assets that generate attractive, predictable and sustainable returns on capital. The Company's objective is to generate long term value for its shareholders. Management seeks sound investment opportunities to meet its business characteristics and valuation criteria.

The Company holds a limited partnership interest in Security Land and Development Company Limited Partnership ("Security Land"), which owns and operates 34.3 acres of land and rental property of approximately 717,000 square feet in Woodlawn, Maryland, which is occupied by the United States Social Security Administration's Office of Disability and International Operations. In November 2000, the Company acquired a 5% limited partnership interest in 1500 Woodlawn Limited Partnership, the general partner of Security Land. See Note 2, "Investment in Security Land and Development Company Limited Partnership."

In addition, Regency Power Corporation ("Regency Power", 100% owned subsidiary of the Company) owns a 50% interest in MESC Capital, LLC, a Delaware limited liability company ("MESC Capital"). MESC Capital owns a 100% interest in Mobile Energy Services Company, LLC, an Alabama limited liability company ("Mobile Energy"), which owns an on-site energy facility that supplies steam and electricity to a Kimberly-Clark tissue mill in Mobile, Alabama. See Note 3, "Investment in MESC Capital LLC."

In April 2016, Regency formed a new, wholly owned subsidiary, RSS Investments LLC ("RSS"). RSS entered into a joint-venture, acquiring a majority ownership (80%) of SSCP Harrisburg Holdings, LLC, a Delaware limited liability company ("Harrisburg Holdings"). Harrisburg Holdings is the sole member of SSCP Harrisburg Intermediate Holdings, LLC, a Delaware limited liability company ("Intermediate Holdings"). Simultaneously with RSS's investment in Harrisburg Holdings, Harrisburg Intermediate Holdings acquired a portfolio of five self-storage facilities in Harrisburg, Pennsylvania. Through our controlling interest of SSCP Harrisburg Holdings, LLC, we are focused on the ownership, operation, and acquisition of self-storage properties located within the Harrisburg, Pennsylvania area.

Principles of Consolidation

These consolidated financial statements include the accounts of the Company, and its wholly owned subsidiaries, Regency Power and RSS. All significant intercompany balances and transactions have been eliminated in consolidation.

Note. 1. Summary of Significant Accounting Policies (continued)

Noncontrolling Interest

The Company consolidates its 80% equity interest in Harrisburg Holdings and reports the remaining 20% interest by the third party, SSCP Management LLC, as a noncontrolling interest on the consolidated balance sheets. At December 31, 2017 and 2016, the noncontrolling equity interest was $38,785 and $86,531, respectively. The net income or net loss of Harrisburg Holdings is allocated based on the ownership percentages on the consolidated statements of income. For the years ended December 31, 2017 and 2016, Harrisburg Holdings had net loss of $75,472 and $1,257,920, respectively, resulting in net loss attributable to the noncontrolling interest for the years ended December 31, 2017 and 2016 of $15,096 and $251,584, respectively.

The Company's LLC agreement terms provide RSS with a 7.5% per annum preferred return on its initial capital contribution of $11,230,744, and a 7.5% per annum preferred return to SSCP on its base contribution amount of $350,000. Management has elected to make quarterly distributions of these returns to its members. After satisfaction of the preference amounts, 80% of surplus cash flow may be allocated to the RSS and 20% to SSCP. Dividends paid to RSS are eliminated upon consolidation. During the years ended December 31, 2017 and 2016, distributions of $32,650 and $11,885, respectively, were paid to the noncontrolling interest members.

Cash and Cash Equivalents

Cash and cash equivalents represent cash and short-term highly liquid investments with original maturities of three months or less. The Company places its cash and cash equivalents with high credit quality financial institutions that may exceed federally insured amounts at times. As of December 31, 2017 and 2016, the Company's cash equivalents were $4,488,345 and $4,145,850, respectively.

Restricted Cash

The self-storage facilities hold escrow funds in money market trust accounts for real estate taxes, insurance and replacement reserves disbursements to be paid when due, pursuant to the terms of the bank financing agreement.

Inventory

Inventory consists of purchased finished goods held by RSS and is valued at the lower of cost or net realizable value using the first-in, first out (FIFO) valuation method.

Self-Storage Properties

Self-storage properties are carried at historical cost less accumulated depreciation and any impairment losses. Major replacements and betterments, which improve or extend the life of an asset, are capitalized. Expenditures for ordinary repairs and maintenance are expensed as incurred and are included in self-storage cost of operation. Estimated depreciable lives of self-storage properties are determined by considering the age and other indicators about the condition of the assets at their respective dates of acquisition, resulting in an estimated useful life for assets within each category. All self-storage property assets are depreciated using the straight-line method. Buildings and improvements are depreciated over estimated useful lives of 39 years.

When a self-storage property is acquired in a business combination, the purchase price of the acquired self-storage property is allocated to land, buildings and improvements, furniture and equipment, customer in-place leases, assumed real estate leasehold interests, other assets acquired and liabilities assumed, based on the estimated fair value of each component. When a portfolio of self-storage properties is acquired, the purchase price is allocated to the individual self-storage properties based on the fair value determined using an income approach with appropriate risk-adjusted capitalization rates, which take into account the relative size, age and location of the individual self-storage properties.

Note 1. Summary of Significant Accounting Policies (continued)

Self-Storage Properties (continued)

These items consist of the following at:

	December 31,	
	2017	2016
Land	$ 4,870,000	$ 4,870,000
Building and improvements	30,193,771	30,193,771
Furniture and equipment	23,805	14,588
	35,087,576	35,078,359
Less: Accumulated Depreciation	(1,325,507)	(548,565)
	$ 33,762,069	$ 34,529,794

Depreciation expense on these properties was $776,942 and $548,565 for the years ended December 31, 2017 and 2016, respectively.

Customer In-place Leases

In allocating the purchase price for an acquisition accounted for as a business combination, the Company determines whether the acquisition includes intangible assets. The Company allocates a portion of the purchase price to an intangible asset attributed to the value of customer in-place leases. This intangible asset is amortized to expense using the straight-line method over 12 months, the estimated average rental period for our customers. Substantially all of the leases in place at acquired properties are at market rates, as the leases are month-to-month contracts.

Acquisition Costs, Organizational and Offering Expenses

The Company incurred title, legal and consulting fees, and other costs associated with the completion of self-storage property acquisitions. Such costs are included in acquisition costs in the accompanying statements of income in the period in which they are incurred. The Company also incurred legal fees and filing fees in connection with the organization of the Company and its subsidiaries, which are charged to expense in the period incurred.

Commissions, legal fees and other costs that are directly associated with equity offerings are capitalized as deferred offering costs, pending a determination of the success of the offering. Deferred offering costs related to successful offerings are charged to equity in the period it is determined that the offering was successful. Deferred offering costs related to unsuccessful offerings are recorded as expense in the period when it is determined that the offering is unsuccessful. Other costs related to equity offerings, such as audit fees associated with the operations of our self-storage properties for periods preceding the related contribution and formation transactions, are charged to expense in the period incurred.

Property, Plant and Equipment

Property, plant and equipment is carried at cost. Depreciation is provided over the estimated useful lives of the assets using the straight-line method as follows: buildings and improvements 39 years; machinery and equipment 7 years. Repairs and maintenance costs are expensed as incurred.

Note 1. Summary of Significant Accounting Policies (continued)

Property, Plant and Equipment

These items consist of the following at:

	December 31, 2017	December 31, 2016
Machinery and equipment	$ 43,822	$ 37,291
Less: Accumulated depreciation	(18,695)	(14,358)
	$ 25,127	$ 22,933

Depreciation expense was $4,337 and $2,606 for the years ended December 31, 2017 and 2016, respectively.

Investments in Partnerships / LLC

The Company uses the equity method of accounting for investments in equity securities in which it has more than a 20% interest, but does not have a controlling interest and is not the primary beneficiary. The Company uses the cost method of accounting for investments in equity securities in which it has a less than 20% equity interest and virtually no influence over the investee's operations. Investments owned over 50% with a controlling interest are consolidated within these financial statements.

Evaluation of Long Lived Assets

Long-lived assets are assessed for recoverability on an ongoing basis. In evaluating the fair value and future benefits of long-lived assets, their carrying value would be reduced by the excess, if any, of the long-lived assets' carrying value over management's estimate of the anticipated undiscounted future net cash flows of the related long-lived assets.

Fair Value of Financial Instruments

The fair values of cash and cash equivalents, other current assets, and accounts payable and accrued expenses approximate their carrying values because of the short maturity of these financial instruments.

Revenue and Expense Recognition

Management has determined that all of our leases are operating leases. Substantially all leases may be terminated on a month-to-month basis and rental income is recognized ratably over the lease term using the straight-line method. Rents received in advance are deferred and recognized on a straight-line basis over the related lease term associated with the prepayment. Promotional discounts and other incentives are recognized as a reduction to rental income over the applicable lease term. Other property-related revenue consists of ancillary revenues such as tenant access fees for insurance and commissions and sales of storage supplies which are recognized in the period earned.

Property tax expense is based on actual amounts billed, or estimates of anticipated bills or assessments that have not yet been received from the taxing authorities. Cost of operations, general and administrative expense, interest expense, and advertising expenditures are expensed as incurred.

Note 1. Summary of Significant Accounting Policies (continued)

Advertising Expenses

The Company expenses advertising costs when incurred. Advertising and marketing costs totaled $65,323 for the year ended December 31, 2017.

Stock-Based Compensation

The Company accounts for stock and stock options issued for services and compensation to employees under the fair value method. For non-employees, the fair market value of the Company's stock is measured on the date of stock issuance or the date an option/warrant is granted. The Company determines the fair market value of the options issued under the Black-Scholes Pricing Model. The Company follows the requirements of Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 718-10, "Compensation – Stock Compensation," which establishes accounting for equity instruments exchanged for employee services. Under the provisions of FASB ASC 718-10, share-based compensation cost is measured at the grant date, based on the fair value of the award, and is recognized as an expense over the requisite service period (generally the vesting period of the equity grant).

Income Taxes

The Company utilizes FASB ASC 740-10, "Income Taxes", which requires an asset and liability approach to financial accounting and reporting for income taxes. The difference between the financial statement and tax basis of assets and liabilities is determined annually. Deferred income tax assets and liabilities are computed for those temporary differences that have future tax consequences using the current enacted tax laws and rates that apply to the periods in which they are expected to affect taxable income. In some situations, FASB ASC 740-10 permits the recognition of expected benefits of utilizing net operating loss and tax credit carryforwards. Valuation allowances are established based upon management's estimate, if necessary. Income tax expense (benefit) is the current tax payable or refund for the period plus or minus the net change in the deferred tax assets and liabilities.

The Tax Cuts and Jobs Act (the "Tax Act") was enacted on December 22, 2017. The Tax Act reduces the U.S. federal corporate tax rate from 35% to 21%. As of the completion of these consolidated financial statements and related disclosures, the Company has made a reasonable estimate of the effects of the Tax Act. This estimate incorporates assumptions made based upon the Company's current interpretation of the Tax Act, and may change as the Company may receive additional clarification and implementation guidance and as the interpretation of the Tax Act evolves.

Use of Estimates

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities as of the date of the financial statements, and also affect the amounts of revenues and expenses reported for each period. Actual results could differ from those which result from using such estimates. Management utilizes various other estimates, including but not limited to, assessing the collectability of accounts receivable, the valuation of inventory, determining the estimated lives of long-lived assets, determining the potential impairment of intangibles, the fair value of stock options, the recognition of revenue, and other legal claims and contingencies. The results of any changes in accounting estimates are reflected in the financial statements in the period in which the changes become evident. Estimates and assumptions are reviewed periodically and the effects of revisions are reflected in the period that they are determined to be necessary.

Note 1. Summary of Significant Accounting Policies (continued)

Limitations

Fair value estimates are made at a specific point in time, based on relevant market information and information about the financial statements. These estimates are subjective in nature, involve uncertainties and matters of significant judgment, and therefore cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

Subsequent Events Evaluation

The Company has evaluated subsequent events through July 17, 2018, which is the date these financial statements were available to be issued.

Note 2. Investment in Security Land and Development Company Limited Partnership

The Company owns a limited partnership interest in Security Land, which owns and operates an office complex. The Company has limited voting rights and is entitled to certain allocations of the profit and loss and operating cash flow distributions of Security Land.

For the years ended December 31, 2017 and 2016, the Company's income from its equity investment in Security Land was $4,368,370 and $3,858,770, respectively.

The Company also owns a 5% limited partnership interest in 1500 Woodlawn Limited Partnership, the general partner of Security Land. The Company recognized income of $11,497 and $10,154 for the years ended December 31, 2017 and 2016, respectively, from this investment.

Summarized Balance Sheet information for Security Land is as follows:

	December 31, 2017	December 31, 2016
Balance Sheet Data		
Cash and cash equivalents	$ 85,245	$ 150,680
Restricted cash	3,425,360	2,372,915
Real estate, net	4,865,934	7,551,756
Deferred charges, net	349,333	984,996
Receivables and other assets	1,151,095	1,143,956
Due from affiliate	-	-
Leasing cost, net of accumulated amortization	269,755	538,734
Total Assets	$ 10,146,722	$ 12,743,037
Accounts payable and accrued expenses	$ 361,558	$ 359,817
Project note payable	17,040,169	24,321,658
Accrued interest payable	135,790	50,852
Total Liabilities	$ 17,537,517	$ 24,732,327
Partners' deficit:		
Total Partners' Deficit	(7,390,795)	(11,989,290)
Total Liabilities and Partner's Deficit	$ 10,146,722	$ 12,743,037

Note 2. Investment in Security Land and Development Company Limited Partnership (continued)

Summarized Statements of Income information for Security Land is as follows:

	For the Years Ended December 31, 2017	2016
Revenues	$ 14,025,130	$ 13,803,667
Expenses	9,426,635	9,742,015
Net income	$ 4,598,495	$ 4,061,652

Note 3. Investment in MESC Capital LLC

The Company owns a 50% membership interest in MESC Capital, which, through its subsidiary, owns an on-site energy facility that supplies steam and electricity to a Kimberly-Clark tissue mill in Mobile, Alabama pursuant to an Amended and Restated Tissue Mill and Energy Services and Site Coordination Agreement that expires on or about April 30, 2019.

The Company accounts for the Investment in Partnerships using the equity method, whereby the carrying value of these investments are increased or decreased by the Company's allocable share of book income or loss. The Company recognized income of $1,749,048 and $3,420,423 for the years ended December 31, 2017 and 2016, respectively, from this investment.

On April 24, 2017, Kimberly-Clark notified MESC Capital of its intention to not renew the lease upon its expiration on April 30, 2019.

The Company recognizes losses on equity-method investments in excess of what would otherwise be recognized by application of the equity method when factors indicate a decrease in value of the investment has occurred that is other than temporary. As of December 31, 2017, the Company evaluated an investment of its interest in MESC Capital, given Kimberly-Clark’s decision not to renew the lease. The Company determined that there were no additional losses to record in excess of what the Company has recognized under the equity method.

Note 3. Investment in MESC Capital LLC

Summarized Balance Sheet information for MESC Capital LLC is as follows:

	December 31, 2017	December 31, 2016
Balance Sheet Data		
Cash and cash equivalents	$ 2,050,457	$ 1,143,816
Restricted cash	8,097,742	6,751,878
Trade receivable	1,782,114	3,453,963
Current portion of net investment in direct financing lease	2,893,980	460,402
Inventory	138,850	2,673,876
Prepaid expenses and other current assets	143,841	168,488
Total current assets	15,106,984	14,652,423
General plant, net	8,386	12,256
Investment in direct financing lease, net of current portion	239,753	3,883,733
Other assets- Inventory, net of current portion	1,236,509	3,637,632
Total assets	$ 16,591,632	$ 22,186,044
Accounts payable	$ 243,418	$ 266,705
Accounts payable to related parties	510,050	550,280
Accrued liabilities	56,437	58,603
Current portion of long-term debt	3,434,250	2,881,350
Total current liabilities	4,244,155	3,756,938
Long-term debt, net of current portion	2,014,776	5,403,688
Total liabilities	6,258,931	9,160,626
Members' equity	10,332,701	13,025,418
Total liabilities and members' equity	$ 16,591,632	$ 22,186,044

Note 3. Investment in MESC Capital LLC

Summarized Income Statement information for MESC Capital LLC is as follows:

	For the Years Ended December 31, 2017	For the Years Ended December 31, 2016
Revenues	$ 15,767,431	$ 16,138,819
Expenses	12,041,677	8,990,418
Income from operations	3,725,754	7,148,401
Other expenses	(227,661)	(307,557)
Net income	$ 3,498,093	$ 6,840,844

Note 4. Self-Storage Property Acquisition

On April 6, 2016, the Company formed a new, wholly owned subsidiary called RSS Investments LLC ("RSS"), a Delaware limited liability company. On April 18, 2016, RSS entered into a joint-venture, acquiring 97% of the outstanding preferred shares and 80% of the outstanding common shares of SSCP Harrisburg Holdings, LLC ("Harrisburg Holdings"). Harrisburg Holdings is the sole member of SSCP Harrisburg Intermediate Holdings, LLC ("Intermediate Holdings"). Also on this date, Intermediate Holdings completed its acquisition of a portfolio of five stand-alone self-storage facilities in the Harrisburg, Pennsylvania vicinity, for a total purchase price of $35 million. The facilities comprise approximately 330,000 square feet of net rentable space consisting of in excess of 2,500 climate and non-climate controlled storage units.

RSS funded the acquisition with proceeds from Regency's private stock offering (See Note 13) and Regency's working capital. The purchase price and related transaction expenses were financed with an $11,230,744 acquisition cash capital contribution by RSS to its joint-venture purchaser and a $25,250,000 non-recourse debt financing with a ten-year term, 4.95% fixed interest rate, and 30-year amortization commencing after a four-year interest only period. The joint-venture terms provide the Company with a 7.5% per annum preferred return on its initial capital contribution, and a 7.5% per annum preferred return to SSCP Management, LLC, the minority joint-venture partner, on its base contribution amount of $350,000. After satisfaction of the preference amounts, 80% of surplus cash flow is allocated to the Company and 20% to SSCP Management, LLC. The facilities were managed on a day-to-day basis by a newly-engaged third party property management company, who is an affiliate of SSCP Management, LLC, until July 31, 2017.

Regency accounts for its Investment in Harrisburg Holdings on a consolidated basis, reflecting the minority joint-venture partner's equity and share of net income or loss within the noncontrolling interest accounts. The fair value of the purchase price has been allocated to the assets acquired and liabilities assumed based on their estimated fair values. The following table summarizes the allocation of the fair value of identifiable assets acquired and liabilities assumed in the acquisition.

	Allocation of Fair Value
Land	$ 4,870,000
Building and improvements	30,193,771
Property, plant and equipment, net	35,063,771
Inventory	3,668
Prepaid expenses and other current assets	
Assets acquired	35,069,269
Accounts payable and accrued liabilities	(58,973)
Tenant security deposits	(10,296)
Liabilities acquired	(69,269)
Net assets acquired over liabilities acquired	35,000,000
Total purchase price	$ 35,000,000

Note 5. Stock Based Compensation

2003 Incentive Stock Plan

Effective as of March 17, 2003, the Company's Board of Directors and Stockholders approved and adopted the 2003 Stock Incentive Plan (the "2003 Plan"). The 2003 Plan allows the Administrator (as defined in the 2003 Plan), currently the Compensation Committee, to determine the issuance of incentive stock options, non-qualified stock options and restricted stock to eligible employees and outside directors and consultants of the Company. The Company has reserved 500,000 shares of common stock for issuance under the 2003 Plan. The exercise price of any option granted under the 2003 Plan is determined by the Administrator, and no option or award exercise date can exceed ten years from the grant date. On August 13, 2008, the Company's Board of Directors approved an amendment to the 2003 Plan that increased the total number of authorized shares available from 500,000 to 750,000. All other terms of the Plan remain in full force and effect.

Total stock-based compensation expense recorded within General and Administrative Expenses in the Consolidated Statements of Income was $38,640 and $33,485 during the years ended December 31, 2017 and 2016, respectively. These amounts recognize the vested portion of the requisite grant terms. Unamortized stock-based compensation for these option awards as of December 31, 2017 was $44,626 and will be amortized over a remaining period of 3.5 years.

As of December 31, 2017, 75,000 shares remain available for issuance under the 2003 Plan.

Note 5. Stock Based Compensation, continued

The following is a summary of the status of the Company's options for the years ended December 31, 2017 and 2016:

	Exercise Price Range	Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life
Outstanding at January 1, 2016	$ 2.60-9.50	205,000	$ 5.45	2.61
Issued	9.50	35,000	9.50	9.63
Exercised	6.27	(50,000)	6.27	
Outstanding at December 31, 2016	$ 2.60-9.50	190,000	$ 5.98	3.93
Exercisable at December 31, 2016	$ 2.60-6.50	155,000	$ 5.18	2.70
Issued				
Exercised	5.10	(50,000)	5.10	
Outstanding at December 31, 2017	$ 2.60-9.50	140,000	$ 6.29	4.11
Exercisable at December 31, 2017	$ 2.60-6.50	112,000	$ 5.49	3.05

Note 6. Income Taxes

As referred to in Note 1, the Company accounts for income taxes under FASB ASC 740-10, “Income Taxes”. The deferred taxes are the result of temporary differences between financial reporting and tax reporting for depreciation, earnings from the Company’s partnership investment in Security Land and the recognition of income tax carry-forward items.

The Company files consolidated income tax returns with its wholly owned subsidiaries. As of December 31, 2013, for regular federal and state income tax purposes, the Company has utilized all of its net operating loss carryforwards (NOLs). The Company believes it is no longer subject to income tax examinations for years prior to 2013 by the respective taxing authorities.

The Company and the general partner of Security Land are in disagreement as to the manner in which taxable income of Security Land is to be allocated pursuant to the partnership agreement and applicable law, and for years 2004 through 2015, the Company has reported taxable income (loss) from Security Land in a manner it believes is proper, but which was different than the manner reported by Security Land. An investigation or other action by the applicable tax authorities to resolve this difference could have an adverse impact on the Company’s operations and financial results.

The Company’s 2014 tax return is under examination by the Internal Revenue Service (“IRS”).

To safeguard itself from any possible negative impact, in February 2016, the Company purchased an insurance policy and binder to insure against the negative tax consequences should any arise from the disagreement with Security Land regarding reported taxable income allocations (See Notes 2 and 7). The Company paid $633,900 for the policy and binder which provide coverage of up to $10 million over the next seven years in the event the IRS or a state taxing authority were to investigate and reject the Company’s tax positions taken. The policy is subject to certain limitations, exclusions and retentions.

For the years ended December 31, 2017 and 2016, the Company has recorded tax expense (benefit) of $813,203 and $860,090, respectively, including expense of $(193,730) and $113,762, respectively, for state income taxes. The Company’s applicable statutory tax rates are 34% and 5.5% for federal and state tax purposes. The reconciliation of the Company’s income tax expense for the years ended December 31, 2017 and 2016 is as follows:

	For the Years Ended December 31,	
	2017	2016
Income tax at federal statutory rate	$ 1,446,296	$ 1,324,821
State taxes, net of federal benefit	(196,730)	113,762
Permanent differences	(439,363)	(521,647)
Other	-	(56,846)
Total income tax expense (benefit)	$ 813,203	$ 860,090

Note 7. Related Party Transactions

Effective June 1, 2012, the Board of Directors authorized the Company to compensate each Board director an annual fee of $20,000, payable $5,000 quarterly, in arrears, for each fiscal quarter served. Subsequent annual 3% increases have been approved through 2017.

During the years ended December 31, 2017 and 2016, the Company incurred directors' fees of $45,008 and $43,697, respectively. As of December 31, 2017 and 2016, directors' fees of $0 and $0, respectively, were outstanding.

In May 2016, the Company entered into a consulting agreement with a non-independent member of its Board of Directors, to provide consulting, financial analyses, and due diligence services for any new potential investment available to the Company, and ongoing financial monitoring of existing investments. Terms of the agreement include an initial fee of $7,500 and a fee of $7,200 each month thereafter. In addition, the agreement called for a 25,000 non-qualified common stock option award, exercisable at $9.50 per share with a term of 10 years and vesting of 5,000 options per year over a 5-year period. The Company may terminate the agreement at any time for cause; the consultant may terminate the agreement at will. The fair value of the options granted was $83,400. During the years ended December 31, 2017 and 2016, the Company recorded stock-based compensation expense of $27,601 and $23,918, respectively, related to this stock option. In addition, under the terms of the agreement, the Company paid $86,400 and $47,100 to the consultant during the years ended December 31, 2017 and 2016, respectively.

Pursuant to a property management agreement entered into with SSCP Property Management, LLC, an affiliate of SSCP, SSCP must pay 5% of the monthly gross receipts as a management fee to an entity wholly-owned by the noncontrolling equity interest. The expense incurred was $104,000 and $109,370 during the years ended December 31, 2017 and 2016, respectively. No amounts were owed to this party as of December 31, 2017. On July 31, 2017 this property management agreement was terminated and the Company entered into an agreement with an unrelated third party to provide these services.

Note 8. Contingencies, Risks, and Uncertainties

The Company is subject to numerous contingencies, risks and uncertainties including, but not limited to, the following that could have a severe impact on the Company:

A default in the Lease or sudden catastrophe to the Security West Building from uninsured acts of God or war could have a materially adverse impact upon the Company's investment in Security Land and Development Company Limited Partnership and, therefore, its financial position and results of operations (See Note 2).

Royalty, an affiliate of the Company's management, beneficially owns approximately 60% of the Company's common stock. As a result, Royalty has the ability to control the outcome of all matters requiring shareholder approval, including the election and removal of directors and any merger, consolidation or sale of all or substantially all of the Company's assets.

There are many public and private companies that are also searching for operating businesses and other business opportunities as potential acquisition or merger candidates. The Company will be in direct competition with these other companies in its search for business opportunities. Many of these entities have significantly greater financial and personnel resources than the Company.

Note 8. Contingencies, Risks, and Uncertainties (continued)

The Company and the general partner of Security Land are in disagreement as to the manner in which taxable income of Security Land is to be allocated pursuant to the partnership agreement and applicable law, and for years 2004 through 2016, the Company reported taxable income (loss) from Security Land in a manner the Company believes is proper, but which was different than the manner reported by Security Land (See Note 5). This may result in an investigation or other action by the applicable tax authorities and any action taken by tax authorities to resolve this difference could have an adverse impact on the Company's operations and financial results. In February 2016, the Company obtained an insurance policy to protect against such losses, however, it may not be sufficient under all circumstances to cover all potential losses to the Company in the event of any such adverse determinations.

In September 2016, the Company received an Internal Revenue Service letter indicating its 2014 Federal Form 1120 was selected for examination. Management has submitted the initial documentation requested.

On April 24, 2017, Kimberly-Clark notified MESC Capital of its intention to not renew its lease.

The Company entered into a facilities management agreement with CubeSmart Asset Management LLC for an initial term of 3 years effective August 1, 2017. Under the agreement the company is required to pay a monthly management fee equal to the greater of 5.375% of gross revenue or $2,000 for each location. The management fee expense from August 1, 2017 through December 31, 2017 was approximately $74,051.

Note 9. Lease Commitments

In January 2016, Regency paid a $201,329 security deposit and entered into a new, seven-year office lease agreement, for a 4,081 square foot space for its New York City location. Base rental payments under this agreement are $74 per square foot per year, with a 1.75% fixed annual escalation. In addition, the Company is responsible to pay the tenant's share of real estate tax increases above the 2016/2017 base year and electricity usage. A rent concession has been granted to waive the first three months' rent. On the third anniversary of rent commencement, and provided the Company is not in default of any rental obligations, the landlord agrees to reduce the security deposit to six months' base rent, or approximately $151,000. The lease also contains an early termination clause which is effective after five years, with proper notice and payment of an early termination fee. The office relocated in May 2016, the first month of the lease term. Rent expense for the years ended December 31, 2017 and 2016 was $307,312 and $205,022, respectively.

As of December 31, 2017, future minimum payments under this operating lease are as follows:

For the Years Ended December 31:		
2018	$	310,864
2019		316,304
2020		321,839
2021		327,471
2022		333,202
Thereafter		111,709
Total	$	1,721,389

Note 10. License Agreement

In May 2016, a new License Agreement commenced with an unrelated entity which provides the use of leased space within the Company's New York City office, for $8,833 per month, plus monthly office service fees, through June 2018. Annual one-year renewal periods are available, with license and service fee increases of 2.25% and 2.5%, respectively, until the expiration of the office lease.

License fee income and related service fees for the years ended December 31, 2017 and 2016 was $106,989 and $54,522, respectively.

Note 11. Simplified Employee Pension- Individual Retirement Account (SEP-IRA)

The Company adopted a SEP-IRA Plan in 2004. During the years ended December 31, 2017 and 2016, the Company expensed contributions of $117,325 and $113,883, respectively, to the SEP-IRA Plan. The SEP-IRA Plan covers all employees who receive compensation from the Company during the year. Employer contributions are discretionary and determined annually. In addition, the SEP-IRA Plan allows participants to make elective deferral contributions through payroll deductions.

Note 12. Private Offering of Stock

On March 16, 2016, the Company commenced a private stock offering of up to 1,212,121 shares of common stock at a purchase price of $8.25 per share, to its shareholders of record as of January 22, 2016, who are accredited investors as defined in Rule 501 of Regulation D under the Securities Act of 1933. The offering, originally set to expire on April 7, 2016, was extended to May 12, 2016. At the close of the offering, 1,078,633 common shares were sold for total gross proceeds raised of $8,898,722. These funds were used in the Harrisburg Holdings acquisition (See Note 4).

Note 13. Dividends

The Board of Directors has a dividend policy whereby the Board expects to declare a total annual dividend to common shareholders of $0.25 per share, to be paid in equal, quarterly installments of $0.0625 per share, provided that the determination to pay any cash dividends for any quarterly period will be made at the applicable time by the Board, in the Board's sole discretion, in compliance with the requirements of applicable law, and with consideration of the Company's future earnings and financial condition and other factors as may be deemed appropriate for consideration by the Board. The dividend policy will remain in effect until the Board determines, in its sole discretion, that it is in the best interests of the Company and its common shareholders to terminate the dividend policy.

In March 2017, the Board of Directors declared a quarterly cash dividend $0.061 per share of issued and outstanding common stock to holders of record as of the close of trading on March 31, 2017, totaling $291,467, payable on April 6, 2017. The dividend was paid on April 7, 2017.

In June 2017, the Board of Directors declared a quarterly cash dividend of $0.061 per share of issued and outstanding common stock to holders of record as of the close of trading on June 30, 2017, totaling $291,467, payable on July 6, 2017. The dividend was paid on July 7, 2017.

Note 13. Dividends (continued)

In September 2017, the Board of Directors declared a quarterly cash dividend of $0.0625 per share of issued and outstanding common stock to holders of record as of the close of trading on September 30, 2017, totaling $299,457, payable in October 6, 2017. The dividend was paid on October 6, 2017.

In December 2017, the Board of Directors declared a quarterly cash dividend of $0.0625 per share of issued and outstanding common stock to holders of record as of the close of trading on December 29, 2017, totaling $299,457, payable on January 5, 2018. The dividend was paid on January 5, 2018.

Note 14. Mortgage Note Payable

On April 18, 2016, the Company, through its subsidiary SSCP, obtained a $25,250,000 bank note to fund the acquisition of SSCP. The note is a non-recourse debt financing with a ten-year term, 4.95% fixed interest rate, and has a maturity date of May 6, 2026. The note is guaranteed by the owners of SSCP Management LLC, and is secured by all assets of Harrisburg Holdings. The net book value of these assets at December 31, 2017 was $34,513,980.

The Company paid underwriting fees of $126,250 in conjunction with the issuance of the note. The fees were recorded as a debt discount and are amortized over the life of the agreement. Amortization of debt discount was $12,624 and $8,417 for the years ended December 31, 2017 and 2016, respectively. The only amount due during the first four years of the note is interest.

Under the terms of this agreement Harrisburg Holdings is required to meet and maintain certain financial covenants. The covenant for the trailing twelve months ended December 31, 2017 is:

Minimum Debt Service Coverage Ratio	1.45 to 1.00
Actual Debt Service Coverage Ratio	1.56 to 1.00

As of December 31, 2017, future minimum principal payments due under the note are as follows:

For the Years Ended December 31:		
2018	$	-
2019		-
2020		248,531
2021		388,486
2022		408,158
Thereafter		24,204,825
Total	$	25,250,000

Note 15. Fair Value Measurements

The Company follows guidance in ASC 820 for its financial assets and liabilities that are re-measured at fair value at each reporting period, and non-financial assets and liabilities that are re-measured and reported at fair value at least annually.

The fair value of the Company's financial assets and liabilities reflects management's estimate of amounts that the Company would have received in connection with the sale of the assets paid in connection with the transfer of the liabilities in an orderly transaction between market participants at the measurement date. In connection with measuring the fair value of its assets and liabilities, the Company seeks to maximize the use of observable inputs (market data obtained from independent sources) and to minimize the use of unobservable inputs (internal assumptions about how market participants would price assets and liabilities). The following fair value hierarchy is used to classify assets and liabilities based on the observable inputs and unobservable inputs used in order to value the assets and liabilities:

- Level 1: Quoted prices in active markets for identical assets or liabilities. An active market for an asset or liability is a market in which transactions for the asset or liability occur with sufficient frequency and volume to provide pricing information on an ongoing basis.

- Level 2: Observable inputs other than Level 1 inputs. Examples of Level 2 inputs include quoted prices in active markets for similar assets or liabilities and quoted prices for identical assets or liabilities in markets that are not active.

- Level 3: Unobservable inputs based on our assessment of the assumptions that market participants would use in pricing the asset or liability.

The following table presents information about the Company's assets that are measured at fair value on a recurring basis at December 31, 2017 and 2016, and indicates the fair value hierarchy of the valuation inputs the Company utilized to determine such fair value:

	Assets at Fair Value as of December 31, 2017			
	Level 1	Level 2	Level 3	Total
U.S. Treasury Bills	$ 4,488,345	$ -	$ -	$ 4,488,345
Total	$ 4,488,345	$ -	$ -	$ 4,488,345

	Assets at Fair Value as of December 31, 2016			
	Level 1	Level 2	Level 3	Total
U.S. Treasury Bills	$ 4,145,850	$ -	$ -	$ 4,145,850
Total	$ 4,145,850	$ -	$ -	$ 4,145,850

Note 16. Subsequent Events

In March 2018, the Board of Directors declared a quarterly cash dividend of $0.0625 per share of issued and outstanding common stock to holders of record as of the close of trading on March 30, 2018, totaling $299,457, payable on April 6, 2018. The dividend was paid on April 6, 2018.

In June 2018, the Board of Directors declared a quarterly cash dividend of $0.0625 per share of issued and outstanding common stock to holders of record as of the close of trading on June 29, 2018, totaling $299,457, payable on July 6, 2018. The dividend was paid on July 6, 2018.

Subsequent to December 31, 2017 through the date of this report, the Company received $1,900,000 in distributions from its investment in MESC.