

APRA Advisor

Association of Professional Reserve Analysts is a nonprofit corporation established in 1995 by principals of America's leading reserve study companies. The purpose of APRA is to provide a forum to establish a common base of knowledge, standards of care and professionalism within the reserve study industry.

The **APRA Advisor** is a bimonthly publication designed to expand the understanding of reserve planning and increase awareness of **Professional Reserve Analysts**.

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Policizing Reserves

Planning for future repairs and replacements is one of the most critical and beneficial things a homeowner association should do. A Reserve Study is a long range planning tool that identifies common element building and grounds components that have useful lives of 2-30 years, the current cost of repair or replacement of each and a funding plan to accumulate the money to accomplish the work.

A Reserve Study is an indispensable planning process. But the study itself doesn't commit the Board or Members to follow it. A formal policy should be adopted that *commits* the HOA and Board to the reserve planning process and holds future Boards to the standards. For that, a **Reserve Study and Funding Policy** is called for. Without it, a future Board could decide to set the plan aside or worse, spend reserve funds on something they were never intended for.

A Reserve Study and Funding Policy obligates the homeowner association to follow the recommendations of the study. For many homeowner associations that have been handling costs by special assessment, this is a radical paradigm shift. So, formalizing the commitment to change will help ensure that some future Board won't drop the ball or shift back to old and bad habits.

Below is a policy which can be adapted to your HOA's use. Whether you already have a Reserve Study or are thinking about getting one, consider enacting this policy to formalize the commitment.

Nottacare Condominium Sample Policy Resolution # _____ Reserve Study & Funding

WHEREAS, Section ____ of the Homeowner Association Bylaws grants the general power to conduct the

business and affairs of the Homeowner Association to the Board of Directors, whose members shall be members of the Homeowner Association; and

WHEREAS, the Board of Directors has the responsibility to plan for the maintenance, repair and replacement of the common elements; and

WHEREAS, the members have the responsibility to fund the proper care of common elements; and,

WHEREAS, proper care of the common elements directly impacts the value of members' homes,

NOW, THEREFORE, BE IT RESOLVED THAT in order to properly maintain the common area, protect market value of members' homes and livability in the community, the Board of Directors establishes a policy as follows:

Reserve Study Defined. The Board shall follow a Reserve Study that includes this criteria:

- Identifies all components that are the homeowner association's responsibility to repair or replace that have a useful life of 2 to 30 years.
- Assigns a reasonable cost of repair or replacement to each component based on current costs for the area.
- Assigns a reasonable useful life to each component based on local conditions.
- A 30 Year Repair & Replacement Schedule which identifies the years when each component work will be performed including the inflation adjusted cost.
- Establishes a 30 Year Funding Plan which takes into consideration the costs of repairs and replacements, contributions from members, impact of inflation, revenue generated from invested reserve funds and taxes owing on interest earned. The

Funding Plan shall include monthly contributions from members adequate to meet projected costs without the need for special assessments.

- The Funding Plan shall include a "Percent Funded" factor which indicates the percent of actual reserve funds on hand versus the ideal of 100%.

Permitted Uses of Reserve Funds.

Reserve funds are to be used only for the repair and replacement of the specific components identified in the Reserve Study.

Annual Review. The Board shall review and revise the Reserve Study annually to reflect changes in costs, inflation and interest yield on invested funds. Component information shall be amended to reflect new information received, component additions or deletions. With this revised information, a new 30 Year Reserve Study projection shall be generated and used in conjunction with the Annual Budget process.

Borrowing Reserve Funds. Under special circumstances, like an unanticipated Operating Budget shortfall or an emergency, and if allowed by state statute, the Board may borrow from reserve funds. In such cases, the Board shall adhere to a strict repayment plan that will replace borrowed reserve funds within 12 months.

Investing Reserve Funds. In order to reduce the amount of member contributions, the Board shall invest reserve funds to generate interest revenue that will be added to the reserve account. Unless otherwise approved by the membership, all investments will be FDIC (Federal Deposit Insurance Corporation) insured or guaranteed by the United States Government. Investments should take into consideration the repair and replacement schedule so that there is no loss of interest for early withdrawal. The Board shall review the reserve fund investment plan at least annually to ensure that the funds are receiving competitive yields and make prudent adjustments as needed. The Board may hire an investment counselor to assist in

formulating an investment plan.

Performing the Reserve Study & Annual Review. To ensure objectivity and competence, the Board shall hire only a third party Reserve Study professional with experience, references and credentials to do the Reserve Study.

Dated: _____, 200__

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Ask the Reserve Analyst

Q Our HOA is trying to get on track after years of self management and neglect. Lots of people were well intended but hadn't a clue of what being a board member really meant. Any advice on getting pointed in the right direction?

A One of the first things to get done is a reserve study so that the scope and cost of your current and future repairs can be fully understood. Consider hiring a homeowner association management company to handle your business. There is simply too much going on for unpaid and untrained volunteers, even if they have the best of intentions. And no one should have to enforce rules on or collect money from their neighbors. (See Regenesi.net Manager Issues for things to consider when hiring a professional manager).

Above all, be patient but persistent. Change comes slowly to some. Years of management by neglect is a hard mindset to change. Encourage more flexible minds to run for the Board.

Q Our HOA is considering doing a reserve study. We have an owner who is a CPA that says he will do one for nothing. While free is a good price, what are the downsides of this arrangement?

A HOA members (regardless of profession) are rarely qualified to do reserve studies unless they have extensive construction background and knowledge of HOA operations. A reserve study is meaningless if the numbers are not reality based. Homeowners typically do not have access to reliable construction cost information or contractors so end up guessing at or using off the cuff estimates given by contractors over the phone. Accurate reserve studies require site work by trained experts that know what they are looking at.

The issue of conflict of interest with a homeowner generated reserve study is also a real one, especially if you have members pressing for lower homeowner fees (almost always the case). There will be a steady pressure to suppress reality to justify reducing fees. This is always detrimental to the asset values and livability of the community.

Have your Reserve Study done by a trained professional with both credentials and local references to prove capability. Having and following a good Reserve Study can dramatically increase asset values and marketability. Having none or a bad one is like an appendix: absolutely useless and one day may do you in.

Q The Board recently decided that each owner should maintain the fence that adjoins the property even though the fences belong to the HOA. They say it's to save the homeowner association money.

A If the fences are common elements, the Board cannot unilaterally reassign

maintenance responsibility to the owners. To do this, an amendment to the governing documents must be approved by the owners. But even if it could be done, this is ill advised. One of the advantages of an HOA is reducing the cost of maintenance by joining together and making sure the maintenance gets done properly and in a timely manner. Requiring individual owners to be responsible is more expensive and bound to fail due to inadequate or improper maintenance.



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Pernicious Contradiction

There is a vicious rumor going around. The Board is talking about raising the dues again and everyone's up in arms. They raised the dues last year! And the year before! It's time to fire up the tar and pluck the chicken!

Ever hear this kind of thunder roll through your community? At the core of this storm is a pernicious contradiction. Members want the property taken care of but expect the Board to do it on a slumlord's budget. With too little money chasing too many expenses, maintenance suffers, home values slide and livability diminishes. Yet, year after year, the Spend No Money Drum gets beaten.

But it wasn't always thus. In the beginning, when the homes were new and the future bright, members basked in the glow of their own ignorance. The developer kept the homeowner fees low and, heck, why shouldn't they be? It doesn't cost anything to maintain something that's new. Let's worry about that when the time comes. Well, the time is now, the pot is empty, the assets worn out and recriminations abound. A \$3000 special assessment! Who's responsible for this? Why wasn't money being socked away years ago? I can't pay it! I *won't* pay it! Where's my lawyer?

It's at times like these that outside professionals are called for. The Board is authorized to hire the expertise it needs to run HOA business. HOA consultants like managers, lawyers, architects and engineers can assist the Board in making its case to the members. In the case of deferred maintenance and inadequate reserves, the Board should hire a Professional Reserve Analyst to perform a reserve study. A reserve study will consider all the repair and replacement issues, not just the urgent ones. A reserve study looks thirty years down the road and charts a course to proactively deal with these issues. The Reserve Study will identify priorities which the Board can further prioritize according to funding.

Hiring a knowledgeable consultant to supervise each project is a real bonus. For example, roofing projects should have a roofing consultant who can detail the scope of work, draft a contract, gather proposals from qualified contractors, ensure that the project is done to proper specifications and lien waivers executed. Consultant oversight ensures that the material warranty is not voided because of faulty installation. The cost of a consultant is typically only a small percentage of the total project cost. Clearly, this is an investment worth making. The same principle applies to other major projects like structural repairs, painting and landscape renovation.

Playing catch up on major repairs costs a lot of money over a short time period. In an effort to soften the blow to the members, the tendency may be to piecemeal the repairs over a number of

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danh@hoareserves.com

years and break large costs into more manageable chunks. But, piece mealing causes the costs to go *up*! The bigger the project, the cheaper the cost per unit. Piece mealing also creates an imbalance in member asset values. If Building A gets new paint this year, those units are more attractive and valuable from a buyer's perspective than those in unpainted Buildings B, C and D. This inequity will lead to resentment among the members that didn't get the benefit of the repairs.

To avoid these costly traps, the Board should only perform complete projects. If repairs must be split up by years, do them by type, not location. If painting is to be done, do all buildings at the same time. Same for roofing. Do it all at once, minimize disruption, get it over with and save a bundle.

If your HOA is suffering from deferred maintenance, consider raising the money to do multiple projects the same year. For example, if siding needs to be replaced, those energy inefficient windows should be replaced as well. The improved livability and value increase always far exceeds the cost so this is one of the best investments the members can make. And just consider the advantages to ending the bickering, debate and back biting. The sooner completed, the sooner the community

chest will swell with pride and past resentment forgotten.

So, recognize your HOA's pernicious contradiction when it raises its ugly head. This is one monster that's best dealt with directly and quickly. The harmony of your community hangs in the balance.

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HOA Wellness Survey

The health of a homeowner association is important to measure from time to time. Fortunately, even poor health is curable but identifying the problem precedes the cure. Here are a series of self-diagnosis questions:

1. Are all board meetings open to members? Yes No
2. Are all rules necessary, reasonable, uniformly enforced and include a right of appeal? Yes No
3. Do owners have an opportunity for input at board meetings? Yes No
4. Are all meeting minutes made available to members? Yes No
5. Do new owners receive informational packets to get them started on the right foot? Yes No
6. Is there an Owner Forum provided at Board Meetings to allow member comment? Yes No
7. Does your HOA have and follow a Reserve Study? Yes No
8. Does the Board consult with an attorney when proposing to new

- policies or rules? Yes No
9. If self managed, do you have a reliable system for emergency response? Yes No
 10. Do you have a sustained volunteer recruitment program? Yes No
 11. Does the Board follow an Annual Planning Calendar? Yes No
 12. Regular financial reports reviewed by the Board and then distributed to the members? Yes No
 13. Are records available for inspection by members? Yes No
 14. Is a newsletter distributed on a regular basis? Yes No
 15. Are rules and architectural guidelines that are easily available to the owners? Yes No
 16. Are rules and policies written in a positive tone to encourage compliance rather than dictatorial that promotes defiance? Yes No
 17. Do members receive timely notice of rules and policies? Yes No
 18. Are members kept informed of ongoing litigation? Yes No
 19. Are members given a chance to comment on proposed rules and policies? Yes No
 20. Does the HOA have a website which has regularly updated need-to-know information? Yes No

This survey hits on many things that smooth out HOA business. Requesting feedback is an important step to promoting volunteers. Adapt to your use so that you can get a clear picture on where there are wound that need treatment. Heal thyself!

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