

APRA Advisor

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Association of Professional Reserve Analysts (APRA) 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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Reserve Fund Adequacy

Over the years, there have been various positions taken by reserve study providers as to what constitutes "adequate" funds to repair or replace the common area components. Sometimes, the reserve study provider's recommendation differs from what the HOA board thinks is reasonable. Typically, the reserve study professional's recommendation is more conservative (more money in reserves) than the board's. Regardless, the funding philosophy that the professional and board present should be unified. To do otherwise invites challenge from members who are looking for a way to reduce their HOA costs.

There are three types of Funding Plans typically considered. Each offers a different level of financial risk.

1. Baseline Funding has a goal of keeping the reserve cash balance above zero over the period of the reserve study (usually 30 years). This is the riskiest method since future costs are unpredictable due to material and labor costs which can swing radically from year to year. Guess wrong and there could not enough money to pay for a critical and urgent repair.

2. Threshold Funding has a goal of keeping the reserve fund balance above a specified dollar or percent funded amount over the period of the reserve study (like \$50,000 or 50% of Full Funding). Threshold funding could be any level that the board determines it should be above Baseline (0%). While 50% funded (or whatever level the board sets above 0%) is safer than 0%, anything less than Full Funding exposes the HOA members to greater risk of a shortfall. The greater the gap between Full and Threshold Funding, the greater the risk.

3. Full Funding has a funding goal of attaining and maintaining reserve funds at or near 100% funded over the period

of the reserve study and is the least risky approach. A simple example of 100% funded: If a component has a 10 year useful life and current replacement cost is \$10,000, then \$1000 per year would be set aside to be 100% funded (\$1000 in Year One, \$2000 in Year Two, etc.) When a current inflation factor is added, the number of total dollars needed will be adjusted each year according inflation so that the funds will be there when needed. Full Funding also has the express goal of getting all members along the 30 year timeline to contribute their fair share of the total cost. This is important for the board to fulfill its fiduciary duty to current and future members.

Most funding plans are "Cash Flow" models where relatively level annual reserve contributions are designed to offset highly variable annual reserve expenditures (for example, \$10,000 one year and \$100,000 the next). Annual contributions must accumulate enough funds to pay for high expense years.

Another wrinkle in reserve funding...FHA underwrites the majority of condominium mortgage loans. It requires that a minimum of 10% of the annual budget be set aside into reserves. While the average condominium project should put an average of 25-35% of its annual budget into reserves to be fully funded, FHA has put a minimum standard in place for those condominium projects that are not reserving properly or at all. Those condominium projects that fail to comply with the 10% reserve minimum lose access to FHA loans. Not having access to FHA financing directly affects a condo's market value.

As more homeowner association implement and fund reserves adequately, it puts pressure on those that are not to stay competitive. The informed buyer now considers reserve funding in the buying decision. If faced with comparable properties, one highly reserved and the other lowly reserved,

which would be the safer investment? In the final analysis, following an adequately funded reserve plan simply makes sense.

By *Richard L. Thompson* - www.Regensis.net **APRA**

APRA Symposium April 20-21, 2013 San Diego California

Each year, the **Association of Professional Reserve Analysts** hosts a Symposium for reserve study professionals to brainstorm, debate and receive cutting edge education. APRA members receive special discounts and those holding the industry's most prestigious credential **Professional Reserve Analysts (PRA)** earn continuing education credits. The future is bright for the reserve study industry. Won't you join us? For a brochure and registration form, see www.apra-usa.com

The Great Siding Debate

The purpose of a reserve study is to schedule and fund common component repairs and replacements. Following the study recommendations will help minimize or avoid special assessments. Siding systems, whether stucco, wood composite, cementitious, wood or vinyl, are often left out of the reserve study's typical 30 year projection period because they are assumed to have a 40-50 year useful life. Unfortunately, many aging HOAs are now being faced with replacing siding without the reserve funds to do so. The result is a significant special assessment.

Siding manufacturers have come a long way in products and warranties which afford some assurance of protection. However, there are many factors that affect the performance and useful life of siding systems. Homeowner associations should be aware of the potential challenges of each.

Stucco comes in several varieties:

1. Exterior Insulation & Finishing

System (EIFS). This stucco adaptation is installed over a thick foam board. Over the past three decades, it has experienced widespread water intrusion and dryrot problems, some leading to structural failure. The EIFS foam barrier provides ideal conditions for dryrot to grow (moisture, cool temperatures, darkness) and accelerate over a short period of time. If your buildings have it, removing and replacing it with traditional stucco (no foam barrier) or another siding alternative is recommended, the sooner the better.

2. **Traditional Stucco** is applied over cement block, stone or a cement board. When properly installed, it needs cleaning (power washing) plus crack and caulking repairs every 5-10 years to remain serviceable. It has been in use successfully for hundreds of years. The key is keeping it watertight.

Wood Composite Siding. This kind of siding was very popular in the 1970s and 80s and is made of wood sawdust and glue compressed into panels or siding boards to mimic wood. It was marketed by a number of companies including Louisiana Pacific (LP), Georgia Pacific (GP) and Masonite. Unfortunately, it had a tendency to delaminate under wet conditions and absorb water like a sponge. This tendency fostered dryrot in the siding and structure. Due to wide spread failure, much of it was removed and replaced in the 1990s. If your buildings have it, make sure to aggressively maintain the caulking and paint to protect it from rain water damage. This is particular important on the caulked and drip edges of the siding where, left unprotected, water will wick up into the siding. When it comes to repair or replacement, to achieve a similar look, use a cementitious siding.

Cementitious Siding. This siding is made mostly of cement with sawdust and glue as binders. It has a number of advantages including being water resistant, pest proof and fire resistant. It comes in many styles including panels, board and shakes. It typically carries a long warranty (50 years). When installed properly, it requires caulking and painting every 8-12 years.

Wood Siding comes in a variety of wood types, designs and qualities.

Common types include cedar, redwood and spruce. Cheaper quality wood siding may be thinner, have knotholes and a greater tendency to warp, cup and split. High quality wood siding can last many decades when properly installed maintained. It is important that deteriorated sections be replaced prior to any staining, painting or waterproofing project. This is particularly important for siding that has greater exposure to wind, rain and salt air.

Wood Shakes/Shingles have a wonderful warm look but require intensive maintenance when used as siding. Only use the highest quality material available for installations and repairs. Because of high maintenance costs, it is advisable to use them only as a decorative siding feature, like the gable end roof area of a building rather than as a full siding application.

Vinyl Siding requires periodic repair and cleaning (power washing). As the buildings age, the siding will fail due to missing flashing, fasteners or warping. While vinyl siding can seem cost effective since it requires no paint, you are stuck with whatever color vinyl is selected for decades and darker colors fade in the short term. It also fails to keep the structure water tight in areas subject to wind driven rain.

New Siding Designs. Some architects love to try new (read "unproven") siding or building envelope applications. While these might be fine in a Class A Office Building that is maintained by trained building facility maintenance staff, it is not recommended for the average homeowner association that does not have this kind of expertise.

If your HOA has an old or failing siding system, it's time to include a siding replacement component in your reserve study. There are contractors in your area that specialize in siding replacement. Be very careful to choose only those that have many references. This kind of work can easily run \$10,000/per unit and up. For most homeowner associations, easy maintenance and long life should figure prominently in the siding selection.

By *Richard L. Thompson* - www.Regensis.net **APRA**

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Reserve Funds Investment Policy

Investing reserve funds prudently produces enormous fruit for a homeowner association. Invested reserves can produce tens or hundreds of thousands of dollars over a 30 year period. Interest earnings reduce the amount of contributions required of the HOA members. So, it behooves the board to establish and closely monitor a good reserve fund investment policy. Here is a sample which can be adapted to your use:

Nottacare Condominium

Reserves Investment Policy

We, the board of directors of [name of homeowner association], a corporation organized under the [applicable state statute] do approve the following policy:

WHEREAS the board of directors desires to manage reserve funds as good stewards, BE IT RESOLVED THAT the following reserve funds investment policy be adopted:

Goals & Objectives. Reserve funds shall be invested to achieve the these objectives:

- No loss of principal
- Adequate liquid funds available for reserve needs
- Achieve highest long-term investment performance

Investment Strategy:

A. Base Liquid Funds. On an annual basis, the board will review the reserve

schedule for the upcoming year to determine anticipated funds required for expected expenditures plus a 20% cushion. This amount constitutes the "Base Liquid Funds".

B. Non-Liquid Funds. Funds over and above the Base Liquid Funds will be invested as follows:

Laddering Strategy. Invest in federally insured securities that have maturities of three months or more. If funds permit, buy securities with varying maturity dates (laddering) rather than invest a lump sum in one security with one maturity date. Laddering allows securities to mature at various times so some funds come available periodically without invoking early termination penalties. If interest yields are relatively low, board will invest for shorter terms with the anticipation that rates will rise in coming months. If rates are relatively high, board will invest for longer terms to take advantage of the higher yield.

New Funds. Liquid portion of the reserves grow from interest earnings as well as from reserve contributions and become investable if they are in excess of the Base Liquid Funds. These funds can be combined with proceeds from laddered securities as they mature or purchase new laddered securities.

Approved FDIC Investment Classes

- Savings accounts
- Money market accounts
- Certificates of deposit in FDIC-insured financial institutions with no more than \$250,000 in any one institution, unless additional private deposit insurance is provided by the bank.
- Treasury bills, notes or bonds.

Review & Control. All investments will be purchased in the name of the homeowner association.

The signatures of the President and Treasurer are required for withdrawals or transfers of reserve funds.

The board will review regular financial statements and make adjustments as needed to ensure Goals & Objectives are being met.

Recorded in the Book of Minutes on

[Date]

President - Board of Directors

Attested to by:

Secretary - Board of Directors **APRA**

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Board in Denial

The board of Nottacare Condominium has just convened to discuss a painful but avoidable issue, a special assessment. The roof is five years overdue for replacement and many of the temporary patches have failed, drenching four different units repeatedly. Mary in 1A has made many desperate appeals that something be done and Bob in 4B peppers his demands with four letter Anglo-Saxonisms. Two owners are talking to their lawyers. There is a smell of tar in the air. And as bad as it is for these residents, the cure will be painful for one and all.

Nottacare's situation is not unlike that at many HOAs across the country. Nottacare's failed roof is what accountants call "an unfunded liability". A liability is a debt or obligation, in this case, the obligation is to replace a roof. Unfunded means there is no money to fulfill that obligation. Do the math: UL + \$0 = MSA. (Unfunded Liabilities + No Dough = More Special

A reserve study is a fundamental planning tool that every homeowner association needs to function properly.

APRA members carry the Professional Reserve Analyst (PRA)[™] credential which requires extensive education, years of experience and client references.

APRA members provide high quality reserve study service throughout the United States, Canada and Australia.

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Assessments) Caramba!

Most HOA boards trip merrily along seemingly oblivious that all things wear out, ignoring the high costs of imminent repairs, failing to prepare for those events and clueless how to overcome being clueless. Denial is not a river in Africa. It's a deadly mindset that not only leads to erosion of HOA assets and home values but also creates a pervasive mistrust, hostility and resentment within the community. So at Nottacare Condos, some are wailing "Raindrops Are Falling on My Head" and all are steamed because here comes another unwelcome and unfair special assessment!

Okay, you get the picture and it ain't pretty. But the good news is that Nottacare is a mythical place and your HOA is real and the board fully prepared to meet these challenges. What's that you say? You just had a special assessment or the board's talking one up as we speak? Holy guacamole! Don't they know that special assessments are the product of poor planning? Don't they know they penalize innocent victims (the current owners) that are forced to pay for former owners who bailed out before the ax fell? Don't they know a properly

funded reserve study could have avoided all of this and made them heroes instead of zeros?

A reserve study is a scientific approach to analyzing future repair and replacement needs and charting a maintenance and funding plan that the board, the manager and members at large can follow with ease. It answers the bottom line question "How much is enough?" The funding plan shares costs fairly among all owners, not just the poor suckers who get stuck at special assessment time. And with money in the bank, the board will never have the excuse of not doing things when they need doing. No more Raindrop Water Torture. The place will look so good, you'll never want to move!

Denial is a dangerous place to be. There is lots of turbulent water and crocodiles waiting to munch the board in denial. Before you round the bend and meet face to face with avoidable catastrophe, investigate the benefits of a reserve study.

By *Richard L. Thompson* -
www.Regensis.net **APRA**

It's Spring! Checklist

Finally! The sun is shining and plants are beginning to poke their heads out of the ground. But before getting mesmerized by Spring Fever, do a quick "walk about" for post winter grounds and building maintenance:

Buildings. Look for sagging gutters, loose/missing siding, deteriorating concrete or brickwork, missing roof shingles or water damage.

Landscaping. Clean up fallen branches and leaves. Use a mulching mower to spread clippings evenly over the lawn and fertilize naturally. Loosen the soil around perennials; plant annuals or a vegetable garden. Prune shrubs and trees; repair sprinkler system.

Patch & Paint. Repair siding; Paint as necessary.

Windows. Wash and repair caulking.

Check Vents. Make sure all exhaust fans and are clean and remove lint buildup from clothes dryer vents.

Repair Wood Decks. Replace loose nails with galvanized deck screws. Replace broken boards or rails. Use a pressure washer to clean dirt and mildew from the wood, then apply an all-weather sealer or stain.

Repair Fences. Repair/replace broken/missing fence boards and seal them as needed.

Prepare for Pool Opening. Purchase pool chemicals. Schedule and perform cleaning. Clean pool furniture.

Clubhouse Cleaning. Wash heat registers. Clean window treatments. Clean carpeting and bathrooms. Wax floors. Polish woodwork.

Hopefully all you have to do is identify the work and assign it, not actually do it. But put these things in motion so your HOA can hit the ground running. May Day! May Day! It's Spring!

By *Richard L. Thompson* -
www.Regensis.net **APRA**

In the Gutter

Rain gutters are an inconspicuous but necessary building component that homeowner associations deal with. Their need to perform consistently triggers ongoing maintenance and repair to themselves, exterior paint, siding, roofs and trees. Failure to keep the gutter system running smoothly causes overflows, water intrusion, interior damage, structural dryrot and enormously expensive repairs. There is a lot riding on this often ignored building component.

Until the late 19th century, virtually all rain gutters were made of wood. With the advent of metal roll forming machines around 1900, the ability to create metal gutters became possible. The roll forming process shapes long coils of flat metal into long, formed sections of gutters in a variety of designs. Up until the 1970s, most rain gutter was produced on stationary roll forming machines weighing up to several tons. Then, lighter portable roll formers on trailers became available. With portable roll formers, contractors measure and form gutters onsite.

The three most common metal gutter systems are made of aluminum, steel and copper. The first two have the advantage of being custom painted while copper (unless properly clear coated) will weather and change color over time. All metal gutter options have a 20+ year life or more as long as they are not damaged. Aluminum is the lightest weight metal option and most easily damaged. Downspouts should be located away from areas where damaging forces are likely (vehicle, pedestrian, etc.) or properly protected with landscaping or posts that prevent contact.

One of the most important functions of rain gutters is to prevent foundation movement due to water. Once rainwater has made it to downspouts, the downspouts need to direct the water away from the foundation, either in subterranean rain drains which lead to a french drain (a cistern like system that allows the water to be gradually reabsorbed into surrounding soil), run off to an above ground ponding facility that also allows gradual absorption into the soil or connection to a grid of storm water drains that carry to water back to streams and rivers. Some states and

jurisdictions have restricted hard surface (roof, street, parking lot) storm water run-off to onsite collection facilities to avoid contamination of streams and rivers.

Splash blocks are a low tech alternative that move water away from the foundation. A splash block is a rectangular wedge about a foot wide and two feet long that is placed under the downspout outlet. Rainwater hits the block and is diverted away from the building and works well as long as there is positive drainage. However, in areas with high volumes of rain, splash block drainage may create additional problems with boggy areas in the landscaping or flooding downstream neighbors. In these areas, more sophisticated drainage systems are in order.

An ongoing maintenance issue with gutters is the accumulation of tree and roof debris that block or slow water drainage. This is particularly burdensome in areas of heavy deciduous tree cover. In those areas, ongoing tree pruning and selected tree removal is necessary to reduce the problem and related costs. Gutters typically should be cleaned at least twice a year. Heavy tree cover will trigger "hotspots" where more frequent cleaning is necessary. The HOA should identify these hotspots and do regular preventive maintenance to minimize damage caused by overflows.

Airborne dirt and roofing granules wash into the gutters and accumulate in gutters and create a hindrance to water flow. Removal of this sludge requires hand work by scooping, flushing with high pressure water hose or blowing out with a leaf blower. The last two can be create additional mess to the landscaping, walkways and building but are quicker and cheaper to accomplish.

There are quite a few options for gutter covers that claim to eliminate the need for gutter cleaning. They come in many different designs and price points and do reduce the need and frequency of cleaning but none can prevent the accumulation of sludge that finds its way passed even the best gutter cover systems. Since these systems are expensive, part of the selection criteria should be ease of removing the sludge.

Gutters and downspouts are a wonderful piece of engineering when properly installed and maintained. While "in the gutter" is a description for someone that is "down and out", rain gutters are indispensable for getting rainwater down and out to where it does no damage. **APRA**

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10 Rules of Life

1. Never give yourself a haircut after three alcoholic beverages.
2. Always have WD-40 and duct tape on hand. If it doesn't move and should, use WD-40. If it moves and shouldn't, use the tape.
3. The five most essential words for a healthy relationship are "I apologize" and "You're right".
4. Everyone seems normal until you get to know them.
5. When you make a mistake, make amends immediately. It's easier to eat crow while it's still warm.
6. If someone says that you are too good for them...believe them.
7. Learn to pick your battles. Ask yourself, Will this matter a year from now? A month? A week? A day?
8. If you woke up today, congratulations! You have one more chance to get it right!
9. Being miserable because of a bad relationship just might mean that the other person was right about you.
10. Work is good, but it's not really that important. **APRA**