Special Assessments

Special assessments...Are they really special or are they a huge supplement to underfunded reserves or a poorly developed budget?

Special assessments have become a daily occurrence in our office recently. With so many communities in so many places, it is understandable that even if an assessment were vitally necessary, the number of them would be fairly high. But so many of these assessments would easily be avoidable if the budgets were adequate and the reserves were adequately funded.

What has become concerning is what these assessments are going to be used for and why. As a long time practitioner in this industry, it has been drilled into me that if a community has common areas that contain roads, gates, irrigation, entry features, perimeter enclosures, sidewalks, storm drains, retention/detention ponds, pools, cabanas, clubhouses, meeting rooms, pavilions, bridges, street lights or other items that have a specific useful life, that will ultimately require replacement at great cost, then the estimated useful life of the component should use as a guide for determining how much should be put away every year to replace that item when it's useful life has expired. Reserves should be, and in many cases in many states, are mandatory. If they are not mandatory, then the Board has a duty to at least address the future costs that will inevitably be incurred by the membership. The only fair way to levy the cost of the replacement of a capital component, is for everyone to pay their share while they are using it. Many communities embrace the "green banana syndrome". "They don't buy green bananas, because they may not be around to eat them when they ripen", so why should they pay for something they may not be there to use when it comes time to replace it? Most often, this is for long term items such as roofs (obviously necessary), roads, elevators, clubhouses, pools that are very costly to replace. Using straight line depreciation, a $50,000 dollar item with a 20 year useful life in a community of 100 owners = $2.08 per month per unit added to the budget. I think I'd much rather pay this $2.08 than a $500 special assessment at one time.

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Special assessments affect associations in many ways. For instance, if you're a condominium owner, the ability of a new owner to obtain financing may be incumbent upon the fact that your association has planned well and your community has Reserves for specific components. That dreaded "Condo Questionnaire" that many of us have experienced asks the following about special assessments:

•What is the purpose of the Assessment?

•Does the assessment affect the marketability of any of the units?

•Have other special assessments been required (if the answer is yes, a complete explanation regarding the purpose and timing of those assessments must be provided)

•When is the assessment to be paid (i.e. required to be pre-paid or is it payable over a specified period of time?)

•How is the overall financial stability of the project impacted by the assessment?

•What impact will the assessment have on the future value and marketability of the property?

In addition to the tough questions above, lenders often look at special assessments closely to see if they are being used for things that should be an operational or basic maintenance expense that should be funded by the operational budget. Generally, if an assessment is needed to make up a small shortfall, or to improve the property by adding an amenity or updating an existing amenity, it won't be considered detrimental. However, if it is being used to pay regular bills, or make up deficits due to a budget that is inadequate for the property's requirements in order to keep the assessment artificially low, this would be considered a detriment and an impairment to obtaining a loan for the property.

The reason "special assessments" are called "special" is they should not be anticipated to take the place of adequate assessments to maintain the common areas or common elements. Generally, a special assessment is for the purpose of augmenting shortfall in Reserves, for a component that requires replacement now; for a capital improvement that increases the value of the property; or an emergency that requires funds to begin major repairs after an unusual event, i.e. tornado, hurricane, flood, earthquake. Sometimes, a special assessment is levied to make up shortfall or deficit in the prior year's budget either as a result of unanticipated extraordinary expenses, uncollected assessments or sometimes just poor planning and an unwillingness to address rising maintenance costs of an aging infrastructure.

Special assessments are generally required for a project with a specified project completion time. I am aware of a community (shall remain nameless) that passed a $144.00 special assessment that was payable over a period of 5 years at $2.40 per unit per month... Seriously? The costs associated with a long term special assessment like this outweigh the benefits of the income and obviously the need for the funds was not immediate or a life and death matter that it could not have been added in to the normal operating budget.

A special assessment requires planning. It may take weeks or some months to go through planning for the project for which the funds will be needed. Obtaining bids, assessing current available capital, planning out the physical impacts of the project on the community, how long it will take, planning for change orders or cost overruns, adding in a reasonable cushion to cover unknowns and of course, for those owners who may not pay timely or may not pay at all. If the assessment will be payable in a one-time payment or, if there will be installments. Your manager will play an integral role with you in this planning. So, now it's taken awhile for the board to finalize the decision about the fact that a special assessment is the way to go, there's still some more planning to be done, how to communicate this to the owners.

Obviously, consulting your documents will be high on the list of priorities. Checking to see if the Board has the ability to even levy a special assessment, if

they have the ability to approve the special and what requirements there are for notification to the members, both before and after. In most cases, a meeting is required. In many states, notice to the owners providing the day, date, time and place of the meeting and as one or maybe even the only item on the agenda is the adoption of a special assessment. If the members are required to approve, you'll need to know how many affirmative votes of the membership it will take to approve the assessment. You'll need to be prepared to lay out the details for the membership: what the project is; the process the board has gone through to obtain bids; interview contractors; the physical impact on the community; how long it will take, and of course the anticipated result.

So now, before we go to the meeting, let's discuss the process of adopting a Resolution to set out the parameters of the Special Assessment and some options for payment. This is a very real issue to consider because it will ultimately affect the income from the special to the Association.