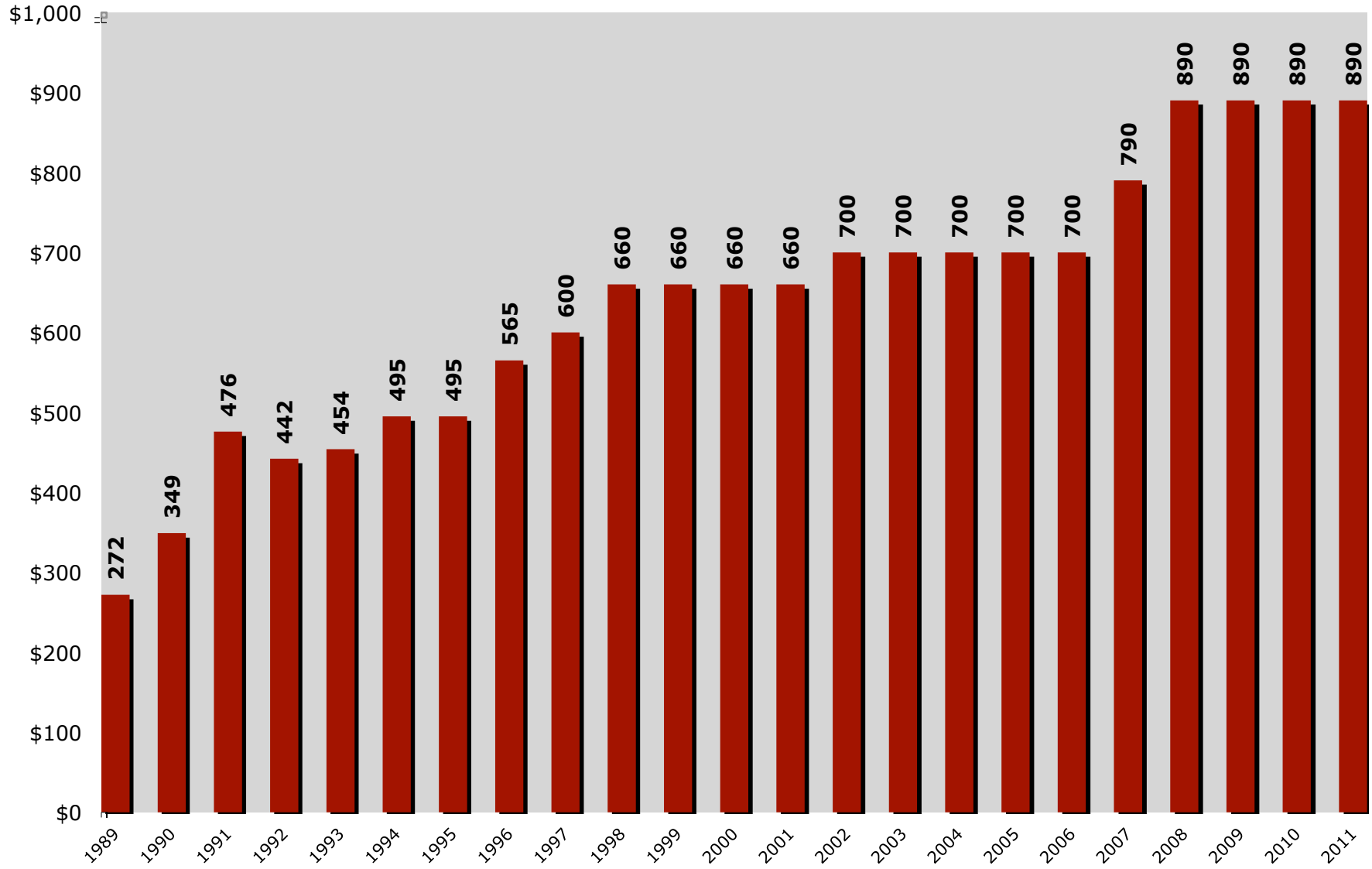


## Fleetwood Quarterly Assessment History



Please read prior  
to the next Open  
Board/Officer  
meeting on  
Wednesday,  
June 15, 2011

By Marvin J. Nodiff, Esq.

# Avoiding the Special Assessment

# TRAP



BORGE



MANY COMMUNITY associations turn to special assessments when confronted by unanticipated repairs, but boards need to avoid making hasty decisions to fund these surprise expenses.

Special assessments should be the last resort—not the first step—in funding an expensive repair; they're unwelcome surprises and can cause financial hardship. Moreover, they are inherently inequitable because they fall on the people who happen to own at the time payment is due, without regard to length of ownership—a measure of how much an owner “consumed” the component being repaired. Given these dynamics, it should not be surprising that some owners will search every nook and cranny of a special assessment decision and may emerge with troublesome defenses.

Owners may dispute a special assessment for many underlying reasons. The challenges come from the disgruntled owner who simply doesn't like the board or from the guy who disputes the wisdom of the project, timing, cost or the specifications.

The owner's personal agenda doesn't matter because he refuses to pay, but he will not stop there; misery loves company. He will organize his neighbors, start a petition, appear at your next board meeting with a circle of supporters and wag his finger or wave his fist in your face.

Worse, he will encourage others not to pay. Then the board may realize it doesn't have enough support for the project. Further, the board may be faced with difficult collection actions, lawsuits that cost money and create tension, and may need to delay the very work that the special assessment was intended to cover.

#### LITIGATION LEADER

In the experience of my law firm in collection work for community associations, special assessments are one of the leading sources of litigation.

Just when you think you have done everything correctly, you may find yourself embroiled in a legal dispute. There will be a clever attorney on the other side, skillfully probing every step in your decision-making process. Believing his

## The adverse impacts of financial surprise and inequity are often too much to OVERCOME.

claim has great merit, he will cloud the issues with distracting defenses, bury you under an avalanche of paper discovery, file an endless stream of meddlesome motions and posture for his client who sits by his side cheering him into battle. It won't be fun.

Often the dispute is about more than just money. Here are some examples:

**Case Note #1.** A condominium association of 108 units in St. Louis County, Mo., levied a special assessment to replace the roofs on all the buildings. One owner, whose share was \$1,700, refused to pay. Initially, he contended that his roof didn't leak, but at trial he argued that the special assessment was unauthorized because the board was not properly elected since the annual meeting lacked a quorum. There was no dispute that the meeting did not have a quorum, but the board contacted owners afterward and obtained enough proxies. The court of appeals upheld the special assessment, reasoning that the governing documents did not prohibit the practice of obtaining quorum by collecting additional proxies after the meeting, and the practice was in keeping with the spirit of the documents that a significant portion of the membership participate in elections. —*Braeshire Board of Managers v. Brinkmeyer*, 841 S.W.2d 217 (Mo. App. E.D. 1992).

**Case Note #2.** A condominium association in Franklin County, Ohio, levied a special assessment averaging \$1,000 per unit to repair carport roofs and repave roads. An owner contend-

ed that state law prohibited a lump-sum special assessment for improvements. The court of appeals ruled in favor of the association. Although state law obligates the association to budget sufficient reserves so it does not have to levy a special assessment, the statute does not preclude an association from doing so if, despite careful budgeting, a special assessment becomes necessary. The court also held the purpose was for repairs, not “improvements.” —*Olentangy Condominium Association v. Lusk*, 2010 Ohio App., Tenth Appellate District, LEXIS 851 (March 16, 2010).

**Case Note #3.** An urban homeowners association of 400 homes in St. Louis, near the site of the 1904 World's Fair, was situated across the street from a late-night watering hole that featured a menu of muggings and assaults. The homeowners wanted to retain a private security patrol, but the ancient governing documents contained a cap on assessments of only 50 cents per front foot, which was clearly inadequate. The board, with the owners voting 188 to 5, levied a special assessment of \$50 per lot. Several owners filed suit, contending the assessment was unauthorized. The court of appeals applied equitable principles, finding that the private security patrol was in the best interests of the community as a whole, was paid by a substantial majority of the owners, and that a few should not get a “free ride” at the expense of all the other owners. —*Colvin v. Carr*, 799 S.W.2d 153 (Mo. App. E.D. 1990).

These cases demonstrate how easily the best-intended special assessment can spawn serious litigation. Going to court has many downsides: It can be expensive and aggravating, and it can tear the fabric of your community. The results are uncertain at best.

#### THE NEED FOR A PLAN

Hopefully, a special assessment never will be necessary. If a board plans properly and builds up its reserves, it may not be.

Unfortunately, some boards want to keep general assessments low, believing that owners consider only the monthly



fee when determining how much they pay the association. This is fiction; you can't play hide-the-ball with a history of special assessments.

The association needs to engage in strategic planning to avoid the necessity of a special assessment; the adverse impacts of financial surprise and inequity are often too much to overcome. Many managers are particularly good at initiating strategic planning because of their professional knowledge and experience, but even self-managed communities can map out a well-developed plan.

Strategic planning calls for an objective look into the future to minimize surprise. What components and systems will need major repair or replacement in the future? How much will they cost? How will these needs be funded?

The board is responsible for preparing the annual budget, including reserves. When asked how they determine reserves, some of my boards say they have been to Disney World, using the Magic Kingdom Formula of 5 percent. Others simply contribute "whatever is left at the end of the year." Both approaches are arbitrary and subjective.

Many state laws and governing documents call for reasonable reserves for repair and replacement. The key word is "reasonable." Since every community is different in terms of construction, quality of materials, level of maintenance, climate and other factors, each must be examined on its own.

The basis for determining what's reasonable for your particular community should be a reserve study by an independent expert—one who does not stand to obtain the repair work, who has professional qualifications in this field and is designated by CAI as a Reserve Specialist (RS). Couple the study with an energy audit to buffer rising energy costs.

If your association does not have a financial plan for reserves, is this a failure to plan or a plan to fail? And what if the association has some reserves, but they are either inadequate or the board doesn't want to spend the entire fund on one project? If that happens, the next best approach is to borrow funds



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from an institutional lender, using an assignment of assessments as collateral. Many lenders now offer such loans for community associations.

Borrowing has many of the equitable features of reserves because the debt service is paid in modest amounts over a period of years. The obligation transfers from one owner to the next as sales occur, thus spreading the costs and benefits in the same manner as reserves.

Of equal importance is that the association would have all the funds up front to complete the project, and would be able to enter into contracts without worrying about whether all owners will pay a special assessment in full, on time and without the delay and cost of chasing delinquent owners.

Without a financial plan, how do you know where your community is going? John Irving wrote in *Hotel New Hampshire*, "If you don't know where you're going, you don't belong where you are." **The challenge for associations—volunteer leaders, homeowners and managers—is to find out where they're going by engaging in strategic planning, starting with an objective reserve study and an energy audit, followed by setting a realistic level of funding. This is the best way to minimize the need for a special assessment.**

If your condominium association doesn't have a financial plan, it also may fall out of favor with the Federal Housing Administration. The agency frowns on special assessments, and it requires that the budget contain a line item of at least 10 percent for reserves. Since Feb. 1, 2010, condominium associations need to get on FHA's approved project list before it supports any mortgages in the communities. Failure to be on FHA's approved project list will discourage real estate listings, leading to reduced marketability and resale values.

#### DUE DILIGENCE

Sometimes, not even fully funded reserves can prevent a special assessment. When it's unavoidable, the board must exercise due diligence before imposing the additional fee. Due diligence can be

## Strategic planning calls for an objective look into the future to minimize SURPRISE.

tedious and time consuming. To cover everything, use the following 10-point checklist and document each step:

1. Ask your attorney to review your plans, applicable statutes and governing documents. Get suggestions for improving them to foster success.
2. Follow all applicable procedures in the governing documents for approving the budget.
3. Make sure you have a full board that is properly elected.
4. Be sure all voters are qualified.
5. Make sure you comply with provisions in statutes and governing documents for adopting a special assessment. Some states have special approval procedures. Virginia, for example, authorizes members to rescind or reduce a proposed special assessment by majority vote at a meeting.
6. Be diligent in identifying and evaluating options. Prepare a comparative analysis. Be objective. For example, if you are replacing the siding because it would cost less than continued repairs, collect reliable data to support this finding.
7. Keep the owners informed throughout the process. Remember your obligation to disclose information about the special assessment on resale certificates. Better to include it, even if it is merely under consideration, than to surprise a new owner.
8. Use competitive bidding to find the lowest and best proposal. Three are usually enough; any more will just drive you and your manager nuts. In selecting a contractor, remember lowest cost is

not always best value. Many of us have learned the hard way that the lowest bidder is usually lowest in quality and reliability, but highest in terms of contract management.

9. Make sure the components and systems to be repaired or replaced are within the association's authority. For example, if you want to replace all the windows in the condominium, make sure the windows are common elements, not part of the units.

10. Get an opinion letter from your attorney to make sure that you have satisfied all substantive and procedural requirements of your state statute and governing documents.

The old carpenter's adage, "measure twice, cut once" is good advice for board members because it's essentially encouraging due diligence. If successfully accomplished, the tasks on your checklist will not only create the foundation for a successful project, but also will minimize the possibility of litigation by contrarian homeowners.

After your due diligence is complete, engage the owners in the process. Avoid top-down implementation or the appearance that the project is entirely driven by the board. Appoint a committee of homeowners to take ownership of the project and be responsible for presenting it to the members. Even if you do everything properly, you will not succeed without broad owner support and acceptance.

**Indeed, there is nothing special about special assessments.** They present lots of moving parts and traps for the unwary. They can lead to litigation involving issues far more complex than the problems they are intended to resolve. **The better approach is to build reserves based on an objective reserve study and to augment funding through a loan.** If you have absolutely no alternative to a special assessment, exercise due diligence in your preparation. And remember that old carpenter's adage. **cg**

MARVIN J. NODIFF practices law in St. Louis, is a charter member of CAI's College of Community Association Lawyers and is the author of *Special Assessment*, a novel.