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October 22, 2024

Dear Residents,

As your Board President, it brings me great pleasure to announce the completion of our community's first comprehensive reserve study. This significant milestone is a testament to our collective commitment to the long-term financial health and sustainability of our condominium.

A special thank you to Larry Smith and Alan Cohn for their hard work and dedication in getting the reserve study done.

The reserve study serves as a critical tool, allowing us to plan for future repairs and replacements of the common elements within our community. Its completion provides us with a detailed road map to ensure that our physical assets are maintained appropriately and that we are financially prepared for any unexpected expenses.

Through this study, we've gained invaluable insights into the projected costs associated with the upkeep of our shared spaces and infrastructure over the next several years. This foresight empowers us to make informed decisions regarding our reserve fund - ensuring that it is adequately funded to meet our future needs without imposing unnecessary financial burdens on our residents.

I want to extend my gratitude to every member of our community for your patience and support throughout this process. It is your cooperation and understanding that have made this achievement possible. Rest assured, the Board is dedicated to acting on the findings of the reserve study, prioritizing projects that are essential to our community's well-being and property values.

In the coming weeks, the Board will be organizing a series of meetings to start our budget process for 2025.

Remember that the study is a roadmap and at times we may have to adjust things along the way due to budgetary constraints and emergency situations that may arise. Please read article regarding reserve funds

Thank you for your continued trust and support. We are excited about the opportunities this reserve study presents us, and we look forward to working with all of you to bring these plans to fruition.

Warm regards,

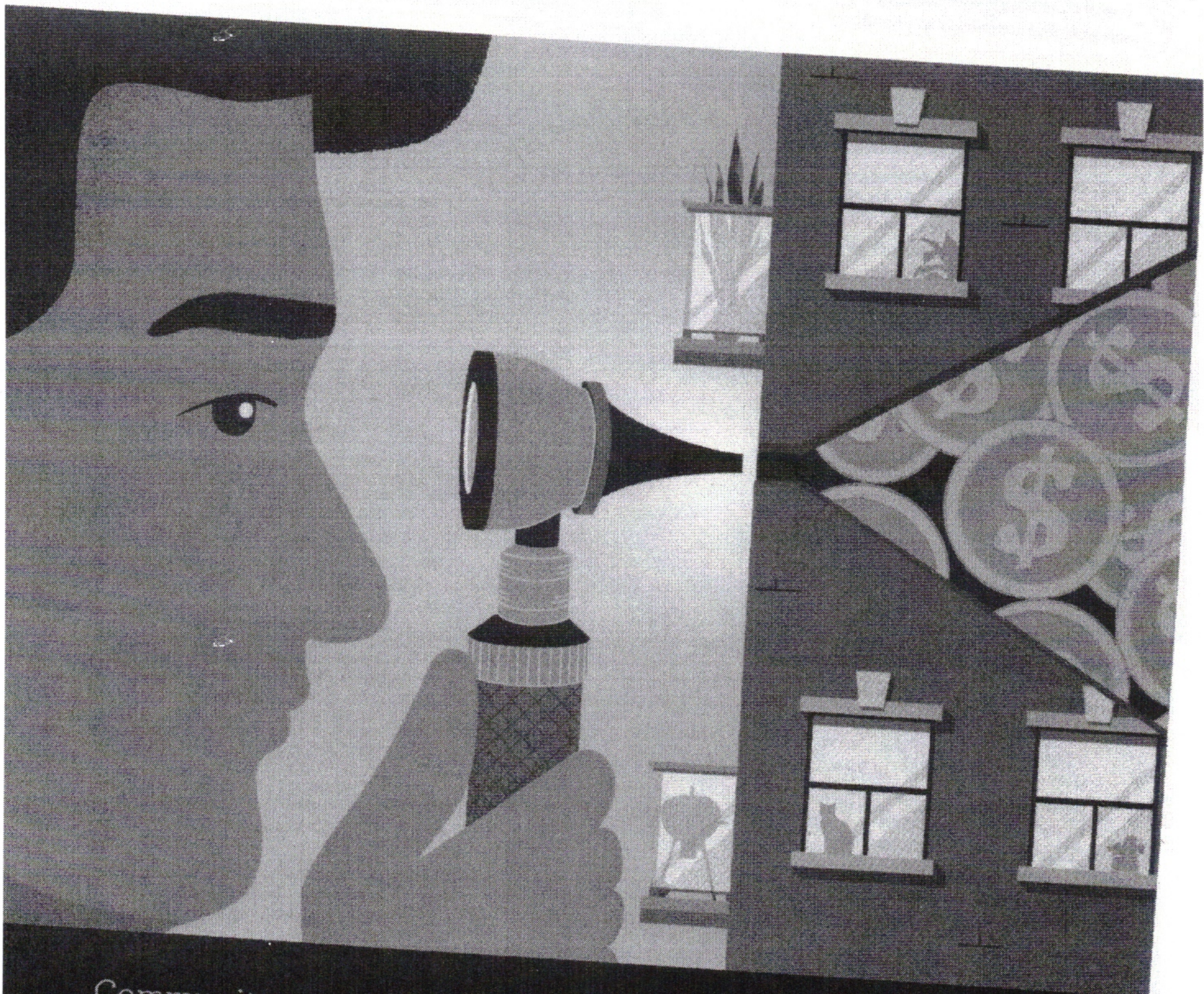
Gina Interdonato

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President, Towne House Apartments at Lido Beach

RESERVES RX

By Michelle Baldry, RS



Community associations need to be on top of current trends and best practices in reserve studies and capital planning in the wake of Surfside and soaring insurance costs. Doctor's orders.

Illustrations by Mike Ellis

AS HUMANS AGE, doctors monitor the wear and tear on our bodies and intervene if necessary. From simple routine checks and scans to more complex issues, we take healthcare seriously and act quickly to prevent potential issues from compounding.

Why should we treat aging communities any differently?

According to the Foundation for Community Association Research's report, *Breaking Point: Examining Aging Infrastructures in Community Associations*, over 80% of communities report encountering unanticipated infrastructure issues over a three-year period. Released two years before the Surfside tragedy, the report also shows that 40% of communities listed deteriorating infrastructure as a top-ranked concern.

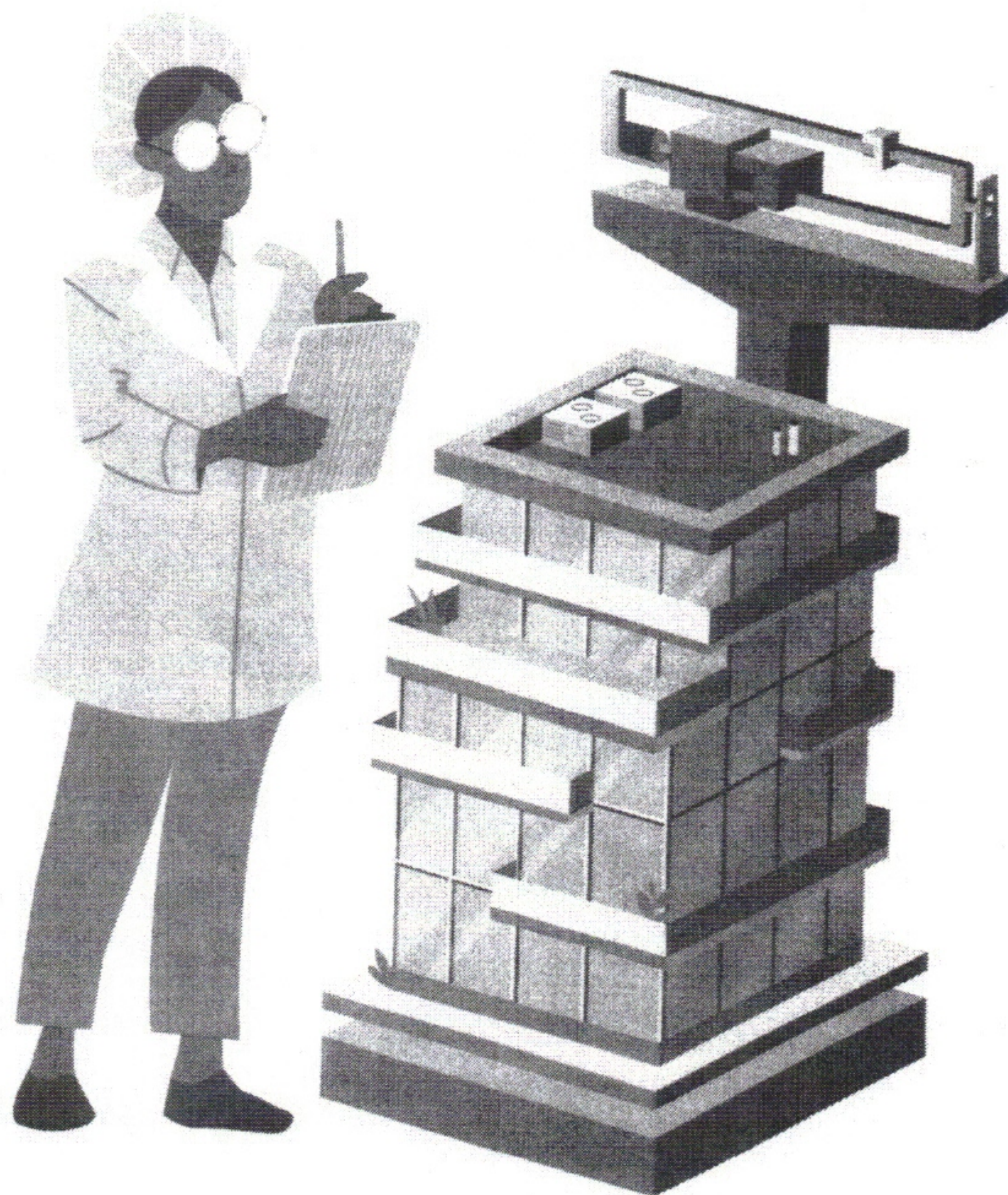
Recent events highlight the urgent need for proactive financial planning and investment in maintenance to ensure the longevity and safety of communities. Without proper maintenance, associations risk costly emergencies and a decline in property values. With the focus on aging communities intensifying, one thing is certain: These issues typically can be anticipated. That's where reserve studies come in.

"Reserve studies are living documents that are always changing and evolving," says Clint Atherton, LSM, PCAM, general manager at Sun City Palm Desert Community Association in Palm Desert, Calif. "Communities need to keep on top of them and update (studies) in real time. It's essentially your master plan."

Because reserve studies reflect an individual community's obligations and intentions, transparency and communication are essential components. Communities need to be proactive, educate homeowners about reserve studies, and give them opportunities to ask questions and discuss options, says Atherton, chair of the reserves task force for the CAI California Legislative Action Committee.

Reserve studies comprise multiple parts — a physical inspection of the association's common property, a financial analysis of its current reserve fund status, and creation of a long-term

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capital plan. If associations adhere to their reserve study's recommendations, they will be able to address any physical areas of concern and have adequate funding to complete projects on time and avoid deferring maintenance.

"A good reserve study is an understanding of what you own and where the money is going, clarity on what the future looks like, and peace of mind that you have a strategy to get there," says Damian Esparza, founder of Smart Property, a company offering a software platform to help community associations manage reserve studies data in San Diego.

Esparza encourages communities to avoid a static approach to reserve studies. Instead, they should be relevant, continuously updated, and reviewed as repairs are made and new projects approved, he says. "This approach will allow you to make better decisions and give you more peace of mind and financial certainty."

STRUCTURAL SYMPTOMS

Associations that fail to adequately budget for necessary repairs and maintenance often find themselves facing costly surprises down the line. Preparing to avoid an emergency is much cheaper than dealing with one. That's why CAI initiated a review of its recommendations on reserve studies.

In March 2022, a task force of 14 community association industry experts began revising CAI's *Reserve Study Standards*. Originally published in 1998, the standards provide a consistent framework for reserve study providers and common interest communities. Since then, the community association and reserve study industries have rapidly grown, and the standards have evolved to reflect the current climate. Updated *Reserve Study Standards* were released in 2023.

Structural issues also have emerged as a major area of focus for lenders with firms increasingly scrutinizing the physical integrity of association properties. Ensuring the soundness of an association's buildings is essential

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LEGISLATIVE INTEREST MOUNTING

Because deferred maintenance can have such grave implications, some states have begun legislating reserve studies and reserve funds for community associations. There are two primary types of legislation: reserve study or funding requirements and statutory guidance for reserves. While some states require periodic reserve studies and reserves funding, others provide a framework outlining how reserve funds should be managed. Legislative mandates can include recommendations or mandates for minimum reserve levels, accounting practices, and reporting transparency to members.

Since the Surfside tragedy, four states have passed legislation requiring reserve studies. Most prominently, **Florida** requires structural integrity reserve studies for condominiums and cooperatives with buildings three stories or higher. (See "An Ounce of Prevention," *Common Ground*, May/June 2024, p. 31.)

Structural integrity reserve studies are focused on structural and systemic components with a replacement cost exceeding \$10,000. Failure to maintain the component negatively affects the structural/system components. Additionally, associations are required to follow funding recommendations outlined in their study and update structural integrity items every 10 years.

In **Maryland**, all condominiums and cooperatives require a reserve study. Homeowners associations whose common components have a combined purchase and installation cost of at least \$10,000 also must have a reserve study. Associations have three fiscal years to attain the recommended funding level if the most recent study is the initial study. Studies must be updated every five years.

New Jersey requires all condominiums, cooperatives, and homeowners associations with at least \$25,000 in common area components to obtain a reserve study. Studies must be updated every five years, and communities are required to adequately fund reserves within two years. The use of proportionate annual increases over 10 years can be used in situations where an existing reserve fund deficiency would necessitate a contribution increase exceeding 10%.

Lastly, **Tennessee** requires condominium associations to conduct a reserve study. Studies must be updated every five years. Though there are no statutory funding requirements, the legislation seeks to inform homeowners and board members of the amount that should be put into reserves each year to minimize the risk of special assessments and structural failures. —M.B.

➤ Find the latest reserve studies and funding legislation at www.caionline.org/advocacy.

to mitigating risk, and stricter lending standards will force communities to place greater emphasis on conducting thorough inspections and assessments. Communities with known structural issues or deferred maintenance pose a financial risk to lenders and potential buyers who could face hefty special assessments. As a result, lenders are insisting on greater transparency and accountability from associations on their long-term maintenance needs. (See "Blacklisted," *Common Ground*, January/February 2024, p.26.)

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After receiving criticism for a lack of transparency, Fannie Mae released a list of properties ineligible for lending. Freddie Mac has a similar list. While the specific reasons for landing on these lists are not explicitly stated, at the forefront are structural deficiencies, deferred maintenance, litigation and prelitigation activity, and failure to conduct reserve studies and properly fund reserves.

With Fannie and Freddie supporting around 70% of the mortgage market, ending up on these lists is a huge drawback for an association's marketability. To keep transparency front and center, both Fannie and Freddie have launched web-based tools that offer insights and guidance into eligibility.

CONTRIBUTING FACTORS

Insurance companies also are taking note of the importance of reserve studies in assessing risk. By examining the adequacy of reserve funds in relation to projected expenses, insurers gauge the association's ability to cover necessary capital projects without resorting to special assessments or loans. Components with deferred maintenance or inadequate funding are more susceptible to failure, leading to increased likelihood of insurance claims. In some cases, insurers have begun limiting useful lives.

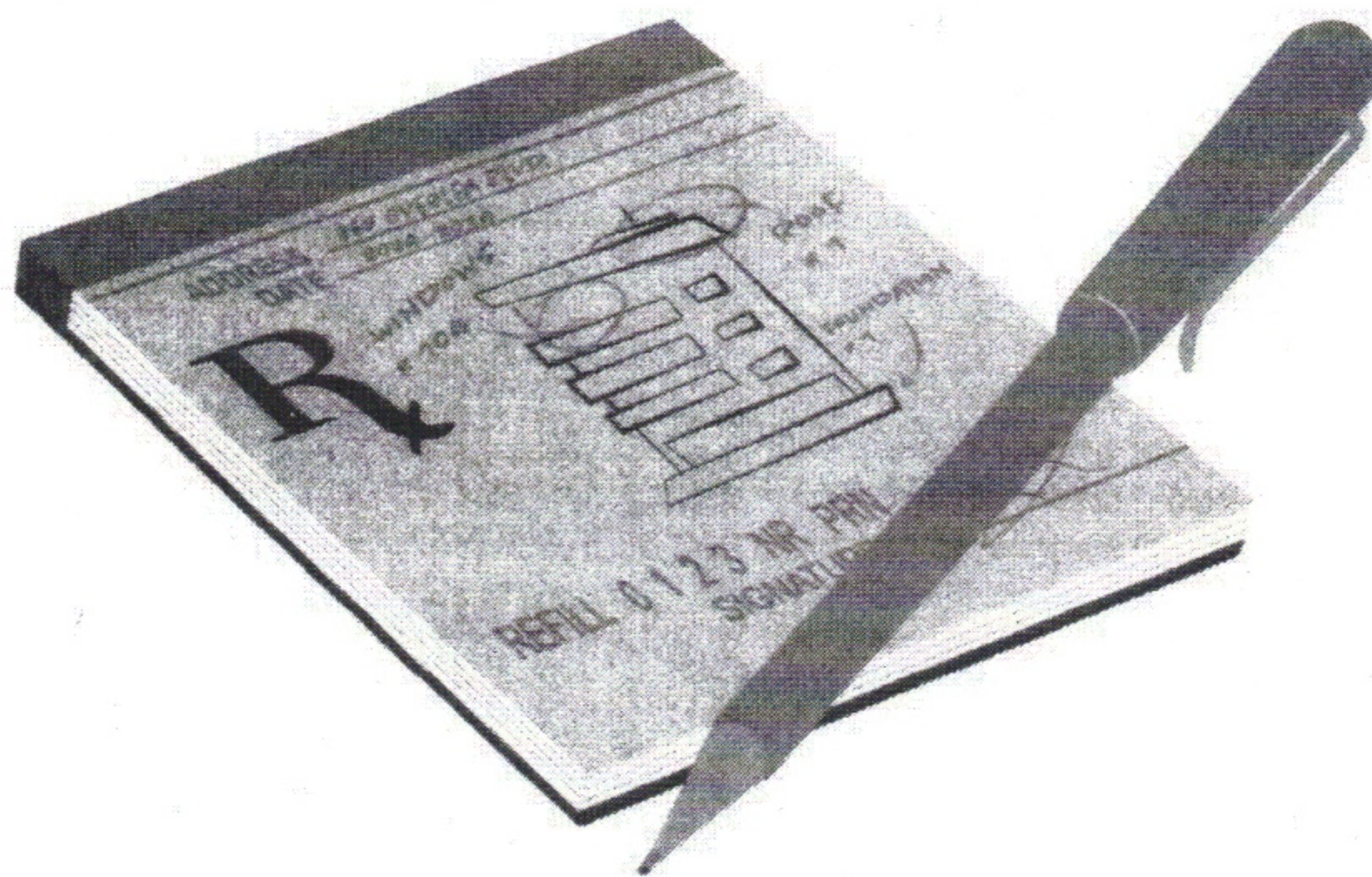
By incorporating data from reserve studies into their risk models, insurers can adjust premiums and tailor coverage to address specific vulnerabilities within a community. Properties that fail to demonstrate sufficient financial preparedness for repairs and maintenance may face higher premiums or coverage restrictions to account for increased risk exposure. In the worst-case scenario, insurance providers may opt to drop the property and not renew coverage. On the flip side, financially sound communities could see higher deductibles and lower premiums because they present less risk.

In its most recent snap survey regarding insurance trends in 2023, the Foundation found that 91% of associations sampled saw increased property and casualty insurance premiums. To fund this increase, 50% of associations increased assessments, according to the survey.

Of the risk management professionals surveyed, 96% reported experiencing significant premium increases for their community association clients. Increases of 11%–25% were the most common. Perhaps more alarming, 83% reported a significant number of property and casualty policy cancellations. The primary contributing factor to rising premiums and cancellations is the community's age followed by the age of the roof, total insurance value, and claims. Notably, 21% reported structural integrity risks as a contributing factor.

While management companies generally do not require reserve studies of their clients, the influx of new education surrounding studies has led to a bigger push by managers to get their communities on board.

With \$27.2 billion contributed to reserve funds in 2023, community management professionals understand reserve funds and community upkeep are not something to oversee haphazardly. Reserve studies allow managers to mitigate deferred maintenance issues and underfunded reserves while relying on independent expertise for smooth operations and their clients' well-being.



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Similarly, reserve studies allow — or force — boards to be increasingly transparent with homeowners. Their willingness to support funding reserves impacts the board's ability to address projects. In turn, insurability, marketability, and lending eligibility also are impacted.

With a reserve study in hand, boards can justify decisions they make for the health and safety of their association and educate homeowners in the process.

“Many homeowners and board members do not understand the importance of these studies — not just doing reserve studies but actually using (the) recommendations to fund reserves in a responsible way,” says Jan Newcomb, president of the Springhurst Townhomes Homeowners Association in Huntington Beach, Calif. “Without adequate reserves, current boards are faced with large assessment increases, special assessments, loans, or deferred maintenance.

“None of these choices make owners happy, and current boards and new owners are stuck with the problems created by people who may not even live in the community any longer,” Newcomb adds. “It’s a very serious issue for many newer communities as they continue to age if they don’t plan for the future.”

GETTING HEALTHY, WEALTHY, WISE

Considering these developments, managers and boards should be increasingly cognizant of the value of proactive

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INSIGHTS, INFORMATION, AND ADVOCACY

Reserve studies are one component of a greater emphasis on building safety in the industry.

CAI took a leadership role toward improving building maintenance and safety when it convened a group of industry task forces to explore changes to laws and best practices after the 2021 Surfside tragedy. Their work led to the comprehensive *Condominium Safety Public Policy Report*, which originally was released in October 2021. The report was updated in June to reflect legislative and policy changes in the three years since the disaster that claimed nearly 100 lives.

In September, CAI published *Reserve Studies and Funds*. The new edition has been updated to reflect the changing climate on maintenance and safety. The book presents the theory behind the preparation of a reserve study, how to view the reserve study as part of the association's overall budget, how to take advantage of the relationship between reserves, maintenance, and structural safety, the methods for developing a realistic funding plan, and a discussion of the various funding techniques. In addition, the reader will find strategies for investing the reserve funds and additional information on financial reporting and tax implications of reserves.

In addition, a new guide to navigating a major capital project helps community association leaders understand the connection between financing, communication, meetings, bids, the project team, and more. Through how-to information and anecdotal tales of tragedy and triumph from the author's personal experience, *Capital Projects: A Case Study* helps readers successfully start and finish their next big undertaking.

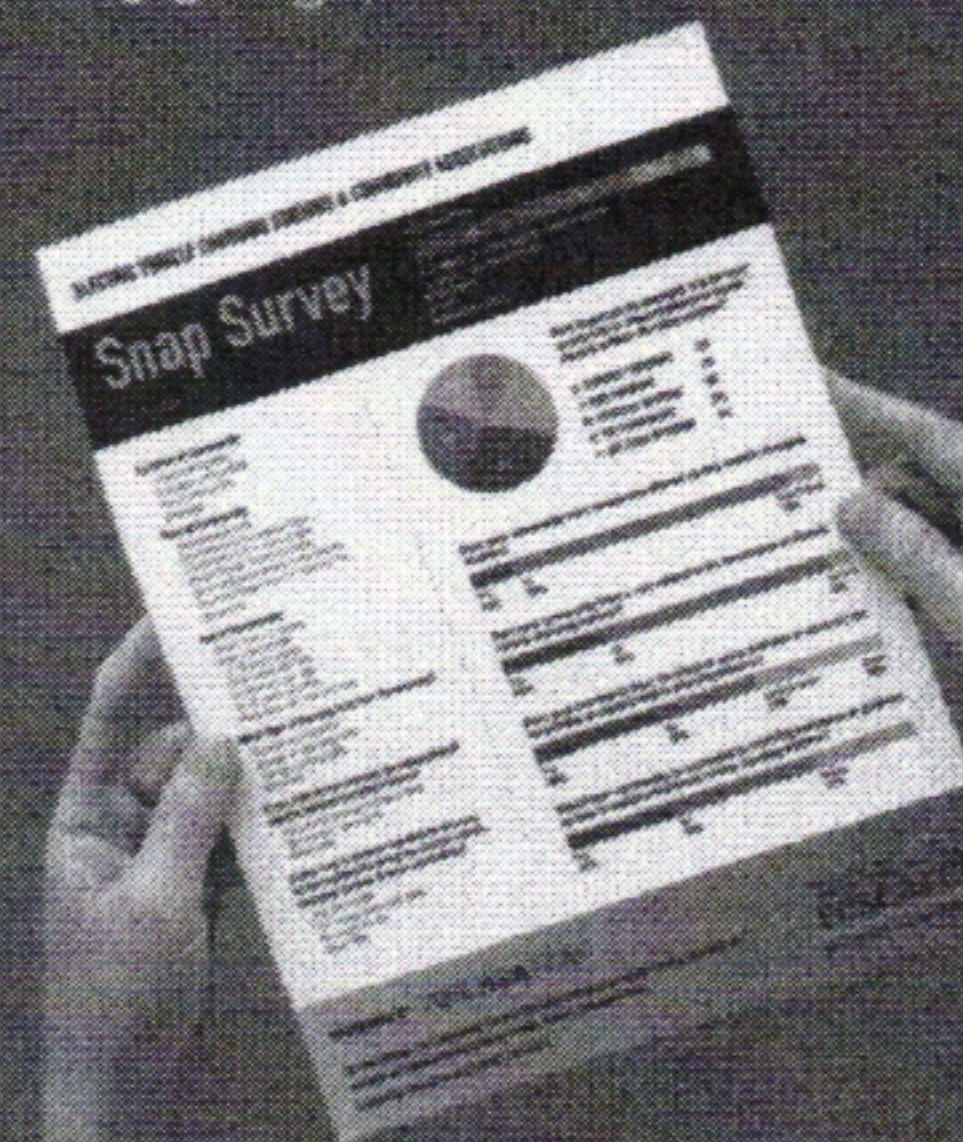
Earlier this year, the Foundation for Community Association Research surveyed industry professionals on structural inspection trends in condominiums, cooperatives, and townhomes. The survey found that 90% of communities have reserve studies but only 32% have existing, pending, or imminent repairs related to the building, parking garage, or balconies.

View snap survey results at www.caionline.org/SurveyBuildingInspections.

Reserve Studies and Funds as well as *Capital Projects* are available in print and digital formats.

www.caionline.org/shop.

Visit www.condosafety.com for more information on reserves and condo safety.



RECAPPING THE REVISED STANDARDS

CAI released revised *Reserve Study Standards* last year to provide communities with an improved framework for effective reserve planning. Among the revisions in the report originally distributed in 1998 are several best practices to avoid structural or system failures before they emerge, including:

- Disclose all association-maintained, long-lived components in the component inventory. Even if long-lived assets may not need funding or maintenance within the 30-year scope of the reserve study, they should be included in the report. Providers should prepare useful life and cost information for these items even if they don't currently require funding. Associations must have a holistic understanding of the cost to maintain them down the road.
- List preventive manuals and structural inspections as supplemental reports to the reserve study. Both elements recognize life-cycle costs are not limited to reserve components. Incorporating these items will minimize life-cycle costs.
- Confirm if preventive maintenance is being performed. If a component is not regularly maintained, it is unlikely to obtain its full useful life. Providers can determine the estimated remaining useful life and create a funding plan to replace it. This is especially important when the useful life has been shortened because of deferred or reactive maintenance. —M.B.

» Read more about the revised standards on p. 38.

A Spanish-language version of the standards was released in 2023. (See p. 46)

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planning and budgeting. Conducting regular reserve studies every three years as recommended by CAI helps associations identify potential maintenance issues early and allocate funds accordingly. This helps safeguard the long-term value of the property and ensures compliance with lender and insurance requirements.

A proactive budgeting approach allows for the timely completion of capital replacement and maintenance projects. Well-maintained communities can enhance an association's overall attractiveness to prospective buyers. Communities with a sound infrastructure and healthy reserve funds are perceived as desirable investments and command higher market value.

The growing focus on reserve studies reflects a broader shift toward risk management and financial diligence in the community association industry. As governments, lenders, insurers, and other institutions place greater emphasis on structural integrity and financial adequacy, boards and managers must adapt by prioritizing proactive maintenance and budgeting practices through regular reserve studies. By doing so, not only can risks be mitigated, but the value of the property can be maintained for years to come.

"Homeowners do not think of community associations as a business, but they are," says Smart Property's Esparza. "They have a mission to preserve, protect, and maintain common area assets. Those that govern and serve on boards have a fiduciary, a legal obligation. To ensure the business of community association living can effectively operate and sustain, we have reserve studies. They are the financial roadmaps designed to better understand the financial health of today and what it will take for tomorrow." **CG**

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