

# DEFERRING REPAIRS? CHOOSE WISELY!



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A Boardmember recently asked what defines “too far” with respect to choosing to do a Reserve project on time or to defer the project. When does deferred repairs get to the point of the Board dangerously incurring liability and financial risk? That was an interesting question, as it reveals the true nature of being a Boardmember with the authority and power to make decisions on behalf of the Association. The homeowners have entrusted the care of the common area assets to the Boardmembers and the Board is in charge, within the limits granted to them by the Association’s governing documents. But what should guide the decision-making process and when do “good intentions” lead to potential liability?



Let’s look at some actual Reserve projects:

Consider a Board that is trying to decide whether to replace (or defer the replacement of) a “pool heater” that has reached the end of its Remaining Useful Life (RUL). One of the first considerations should be “What are the possible consequences of component failure?” For most Associations, it would be of no consequence if the pool heater suddenly failed. At worst, the pool would cool down for a few days until the replacement heater was installed. You may have a few disgruntled swimmers, but it’s not that big a deal.

But deciding whether to repair or replace a failing boiler (with a RUL = 0 years on the Reserve Study) that provides hot water to the entire building is an entirely different matter. If the boiler were to fail suddenly, and everyone in the building has to survive without hot water for a few days, there are going to be some very unhappy homeowners!

So the first question for a Board to ask themselves when faced with the option of deferring maintenance is, “What happens when that happens?” A Board certainly has more flexibility deferring the repair or replacement of reserve component items where catastrophic component failure would be of little consequence.

Presuming the component failure would have significant consequences for the Association, there is a lesser known, but vitally important corporate principle for a Board to consider when evaluating the wisdom of their decisions. This principle is called the Business Judgment Rule (BJR). Boards should be

well-versed in the BJR, because it's intended to protect corporate directors from decision-making liability when their decisions are challenged. In order for a Board's challenged decision to be protected, a judge or jury would need to be convinced that the decision made was:

- 1) Within the authority and power of the Board
- 2) Based on "reasonable inquiry" (to gather facts or wise counsel)
- 3) In the best interests of the Association.

Let's see how this works. Consider a Reserve Study for a condominium Association that indicates the roof will soon (RUL = 1 year) need to be replaced. When a single homeowner experiences a roof leak, the Board contracts with a reputable roofing contractor to make the necessary repairs. At the next Board meeting, the issue is raised as to whether it's time to go ahead and replace the entire roof.

Choosing to repair or replace the roof is clearly within the authority and power of most Boards and the first necessary element of the BJR. One Boardmember wisely suggests asking the roofing contractor for his opinion. If the roofing contractor's position is that the roof is still in generally fair condition, except for the one unit that needed repairs, the Board could decide to wait another year before undertaking an expensive re-roofing project. The Board has complied with the second necessary element of the BJR by making reasonable inquiry, in this case relying on the expert opinion of a professional roofer. A decision to defer roof replacement while still assuring the leaking upper floor homeowner of a water-tight unit for another year would certainly be in the best interest of the Association.

Now, consider the circumstance where the result of the Board's reasonable inquiry is that complete roof failure is imminent- where it was hard for the roofing contractor to tell which area of the roof to fix because it all looked equally bad. What are the implications of the Business Judgment Rule if the Board were to decide to defer roof replacement for another year or two?

Again, the decision is certainly within the Board's authority and power. But if the Board ignores the facts and wise counsel that they've gathered, or worse yet, fails to make reasonable inquiry, the decision would fail to comply with the second necessary element of the BJR. If the Board's decision to defer roof replacement was motivated in part by Boardmembers who couldn't personally afford the necessary special assessment, or were planning to sell their units before the word got out that the roof was in bad shape, or didn't want the inconvenience of coordinating a roof replacement project that year, the Board's decision could be deemed "self-serving" and fail to comply with the third and final element of the BJR- making decisions in the best interests of the Association.

Yes, Boards have the authority and power to make decisions, but no Boardmember wants to stretch their authority and power to the point that it gets them into trouble. The Business Judgment Rule offers a simple but powerful three-part test that can be used to guide important Board decisions. Every day, well-intentioned Boardmembers step outside the protection of the BJR by making decisions "without reasonable inquiry", or that are "self-serving", leaving them needlessly exposed to the risk of personal liability. When a Board is trying to decide between two or more options, it would be wise to ask the right questions of the right people, abide by professional opinions, and act strictly in the best interests of the Association. That is a decision-making process that will keep well-intentioned Boards out of trouble!

For additional information, watch our recorded webinar [Underfunding Reserves and the Business Judgment Rule](#).