

SNEAKY BOARD PRESIDENT



by Robert M. Nordlund, PE, RS
 CEO/Founder
 Association Reserves, Inc.

June 2012

www.reservestudy.com

We recently dealt with a creative (and sharp!) Board Treasurer who was unhappy with our With-Site-Visit (WSV) Reserve Study update for their Association. The Association is made up of single family dwellings, where every homeowner maintains their own residence. The primary common area asset is a mile-long roadway system that meanders throughout the development. In such a situation, the “Asphalt- Remove & Replace” project (Replacement Cost = \$ 350,000) dominates the Reserve Component List. An entryway monument sign (Replacement Cost = \$2000), tot lot (Replacement Cost \$15,000), and all other projects are of insignificant influence in comparison.

Typically, asphalt needs to be removed & replaced every 20-30 years. Upon our inspection, the asphalt roadway system of this 10 year old Association showed some minor age and deterioration and good ongoing care. In our opinion, the asphalt appeared to be deteriorating “on schedule”, so we updated the Component List to reflect the scope and schedule of this reserve project as indicated below:

Component Description	Useful Life (UL)	Remaining Useful Life (RUL)	Cost (\$)
Asphalt- Remove & Replace	30 years	20 years	\$350,000

What this correctly communicated to the Board, the Manager, the homeowners, and any outside interest parties was that the existing 10 year old roadway system had experienced (no surprise) 1/3rd deterioration (i.e., 10 years “used up” out of a 30-yr useful life).

With continuing good maintenance, it was also the Treasurer’s opinion that the asphalt would last about 20 more years. So in the Reserve Study update he had prepared himself for the prior fiscal year, the Component List reflected the scope and schedule of the Asphalt reserve project as indicated below:

Component Description	Useful Life (UL)	Remaining Useful Life (RUL)	Cost (\$)
Asphalt- Remove & Replace	21 years	20 years	\$350,000

We both agreed that the \$350,000 reserve expense was 20 years away. So why was the Board Treasurer upset with us? Let's look at how these two very different Component Lists affect the calculation of the Asphalt's "Fully Funded Balance". Based on National Reserve Study Standards:

$$\text{Fully Funded Balance} = \frac{\text{Component Age (yrs)}}{\text{Useful Life (yrs)}} \times \text{Replacement Cost (\$)}$$

"Fully Funded" Balance	
Our calculation	\$116,667 <i>(10/30 of \$350,000)</i>
Treasurer's calculation	\$16,667 <i>(1/21 of \$350,000)</i>

The Treasurer had erroneously assumed that the only issue of significance was the Remaining Useful Life (RUL). But by ignoring the reality of 10 years of asphalt roadway "deterioration", he had effectively and intentionally manipulated the numbers to minimize the asphalt's "Fully Funded Balance". The result was that he had been able to boast proudly to all Association members at the last annual meeting that their Reserve Fund was "strong" at 95% Funded and that there was "nothing to worry about".

Getting past the fact that his presentation of the numbers (while correctly calculated) were misguided, what were the implications?

When we presented our Reserve Study with the accurate calculations, the Association's Reserve Fund plummeted to a "weak" 17% Funded with a high risk of Special Assessment. The Association was not as prepared for the future as the Treasurer had led the Board and Homeowners to believe, and he was about to be seriously embarrassed.



Bottom line – accuracy matters! All of the numbers... Useful Life (UL), Remaining Useful Life (RUL), Current Replacement Cost (\$), Reserve Fund Balance, Fully Funded Balance, Interest, and Inflation matter. All of the calculations matter. National Reserve Study Standards matter.

Being "clever" by manipulating the numbers does nobody any good. The facts of the matter will eventually reveal themselves when there is insufficient funds to pay for necessary repairs and replacements. Boardmembers, Managers, and homeowners have a right to know the truth about their Association's financial health, and disclosure laws are in place to provide protection to consumers. The truth has a way of coming out, and a reputation of embarrassing those who attempted to hide it, or tell only one side of the full story!