



Capturing the Pulse of the HOA Industry
HOA Industry News, Articles, and Links

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Both interest and inflation considerations are important to the calculation of your future reserve requirements. Unless the association has made a conscious decision to transfer all interest earnings to the operating fund (which is the subject of an entirely different article), it is generally assumed that interest earnings will be retained in the reserve fund. Likewise, inflation is a factor that will cause the prices you pay for future repairs to be higher than the cost you're paying presently for those same repairs and replacements.

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Association of the Week

**2412 Clark Avenue
Condominium**



*2412 Clark Avenue Condominium
is a two-unit project located...*

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Management Search

Your management company or manager is your most important contract. Making the right choice in the professionals who will help you make the financial and legal decisions is crucial as you serve your unique community.

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Business Spotlight

Porter & Company, CPAs

Technology Changes the Industry

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Association of the Week

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2412 Clark Avenue Condominium

2412 Clark Avenue Condominium is a two-unit condominium project located near LAX , Los Angeles International Airport, in Southern California.

The project was built in 1985 and converted to a condominium project with formation of the Association in 1995. Many small projects of similar size exist in California; the result of local governmental units requiring the formation of associations as part of the permitting process in order to shift the burden of certain costs from the public sector to the private sector.

There are very few associations that can boast 100% participation by their members, but this is one of them. By default, both members of the Association serve on the Board of Directors.

Common areas consist of building structures and minimal paved surfaces and landscaped area. The Association has an annual operating budget of less than \$1,500, and annual reserve contributions of approximately \$2,000. The Association is self-managed.

Note from HOA Pulse staff

We have been asked if there are any specific criteria we're looking for in selecting our Association of the Week. The answer is no, not really. As you can see from this week's selection, this is the smallest possible size for an association. We have also featured associations that have several thousand members.

Having worked in the industry for many years and being exposed to many different types and sizes of associations, we simply have an interest in sharing the experience of discovery of new and different associations. Our goal is to provide a broad cross section of associations in type, size, and geographic location so that you, our readers, can also experience something new.

The first few associations we have profiled have been invited by us to share their association with us, because we found them to be interesting associations. We have some more great ones coming up. If you are aware of any associations that you would like to see profiled, please download the application form and have a repre-



Business Spotlight

Porter & Company, CPAs



Porter & Company CPAs provides audit, review, and tax services exclusively to the homeowners association industry. The firm provides audit and review services in California and Nevada, and tax exemption services nationwide.

Gary Porter, owner of the firm, has more than 30 years experience in the industry, and is the creator and coauthor of Guide to Homeowners Associations and Other Common Interest Realty Associations, and Homeowners Association Tax Library, the guides relied upon by virtually every CPA firm serving the industry. The Guides are published by Practitioners Publishing Company, the largest publisher to the CPA profession.

Mr. Porter has written more than 200 articles that have been published in various publications. He is a past CAI "Author of the Year," a recipient of CAI's Distinguished Service Award, and is a past national president of CAI.

Tax exemption services provided by the firm have resulted in more than 60 associations receiving tax exempt status under Internal Revenue Code Section 501(c)(4). The cumulative tax savings to these associations is well over \$15,000,000. This service is so specialized that the firm has established a separate website at www.501c4taxexempt.com devoted solely to this subject.

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Consideration of Interest and Inflation in the Reserve Study

By: Gary Porter, RS, PRA

Both interest and inflation considerations are important to the calculation of your future reserve requirements. Unless the association has made a conscious decision to transfer all interest earnings to the operating fund (which is the subject of an entirely different article), it is generally assumed that interest earnings will be retained in the reserve fund. Likewise, inflation is a factor that will cause the prices you pay for future repairs to be higher than the cost you're paying presently for those same repairs and replacements.

The two questions that continually arise are "Should interest and inflation be included in the reserve study; don't they cancel each other out?" and "How do you calculate what interest or inflation rate to use?"

I believe that both inflation and interest earnings should generally be considered in the funding plan of a reserve study. To ignore these would be to ignore reality. While it is a policy matter of the board of directors whether or not to include these items, it is common practice to include both interest earnings and inflation in the funding plan of the reserve study. Inflation should never be ignored. Failure to consider inflation will generally lead to significant future underfunding, unless the association updates its reserve study and underlying cost assumptions annually.

The fact is that interest earnings do not offset inflation. While interest and inflation rates may be similar, the inflation factor is applied to the total estimated future expenditures for all common area components included in the funding plan. This is (virtually) always a higher number than the current funds set aside for reserves. Conversely, the funds set aside for reserves are (virtually) always a smaller amount. That means that the dollar amount of interest earnings will grow far slower than the dollar amount of inflated costs, even if the rates are the same. An example is that an association may anticipate spending \$3,000,000 over the next 30 years, which includes inflation calculations. The current reserve cash on hand may be as little as a few hundred thousand dollars, as that is all that is required to pay for planned expenditures arising in the next few years. Inflation of 2% on \$3,000,000 is \$60,000 annually. An interest rate of 2% on \$500,000 of cash invested generates only \$10,000 of interest earnings annually, creating an annual funding gap of \$50,000.

The second question, how do you calculate these rates, has no correct answer. Some people use a rule of thumb. Others look at their current interest earnings rates as a guide. Current interest earnings rates cannot be ignored, but if they are unusually high or low, it is not practical to expect those rates to continue indefinitely. However, so long as you keep your assumed interest earnings rate relatively the same as your inflation assumption, you shouldn't get into too much trouble, as they do usually move in tandem. California associations should be aware that California law limits the interest rate assumptions that may be used in a reserve study to 2% above the discount rate published by the San Francisco Federal Reserve Bank.

Since the funding "window" of a reserve study is normally a 30-year projection, many believe it is legitimate to consider average rates rather than current rates in establishing your funding plan. The attached historical tables of interest and inflation rates allow you to put current rates into perspective. Table 1 reflects solely at annual rates. Table 2 reflects the 5-year average rate in any given year. Table 3 reflects the 30-year average rate in any given year. You will note that Table 3 does not contain the sharp peaks and valleys of the annual rates in Table 1. However, general trends are still similar.

Note that regardless of sometimes significant annual variations in rates, the moving 5 and 30-year averages smooth out the rates considerably, eliminating the extreme spikes and valleys that generally occur for only short periods of time. Since the reserve funding plan typically projects for a 30-year period, it is usually safe to ignore current extreme changes in rates in favor of longer term moving averages.

I was forced to address this issue when I first started preparing reserve studies in 1982. Look at the annual rates for that year and you can understand why. If we had used the current interest and inflation rates of that year, NO reserve study could be developed that would provide adequate funding without "breaking the bank" by forcing reserve assessments so high that no one could pay them. We opted then for using approximately 5% interest and inflation rates, because we knew the current situation was abnormal and could not be sustained. Time proved us right on that assumption, but the fact is no one could reliably predict future rates.



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Current interest rates are at an all time historical low. Despite political pressure to keep rates low, they are beginning to trend back up. Inflation rates reported by the government are also at all time lows, actually reflecting a deflationary rate in 2009. However, because of changes made in recent years to the government data as to what is included in their calculations of the official inflation rate, current inflation rates are not comparable to prior data.

Table 1 - Comparison of Annual Interest Rates to Inflation rates 1971 - Present

This chart shows the close correlation of interest rates and inflation rates over long periods of time.

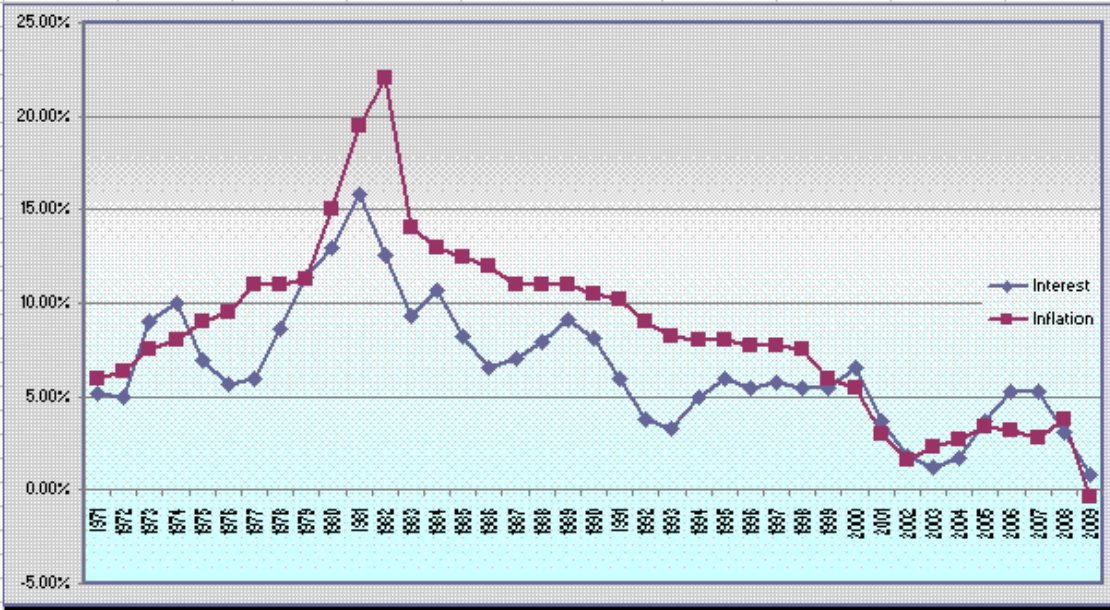


Table 2 - Comparison of 5-Year Average Interest Rates to Inflation rates 1971 - Present

This chart shows how using 5-year averaging smooths out the rates and provides an even closer correlation of interest rates and inflation rates over long periods of time.

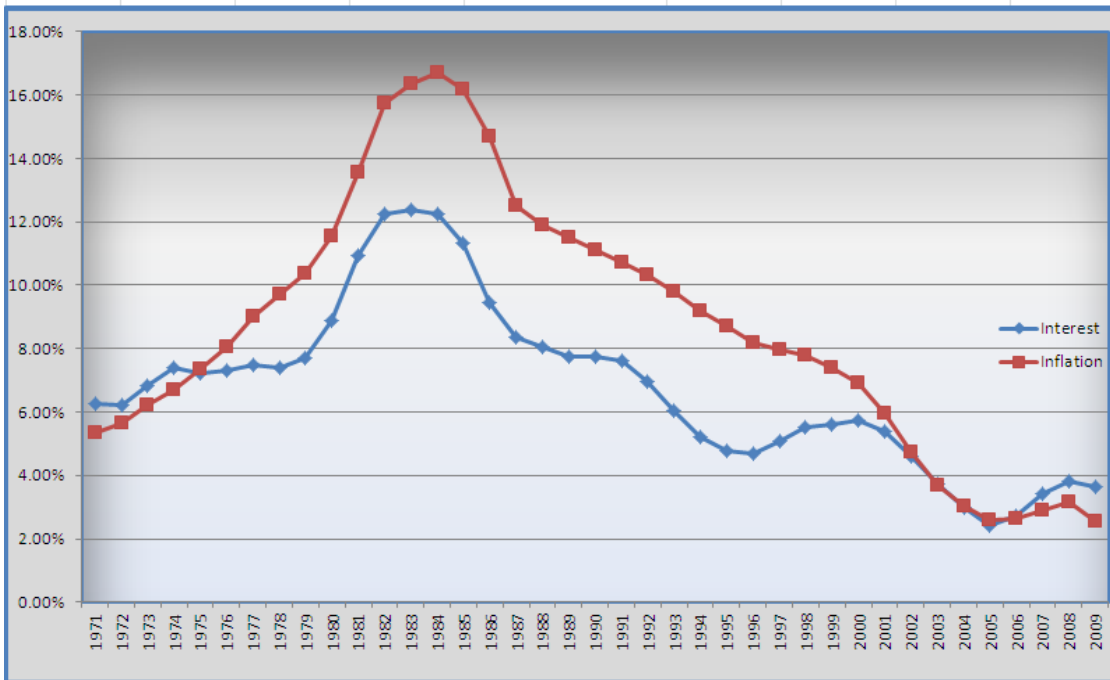
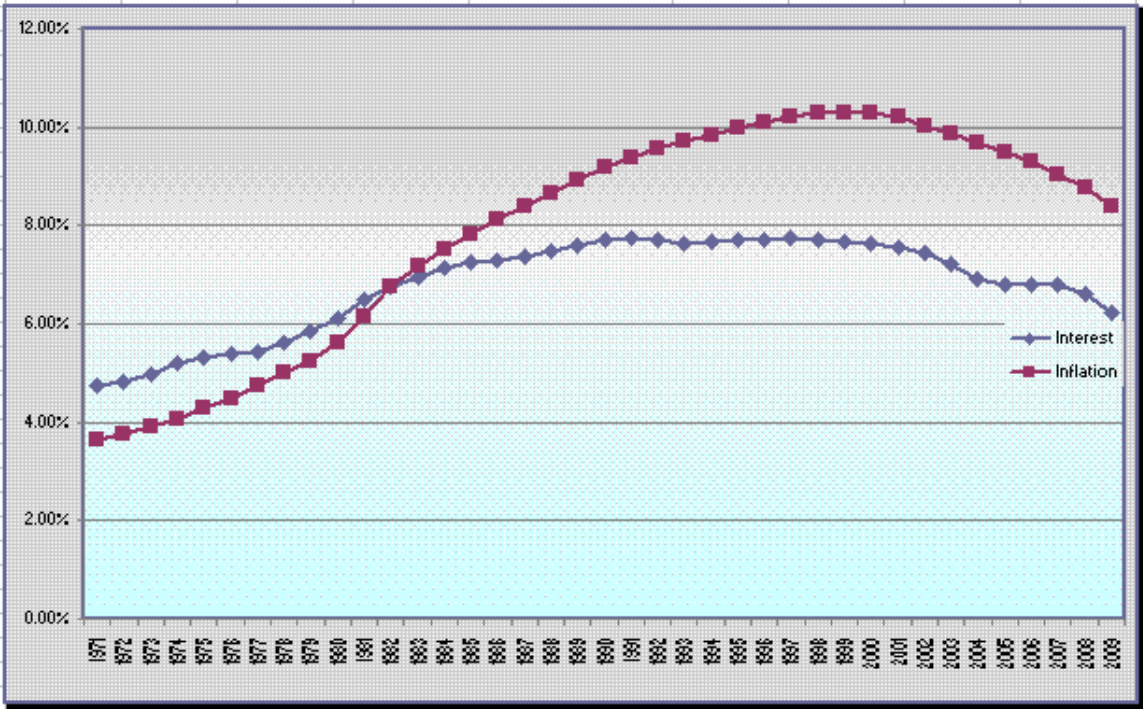


Table 3 - Comparison of 30-Year Average Interest Rates to Inflation rates 1971 - Present

This chart shows how using 30-year averaging smooths out the rates and provides an even closer correlation of interest rates and inflation rates over long periods of time.



Management Search

By Karen Bennett, PCAM®, CCAM®

Our board has always called or sent requests for proposals to a few management companies. Is there a better way to solicit bids?

Benchmarking your current service and defining a more satisfactory level of service expectations will enable your board to make a reasonable business decision. Why change companies and disrupt your residents and owners without first establishing your requirements so that you can compare “apples-to-apples”?

In the past, when we have gone out to bid for a new management company we have been bombarded with questions that we can't answer. Why do management companies have so many questions?

A management company will need to understand your association before they can present a fair and complete proposal. A board can jump from the frying pan into the fire when making a change based on incomplete or erroneous information. Community Association Consulting can liaison with the management companies that are pre-screened to submit a proposal.

By creating detailed specifications for bidding and being able to anticipate and find the answers to the management company's questions, the proposals will be complete and easy to compare.

We are all busy business and professional people who need to make sound decisions for our owners. What can you do for us?

As volunteers who agree to make good business decisions, you must consider the most effective means to accomplish your annual goals. If deciding to change management is a goal of your board, it should be your most important contract decision. You hire experts to advise you on your finances and your legal issues; therefore you should also hire an expert in the community management field to help you find the best manager or management company for your unique community.

Our community is concerned about costs. Why should we spend money with your company to find a new manager?

You can't afford to make a wrong decision. Choosing a management company or manager is your most important contract. Evaluation of the reputation of the companies, verifying satisfaction with similar communities managed, company stability, supervision of the manager, record keeping quality, philosophy of company and educational level of manager assigned are all considered and evaluated in helping you make your decision.

Karen Bennett, PCAM®, CCAM®

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Technology Changes the Industry

Advances Tackle Common Management Problems

By: Craig Huntington

When I started my association management company in 1980, we kept the account history of our homeowners on ledger cards and wrote checks using a "One Write" system. We really were pushing the envelope when we decided to use a Polaroid camera to take pictures of violations. In 1981, we took the plunge, spending \$4,000 for an Apple III with all the necessary components.

Things certainly have changed. Today, my Treo PDA phone has more RAM, storage and computing power than that old Apple III. It's also one-twentieth of the cost, counting inflation. In today's world, technological improvements have allowed us to do a better job both faster and easier. With the coming of age of the Internet, this has taken a quantum leap forward.

Banking and Technology

From the advent of association-specific banking services until now, the focus has been on improving the effectiveness and efficiency of deliverables (lockbox, statements, setting up accounts, etc). Today's "Industry Specific" banks are looking for new ways to improve the workflow and efficiencies of the management companies they work with. Some of those advances are as follows.

Check 21. This was the big news of last year. The key points touted at this time last year were the imaging of all checks, the elimination of cancelled paper checks and the reduction and virtual removal of the "float" – the time it takes for checks to clear and for deposits to be received. Many banks now provide their customers with a check imager. The management company simply images the checks and sends the image to the bank for processing.

Positive Pay. Fraud is becoming more and more prevalent. You now can send a file of the written checks to your bank. If a check is presented that is not in this file, it will be rejected.

Software Integration. Rapid progress is being made on this front. Most banks have the ability to send the lockbox upload file to the management company. Now we are seeing banks team with software companies for much more integration. Soon to come will be:

- Real-time reconciliation of your checking accounts. No more end of the month reconciliation backlog.

- Integration of money transfers. Do the transfer in your own software and the bank is automatically informed.

- Bill Pay also is very close to being perfected. Banks have been offering bill pay to their retail customers for a couple of years now. Because of most associations' requirement for dual approval and the issue of getting the information from the check into the management company's computer, this service has not been offered to management companies. Soon your vendors will be able to go to your website and post their invoice. Upon posting, an e-mail will be sent to all the parties who need to approve the payment. Upon approval, payment will be made in the form of an ACH, no more checks.

Online Services. This continues to grow by leaps and bounds. The ability to go online and see account activity in real-time, view cancelled checks, see past statements and limited cash-management services are available through most banks. The ability to pay assessments online is also on the rise.

Next Generation Caller Identification. Soon your computer will tell you more than just who is calling before you answer the phone. Imagine having all the information about a homeowner on the screen before you answer the phone. This feature also will help companies track time spent on a particular client.



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Advances Tackle Common Management Problems

Document Delivery. Several companies already deliver documents using the Internet. These services are used for resale and loan questionnaires. Homeowners can get copies of condo documents, meeting minutes, budgets and any other document you wish to deliver. There are even special newsletter programs that will allow you to deliver your e-newsletters over the Internet.

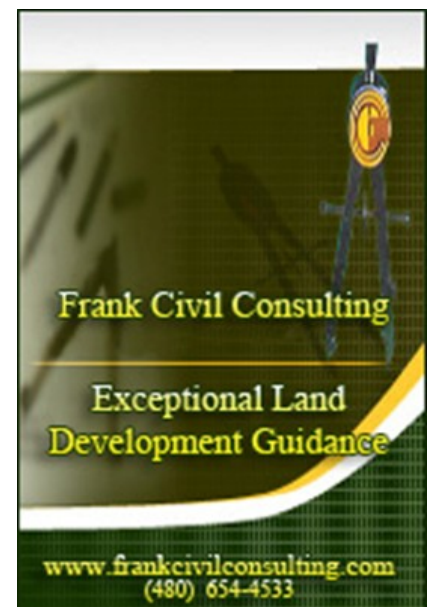
Is technology the answer to all our management problems? Not as long as there are barking dogs, brown lawns and speeding drivers. However, when these technologies become easy-to-use, the efficiency and simplicity they offer will be key drivers in the end for true customer satisfaction. In what is being called the “Experience Economy” (think Starbucks and Amazon.com), client expectations about service have grown exponentially. Technology is a tool that helps us not only to meet, but also exceed client expectations. That translates into client delight, which means client retention....and that makes everyone happy!

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Article Title	Article Summary	State
Indiana House bill protects families against homeowner associations	House members approved a bill that will protect families against HOAs that fail to live up to contract responsibilities.	Indiana
Travis homeowner, association tangle over solar panels	HOA refuses request for homeowner to add solar panels to his home being constructed.	Texas
HOA Adviser: Delinquency in the payment of monthly assessments	Water Damage and delinquency notifications are discussed in this Q & A	California
New state sprinkler law: Shower of safety or just all wet?	New state building code requires all newly constructed homes to have a fire-suppression system installed	Pennsylvania
Neighbors complain about back	Go-kart track is irritating to neighbors but does not violate any codes or zoning laws	North Carolina
You Ask: Why is my HOA tearing down trees?	Trees, that should not have been planted in the first place, are coming down due to concrete and structural damage	Nevada
Handicap parking spaces painted over at Solaire condominiums downtown	Condo Association paints over all handicap parking to make additional parking spaces.	Florida
Combating condo delinquencies	A Florida law helps HOAs stay afloat by allowing them to collect fees directly from renters when the homeowner is in default	Florida
County says no to solicitors	Santa Rosa County Commissioners have passed an ordinance to eliminate solicitors and door to door salesman	California
Where there's smoke, there's ire: Condo conflict lights up in Hessian Hills	Cigarette smoke, seeping through walls and duct systems, can cause health problems and discomfort in neighbors of smokers.	Virginia
Could delinquent owners lose cable and Internet access	Owners and board members are looking to legislators to allow them authority to cut owners' access to cable TV, internet and common areas, when they are behind in payments and association fees.	Florida
Chris Griffith: Pet droppings a big, smelly part of homeowner association restrictions	Pet ownership in a condo association should be well spelled out in the covenants	Florida
Poinciana Getting Youth Facility	HOA reaches out to Boys and Girls Club and has worked out an agreement for them to create a youth center.	Florida
Raleigh HOA accused of spending \$11K on parties, ignoring repairs	Homeowners claim board has budgeted \$11,000 for parties but nothing for repairs and maintenance	North Carolina

Article Title	Article Summary	State
Homeowners should have say in proposed new laws	Approximately a dozen bill draft requests, regarding common-interest communities, have been introduced	Nevada
Pool accessibility rules make waves; HOAs, hotels looking at new expenses	New changes to the ADA will cause a number of HOAs and hotels to make expensive changes to their pools.	South Carolina
Street light law could be changing in Flowery Branch	City pays for street lights in some subdivisions but not in others.	Florida
Misrepresenting status of homeowners association can bring penalties	Community that represents itself to the public as a non-common-interest development can result in damages for violations.	California
Make 3-minute rule work at board meetings	Three-minute rule, HOA documents and insurance are discussed in this Q & A	Florida
People rally for and against HOA reform	People rally for and against HOA Reform	Texas
What is ex-owner's duty in foreclosure?	Home in foreclosure and owners must pay insurance and fees on the home until foreclosure sale has occurred.	Arizona
Woodhaven HOA closes on golf course purchase	Woodhaven Country Club HOA closed on its purchase of the community golf course.	California
Fight over HOA power heads to Austin	Texas lawmakers face the tough debate over HOA reform	Texas
Concerned Homeowners Association Members Coalition Forms	A coalition was formed to represent the interests of individuals and entities in combating the HOA collection process	Nevada
HOAs heave sigh of relief as agency revises plan	Federal Agency backs off a plan to make obtaining mortgages more difficult and ban transfer fees.	National