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NEWS & VIEWS

for Homeowner Associations

October 2020

Assessments Too High?

By David Brock, PCAM

For all common-interest-developments that operate on a calendar year, October is the beginning of “budget season.” There is no doubt that 2020 has been a rough year for just about everyone. Whether it is the COVID-19 pandemic, or a very contentious political season, now we must talk about the HOA budget for 2021. We just can’t seem to get a break. If a poll were taken as to whether most people want their assessments to be lowered, there is little doubt as to how that response would go. The amount of the monthly assessment is the greatest concern of most owners. Since the amount of HOA assessments appears to be something that boards and owners can exert control over, is there really much wiggle room?

There is no magic number that HOA assessments should be as every association is different. The budget, and consequently the monthly assessments must be adequate to meet the needs of the association, both today and in the future. Some may



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The New “Balcony Inspection” Law

By Michael T. Kennedy, Jr.

I. Background

Commonly known as the “Balcony Inspection” law, SB326 (now Civil Code § 5551) was passed in response to several notable structural failures due to unseen deterioration from water intrusion, most notably a tragedy where an apartment balcony collapsed in Berkeley. The 13 people on that balcony fell 40 feet to the sidewalk below and 6 of them were killed. That building was only 7 years old, and an investigation revealed that defective construction had allowed water to become trapped between the cantilevered joists supporting the deck and the plywood underlying the walking surface, rotting the joists.

There has been a visual inspection requirement, conducted as part of the reserve study update, since the 1980’s. That inspection must be conducted every 3 years and, while it must be “reasonably competent and diligent”, it is visual only and usually conducted by the reserve specialist. Structural damage to structural members is almost always invisible behind stucco, siding, or other exterior surfaces, however.

In response to the Berkeley tragedy and similar incidents, this new inspection requirement took effect this year, requiring a more comprehensive inspection every 3rd reserve study update.

II. The Inspection

Every 9 years (or after the first 6 years for a new project) in every residential condominium building with 3 or more units, there must be an inspection of “Exterior Elevated Elements” by a licensed architect or structural engineer. “Exterior

Elevated Elements” are anything with a walking surface at least 6 feet off the ground that extend from the exterior wall of the building that are supported by wood or wood-based products, together with their railings and associated waterproofing system. The inspection must include the load-bearing structural components themselves, such as joists, beams, and other structural supports. The statute specifically includes flashing, membranes, coatings and sealants that protect structural components from damage caused by water exposure.

The inspection must be conducted by a licensed architect or structural engineer, and it is the inspector who determines how many locations to inspect. Architects and engineers experienced in the type of forensic investigations conducted during construction defect claims will have the most relevant experience for this type of investigation and report.

The inspector generates a randomized list of each type of Exterior Elevated Element. The sample size must be a “statistically significant sample” which gives the inspector a 95% confidence level that what they inspected is representative of 100% of the whole. The sample size is likely to vary from project to project; the more decks, the smaller the sample size to achieve the 95% confidence level. There will also be variation



*“The New “Balcony Inspection” Law”:
continued on page 2.*

*“The New “Balcony Inspection” Law”:
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based on the configuration of the project; Southern facing elevations are more weather exposed than Northern facing elevations, and top floor balconies are more exposed than those on lower floors, which are often partially shielded by the balcony above. There is also a qualitative component in addition to the quantitative aspect, because the inspector may increase the number of inspection locations if they find that water has passed into the system, creating the potential for damage.

The inspection is visual only, but must allow for inspection of the structural components themselves, not just exterior surfaces. The statute allows for the least intrusive method, but the inspection will involve removal of/cutting into exterior surfaces to expose structural components. Deck membranes may be covered by concrete, and joists may be hidden behind stucco or siding.

Because of the necessity of exposing internal structural components, the inspector will necessarily require the assistance of a contractor to provide access, and then to patch back exterior surfaces after testing. Contractors may also be able to install inspection hatches, removable vents, and other features to make future inspections more efficient. There is a misconception that the contractor involved in the testing cannot be the same contractor that performs repairs as recommended by the inspector, but that is not true; for apartments the inspection may be conducted by a general contractor, but the same contractor cannot perform repairs. That law does not apply to condominiums, however.

III The Report

The architect or engineer prepares a report of the inspections, which identifies the load bearing components and associated waterproofing, their current physical condition, and whether that current condition presents an “immediate threat to the health and safety of the residents.” This type of testing and report will be very similar to the investigations done and reports prepared in construction defect

claims.

The report must also specify the expected useful performance and remaining useful life, recommendations for necessary repair and replacement, and must be stamped or signed by the architect or engineer. The repair is then incorporated into the Reserve Study, and is an Association record, which members may access, and which must be provided to prospective purchasers of units. The report remains in association records for 2 inspection cycles (18 years).

If an imminent life safety threat is identified, then the inspector must provide the report to the Association immediately, and must provide the report to the local code



enforcement agency within 15 days. The Association must then take preventative measures immediately, including blocking resident access. Resident access cannot resume until the local enforcement agency inspects and approves repairs.

IV Inspection Costs

The costs for these inspections will vary widely depending on the configuration of the balconies, stair landings, breeze ways, and other components to be inspected. Decks with open joist bays and deck boards will be easy (and economical) to inspect. Decks with a walking surface covering the waterproofing, and cladding such as stucco covering the structural elements below, will require expensive destructive testing. Associations should work with inspectors and contractors as soon as possible to obtain an accurate estimate of their anticipated inspection costs; only with an accurate estimate can an Association properly set aside funds for future inspections.

Even setting aside the cost of any necessary repairs, these inspections will be a significant cost to the Association. However, as a necessary and required part of maintenance and reserve planning, the cost of the inspections themselves should be included as a reserve line item, allowing the Association to accumulate funds for future inspections. Additionally, for Associations under 10 years old, the cost of inspections and repairs can and should be passed to the builder under the Right to Repair Act process.

V. Best Practices

The first inspection is due by January 1, 2025, but don't wait. As that deadline approaches, the competent inspectors and contractors will be busy conducting inspections (and resulting repairs) for other Associations. There is a relatively small pool of experienced forensic architects and engineers, and contractors experienced in this kind of testing and repair. If the inspection is done early, these business partners will be more available, and the same will be true every 9 years as the new deadline approaches.

Whether your Association is new or old (the building in the Berkeley tragedy was 7 years old), it is impossible to know what the first report will say. That report will be available to all members, and will affect property values for years. If done early, there is time to perform repairs, and have a new post-repair report prepared; that later post-repair report can then be the official Civil Code 5551 report, minimizing impact on property values. Addressing repairs early will also reduce the cost of repairs (water related damage always gets worse and more expensive to repair, never better and cheaper). And, most importantly for newer Associations, any delay risks losing the ability to charge the cost of inspections and repair to the builder by letting the 10 year deadline to submit a claim run.

This new inspection requirement can have a significant impact on Association finances, but with proper (and early) planning, those costs and the impact to the Association can be controlled. ❖

"Assessments Too High?": continued from page 1.

argue the necessity to fund future needs (i.e. reserves) in an effort to keep assessments as low as possible now. However, as fiduciary board members it is important to realize that deferring the funding of reserves will have an adverse impact in the future. In addition, many people believe that obtaining the lowest cost on service contracts and maintenance work will save money for the association in the long term. This may be true, maybe not, or maybe it's a case of "you get what you pay for."

Many people assume that living in a single-family home is a better choice than living in a HOA community where there are monthly assessments. According to a former HOA board member who recently purchased a single family home, he states that "In reality, it may be less expensive to live in a common-interest-development (aka HOA) than it is to live in a single family home. While it seems that many may not take that position, especially at budget time, the reality is that it is more expensive to operate and maintain a single-family home than it is to live in an HOA."

This former HOA board member continues, "Based on our recent move, I thought I would pass on some information about the cost of living in a condominium versus a single-family home (SFR). Living at the condominium and being on the board we always hear from some owners that the HOA dues are expensive, even though as board members we know the budget is real and pays for a lot of services

that if we owned a home we would have to pay out of pocket. I hear from non-condo owners that HOA dues are a deterrent to living in a condominium. However, from my recent experience it is not that bad. The monthly costs for my new home consisting of insurance, water, trash, electrical, gardening and reserves equals the monthly assessments at the condo."

...it is more expensive to operate and maintain a single-family home than it is to live in an HOA.

An example of the economics making better sense in a HOA pertains to the pool. The cost to maintain a pool, whether in a HOA, or in a SFR is the roughly the same. However, the cost of pool maintenance is borne 100% by the SFR owner, and obviously shared between multiple owners in a HOA. Paying for your pool in your association may cost each owner \$5.00 to \$10.00 per month; however, that number goes to \$100.00 a month, or more, if you had your own pool.

There is another economic advantage of condominium ownership as opposed to a single-family home (SFR). In an area south of Colorado Blvd. in Pasadena, the average cost to purchase a 1400 sq. ft. condominium in early 2020 is \$780,000.00, while the cost to purchase the same square footage in an SFR in the same area is almost \$200,000.00 higher. That difference in value would cost about \$800.00 per month more

for the SFR in mortgage payments each month.

The great challenge for HOA boards is to agree on a budget that will address all the needs of the association. Many boards have found that consistent and incremental small increases each year makes the best sense so the impact of a large increase at one time can be avoided. The issue of increasing assessments is a way of keeping up with the maintenance of the property, which gradually deteriorates over time and with the increasing costs of operating the property. It is tempting to look at the current year, that has been financially challenging, and attempt to avoid meeting the ongoing financial realities of the association. The association must be run like a business and not a charity. There will always be owners who face financial difficulties, and the board can always work with owners who are having financial challenges to structure payment plans.

While talking about money and financial issues is never comfortable to discuss with your neighbors, it is best to maintain the position that small regular increases are necessary.

For many people their home is their greatest investment, and when it is time to sell you will experience the best return if you have maintained your property well, both the interior, as well as the common areas. ❖

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**Reserves To The Rescue?
Carefully Tapping Reserves In A Time Of
Financial Crisis (Covid-19)**
By Robert Nordlund, PE, RS, Founder/CEO, Association Reserve
www.ReserveStudy.com



“Can we use Reserves to cover an Operating Fund shortfall?” is a question we are asked all the time. Under normal circumstances, our standard response would be an emphatic “No!”, because Reserves are for major repair and replacement projects. But now, in a time of (inter)national crisis, Reserves may play a valuable additional role at your association.

In March, our country began the process of “closing down” to prevent the rapid spread of the COVID-19 pandemic, which caused a rapid spike in unemployment. That means associations are, or will soon be, experiencing higher than normal assessment delinquencies. With tight budgets even in good times, rising owner delinquencies put the short-term financial health of associations at risk. Yes, the roof might still need to be replaced in 5 years, but management, insurance, and trash bills all need to be paid now! In times like these, Reserve contributions and the Reserve Fund can also be used to help offset a disruption to essential operating cash flow. But it must be done with caution and care.

Even in the midst of uncertainty, boards still need to act and make wise financial decisions to lead the association. Faced with difficult decisions, the “right” answer *may not be clear*, because standard “best practices” may not apply. Fortunately, boards can limit their liability exposure when making “non-standard” decisions by following the three-step process which flows from the “Business Judgment Rule” if the documentation shows that the board acted:

- In good faith
- In the best interests of the association

- After appropriate due-diligence (seeking wise counsel)

What do we do first?

First, make sure you’ve gathered current financial information (financial reports with bank balances, year-to-date budget, Delinquency report, your most recent Reserve Study), begin your belt-tightening, continue your collection (and communication) efforts, and get in touch with your legal counsel (to find if you have any state-law or governing document limitations). Trying to solve the problem with Reserves is not your first step.

What are the Board options?

There are three ways Reserves can help rescue the association in a financial crisis:

- Conserve Cash (defer Reserve projects)
- Re-Allocate Cash (Reserves to Operating)
- Save Cash (bargain shop)

Conserve Cash (Prioritize your Reserve expenses in 2020)

In a time of financial scarcity, a standard good rule is to minimize your spending. But not all Reserve projects are equal. Prioritize your 2020 Reserve projects - don’t defer projects that will expose owners to even greater problems or expenses! Defer “inconsequential” Reserve projects (new carpet in the rear stairwell), and double-check before replacing the perimeter wood fence (can it last another year with a few repairs?). While the lobby remodel may be a significant “first impression” project for owners and guests worth keeping on schedule, with the clubhouse closed is this really the time to spend \$50,000 on its remodel? If cash permits, go ahead with the remodel (it might be a great opportunity to do the remodel when no one is using it), but if cash is tight, defer it to 2021. And anything like building painting

“Reserves To The Rescue?": *continued on page 5.*

"Reserves To The Rescue?": continued from page 4.

or roofing related to maintaining building integrity? Do them. Don't make things worse by risking expensive problems like dry-rot or water damage that could have easily been prevented. Similarly, projects that protect the best interests of the owners (like the central hot water heater, or automobile gate mechanism) are projects that you should perform on schedule. Make sure you spend precious Reserve cash only on projects in 2020 that cannot be readily deferred to 2021. And remember... deferred projects don't represent savings. You'll still need to do those projects next year.

Re-Allocate Cash

If your Reserve contributions are anywhere close to the 25% of total budget that most associations find is necessary to offset ongoing deterioration and avoid special assessments, perhaps you scale back for a few months. Dropping your contributions by 10% down to 15% immediately offsets a 10% increase in delinquencies. The same effect could be achieved by deferring Reserve contributions for a few months. You could also consider a zero-interest loan from Reserves to Operating. Consult with legal counsel and your Reserve Study provider regarding these three options... which might be the best "fit" for your current needs, in light of your contribution size, Reserve Fund size, and upcoming Reserve projects. Run some cases on your Reserve Study software or ask your Reserve Study provider to run some cases to document the plan (both the borrowing and

the repayment). No guessing! That repayment might take the form of a single or multi-year special assessment, or higher future Reserve contributions, all of which might be minimized by higher-than-normal transfers to Reserves next year when delinquent owners resolve the funds owed to the association.

Save Cash

Certain industry sectors are offering significant savings at this time, particularly those projects with a high labor component (roofing, painting, asphalt...). If the cash is available, now might be a great time to check with your service providers. You may be very encouraged to "stimulate the economy", keep their crews working, and enjoy a 5-10% discount on some of the association's larger projects. Just be careful when updating your Reserve plan, as discounts available in 2020 will likely not be repeatable in future years.

How do I Respond?

Gather information. Confer with your legal counsel. While documenting your process, conserve cash (Reserves) by prioritizing and only spending where the projects have true merit, re-allocate cash going into Reserves or already in Reserves (remember to create a repayment plan), or save cash by performing some Reserve projects now. Make decisions that are in good faith, in the best interests of the association, and after investigating your options. And one of those options may be a new and valuable use of Reserves!



With Passage Of New Law Under Assembly Bill 3182, Coming In 2021, HOAs Lose More Independence
By Kelly G. Richardson, Esq. CCAL

Assembly Member Ting from San Francisco authored Assembly Bill 3182. The bill was amended several times, but was approved on September 1st by the Legislature and awaits the Governor's signature before becoming law on January 1, 2021.

The bill was promoted as a way to help housing supply but will create many problems for California HOAs.

The new law will outlaw full rental bans in HOAs. A new Civil

"With Passage of New Law Under Assembly Bill 3182...": continued on page 6.

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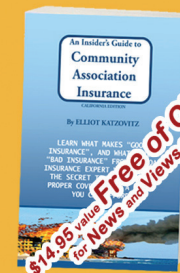
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"With Passage of New Law Under Assembly Bill 3182...": continued from page 5.

Code Section 4741 is created, and it will void any HOA rental limits below 25% of all members. Therefore, any HOAs which presently have a rental cap of less than 25%, including of course also a cap of zero (a full ban), will have those limits become unenforceable next year. HOAs will be permitted to have rental caps of 25% or more of all memberships. Rental caps are normally imposed by HOAs after they are voted upon by the homeowners within the community when they amend their CC&Rs, the contract binding them together. The Legislature has overridden this.

HOAs will specifically be allowed to ban rentals of 30 days or less, but the law will not allow HOAs to have "unreasonable" restrictions on rentals of homes, accessory dwelling units, or junior accessory dwelling units. The law does not define or give examples of what would be considered unreasonable. However, if the HOA is found to have an unreasonable restriction, it could be liable for a \$1,000 civil penalty as well as attorney fees to the complaining party.

There are many different rental requirements HOA memberships often approve by at least a majority vote. For example, a one year minimum lease term, or a waiting period of one year before a new owner can rent a home, or the requirement that the tenant promise to abide by the HOA rules—are any of those "unreasonable"? We do not know. The issue of "unreasonably restricting" rentals is a vague standard, which could lead to litigation between homeowners and their HOA, since the definition of "reasonable" in this context is not obvious to all.

Associations choose to adopt rental restrictions for many reasons. The most common reason is to preserve a higher quality of resident, based upon the belief that owners will take more pride in their home and will behave better than tenants. Another common reason is availability of FHA and FNMA-backed mortgages, since FHA and FNMA will not allow HOA rentals to

exceed a certain maximum amount.

One truly amazing requirement of the new law is that all California HOAs (all 50,000+ of them) must amend their CC&Rs to conform to the new law before the end of 2021. Most HOAs have a very hard time obtaining sufficient participation to amend their CC&Rs and bylaws (no matter how out of date they are). Will HOAs be forced to spend the management and legal cost to at least try for amendments in 2021, so they avoid the risk of being found to have willfully violated the new statute? Apparently, the answer is yes. This is one of the most troubling requirements of the new law, and one that is going to take some thought.

The most negative part of this law is a new amendment to the Government Code, which says that if a local building and safety department does not process and approve a building permit for an accessory dwelling unit or junior accessory dwelling unit, the permission is automatically granted after 60 days. So, public safety and building code compliance is apparently taking a back seat to the rush of California encouraging ADU's and JADU's.

As with last year's SB323, AB3182 is another new idea which does not reflect the complexities of the existing law and disrespects the right of homeowners to manage their own communities as they see fit. Why do Legislators not seek input from the organizations which educate HOAs, such as Community Associations Institute, or ECHO, before tinkering with HOA law?

AB3182 passed the Assembly on June 11 with a substantial number of "no" votes and passed the Senate on the September 1 deadline. The bill is awaiting the Governor's signature, and Newsom is expected to quickly sign the bill into law. To review the bill or any California law, visit www.leginfo.legislature.ca.gov.

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Is The Handyman An Employee? AB5 May Increase HOA Payrolls

By Kelly G. Richardson, Esq. CCAL

Traditionally, many businesses often hire part-time or occasional workers and characterized them as “independent contractors.” The IRS and State Franchise Tax Board had guidelines to help determine who was an employee and who could fairly be called an independent contractor. There were many factors which played a role in that characterization.

HOAs often hire persons they considered “independent contractors” to perform specific maintenance, repair, or other routine tasks. This avoided payroll tax withholding and other legal obligations.

All that began to change in 2018 with a California Supreme Court case called *Dynamex v. Superior Court*, in which the traditional test of employment vs. independent contractor was replaced with a simple 3-part test, often called the “ABC” test. That ruling was incorporated in Assembly Bill (AB) 5, which was quickly signed by the Governor after passing the Legislature. AB 5 creates a new Labor Code Section 2750.3 and affects any hirer, including HOAs, using “independent contractors” which might be reclassified as “employees.”

This new statute adopts the “ABC” test, which determines a worker as an independent contractor if: A) The hirer actually and contractually does not control or direct the person in the course of their work; B) The work performed is outside the hirer’s normal business; and C) The worker also normally and independently performs that work for others. If the hired person meets all of those three requirements, they can be treated as an independent contractor. As before, the element of control over how the person performs their work is key.

Some HOA service providers are expressly exempted from the law, such as attorneys, architects, engineers, and accountants. The more concerning area for associations is hired persons working on the HOA property and paid by the HOA.

One example of an independent contractor would be the plumber who is called to come fix a leak. The plumber is not supervised or told how to perform the repair. The plumber normally works for others as well, and the HOA’s business is not plumbing.

On the other hand, a less clear answer might apply to maintenance

or janitorial workers paid by the HOA. Such workers often are given direction by the manager or board. Furthermore, since the HOA’s job is to maintain the common area, isn’t general property maintenance and cleaning part of the HOA’s “business?”

The conversion of workers to employee status may create sick leave and other obligations for the HOA, including payroll withholding duties. An employee might try to contest their termination, or allege discrimination. Also, employees are subject to Fair Employment and wage and hour laws. Associations should obtain advice from their insurance broker regarding workers compensation coverage.

There will be public resources educating HOAs and managers on the difference between employee vs. independent contractor status. The California Department of Industrial Relations is developing a pertinent web page, but it unfortunately is not ready at present time (www.dir.ca.gov/dlse/faq_independentcontractor.htm). The California Chamber of Commerce has information available at www.calchamber.com.

Managers and their boards should be aware of the simpler standard and avoid erroneously calling workers “independent contractors” if the law does not support that status. Also, remember that personnel (employees) discussions are for closed session, while independent contractors are vendors and should be discussed in open session.

Kelly G. Richardson Esq., CCAL, is a Fellow of the College of Community Association Lawyers and a Partner of Richardson | Ober | DeNichilo LLP, a California law firm known for community association advice. Submit questions to Kelly@rodllp.com. Past columns at www.HOAHomefront.com. All rights reserved®. ♦



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HOA BOARD MEMBER EDUCATION

Education for volunteer HOA board members is essential for success as board members. Due to the ever-increasing complex and changing nature of the laws and regulations that impact common-interest-developments staying on top of these changes greatly increases a board's member ability to succeed in their role, and operate in confidence

There are several ways for board members to be educated, and Beven & Brock offers two free ways.

Upcoming events:

Board Training (not currently scheduled)

Free three-hour training course for current and prospective HOA board members. A course syllabus, informational handouts, and Certificate of Completion are provided. This CAI-sanctioned class is taught by its co-creator Kelly Richardson, Esq. CCAL of Richardson Ober DeNichilo LLP, and is co-sponsored with the Community Associations Institute. Seating is limited, and reservations may be made by emailing: BoardTraining@bevenandbrock.com. Priority is given to current Beven & Brock managed associations due to space limitations. You may get on the waiting list and when we set new dates we can let you know.

October 2020 Due to COVID-19 uncertainties, there is no scheduled event for the remainder of 2020 at this time.

A RESOURCE AVAILABLE FOR HOA BOARDS!

Beven & Brock is pleased to announce the availability of a new resource for Homeowner Association Boards to find information on topics of interest as needed on demand. Over 135 articles have been taken from prior newsletters and gathered in one place, located at <http://www.bevenandbrock.com/topical-article-library/>. The topics are organized into categories, such as Legal, Meetings, Board, Reserves, Insurance, Community, Elections, Maintenance, Management and other subjects.

This area of the website requires a simple one-time registration, and once that is completed, you can freely access a number of articles on a variety of topics that have appeared in *HOA News and Views* over the past eight years. This resource will help HOA Board members to become educated in an easy and accessible way. The goal is to help boards make well-informed decisions in a variety of challenges that they may encounter.



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