

## When a Critical Component Fails Early

**I**t happens to even the most prepared of associations. The roof that was supposed to last 25 years starts leaking after only 15. A harsh winter takes its toll on the parking lot and you're suddenly faced with a large re-paving project 5 years before anticipated. The elevators in a high-rise are constantly out of order, despite their being only 20 years old. These items will need to be immediately replaced or extensively renovated – which means unexpectedly using a significant portion of your reserve budget.

When key common elements fail early, a number of factors will help determine what to do next and how to pay for it. A board member or property manager's primary responsibility is the protection and enhancement of the association's investment.

### **Why the failure?**

Understanding the cause of the damage or failure will be crucial in determining how to pay for it. You may be able to prevent similar or recurring failures as well. Your contractor or engineer should be contacted to immediately investigate the circumstances of the component failure. There are several potential causes for such failure.

If used more frequently (think indoor pools or a multi-unit furnace during a harsh winter), it is not that uncommon for an item to show wear and tear sooner than anticipated. Changing usage patterns, while usually a suitable reason to "borrow" from the reserve fund, will require an adjustment both to your reserve study and to the monthly assessment for this particular item.

Additionally, shoddy workmanship and materials may be a valid reason to use

additional reserve funds. The siding may have been installed improperly and resulted in water intrusion, or the roofing materials and construction practices were substandard, leaving rotted patches or missing shingles.

Mitigating factors, such as extreme weather, or an emergency, such as a flood or fire, can also wreak havoc, even after the initial cleanup and repair are done. In this case (and in those of poor construction quality), consult with your association insurance provider immediately.

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**Before moving ahead with an unplanned repair, it's important to look at the "why" of the failure.**

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### **Was the component in the reserve study?**

If the element was part of a recent reserve study, take a close look at what portion of the budget you have set aside for it in relation to the other elements. What was the estimated useful life, and by how much did it fall short? By shifting capital expenses, it's possible that your reserve budget will have enough to cover an immediate replacement or major repair, which takes care of the urgent problem.

### **What if there are inadequate or, worse, no reserves for this component?**

Although this is a rare occurrence, especially if your reserve study complies with AICPA and CAI standards, it's possible that this failed component was left out of the reserve study. (An example would be termite damage in decks, which are often limited common elements.) Before

moving large amounts of money around, discuss the options with your association's accountant.

If the money simply is not there, your accountant will explain the available options under your state statutes, such as a loan or a special assessment. Looking to the future, it's a good idea to keep the CAI Best Practices in mind when undergoing your next reserve study update. CAI recommends practicing "threshold funding." Keeping the reserve balance above a specified dollar or percent funded amount (the threshold) will create an allowance for unexpected events.

### **What's the first step in getting it repaired?**

When you're ready to move forward with repairing or replacing the affected element, hire a professional engineer to write a specification for the project. You will find that simply soliciting bids from local contractors for projects may generate a wide variety of proposals. The disparity is due to differences in each contractor's approach and the products and materials they choose to use. Starting with a performance specification provided to all contractors will enable you to make "apples to apples" comparisons.

### **Finally...**

Be sure to update your reserve study soon after the repair or replacement, as it should reflect the remaining useful life of all components as accurately as possible. This unexpected use of funds could significantly harm the strength of your reserve account and drop the association to a dangerous "percent funded" level. The engineer who performed the initial reserve study will be able to determine any adjustments to the current reserve plan.

# Do You Have All the Pieces to the Puzzle?

**W**hen a home in a community association changes ownership, a unique opportunity presents itself. Essential information regarding governing documents and bylaws that may not have been communicated to the previous owner can now be properly presented to the new residents. It's up to both the real estate agent and the association management to "pull the pieces together" for the new owners in a clear, concise manner.

One way to accomplish this is for the association to conduct an orientation for any real estate agent who is considering or has a current listing for a home in the community. The meeting would include both a detailed explanation of the bylaws and CCRCs and, just as important, the culture and "feel" of the community. In some associations, for example, children's toys on the front lawn may not be expressly prohibited, but many families prefer the look of a clean lawn, and store toys in the garage or attractive sheds. Be sure to review all materials before handing them over to new residents or an agent; all documents should be up-to-date and easy to understand. You can also let the agent know of any neighborhood-wide festivities such as summer BBQs or winter festivals that would be a sure draw to community-minded residents.

The real estate agent then has the responsibility to impart all pieces of information to potential residents. The new owner must understand fundamental items such as monthly assessments, the financial health of the reserve and operating accounts, and exactly what physical assets are owner responsibility vs. association responsibility.

Suggested roles and responsibilities are in the following chart:

## The Real Estate Agent

- Manage expectations
- Provide full disclosure

Provide buyer with an understanding of:

- Bylaws
- CCRCs
- Management structure
- Operating budget
- Reserves
- Transition (if appropriate)
- Approval process (if appropriate)

## The Community Association

- Manage expectations
- Maintain current information

Provide the real estate agent with:

- Complete documents
  - Historical data
  - Contact issues
- Approval process (if appropriate)

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