SOUTH COAST HOMEOWNERS ASSOCIATION

P. O. BOX 1052, GOLETA, CALIFORNIA 93116
(805) 964-7806
www.southcoasthoa.org
gartzke@silcom.com

Volume 19, Number 3 **May 2006**
Michael J. Gartzke, CPA, Editor

IN THIS ISSUE

Upcoming Meetings – May 23/July 24-25
Publications Available from South Coast HOA
Investing Association Cash
Workers Compensation Insurance – A Mandatory Purchase
The Uncertain Future of Common Interest Developments – Part II
South Coast HOA Featured in the *Santa Barbara News-Press*
Newsletter Sponsors

UPCOMING SOUTH COAST MEETINGS

An evening with Skip Daum, Administrator/Advocate for Community Association Institute's California Legislative Action Committee (CAI-CLAC). For many years, Mr. Daum has lobbied on behalf of Community Associations to the California Legislature along with the Executive Council of Homeowners (ECHO) and the California Association of Community Managers (CACM). Based in Sacramento, Mr. Daum supports appropriate legislation and works with legislative staff and other lobbyists to revise and/or oppose legislation that is not in the best interests of community associations, their boards and their members. Learn about the legislative process, what other groups lobby the legislature on association issues, pending 2006 legislation, why the legislature has such a poor opinion of association board of directors and much, much more. Learn how you can participate in the process and get involved.

Tuesday, May 23, 2006
Holiday Inn, Goleta
5650 Calle Real
7PM

Annual Summer Legal Forum with Beth Grimm. Beth has provided our popular summer legal forum for us since 1999. While the topics for this year's event have yet to be determined, we do have the dates set so that you can mark your calendars.

Monday - July 24 – 7 PM – Holiday Inn, Goleta
Tuesday – July 25 – 7 PM – Quail Meadows West HOA, Santa Maria (New)

PUBLICATIONS AVAILABLE FROM SOUTH COAST HOA

HOA 101 – Course Materials – We have about a dozen of the course books from the HOA 101 seminar given last month. The course material was developed by ECHO for its HOA University class given each year. In addition, our speakers provided supplemental material for the seminar and some of the books contain that material as well. Postpaid Cost - **$15.00 per book.**

We also have 5 of the **2006 ECHO Community Association Statute books** remaining. These 8 ½ x 11 books contain the California laws that you will most likely encounter in operating your association. Postpaid Cost - **$10.00 per book.**

These will not be reprinted or reordered when sold out. First come, first served. Available by mail or for pickup at 5669 Calle Real, Goleta.

2006 Condominium Bluebooks – Our supply has sold out. Additional books are available from the Publisher, $22 for 1 and $20/each for additional copies. Piedmont Press, 2200 Powell Street, Ste 990, Emeryville, CA 94608; Tel 510-595-8400; www.condobook.com

INVESTING ASSOCIATION CASH

MAKE THE MOST FROM YOUR RESERVE FUNDS WITHOUT UNNECESSARY RISK

By: Michael J. Gartzke, CPA

I last visited this topic in the newsletter back in September 2004. Since then, short-term interest rates have increased substantially. An expanded discussion of association investment options follows.

After 2001, interest rates declined rapidly. Interest on association checking accounts virtually dried up and savings and money market account rates declined as well. One well-known brokerage, money market fund paid 0.05% on its money market fund in December 2003. Today, interest rates on checking accounts are still negligible, maybe 0.1%. Savings and money market accounts vary greatly from 3.5% to less than 1%. Many associations tend to leave funds just sitting in these low interest accounts. In September 2004, a good interest rate on a one-year certificate of deposit was 2.8%. The same one-year certificate today can yield over 5%. Compared to a 1.5% money market fund, an association could earn an extra $3,500 (before income taxes) for every $100,000 invested.

As many of you know, I have started to track selected financial information from all the associations that I perform financial statement reviews for (54). One of the items I am tracking is investment income compared to ending cash balances of each association and computing a rate of return. The data is historical. While a fair amount of 2005 information is in the database, there is also a lot of 2004 information waiting to be updated during the year. Rates of return on association funds at this time:

0 – 1% - 22

1 – 2% - 15
2 – 3% - 14
3 – 4% - 3

The median rate of return, where half the rates are higher and half the rates are lower, is 1.27%.

Associations always maintain funds in an operating checking account and should have some funds in a money market checking account to pay reserve expenses that will earn very low interest in today's market. What tends to happen is that some associations keep more funds in a lower-paying money market/savings account than are needed, simply because it's convenient. It does take some effort to invest association funds, even if in certificates of deposit. For example, board members who are authorized to sign checks have to take time out of their busy personal schedule to set up each new CD investment and get signature cards. There is also more accounting overhead involved in having more numerous investments to track.

The Federal Deposit Insurance Corporation insures funds invested in certificates of deposit up to $100,000 per financial institution. So for associations with substantial reserves, how can the association obtain FDIC coverage on its investments?

1) **Multiple banks –** Certificates can be opened at more than one bank. While this allows the association to shop its funds to obtain the best rates, it can be inconvenient. Each bank will require a signed signature card, personal information about the check signers, board resolution authorizing the investment, etc. Banks will cite stronger Federal laws to thwart money laundering and terrorist activity. Different banks will interpret these laws differently so check to see what documentation is needed by the bank prior to placing the investment.

2) **Funds sharing –** Some banks have subsidiaries or have entered into agreements with other banks to share funds to allow for more than $100,000 insurance. If you wish to deal with one bank to invest funds greater than $100,000, ask them if they participate in a shared funds arrangement.

3) **Brokerage account –** Certificates of deposit can be purchased through a stock brokerage account. Certificates purchased through the brokerage are insured. Through a brokerage account, you might acquire certificates from banks other than in your local area. Some brokerage accounts have annual account fees of up to $300. Be sure to find out what these fees are before placing any funds.

4) **"Liquid CD" –** These accounts provide the ability to transfer funds in and out during the investment period without incurring a penalty while maintaining a minimum investment amount. Rates are typically higher than money market accounts but lower than CDs. This type of CD would be attractive to an association that is funding its reserves monthly but has no immediate need for expending reserve funds. Should funds be needed to pay reserve expenses, then a penalty-free transfer could be made to a checking account to pay expenses.

If certificates are redeemed before maturity, an interest penalty will be imposed based upon the length of the investment. With increasing interest rates, that penalty could be substantial. CDs held in a brokerage account can be resold prior to maturity. However, if interest rates have increased since the CD was purchased, its fair market value will be less than what you paid for it and the association could incur a loss. (Conversely, if interest rates decline, the fair market value of the CD would exceed the cost, resulting in a gain on sale). If you have a large reserve expense in the next 12-month period, make sure your Treasurer tracks certificate maturation dates and withdraws the funds at the right time before the funds are needed in a penalty-free manner.

"Laddering" – Associations that have enough funds to spread them over several CDs can use "laddering" to increase the yield from its investments. While in today's interest rate market, there is not much difference in the short and long-term rates, that is not always true. Typically, rates are higher for longer-term investments. For example, an association could take $100,000 from its money market account and purchase four, $25,000 CDs. These CDs would mature in 3,6,9 and 12 months. When the first one matures, that CD can be reinvested for 12 months as the remaining three CDs have moved "up the ladder" and will mature in 3,6 and 9 months. After nine months, all the association's CDs will be invested for 12 months and 25% of the associations will be available every 90 days.

Treasury Bills and Notes – These can be purchased from some banks and brokerages with maturities ranging from 3 months to 30 years. They can also be purchased directly from the Federal Government through the Treasury Direct program. For most associations, interest on Treasury Bills and Notes is state-tax free (typically 8.84% tax rate). If a CD and Treasury Note are paying the same rate, the association will generally keep more of the interest from the Treasury investment since the taxes are less. Redeeming a Treasury Note or Bill prior to maturity will subject your association to market rate risk. If interest rates rise, the value of your note falls to yield the higher market interest rate to the buyer.

"Government" funds are different than "Treasury" funds. Government funds may include mortgage-backed investments such as FNMA, GNMA or Federal Home Loan Bank funds. Income from government funds is subject to tax. California municipal bonds are tax-free. The typical association pays tax on its net investment income at 23.84% total. Municipal bonds will yield less than taxable investments. You will need to factor taxes in to see if municipals are an appropriate investment for your association.

Mutual Funds – Mutual funds are subject to the performance of the stock market and the interest rate environment. They carry risk of loss of principal. Even funds that are conservatively invested can generate poor results. One association's funds were recently invested in a "name company" short-term government bond fund. The December statement showed that the fund was yielding 3.8% at its current per-share price. However, the fund's per-share price had declined since the first of the year. When the decrease in market value of the fund was applied to the investment income received, the yield dropped to 1.8%. The association paid income taxes on the total investment income reported but could not deduct the decline in market value against the income.

The Davis-Stirling Act does not mandate how associations invest their funds. The corporation code specifies a *"business judgement rule"* that allows boards to access the advice of experts in determining what investments are appropriate for your association. The

Davis-Stirling Act does require the entire board to review all investment account statements at least quarterly as part of its duties. The board should consider adopting an investment policy outlining what investments are approved by the board incorporating the factors noted above – type of investments, risk, length of investment, tax impacts, investment ratings, etc.

Workers Compensation Coverage for Common Interest Developments — A Mandatory Purchase

By Timothy Cline, CIRMS, Timothy Cline Insurance Agency, Inc., Santa Monica, CA

Tim's contact information appears at the end of the newsletter. He is a South Coast member, sponsor and contributor, most recently at our HOA 101 Seminar

Truman and Gail Lawson had an unwieldy 50-foot palm tree in their front yard and they wanted it trimmed. It seemed like an easy task. The Lawsons hired Eliseo Lascano, owner of Anthony's Tree Service, to perform the work. Lascano agreed to charge the Lawsons $450 and assigned Miguel Fernandez, one of Lascano's employees with more than four years' tree-trimming experience, to the task. Unfortunately, Fernandez fell from the tree while performing the work sustaining serious injuries.

The California Business and Professional Code requires a contractor's license to trim a tree measuring 15 feet or more. (Bus. & Prof. Code, § 7026.1, subd.(c)). Despite apparent misrepresentations to the contrary, neither Lascano, nor his company, Anthony's Tree Service, were licensed. *State Compensation Ins. Fund v. Workers' Comp. Appeals Board* (1985) 40 Cal.3d 5, 12-16 Labor Code, makes an unlicensed contractor who is performing work for which a license is required an employee of the hirer of the unlicensed contractor, for the purpose of workers compensation. In other words, the Lawson's, by hiring an unlicensed contractor to do the work, had now automatically become the injured worker's employer.

Could the above scenario occur at a common interest development? Absolutely. Despite the constant and well-intentioned warnings of cautious community managers, Boards of CID's often hastily hire vendors to do work and never think of confirming the existence of the vendor's workers compensation policy. California law requires ALL employers to maintain workers' compensation insurance - California Labor Code, Section 3600(a). Furthermore, nearly every set of CC&R's require a Board of a common interest development to purchase workers compensation coverage "to the extent necessary to comply with applicable law."

Nevertheless, many Boards ignorantly argue the coverage is unnecessary thinking that an injured worker will "be covered somehow." Unfortunately nothing could be farther from the truth.

If Miguel Fernandez were injured at a common interest development, could he sue the Association and seek coverage under the Association's general liability coverage? No. All general liability policies covering community associations contain specific exclusionary language which eliminates coverage for "any obligation" of the Association "under a workers compensation (sic) law." (ISO Language — 1992— CG 00 0110 93)

If the Board is sued by the homeowners for failing to purchase coverage, surely the Board would have coverage under their Directors & Officers Liability policy. Unfortunately, again the

answer is “no.” Consistent in every Directors & Officers Liability policy is a specific exclusion for any claim “arising out of, directly or indirectly resulting from or in consequence of, or in any way involving”.., bodily injury or sickness — whether workplace related or not. In other words, if the Board is sued for a failure to maintain workers compensation coverage, they will find themselves without any benefit of D&O protection.

A Workers’ Compensation policy covering a management company can only protect that single entity. (In order for a second entity to be named on a Workers Compensation policy, it must own at least 50% of the stock of the second entity). As a result, the Workers’ Compensation policy covering a management agent cannot be modified or endorsed to extend to a homeowners association client. If the injured individual is deemed to be the employee of the Association, we couldn’t rely on the management company’s workers compensation coverage to protect the community association client.

Since there is actually no “cap” to the benefits paid out on a workers compensation policy, failing to maintain coverage could potentially cost the Association hundreds of thousands of dollars. But the disruption could impact more than just the Association’s pocketbook - a claim could result in preventing homeowners from selling, transferring or refinancing their home.

When an employee is injured while working for an Association who has failed to maintain workers compensation required by law -- and the Association fails to pay or post a bond to pay the compensation due the employee -- the employee’s compensation is paid from California’s Uninsured Employers Fund. The State will then place a lien on the Association for the same amount paid as compensation to the injured worker. No units within the development could be sold or refinanced until the lien is satisfied.

Case law surrounding the issue of employment has consistently held that the most important element in establishing an employer/employee relationship is one of ‘control.” Despite holding him/herself out as an independent contractor, if the Association controls the details of the work performed and the injured worker has no other workers compensation coverage, it is a virtual certainty that the Workers’ Compensation Appeals Board (WCAB) will find that a worker is an employee of the Association and not an independent contractor.

California Labor Code Section 3202 requires that workers’ compensation law be “liberally construed by the courts with the purpose of extending their benefits...” and this consistently happens with questions of employment. If an “independent contractor” does not otherwise have workers’ compensation insurance, the courts, believing they have an obligation to award benefits, may liberally construe the law to find that the common interest development was the employer.

The question is, “How can the association or manager prevent itself from being considered an employer?” Hiring only licensed contractors who maintain their own workers compensation coverage is the single best defense against being roped into an unwanted workers compensation claim.

South Coast Homeowners Association – May 2006

The Uncertain Future of Community Associations Thoughts on Financial Reform – Part II

Author: Tyler P. Berding, Esq.
Berding & Weil, LLP

Editor' Note: Starting in 1999, Mr. Berding wrote a series of articles that appeared in the Executive Council of Homeowners (ECHO) Journal reflecting upon the future of common interest developments. Recently, Mr. Berding re-edited the articles into a small book. With his generous permission, we will serialize the book in successive issues of the newsletter to provoke further thought and discussion on the topic. Mr. Berding received an M.A. and Ph.D. in Government from the Claremont Graduate School and his J.D. from the University of California at Davis. He can be reached at tberding@berding-weil.com.

Part I outlined the concepts of obsolescence of association property, inadequate funding to replace property and four stages of life in a community association. Part II examines obsolete associations.

BEYOND THE FOURTH STAGE

Beyond the Fourth Stage, a project's fate is hard to predict. Certainly, if the deterioration of the physical condition seriously effects habitability, health, and/or safety, local jurisdictions will be forced to intervene and will demand that those conditions be repaired. Given that the lack of ability to reach consensus on funding is the reason that these conditions have been allowed to develop, it is unlikely that the owners, now mostly absentee, will see any point in throwing "good money after bad?' Their cash flow and equity may be non-existent or negative, and the condition of the project makes a sale impossible. They continue to hold their interest in the property only because they receive rental income. The local jurisdiction may condemn some or all of the buildings, accelerating the onset of obsolescence. Absentee owners, deprived of rental income, will simply walk from the project and abandon the property. Resident owners without alternative housing will stay as long as the local jurisdiction will permit occupancy. Criminal activity will make it difficult for anyone to continue to occupy the premises. Redevelopment or other government-backed programs might be called upon in rare cases to rehabilitate the property. However, in most cases, the project will be value less, uninhabitable and unsaleable. Continued ownership will become a clear liability to the remaining investors and wholesale abandonment will ensue. In most cases, legal title to the separate interests will default to various lenders.

An example of such a project was observed in San Bernardino, California several years ago. It consisted of fourplex condominium buildings, approximately 35 years old, now gone beyond a Stage Four. Units were boarded up on burnt out. Whole buildings had been bulldozed and only empty lots remained. There were a few inhabitants, possibly squatters. The surrounding neighborhood was in only slightly better condition, but fully occupied, lessening the chance of a municipal re-development project. The varied condition of the units suggested that they remained under separate titles. The complexity of titles, including the interests of lenders, most likely precluded any uniform scheme to convert the property to a better use.

LESSONS

The modern community association had its birth about forty-five years ago. The average project is probably now about twenty to thirty years old. The four stages of evolution can occur over a life span of up to perhaps forty years, but more likely, signs of obsolescence will begin to appear much earlier. These statistics suggest that the beginning of a serious problem of obsolescence is just now upon us, with its greatest impact to be felt over the next ten to fifteen years.

What lessons are there to be learned? Other than the obvious, the need for prudent financial and business management of each community association, this situation also argues that quick financial fixes maybe illusory. It also suggests that owner equity may often be a lot less than believed, especially if there has been insufficient attention paid by the board or management to periodic inspection, including intrusive testing where appropriate.

The most important lesson may be, however, that the concept of communal responsibility for complex residential real estate is fundamentally flawed. In most states, assessments are essentially voluntary beyond certain basic minimums. Homeowners tend to view increases or special assessments through a veil of self-interest. A first-time buyer may not intend long-term ownership and hence be unwilling to contribute to reserves which may not be used for repairs until well after his expected departure. Owners on fixed incomes have obvious limitations on their ability to pay for repairs. Since they have no ability to negotiate for more affordable repairs, they may simply veto the funding request altogether. Other owners will view the repair-funding request with varying degrees of enthusiasm, or lack thereof, depending entirely upon their individual circumstances and the extent of their understanding of the problem.

OWNERSHIP CYCLE

Reservations about further investment in the property are exacerbated by the ownership cycle. The average length of ownership of an interest in a community association is seven to eight years. Since reserve budgets for long-term repair of such items as roofs and siding frequently project actual repair of those items fifteen to twenty-five years in the future, the average owner can see little advantage to investing in reserves since they won't likely be around to seem them spent. Further, since the lack of adequate reserves is a difficult problem to appreciate, it is difficult to disclose. A prospective buyer, unless he or she is very well informed, will not be able to analyze the financial condition of the reserve account. Therefore, the condition of the long-term reserve may not play any role in a purchase decision since it is not perceived as an asset. If that is the case, owners will not be motivated to improve that "asset'. From their point of view, they are better off investing in personal items, such as new carpets or drapes.

In short, one of the factors that makes single family detached homes such an attractive and perennially solid investment, the right of individual judgment and action on maintenance and repair issues, is conspicuously absent in attached dwelling situations. In the detached situation, the individual owner assesses cost and risk and can act in a manner appropriate to his or her self-interest. With attached housing, the owner has no such right, and is often distrustful of the decisions made by others. Government action of any sort is inherently suspect, but even in a post-Proposition 13 (California's 1978 measure capping property taxes) era, governments still have the right to impose most of the taxation necessary to carry out their legislative enactments. Community associations, with responsibilities not unlike other governments, have no such right, and must often seek owner approval for necessary

projects. “Voluntary” taxation is largely unworkable. It is not surprising therefore that community associations are chronically under funded.

This challenge to the viability of the voluntary assessment concept will no doubt draw the fire (and the ire) of many in the community association industry. Those who object to our assertions are encouraged to take a closer look at the evolving physical and financial condition of community associations and project those conditions ten or fifteen more years. We have interviewed many industry professionals on this subject over the past five years. Not one has expressed doubt about the inevitable obsolescence of many community association projects. Those who manage and service these projects, as well as the boards who govern them, know that raising the necessary funds to deal with both expected and unexpected repair costs is their single greatest challenge. Since individual members will usually vote their self-interest, a collision with community interests is often the outcome. When that collision results in under funding, the project will likely deteriorate over time.

While our discussion of this problem might suggest it, we do not support the notion of legislating mandatory assessments or mandatory funding of reserves, or taking any voting rights away from homeowners. For one thing, that would materially change the nature of what the owners bought. For another, “mandatory” funding of reserves requires that there be developed an objective criteria for setting the amount of the reserves. Most state legislatures has not yet shown an interest in writing laws that can detect and preserve the unique nature of each community association, and therefore can not be counted upon to propose a formula which would have universal application. Finally, enforcement of such a provision would be extremely difficult. Our purpose here is to simply point out, that given the present system, the obsolescence of many community associations is likely.

Changing to a mandatory assessment structure is not the answer. Many older projects have accumulated such a large unfunded liability for future repairs that a legislative edict of “thou shalt” fully fund reserves would have no practical effect and compliance would be unenforceable. Too many years of under funding reserves leaves a gap that residents cannot afford to close. Imposing the large special assessments that would be necessary to close that gap would merely force many residents into abandoning their interests. In other words, “full funding” edicts probably won’t work.

The challenge is not in finding ways to impose mandatory funding or to eliminate individual rights, but rather to achieve better long-term financial management and also to formulate an appropriate exit strategy that will protect the individual’s investment when the inevitable occurs. At present, no appropriate strategy for preserving individual interests in the face of a failed community exists. It should be a legislative priority to find one.

FROM THEORY TO PRACTICE – REAL LIFE EXAMPLES OF OBSOLETE COMMUNITY ASSOCIATIONS

The foregoing chapters posit the theory that the design for funding the long-term repairs and maintenance of community associations is fundamentally flawed. That flaw, the reliance of upon voluntary owner contributions of capital to fund long-term maintenance and repair, has led to a widespread inability by directors of community associations to raise sufficient capital. This, in turn, has been responsible for the poor maintenance and repair of thousands of condominiums and attached planned development projects throughout California and across the nation. The actual evidence of this problem is not just theoretical.

FRANKLIN VILLAS AND FRUITRIDGE VISTA

At a recent seminar for city planners and planning commission members sponsored by the League of California Cities, the author was afforded the opportunity to speak on the impact of community associations on cities and counties. I offered the thoughts contained in the chapters above. These comments were well received, but especially so because my discussion was preceded by another, more compelling presentation that spoke of two real and tragic examples of Stage Four obsolescence in Sacramento, California. Stephen Young, with the Sacramento City and County Redevelopment Agency, described in detail the situation with Fruitridge Vista and Franklin Villas.

Fruitridge Vista consists of forty-four fourplex buildings, totaling 176 units. It was built in the early 1970s and appears to be similar to many projects of this type built by the McKuen Company all over California. It is managed by a single community association. The other development, Franklin Villas, consists of 700 fourplex units and 243 townhouse-style units for a total of 943. This project was built in the 1960's. There are five separate owner's associations. These two projects had clearly reached the end of their useful lives and the oldest was just forty years old.

Young stated, "Both developments suffered from the same causes of decline: dysfunctional homeowner's associations that would not spend the money necessary to do basic maintenance," or employ proper management. Bad tenants who were evicted could simply move into a nearby unit and continue "their criminal or anti-social activities." Further responsibility for the deterioration was laid on the poor design of the original construction. These accounts made our comments about widespread underfunding especially poignant and relevant. From the questions that came from this group of planners, it was clear that the idea that community association projects might one day end up back in their laps had not occurred to them.

The legal title to such projects is held by hundreds of individuals and entities, many of whom are in default or can not be located. This leads to the disturbing inability of the owners to salvage equity from such property which nobody can sell. These were Stage Four projects with no way out except for the local public agencies to exercise their powers of Eminent Domain and a massive investment of public funds.

KING-GARVEY COOPERATIVE

Another real-life story of a "Stage Four" project surfaced in the March 23, 2002 edition of the *San Francisco Chronicle*. An article entitled, "Co-op Residents Up Against the Wall" writer Hene Lelchuk described the sad state of the Martin Luther King-Marcus Garvey Cooperative Apartments. A "cooperative" is another form of community association, with residents owning shares of the project which entitle them to the use of an apartment unit. The opportunity to accumulate equity through home ownership was a major part of the promise made to those who acquired these units. It opened in the 1970's as a non-profit HUD-sponsored housing project. In 1982, the project was converted and sold to the tenants. The story is significant for several reasons: first, it is yet another compelling illustration of the failure of a community association to adequately fund itself; and, second, it shows how quickly this can occur (about twenty years). Finally, and most important, it illustrates the extraordinary level of naiveté of some government policies. Excerpts from the article best illustrate these points.

"Thirty years after the pioneering complex was built (and twenty years after it was sold to individual owners,) the 400-plus residents are watching it crumble into a mess of peeling paint, unpaid bills and bureaucratic bickering between their elected board of directors and the U.S. Department of Housing and Urban Development. Ultimately they could be looking at the loss of all the equity they've built up."

"HUD ordered the development's resident board of directors this month to repair the federally financed buildings and pay off debts, or at least come up with a plan, by early April."

"It's not hard to spot the deterioration. (One resident) can see water stains on her ceiling and stucco cracking off in her bedroom closet, where the roof leaked in the 1990's. 'You can see the mold growing' (she) said. Her neighbor's apartment was flooded when a bathroom fixture broke last summer. And sometimes when (the) resident steps into the shower the water scalds her."

"A lot of the work I've requested, they tell me it's my responsibility."

"As bad news piled up, residents representing more than one hundred households at King-Garvey signed petitions last week to recall their board. That's well over the majority needed to oust the directors."

"This month, HUD inspectors summed up what was wrong: A laundry list of defects-damaged security gates, broken windows, fire extinguishers that didn't work, leaks, roach infestations and more—were never dealt with, despite years of warnings from HUD and city building inspectors."

"The complex let its property insurance lapse and ended up paying exorbitant premiums (to get it re-instated.)"

"There's a history of liens filed on the property. The complex also owes numerous fines for failure to fix fire and health hazards found by city building inspectors. "We have resident complaints going back to 1997 that haven't been addressed. There's no excuse for letting this stuff drag on,' said city housing inspector James Sanbonmatsu... he found black mold in carpeting, fire hazards, stoves that didn't work, leaks, peeling paint and more."

"We never really had enough money to operate'. King-Garvey needs (government funds) and another $500,000 for building repairs."

This last statement says it all. Inadequate funding from the beginning of the project results in a substantial unfunded liability for repairs and many other things. There is no discussion in the article of alternatives to a government bailout. That's likely because there are no other options. The residents have obviously reached the point where they will not or cannot support the project with additional contributed capital. No doubt commercial lenders have long ago refused to invest in the development. Because of its history as a HUD project prior to conversion to a co-op, there is the continuing expectation that HUD should take care of things. "We feel that HUD owes us this opportunity to start over," says one resident.

Whether HUD sees it the same way remains to be seen, but in truth, a government bailout appears to be the only option left for the three projects that we have discussed. In fact, Franklin Villas has already been the object of a major investment by the Sacramento Redevelopment Agency. Community associations which reach Stage Four have run out of all conventional means of funding repairs and many operational expenses. The King-Garvey project is, however, a prime example of a developer (in this case, the Federal Government) sadly raising the expectations of prospective buyers about the benefits of owning the units by not disclosing to them the true cost of long-term ownership.

By the time these owners found out the truth, it was way too late to do anything but pray.

Next Issue – A Survey of Reserve Accounts and the Impact on Affordable Housing

2006 LEGISLATION

AB 770/SB 551 – Would create an "ombudsman" agency within the California Department of Consumer Affairs to provide information resources to HOAs and their members and offer dispute mediation services.

SB 1560 – Would make some technical changes to the new elections laws that are effective July 1, 2006. Among them are that election inspectors can appoint a third party to assist, secret ballots can be used without a meeting, proxies are not ballots. The double envelope system of voting remains. See our January newsletter for further information and Civil Code Section 1363.03. Passed State Senate 39-0 – to Assembly

AB2100 – Would amend reserve fund disclosures to require the board to justify decisions to defer or not to repair common area components and how the association will fund its reserves. Passed Assembly 78-0 – to Senate

AB2851 – Would allow the members of the association to amend the condominium plan without a unanimous vote of the members.

Other bills pertaining to construction defects and nonjudicial foreclosure are also pending.

SANTA BARBARA NEWS-PRESS FEATURES SOUTH COAST HOA

On April 16, the *Santa Barbara News-Press* ran a feature story on the activities of South Coast HOA in the business section. We obtained permission to reprint for you, especially those outside the South County who would not have seen it. We have also posted it on our web site, www.southcoasthoa.org.

The story ran to coincide with our HOA 101 class last month and indeed, about 8 people attended the class that would have not otherwise known about it. Thank you to the *News-Press* for your interest in our organization.

SANTA BARBARA NEWS-PRESS

SUNDAY, APRIL 16, 2006

Helping condo boards through the legal maze

MARIA ZATE
NEWS-PRESS STAFF WRITER

A boom in condominiums has taken over the South Coast, particularly in Santa Barbara, where single-family homes are being rapidly replaced by new, multifamily structures that allow for more households on the area's expensive plots of land.

Of the 192 building permits for new housing issued in Santa Barbara last year, single-family homes comprised only 19 of the total. The remainder of the new units were in mixed-use projects and multifamily housing, with condos making up the majority, according to the city's Community Development department. And many more condos are in the pipeline across the South Coast.

Despite the promise of low-maintenance living – including never having to do yard work and sharing the expense of having a swimming pool – owning a condo typically involves following a number of complex regulations mandated by California laws.

Those buying a condo for the first time often purchase their units unaware of the long list of legal requirements involved with properties that are part of a community development with multiple owners. Once the developer sells the final unit in a new condo project, the management is turned over to the owners, who typically have to fend for themselves.

"New owners usually don't know what to do. And there's no local or state government agency that they can turn to for help," said Michael Gartzke, a local accountant and founder of the South Coast Homeowners Association, www.southcoasthoa.org.

The nonprofit public interest group based in Goleta provides valuable information and resources to condo associations on the South Coast. Formed in 1988, South Coast HOA will likely attract more interest and members these days as the number of condo developments multiplies.

Condos and other community-interest developments on the South Coast range in size from two units to nearly 1,000 homes, such as in Hope Ranch.

While larger condo developments with 30 or more units can usually afford to hire a professional property management company, smaller properties with 10 units or less may struggle to pay for outside assistance. Most of the new condos being built or proposed these days are part of developments with fewer than 10 units.

About half of the 600 or so condo associations on the South Coast use an outside management company or financial firm to handle some of their duties, Mr. Gartzke said. But management companies typically charge a minimum fee of several hundred dollars a month.

That leaves half that are "self-managed." Volunteer board members do the work required to stay in legal compliance, as well as handle the finances and property management.

Back in 1980, when Mr. Gartzke bought his first home in a Goleta condo development called Meadow Tree, there were few resources available to help local condo associations. Because Mr. Gartzke was an accountant, he was tapped to become treasurer of his self-managed association, where he served for five years.

"The thing that frustrated me was not having resources for issues related to condo associations, such as where to go for information and how to meet board members of other condo associations," he said.

Although the national group Community Association Institute was around at the time to provide resources for condo associations, the closest chapter was in Ventura. Mr. Gartzke and three others, including local attorney Jim Smith and property manager Sandra Foehl, decided to start a similar group on the South Coast, and the South Coast Homeowners Association was born.

An estimated 3,000 area homeowners volunteer to serve as directors on their condo association boards. Usually, the only criteria to become a board member is ownership of a unit on the property.

"It's a challenge dealing with people and their homes. The emotional level runs really high," said Mr. Gartzke. "Yet board members have to apply ever-burgeoning laws that only continue to get more complex."

Regardless of whether they have two units or several hundred, all condo associations must meet several basic requirements: they must conduct association business at meetings publicized in advance; hold an annual meeting to elect a board of directors; develop an annual budget to set assessments; and disclose future major maintenance costs for the common areas and how these costs will be funded. Also, regulatory filings are required with California's secretary of state and Franchise Tax Board.

The South Coast Homeowners Association has members representing 142 condo associations countywide, or roughly one out of five in the region.

The organization holds meetings each quarter and membership dues run about $60 a year. On April 22, the group will hold a one-day seminar, called "HOA 101" to educate board members on the fundamentals of condo association operations.

Given the large number of new condo developments in the works, "I don't think our work here is going away anytime soon," Mr. Gartzke said.

e-mail: mzate@newspress.com

SOUTH COAST NEWSLETTER SPONSORS

ACCOUNTANTS

Cagianut and Company, CPAs
Gayle Cagianut, CPA
4587 Telephone Rd #209
Ventura, CA 93003
805-642-4658

Michael J. Gartzke, CPA
5669 Calle Real #A
Goleta, CA 93117
805-964-7806

Hayes & Hayes, CPAs
James L. Hayes, CPA
501 S. McClelland St
Santa Maria, CA 93454
805-925-2675

BOOKKEEPING SERVICES

The Bottom Line
Nancy Gomez
P. O. Box 91809
Santa Barbara, CA 93190
805-683-3186

ATTORNEYS

Price, Postel & Parma
Steven K. McGuire
200 E. Carrillo St. #400
Santa Barbara, CA 93101
805-882-9871

Beth A. Grimm
www.californiacondoguru.com
3478 Buskirk #1000
Pleasant Hill, CA 94523
925-746-7177

James H. Smith
Grokenberger & Smith
1004 Santa Barbara St.
Santa Barbara, CA 93101
805-965-7746

David A. Loewenthal
Loewenthal, Hillshafer & Rosen
15260 Ventura Blvd #1400
Sherman Oaks, CA 91403
866-474-5529

Attorneys (Cont)

J. Toby Noblin/Jason Adams
Adams Noblin Vrataric LLP
305 S. Kalorama #C
Ventura, CA 93001
805-653-7700

FINANCIAL SERVICES

First Bank Association Services
Judy Remley/Linda White
2797 Agoura Rd
Westlake Village, CA 91361
800-539-9616

ASSOCIATION MANAGEMENT

Sandra G. Foehl, CCAM
P. O. Box 8152
Goleta, CA 93116
805-968-3435

Santa Barbara Resources, Inc.
Phyllis Ventura, CCAM
P. O. Box 6646
Santa Barbara, CA 93160
805-964-1409

Spectrum Property Services
Cheri Conti
1259 Callens Rd #A
Ventura, CA 93003
805-642-6160

Brenda D. Wilson CCAM
P. O. Box 6882
Santa Barbara, CA 93160
805-692-4901

Town'n Country Property Management
Connie Burns
5669 Calle Real
Goleta, CA 93117
805-967-4741

Association Management (Cont)

Goetz & Associates
Manderley Property Services
North Santa Barbara/SLO Counties
Gordon Goetz, CCAM
805-937-7278

Good Management Co.
Michelle Armstrong, PCAM
1 N. Calle Cesar Chavez #230A
Santa Barbara, CA 93103
805-564-1400

RESERVE STUDIES

Stone Mountain Corporation
Chris Andrews
P. O. Box 1369
Goleta, CA 93116
805-681-1575
www.stonemountaincorp.com

The Helsing Group
Roy Helsing
2000 Crow Canyon Place, Suite 380
San Ramon, CA 94583
800-443-5746

INSURANCE

State Farm Insurance
Buzz Faull
1236-G Coast Village Circle
Santa Barbara, CA 93108
805-969-5838

State Farm Insurance
Ed Attlesey
160 N. Fairview #3
Goleta, CA 93117
805-964-9988

Timothy Cline Insurance Agency
Tim Cline, CIRMS
725 Arizona Ave #200
Santa Monica, CA 90401
800-966-9566

Insurance (Cont)

Nina Corman
Allstate Insurance
830 E. Ocean Ave.
Lompoc, CA 93436
866-736-8944

CONSTRUCTION MANAGEMENT

Stonemark Construction Management
Bart Mendel
290 Maple Court, Suite 120
Ventura, CA 93003
800-844-9240

GENERAL CONTRACTOR/REPAIR

Raymond Arias Construction
Raymond Arias
1 N. Calle Cesar Chavez #230-B
Santa Barbara, CA 93103
805-965-4158

Formatted

PAVING CONTRACTOR

Smith-Patterson Paving
David/Jim Smith
1880 N. Ventura Ave.
Ventura, CA 93001
805-653-1220

ROOFING CONTRACTOR

Derrick's Roofing
Frank Derrick
650 Ward Drive, Suite F
Santa Barbara, CA 93111
805-681-9954

LANDSCAPE CONTRACTOR

Kitson Landscape Management
Sarah Kitson
5787 Thornwood`
Goleta, CA 93117
805-681-7010

POOL SERVICE

Avalon Pool & Spa Service
Brandon Fennell
P. O. Box 8026
Goleta, CA 93118
805-637-4745

ORGANIZATIONS

Community Associations Institute – Channel Islands Chapter
P. O. Box 3575
Ventura, CA 93006
805-658-1438
www.cai-channelislands.org

Executive Council of Homeowners
ECHO
1602 The Alameda #101
San Jose, CA 95126
408-297-3246
www.echo-ca.org

.