Finance Committee Report for CY2019
- Challenges and Opportunities -

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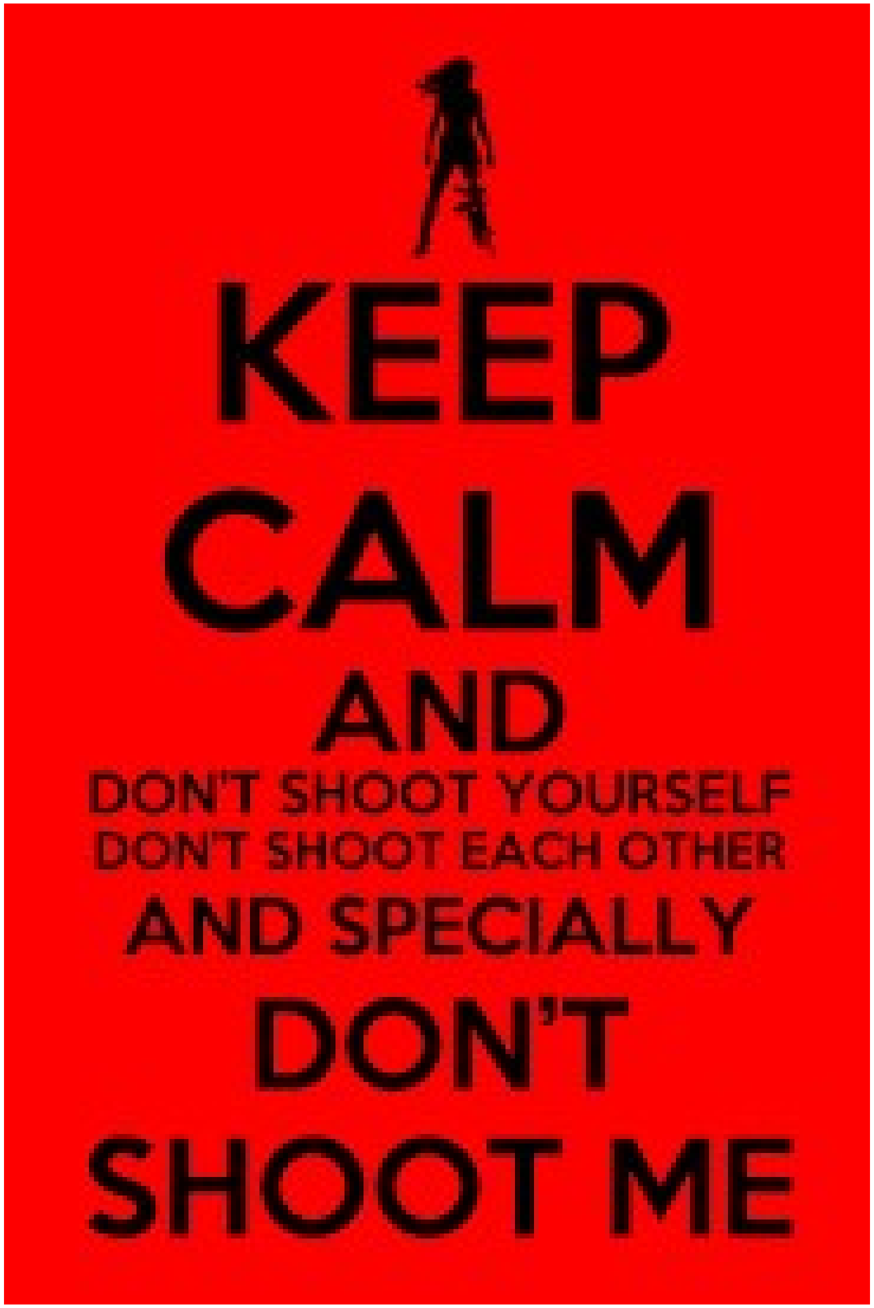
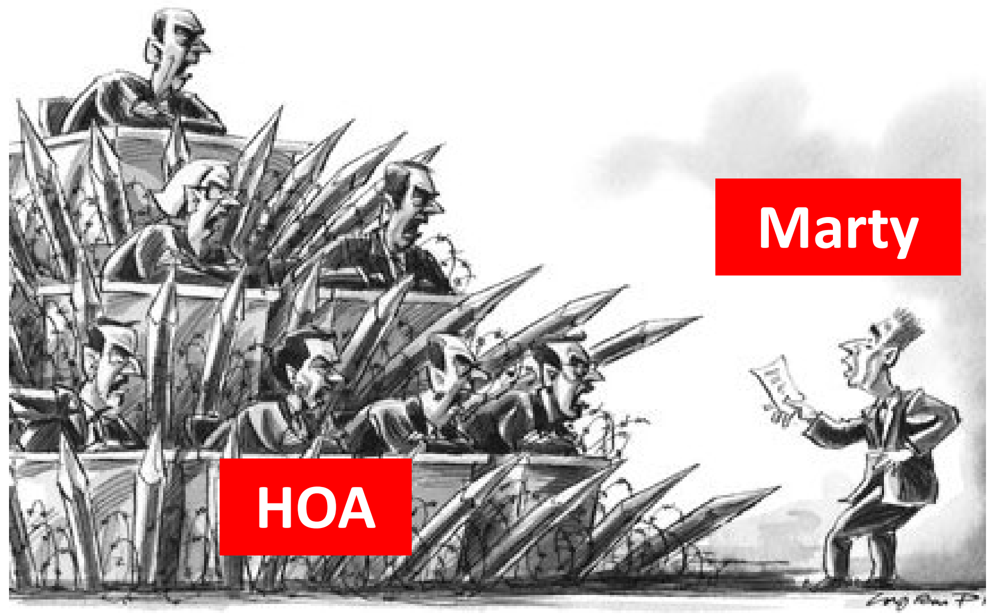
Finance Committee:
Eric Schindwolf, Treasurer
Gary Clarke, Martin Pilch, Blair Wolf

November 2019
Nature Pointe


KEEP
CALM
AND
DON'T SHOOT YOURSELF
DON'T SHOOT EACH OTHER
AND SPECIALLY
DON'T
SHOOT ME


Marty
HOA

The business model is a tool to explore strategies to ensure financial sustainability of NP HOA, i.e., no Special Assessments (SAs)

- **A Special Assessment (SA) is a one-time tax, levied by the HOA against members above and beyond normal dues, to pay for specific expenses when the HOA does not have enough funds**
- **Financial sustainability requires a long-term view (30 yrs) to anticipate and plan for large expenses in the future**
  - **Income**
    - **HOA dues, wedding income, apartment rent, investment income, etc**
  - **Annual operational expenses (including annual maintenance)**
    - **Management company, staff, utilities, landscaping, pool, taxes, bookkeeping, etc**
  - **Reserve expenses (2014 reserve study on NP HOA web site)**
    - **Road maintenance and resurfacing, stucco replacement, roof replacement, heating/cooling system replacement, etc**
  - **Federal and State income taxes**

Sustainability requires long-term planning

Financial sustainability means no special assessments (SA)

- Realistic alignment of expectations and resources.
- You need a plan – understand the true cost of running the HOA
- Avoid legal risks
  - Understand and comply with all applicable codes, laws, and SUP/mediation agreements
  - Avoid obvious liability traps
- **Note: We continue to be plagued by large unplanned or premature "surprise" expenses (i.e., over $100K)**

Operational sustainability

- Break our dependence on *heroic* volunteerism
- Focus on strategic planning and get out of the business of managing the details of day-to-day operations
- Document and archive processes, procedures, and important Board decisions (and the basis for those decisions) – poor organizational memory makes it feel like "50 first dates"
- Engage the HOA management company in operations and maintenance –this is their area of expertise.

2014 reserve study - NP Reserve only 11% funded – high risk of special assessments

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ASSOCIATION RESERVES
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"Full" Reserve Study

Nature Pointe HOA
Tijeras, New Mexico

Report #: 27360-0
For Period Beginning: January 1, 2015
Expires: December 31, 2015

Date Prepared: October 25, 2014

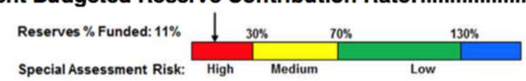
WILL SHAFER
CAI-RS
00187
DESIGNATION
RESERVE SPECIALIST

3- Minute Executive Summary

Association:	**Nature Pointe HOA**	**#: 27360-0**
Location:	**Tijeras, New Mexico**	**# of Units: 112**
Report Period:	**January 1, 2015 through December 31, 2015**	

Findings/Recommendations as-of 1/1/2015:

Projected Starting Reserve Balance:	$79,800
Current Fully Funded Reserve Balance:	$724,886
Average Reserve Deficit (Surplus) Per Unit:	$5,760
Recommended 2015 Monthly "Full Funding" Contributions:	$8,100
Alternate Minimum Contributions* To Keep Reserves Above $0:	$6,700
Recommended 2015 Special Assessment for Reserves:	$0
Most Recent Budgeted Reserve Contribution Rate:	$833



Economic Assumptions:

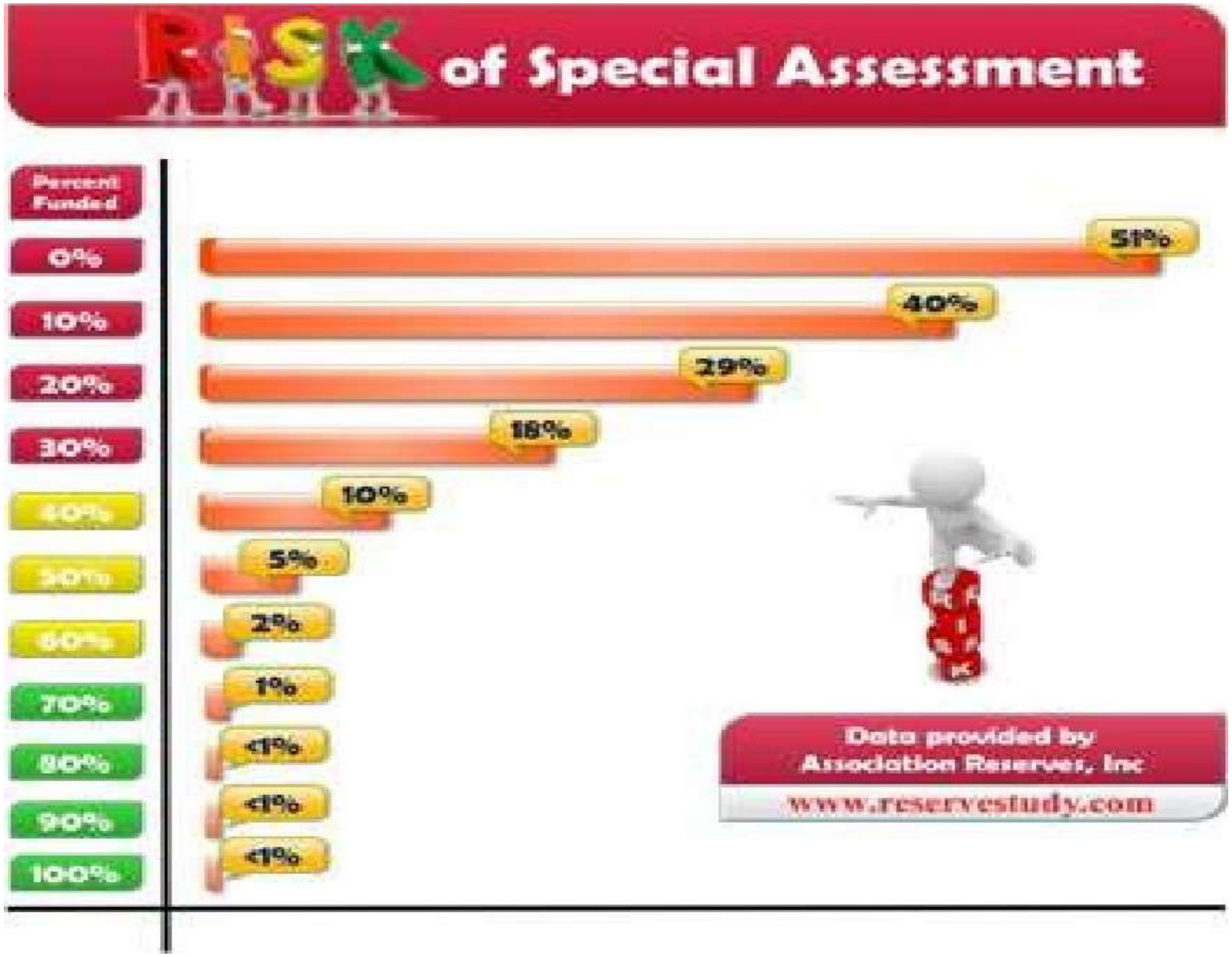
Net Annual "After Tax" Interest Earnings Accruing to Reserves	1.00%
Annual Inflation Rate	3.00%

- This is a "Full" Reserve Study (original, created "from scratch") based on our site inspection on August 25, 2014. It was prepared by a credentialed Reserve Specialist (RS).
- The Reserve expense threshold for this analysis is $1,000. This means no expenses under $1,000 are funded in the Reserve Study.
- Because your Reserve Fund is 11% Funded, this means the association's special assessment & deferred maintenance risk is currently high. The objective of your multi-year Funding Plan is to Fully Fund your Reserves, where associations enjoy a low risk of Reserve cash flow problems.
- Based on this starting point and ... recommendation is to increase ... $8,100/month. Annual increases ... and strengthen Reserves (see t...

*officially called "Baseline Funding"

Recommended reserve contribution $97,200 / year

Reserve Fund Strength >30% = Lower SA risk



Reserve Fund Strength for most HOAs is generally in the Medium Risk Range (30% to 70%). Very few HOA Reserve Accounts are 100% funded.

What's under the hood of a reserve study?

Reserve funds need to be set aside to cover annual deterioration and replace assets when their useful life has expired

- **Component:** Family car
- **Replacement cost:** $30,000 (no salvage value)
- **Useful life:** 10 years
- **Reserve contribution:** you need to save $3,000/yr in order to replace the car when its useful life has expired
- **Fully funded reserve balance:** After 3 years, you should have $9,000 in your reserve fund
- **Reserve fund strength:** If you have only $900 in the reserve fund, then your reserve fund strength is 10% or you would say that your reserve fund is 10% funded
- **Plan:** Save more, replace with a bicycle (i.e., change expectations), borrow from kids' college fund, or demand a "contribution" from family members (i.e., special assessments)

Snippet of our reserve calculation

Should be a resource for annual planning
in collaboration with Maintenance Committee

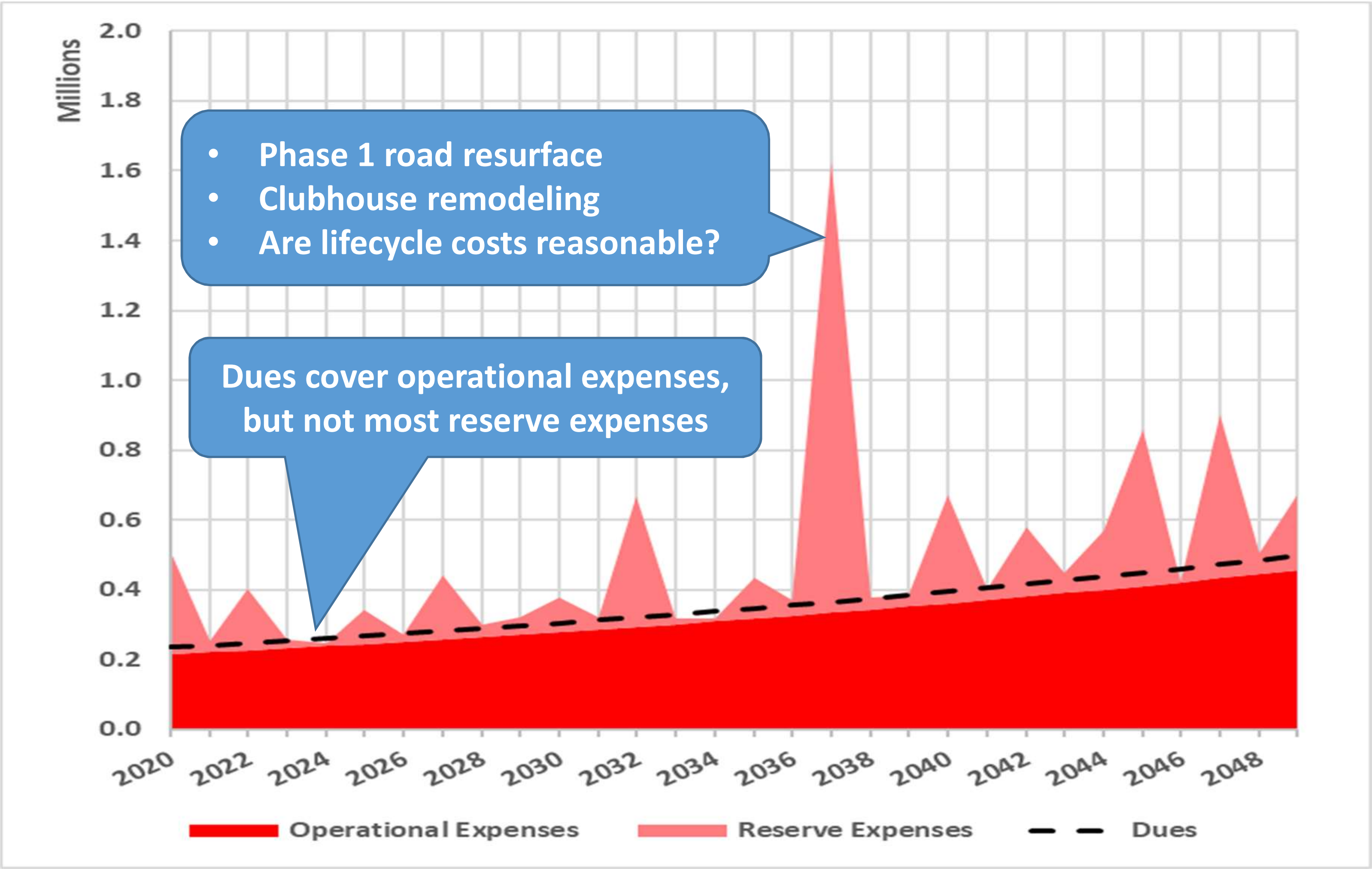
Component	Description	Service Yr	Useful Life	Remaining Life	CY19 $ Low	CY19 $ High	CY19 Cost
Concrete - Repair	Numerous Sq Ft	2007	5	0	1816	2457	2136
Parking Lot - Resurface	26800	2007	30	17	30724	57254	43989
Parking Lot - Seal/Repair	26800	2017	5	2	2396	4280	3338
Phase 1 Asphalt - Resurface	256316	2007	30	17	293842	547578	420710
Phase 1 Asphalt - Seal/Repair	256316	2017	5	2	22917	40933	31925
Phase 2 Asphalt - Resurface	73684	2010	30	20	84472	157415	120944
Phase 2 Asphalt - Seal/Repair	73684	2017	5	2	6588	11767	9178
Phase 5 Asphalt - Resurface	35468	2015	30	25	40661	75771	58216
Phase 5 Asphalt - Seal/Repair	35468	2015	5	0	3171	5664	4418
Phase 6 Asphalt - Resurface	37700	2019	30	29	43220	80540	61880
Phase 6 Asphalt - Seal/Repair	37700	2019	5	4	3371	6021	4696
Phase 3/4 Asphalt - Resurface	35946	2024	30	34	41208	76792	59000
Phase 3/4 Asphalt - Seal/Repair	35946	2024	5	9	3214	5740	4477
Phase 1 Street Signs - Replace	12	2015	30	25	12819	15382	14100
Phase 1 Street Signs - Refurbish	12	2015	15	10	1282	1538	1410
Phase 2 Street Signs - Replace	12	2018	30	28	12819	15382	14100
Phase 2 Street Signs - Refurbish	12	2018	15	13	1282	1538	1410
Coyote Fence - Replace	Approx 600 LF	2007	30	17	17091	21364	19228

- 125 components
- Oversights added
- Planned growth added

- Cost ranges from database
- Modified in some cases if we have local estimates or replacement experience

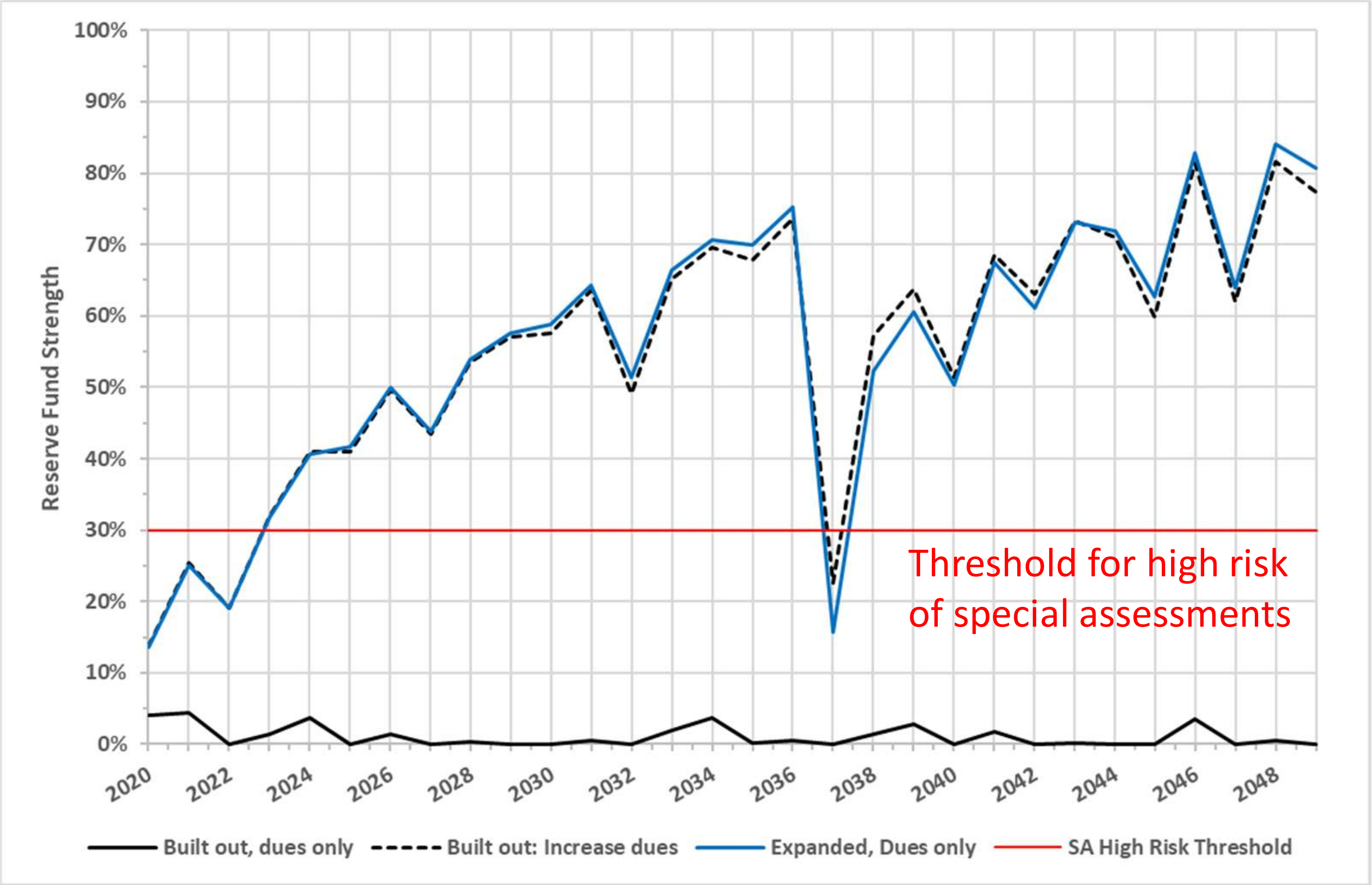
Current HOA dues too low to cover projected expenses without Weddings – even if the community was built out today

Scn#	Description	Growth: L/H per yr	Dues: Hm/Lot	Wed	Rental: CH/Shop	30 Yr Tot $$ all SA's	Average $$/Lot/SA
1	Built out, dues only	112	175/-----	No	No	3,117,717	2,141



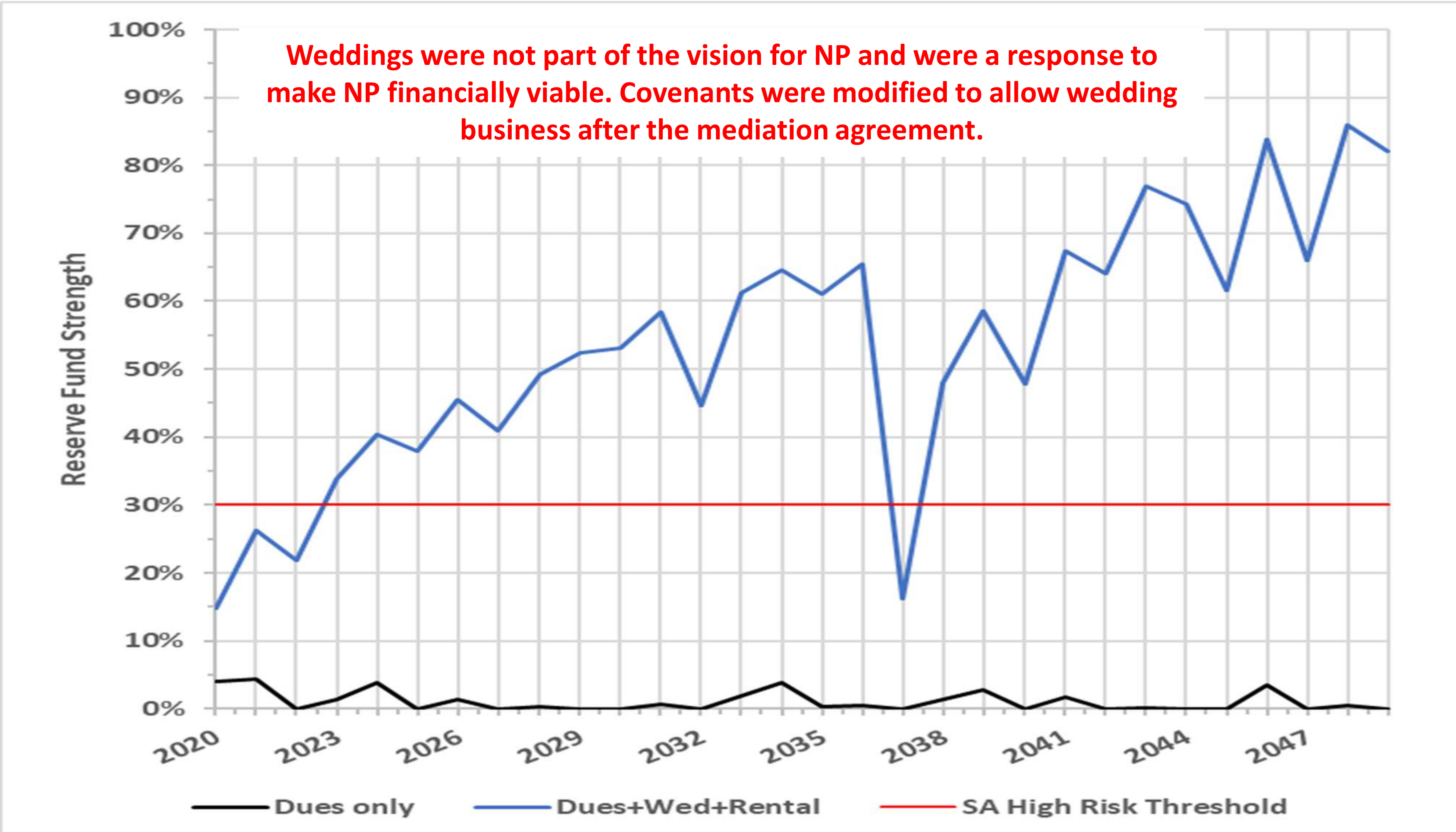
Our dues are too low to support assets – even if built out - need a minimum of 165 homes

Scn#	Description	Growth: L/H per yr	Dues: Hm/Lot	Wed	Rental: CH/Shop	30 Yr Tot $$ all SA's	Average $$/Lot/SA
1	Built out, dues only	112	175/-----	No	No	3,117,717	2,141
1a	Built out: ▲ dues only	112	245/-----	No	No	0	0
2	Expanded, dues only	165	175/-----	No	No	0	0



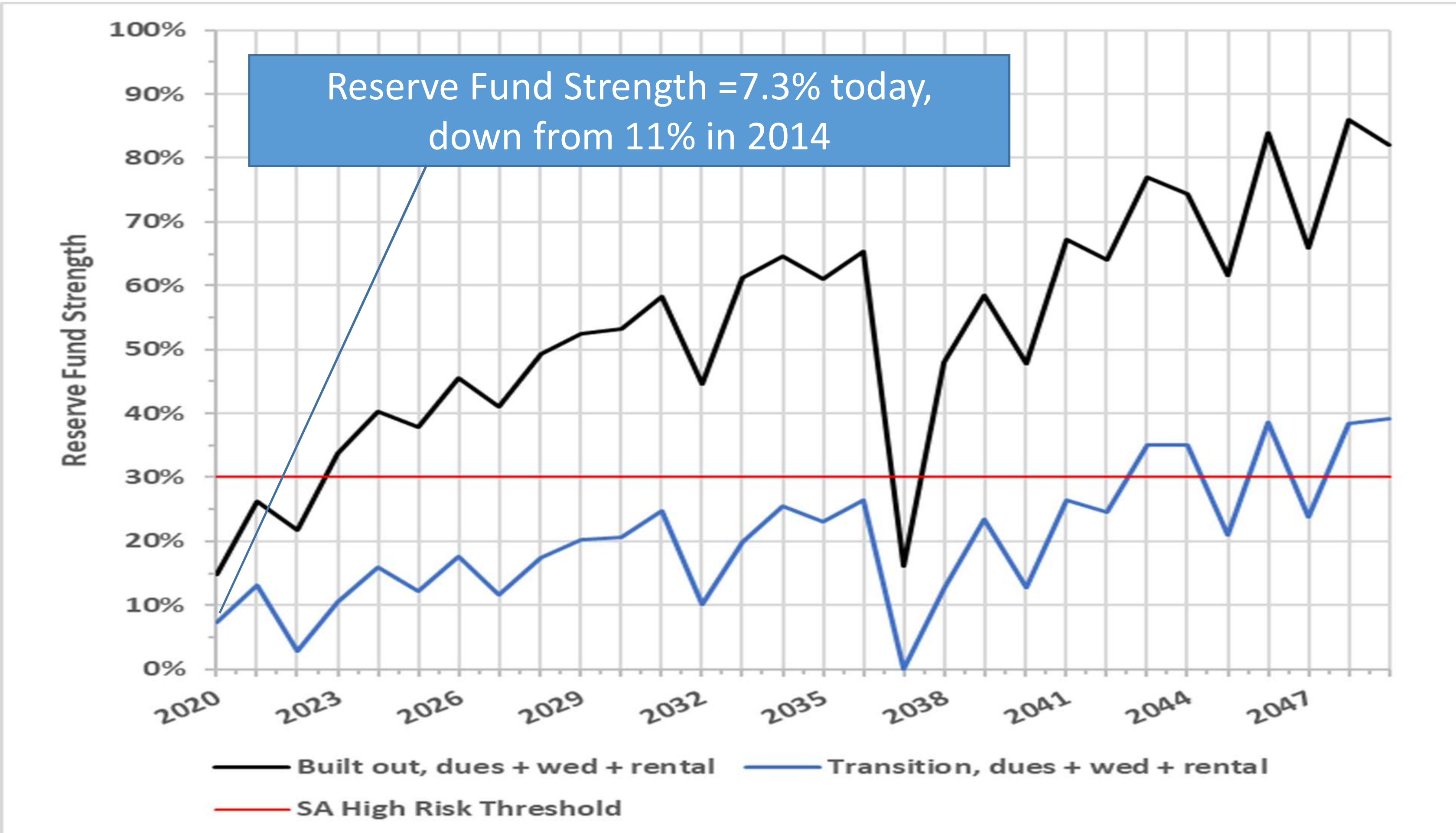
Weddings are needed to meet the long-term costs
Even when built out!

Scn#	Description	Growth: L/H per yr	Dues: Hm/Lot	Wed	Rental: CH/Shop	30 Yr Tot $$ all SA's	Average $$/Lot/SA
1	Built out, dues only	112	175/-----	No	No	3,117,717	2,141
3	Built out, dues + wed + rental	112	175/-----	39	1250/760	0	0



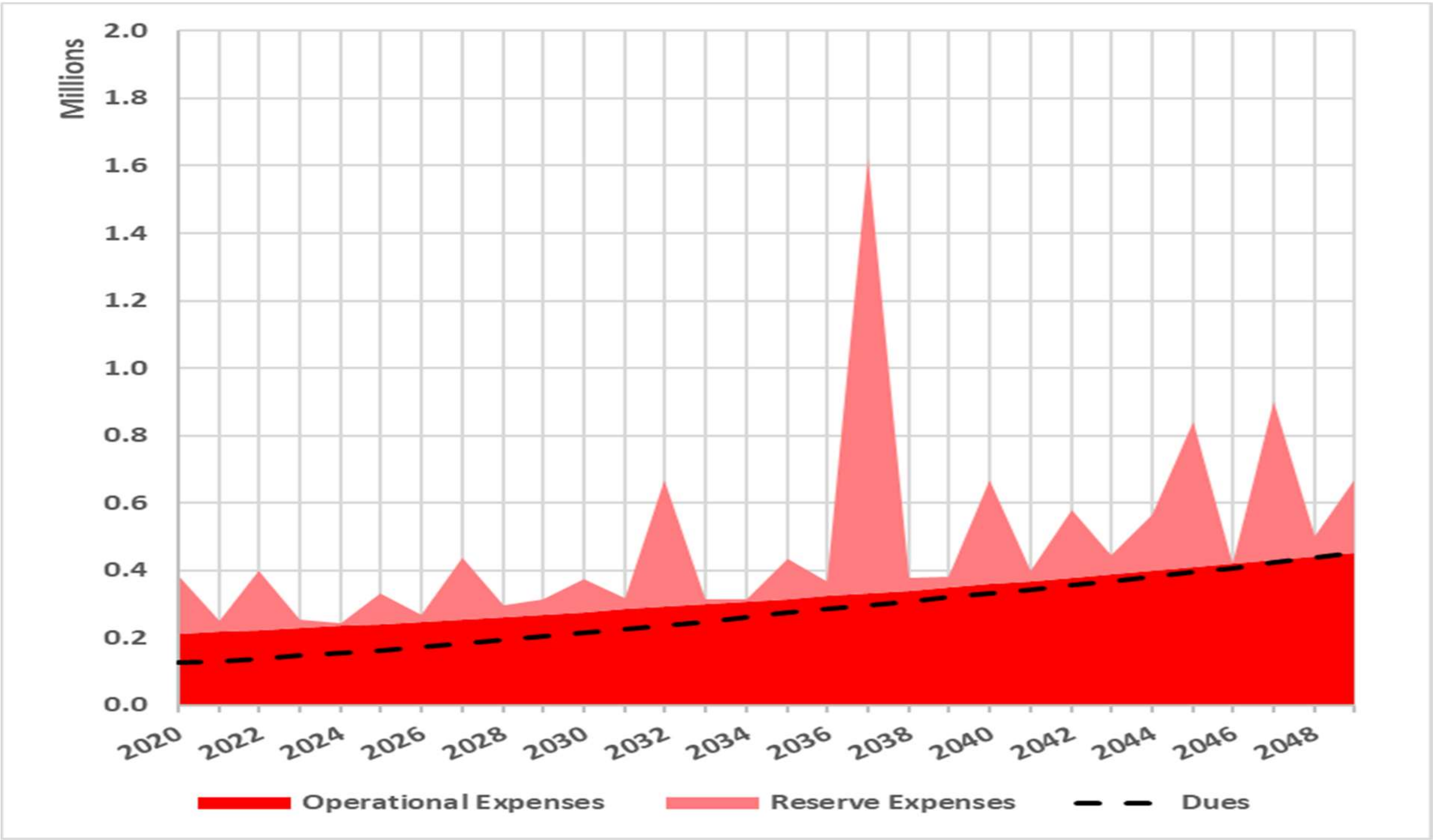
There was no plan to transition from birth to built out, NP's financial future is fragile - *even with weddings*

Scn#	Description	Growth: L/H per yr	Dues: Hm/Lot	Wed	Rental: CH/Shop	30 Yr Tot $$ all SA's	Average $$/Lot/SA
3	Built out, dues + wed + rental	112	175/-----	39	1250/760	0	0
4	Transition, dues + wed + rental	2/2	175/100	Yes	1250/760	541,122	5,105



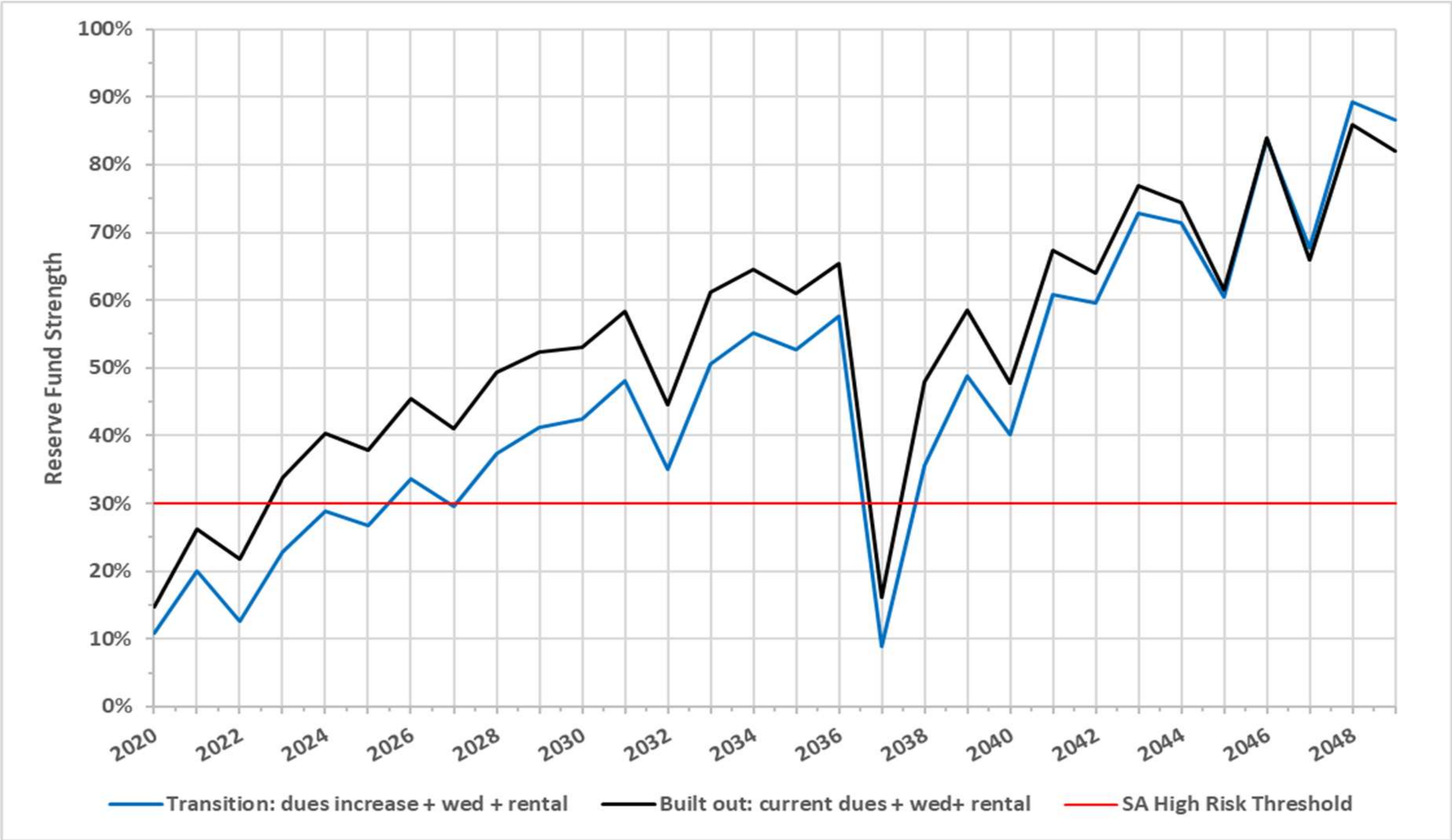
In the near-term dues will *NOT* cover operational expenses

Scn#	Description	Growth: L/H per yr	Dues: Hm/Lot
4	Transition, dues + wed + rental	2/2	175/100



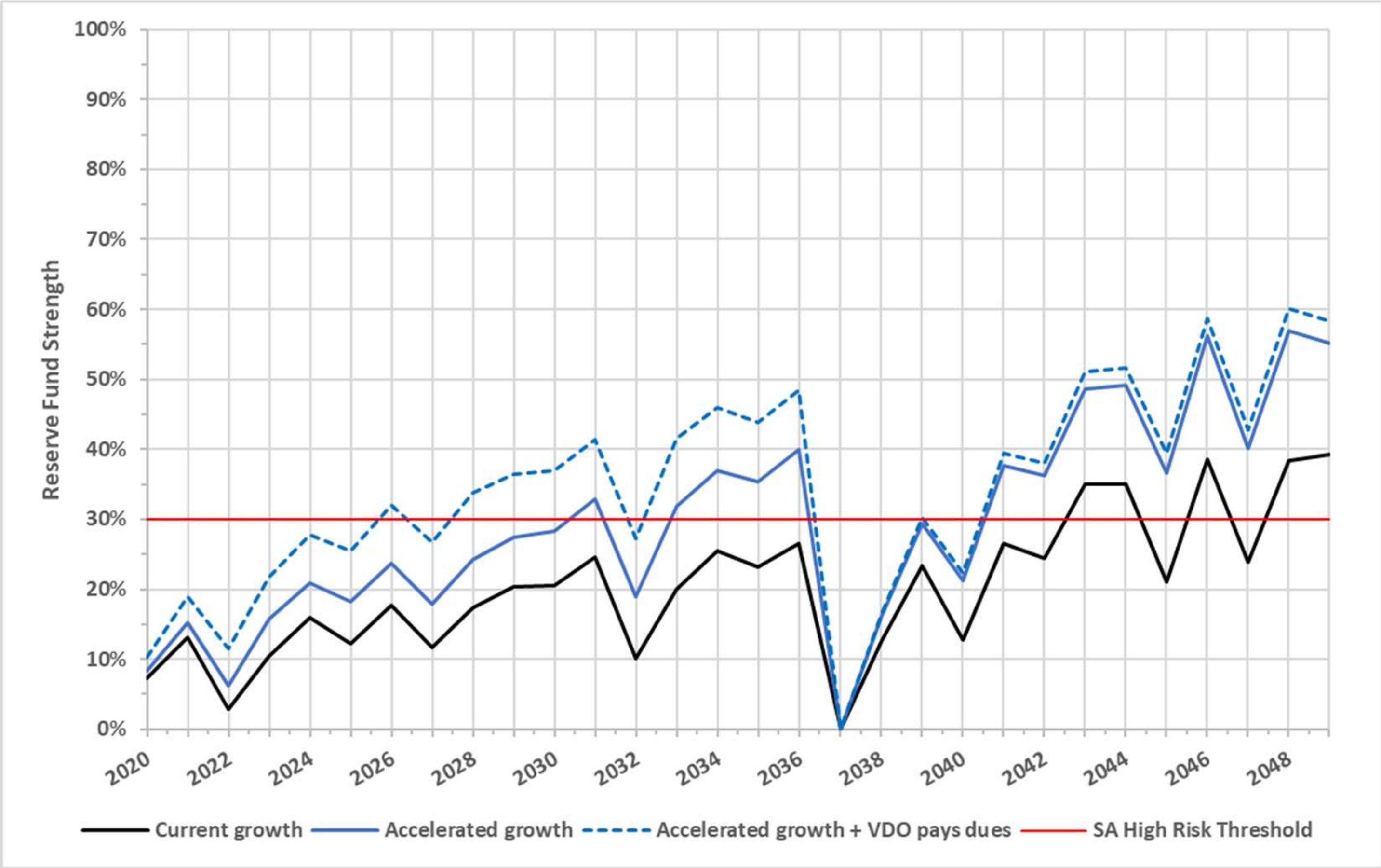
Reasonable HOA dues increase… current market?
Lot owners' dues = 75% homeowner’s suggested by covenants

Scn#	Description	Growth: L/H per yr	Dues: Hm/Lot	Wed	Rental: CH/Shop	30 Yr Tot $$ all SA's	Average $$/Lot/SA
3	Built out, dues + wed + rental	112	175/-----	39	1250/760	0	0
5	Transition, ▲ dues + wed + rental	2/2	200/150	Yes	1250/760	0	0



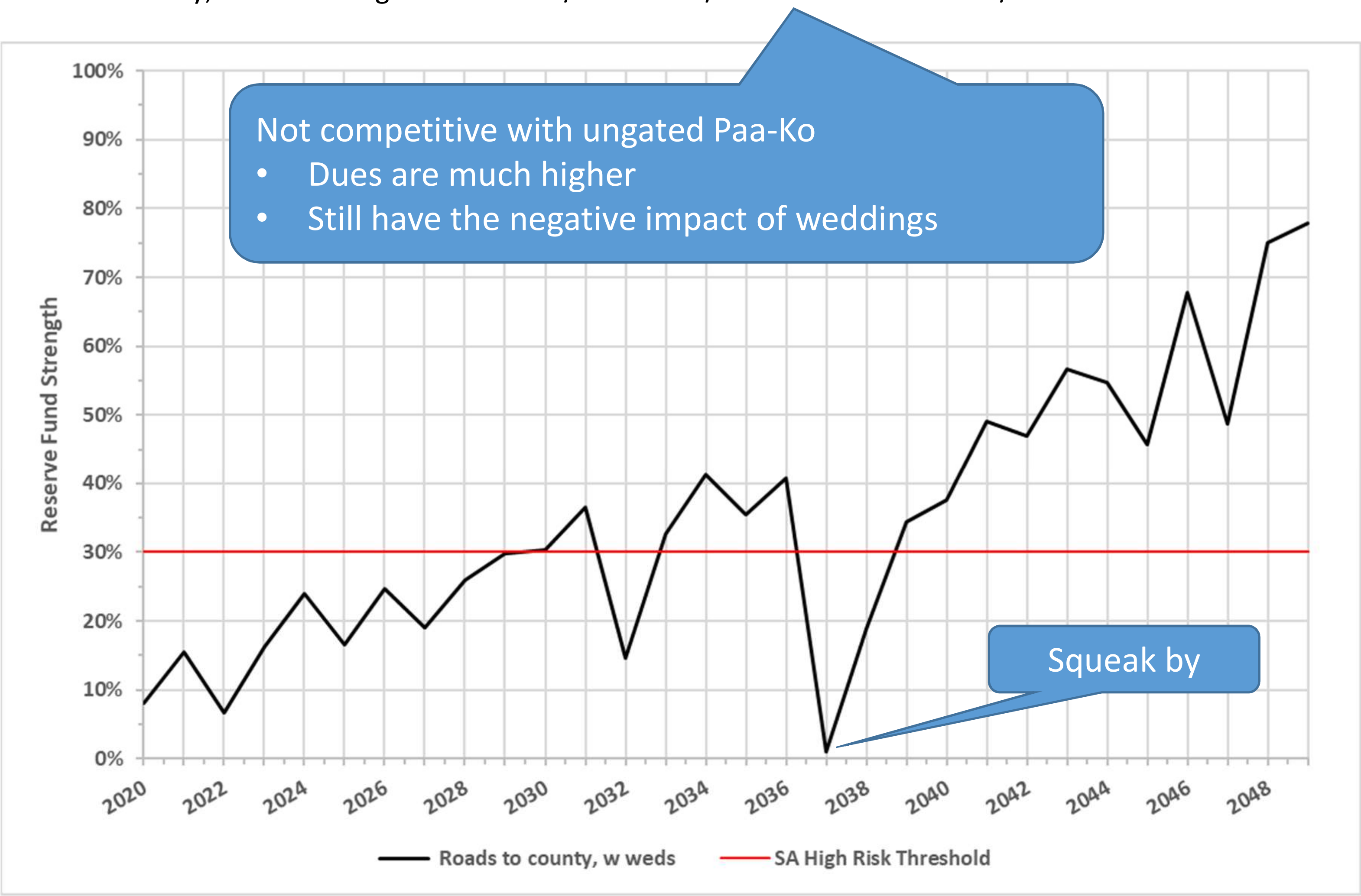
Can we rapidly build out of the problem? Doubled growth rate reduces the risk of SAs

Scn#	Description	Growth: L/H per yr	Dues: Hm/Lot	Wed	Rental: CH/Shop	30 Yr Tot $$ all SA's	Average $$/Lot/SA
4	Transition, dues + wed + rental	2/2	175/100	Yes	1250/760	541,122	5,105
6	Accelerated growth	4/4	175/100	Yes	1250/760	203,794	1,870
7	Accel growth + VDO pays dues	4/4	175/100	Yes	1250/760	12,868	118



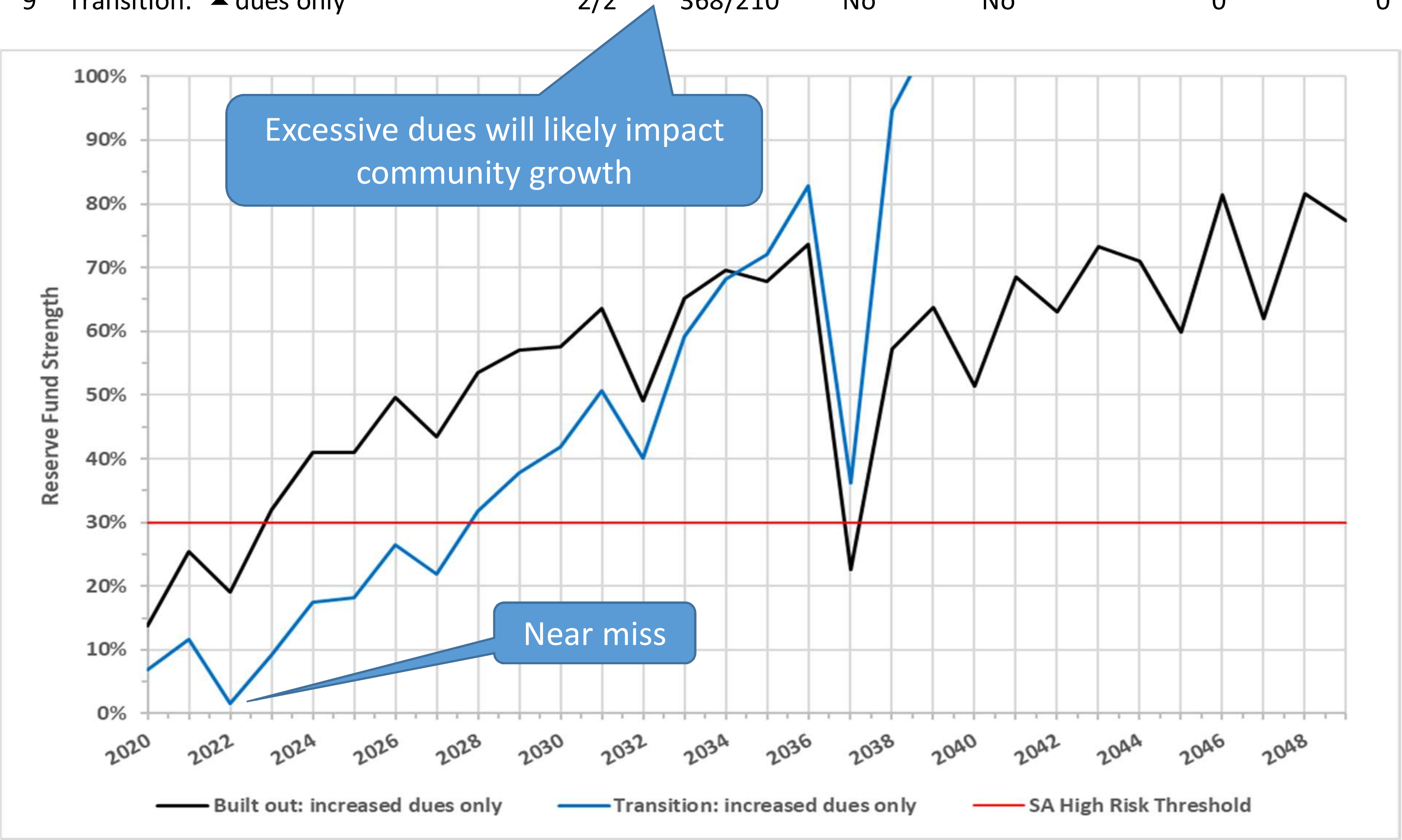
Other approaches…remove the gates and turn road ownership over to the County

Scn#	Description	Growth: L/H per yr	Dues: Hm/Lot	Wed	Rental: CH/Shop	30 Yr Tot $$ all SA's	Average $$/Lot/SA
8	Roads to county, with weddings	2/2	175/100	Yes	1250/760	0	0



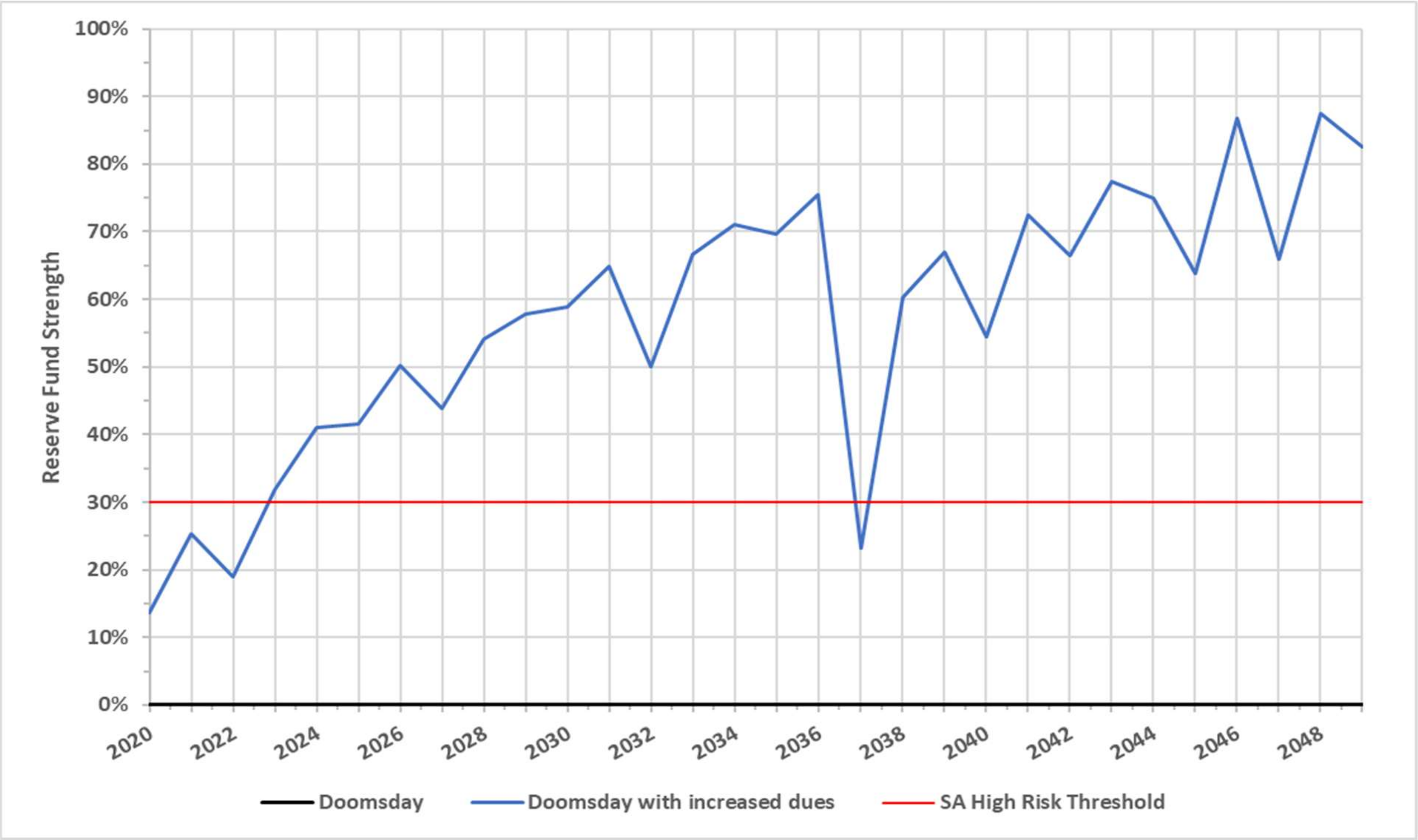
No weddings require much higher dues

Scn#	Description	Growth: L/H per yr	Dues: Hm/Lot	Wed	Rental: CH/Shop	30 Yr Tot $$ all SA's	Average $$/Lot/SA
1a	Built out: ▲ dues only	112	245/-----	No	No	0	0
9	Transition: ▲ dues only	2/2	368/210	No	No	0	0



Worst case - we lose weddings
What happens next?

Scn#	Description	Growth: L/H per yr	Dues: Hm/Lot	Wed	Rental: CH/Shop	30 Yr Tot $$ all SA's	Average $$/Lot/SA
10	Doomsday: frozen, 2/3 lots defaults	0/0	175/100	No	No	9,467,654	4,152
11	Doomsday with increased dues	0/0	595/340	No	No	0	0



Scenarios developed from the model

Scn#	Description	Growth: L/H per yr	Dues: Hm/Lot	Wed	Rental: CH/Shop	30 Yr Tot $$ all SA's	Average $$/Lot/SA
1	Built out, dues only	112	175/-----	No	No	3,117,717	2,141
1a	Built out: ▲ dues only	112	245/-----	No	No	0	0
2	Expanded, dues only	165	175/-----	No	No	0	0
3	Built out, dues + wed + rental	112	175/-----	39	1250/760	0	0
4	Transition, dues + wed + rental	2/2	175/100	Yes	1250/760	541,122	5,105
5	Transition, ▲ dues + wed + rental	2/2	200/150	Yes	1250/760	0	0
6	Accelerated growth	4/4	175/100	Yes	1250/760	203,794	1,870
7	Accel growth + VDO pays dues	4/4	175/100	Yes	1250/760	12,868	118
8	Roads to county, with weddings	2/2	175/100	Yes	1250/760	0	0
9	Transition: ▲ dues only	2/2	368/210	No	No	0	0
10	Doomsday: frozen, 2/3 lots defaults	0/0	175/100	No	No	9,467,654	4,152
11	Doomsday with increased dues	0/0	595/340	No	No	0	0

Summary of decision space and scenarios considered

Option 1

NP as we bought into
- With clubhouse
- Gated community

With weddings, but also requires
- Enhanced community growth
- Hard decisions by Board i.e., manage expectations and/or dues increase
- Manage legal and community issues related to SUP/mediation

No weddings, not sustainable
- Dues would have to be well above market
- Which would have a negative impact community growth

→ **Option 2**

Option 2

Reduced expectations
- With clubhouse
- Turn roads over to county (no gates)
- **Diminished property value for members?**

With weddings, not sustainable
- Squeak by financially, but
- Community not competitive (e.g., Paa-Ko)

→ **Option 3**

No weddings, not sustainable
- Dues would have to be well above market
- Which would have a negative impact community growth

→ **Option 3**

Option 3

Dissolve community
- Sell clubhouse?
- Turn roads over to county (no gates)
- **Diminished property value for members**

Without gates or clubhouse, there is little to distinguish NP
- **No dues**

Managing our future risks - legal and liability

we insure against some risks, but a large claim could touch members and affect our ability to obtain HOA insurance or run a wedding business

- Comply with terms of SUP and mediation agreements – legal and community issues related to SUP/mediation need to be managed
- Confirm or correct clubhouse property line
- Eliminate weddings – not viable
  - Wedding LLC to protect HOA/member assets – currently being researched
  - Personal umbrella and personal HOA insurance for excess liability claims (liquor related suites may be excluded) – affordable, but individual responsibility
- Close the gates and lock the clubhouse – essentially done
- Bridge – repairs completed
- Playground - removed
- Pond – live with risk
- Pool – managed through better access control to clubhouse, keeping cover closed when not in use
- Pond/bridge decking – uneven surface, think high heels not hiking boots
- Water catchment tanks – 4 ea. at 20,000 gal/tank, each is 10 ft X 30 ft
  - Pair next to lower leach field leak 240,000 gal/yr, resolve uncertainty with respect to cave-in potential
  - Second pair between clubhouse and apartment also leak, structural state unknown, uphill of shop
- Miscellaneous
  - Phase 6 rip-rap (rock pile) and junk – improved but not eliminated
  - Pocket park log pile – improved but not eliminated
  - Leach field – concrete culvert and logs left over from playground demolition
  - Shop lot – cleanup completed

Change reporting related to the reserve fund to better understand and manage true cost of running the HOA

- **Reserve fund strength needs to be computed and reported (annually)**
- **Update or commission a new reserve study**
  - Maintain and update reserve ledger as reserve decisions are made
- ***Manage* reserve account separately from the operational account**
- **Pay *all* reserve expenses, and *only* reserve expenses, from the reserve account**
- **Adequately fund reserve accounts by setting targets, funding reserve account as a priority, and reporting progress to the HOA**
- **Implement a lessons learned policy (root cause analysis) for large surprises to anticipate or avoid similar issues in the future**
- **Plan for *all* life cycle costs for *all* capital asset acquisitions and replacements**
  - Cost, useful life, required maintenance, collateral effects (e.g., insurance, impact on SUP/mediation agreements) – input from Finance Committee and Maintenance Committee
  - Inspection and maintenance pays, plan for it explicitly

Taking an integrated view of HOA operations

- HOA operations are wider and more encompassing than just the "laser focus" on the conduct and finances of weddings
- Continue alignment with best practices
  - Board has implemented Generally Accepted Accounting Principles (GAAP) per covenants
  - Periodic audit of all financial processes is recommended to ensure that we have strong financial controls in place
  - Adopt or develop a Conflict Of Interest (COI) policy with annual statements signed by all Board members
  - Fund a management reserve in the annual budget at 5% of operational expenses as a hedge against surprise
- Explore opportunities in all aspects of HOA finances
  - Work with CPA to find ways to shelter reserve contributions from Federal and State income taxes – being researched
  - What is an appropriate role for the HOA to accelerate community growth?
  - Perform market study for dues and apartment rents
  - Encourage community members to take a deep dive in all HOA expenses and make recommendations for cost savings
    - $10,000 in annual savings leverages into $170,000 in the bank when large reserve expenses come due
  - HOA might consider opening a line of credit to soften the blow to members by effectively spreading the SA over a loan period
  - Management company for HOA "event" sales and execution – being researched