

HOUSE BILL REPORT

HB 1309

As Reported by House Committee On: Judiciary

Title: An act relating to reserve accounts and studies for condominium and homeowners' associations.

Brief Description: Concerning reserve accounts and studies for condominium and homeowners' associations.

Sponsors: Representatives Roberts, Appleton, Rodne, Springer, Hasegawa, Ryu, Eddy, Green, Kagi and Kelley.

Brief History:

Committee Activity:

Judiciary: 2/3/11, 2/10/11 [DPS].

Brief Summary of Substitute Bill

- Requires homeowners' associations with significant assets to prepare an initial reserve study and update the study annually.
- Encourages homeowners' associations to establish reserve accounts to fund major maintenance, repair, and replacement of common elements.
- Requires the board of directors of condominium associations and homeowners' associations to disclose information to owners regarding reserve studies with the annual budget summary.

HOUSE COMMITTEE ON JUDICIARY

Majority Report: The substitute bill be substituted therefor and the substitute bill do pass. Signed by 13 members: Representatives Pedersen, Chair; Goodman, Vice Chair; Rodne, Ranking Minority Member; Shea, Assistant Ranking Minority Member; Chandler, Eddy, Frockt, Kirby, Klippert, Nealey, Orwall, Rivers and Roberts.

Staff: Kelly Pfundheller (786-7289).

Background:

This analysis was prepared by non-partisan legislative staff for the use of legislative members in their deliberations. This analysis is not a part of the legislation nor does it constitute a statement of legislative intent.

Condominium Associations.

In 2008 the Legislature amended the Condominium Act and the Horizontal Property Regimes Act to require condominium associations to conduct an initial reserve study by a reserve study professional, updated annually with a visual site inspection every three years, unless doing so would impose an unreasonable hardship.

A "reserve study" identifies the major maintenance, repair, and replacement expenses that a condominium association will incur over time that are not practical to include in an annual budget. The purpose of a reserve study is to evaluate the expected cost of future repair and maintenance of common elements. A reserve study must include a variety of information such as a reserve component list and the balance of the association's reserve account. A condominium association is not required to conduct a reserve study if the cost of a study exceeds 10 percent of the annual budget.

Condominium associations are authorized and encouraged to establish "reserve accounts" independent of the annual operating budget, administered by the board of directors, to fund the maintenance, repair, and replacement of common elements. A reserve account consists of funds contributed by condominium owners, supplemental to the association's annual operating budget, to fund major maintenance, repair, and replacement of common elements that will be required within 30 years. Examples of common elements include a condominium's lobby, roof, parking lot, recreational areas, roads, and sidewalks. The purpose of the reserve account is to offset the financial burden of necessary future renovations that, in the absence of a reserve account, would require the condominium association to impose a special assessment upon the owners.

Homeowners' Associations.

A homeowners' association (HOA) is a legal entity with membership comprised of the owners of residential real property located within a development or other specified area. A HOA typically arises from restrictive covenants recorded by a developer against property in a subdivision. A HOA is managed by a board of directors who are elected by the members once the developer relinquishes control. In general, the purpose of a HOA is to manage and maintain a subdivision's common areas and structures, to review design, and to maintain architectural control.

Under the Homeowners' Association Act, the HOA may exercise powers necessary and proper for the governance and operating of the association, including: adopting and amending bylaws and rules; adopting and amending budgets; imposing assessments on homeowners; entering into contracts; acquiring and conveying property; maintaining and repairing the common areas; granting easements through the common areas; and imposing and collecting payments, fees, or charges for use and operation of the common areas.

The HOAs are required to prepare annual financial statements and to provide homeowners with notice of and a ratification process for the annual budget. The HOAs are not required to conduct reserve studies or to maintain reserve accounts.

Summary of Substitute Bill:

The requirements of condominium associations concerning reserve components and summaries of annual budgets are amended. The reserve study and reserve account requirements related to condominium associations are adopted with respect to the HOAs.

Condominium Associations.

A condominium association is required to comply with the reserve study requirement if the association has significant assets. "Significant assets" means that the current total cost of major maintenance, repair, and replacement of the reserve components is 50 percent or more of the gross budget of the association, excluding reserve account funds.

A reserve study's reserve component list must include roofing, painting, paving, decks, siding, plumbing, windows, and any other building component that would cost more than 1 percent of the annual budget for major maintenance, repair, or replacement. If one of the components is not included, the study must explain the basis for the exclusion.

The board of directors must disclose information to owners regarding reserve studies with the summary of the annual budget. The list of required information is set forth in the bill and includes:

- the current amount of regular assessment budgeted for contribution from the reserve account;
- any regular or special assessments and the date of such assessments;
- the sufficiency of reserve funds for the next 30 years, and if the funds are insufficient, notice of a possible assessment; and
- the projected balances of the reserve account at the end of the next five budget cycles.

Homeowners' Associations.

Homeowners' associations with significant assets are required to prepare an initial reserve study based upon a visual site inspection conducted by a reserve study professional. The study must be updated annually and must include a visual site inspection every three years by a reserve study professional. "Significant assets" means that the current replacement value of the major reserve components is 50 percent or more of the HOA's gross budget, excluding reserve account funds. Also, a HOA is not required to comply with the reserve study requirements if the cost of the reserve study exceeds 10 percent of the HOA's annual budget. Similar to the new requirement for condominium associations, the HOAs must disclose information to owners regarding reserve studies with the summary of the annual budget.

Homeowners' associations are encouraged to establish reserve accounts, supplemental to the annual operating budget, to fund major maintenance, repair, and replacement of common elements.

Substitute Bill Compared to Original Bill:

Definitions for several terms are added with respect to the HOAs, including assessment, baseline funding plan, full funding plan, lot, and owner. Definitions for terms are also added

for condominium associations, including baseline funding plan, full funding plan, and significant assets.

The requirement for condominium associations to conduct reserve studies is amended to only apply to associations with significant assets. The reserve component list for a reserve study with respect to the HOAs is changed to include only major reserve components that would cost more than 1 percent of the association's annual budget (rather than specifically including roofing, painting, paving, decks, siding, plumbing, and windows).

Technical changes are made throughout for clarity and consistency between sections.

Appropriation: None.

Fiscal Note: Not requested.

Effective Date of Substitute Bill: The bill takes effect 90 days after adjournment of the session in which the bill is passed.

Staff Summary of Public Testimony:

(In support) Homeownership entails significant financial responsibility. Many homeowners are members of homeowners' associations and share ownership of roads, parks, and other common elements. Unfortunately, owners are not kept well-informed regarding potential future costs for maintaining common elements or the association's financial situation. The bill addresses this issue by requiring associations to conduct annual reserve studies and encouraging the establishment of reserve accounts.

The current law requiring condominium associations to conduct reserve studies and encouraging the establishment of reserve accounts has been successful and should be extended to homeowners' associations. Some homeowners may not want to conduct studies or prepare for the future because they do not intend on maintaining their homeownership. However, this perspective ignores the true costs of owning a home. Homeowners' associations with low assessments are not always the best deal if owners will end up paying the same costs in the long run. Reserve studies will provide homeowners with information about future costs, and early distribution to reserve accounts will help offset those costs.

(Opposed) The bill does not address the complications of conducting reserve studies and establishing reserve accounts. Specifically, the bill does not recognize the tax law impacts related to money held in reserve accounts or the complexities of bookkeeping. For example, non-capital reserve funds are viewed differently by the Internal Revenue Service. The cost allocation of certain types of reserves also complicates the process. If a condominium association is comprised of several buildings, and the roof of one building is replaced, then the owners of units in that specific building are responsible for the costs, not all of the owners.

Persons Testifying: (In support) Representative Roberts, prime sponsor; Kathryn Hedrick, Community Associations Institute Washington State Chapter; Beth Dunham; Samantha Hamilton; and Jim Talaga.

(Opposed) Ray Pedersen.

Persons Signed In To Testify But Not Testifying: None.