

The Glen of Pacific Grove Homeowners Association

*1996
Reserve Study
Annual Update*



*Prepared By
Community Associations Consulting*

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*for the benefit of The Glen of Pacific Grove Homeowners Association, their members and the
Board of Directors*

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Contents

Introduction	4
Methodology	5
What is a "Major Component?"	5 Through 7
Recommendation	8 Through 9
Table 1- Replacement Cost/Life - Analysis	Table-1
Table 2 - Thirty Year Cash Flow Analysis	Table-2
Chart 1- Expected Annual Reserve Expenditures	Chart-1
Chart 2 - Thirty Year Cash Flow Projection	Chart-2

Introduction

The Glen of Pacific Grove Homeowners Association
Reserve Study Annual Update Prepared July 12, 1996

This property is a planned unit development as defined in California Civil Code 1351(c)(3). The improvements are owned by the Association. The Board of Directors is accountable to the membership for the management and operation of the Association. One of the primary duties of the Board is to see that a Budget is prepared annually. This budget requires that there be reserve study. California Civil Code 1365 provides the guidelines for homeowners associations. Among the requirements is that at least every three (3) years a study be prepared and at least annually the Board review the existing budget study and make the necessary adjustments for the upcoming fiscal/budget year.

The State law requires that the budget (including the reserve study) contain the following:

- ☛ Identification of the "Major Components" for which the Association is obligated to repair, replace, restore or maintain; as of the date of the study have a life of thirty (30) years or less.
- ☛ The estimated replacement cost, estimated remaining life or useful life of each component.
- ☛ As of the end of the fiscal year during which the study is prepared: (a) The current estimate of the amount of cash reserves necessary to repair, replace, restore or maintain the major components. (b) The current amount of accumulated cash reserves necessary to repair, replace, restore, or maintain major components.
- ☛ A statement giving the percentage of reserve funding.

- ☛ Does the Board of Directors expect that there be any special assessments.

In addition, this report will provide the Association with at least the following information:

1. Provide an economic model to assist the Board and its Management to plan, revise and operate the Association's long term fiscal issues.
2. It also provides an orderly means of recording the assumptions used in preparing this economic model. Like other economic models it should be constantly revised and updated. This report is a tool or instrument to be used on an ongoing basis. The less you use its potentials the less likely the model will provide accurate guidance.

About the Report

Reading the report is intended to be straight forward and lead the reader to several answers. How much is recommended to be placed into the reserves this year. This information can be read from the table titled "30 Year Cash Flow Projection" on Table-2. In the first column is the year; 1995, 1996 etc. In the last column the reserve assessment amount per member per month that is recommended by this report to maintain a positive cash fund balance over the next thirty (30) years.

The next to last column provides the reader the amount recommended to be contributed over a twelve (12) month period. This amount is the amount collected from the members in the Association budget year. The Association's budget

year does not necessarily have to be a calendar year.

Methodology

The method employed in this report is generally referred to as the pooling or fund approach. State law does not require the segregating of reserve funds by component. Rather, it is understood that this is an economic model that is dependent on many variables. It is impractical in the beginning to estimate with absolute precision the cost at the time the event or expenditure occurs for each item.

For example; while professionals will agree that a particular type of roofing system will last 20 years, this is just an average. This estimate considers a variety of issues. The roof may or may not last exactly 20 year. Major components do not become worn out without advance signals. A roof does not fail all at once, it shows signs of deterioration before the first leak. Leaks are not always a sign of a roofing system failure but they might be early warnings. Other components have their own signaling system. Facilities managers are aware of these signals.

Facilities managers agree that the best spent money is the money spent for "preventive maintenance." An association that diligently inspects and repairs/maintains the properties will spend far less than an association that does not. Generally, this reserve reporting process will provide some measures to support a "preventive maintenance" program. This study does not recommend that funds put into the reserves be used to be the funding source of the preventive maintenance program. This report can not replace an active maintenance management program.

A word of warning, many associations have waited for the catastrophe to worry about the issues. The "general standard of care" that fiduciaries can be held to is the "ordinarily prudent person rule." If other associations have a "preventive maintenance program" and your association does not, a member may accuse you and management for failure in your fiduciary duties.

What is a "Major Component?"

We are glad you asked. The reason that we're glad you asked is that it needs to be discussed but we can't give you a simple answer. There are no independent authorities we can sight to give a simple answer to "what is a major component." Those of us who have been preparing reserve budgets have come to a conclusion that a "major component" is something that we define in the report. Thus a "major component" is something we say is a "major component." We do have some Generally Agreed Practices (GAP) or guidelines. None are rules or laws but they are intended assist us in identifying the scope of the study.

But let us digress for a moment. If the item is not in the current list of "major components" it does not invalidate the reserve study. Their are criteria for adding items to the reserve study. To illustrate, an item that might be added over time is concrete walkways. Usually this component (the walkway) is not in the first reserve study. The reasons are at least three fold. (1) It is extremely difficult in a new property to determine when the event will occur; (2) How much will occur at any one time is usually conjecture; (3) The nature of the event is that it requires that the Association do something almost immediately upon discovery. Each event is usually less than a \$100 - \$200 item. The cost of taking money/appropriating reserve funds will exceed the cost of the event. Thus, it is economically unsound to try to fund minor expenditures from the reserves.

State law requires at a minimum that at least one director and one officer of the Association approve the expenditure of any reserve funds. We strongly suggest that reserve funds should not be used to fund reactive events. Rather, the Reserve Fund/Study is a funding device for those items which can be planned for.

The integrity and soundness of the reserve fund may be jeopardized if it becomes confused with the day-to-day operational events. This discussion does not intended to instruct but to provide information so

that the policy body/the Board can consider a variety of options. The Board is entitled to rely upon information from sources who by their education and experience are expert in their area. Information coming from sources who have no prior experience with the issues at hand should not be given the same consideration as those who have the education and experience.

Usually a good measure of a reservable item is an expenditure event which by its nature is not annual but will be done by large contracts. A contract must have specific beginnings, endings, scope and specifications.

Painting in some communities is handled as a reserve component because of the way they have structured financial funding and operations programs. In other associations it has not been an item of the reserve fund because it is part of an annual operating budget. There are some proponents that say that if you put funds into the reserves for painting you will cause the association's tax position to be negatively effected.

The IRS has ruled that Associations seeking the benefits of the regular corporation tax filing, can not make contributions of money to the Association's reserve fund for maintenance. Painting is defined as a maintenance expense. If the funds were for the acquisition of a new clubhouse, or replacing the roof, the expenditure is an addition to the capital value. This is a permissible usage of capital contributions. Capital contributions by stock holders in a corporation is exempt from of income taxes.

Other authorities, such as the State of California Department of Real Estate in the "Operating Cost Manual" has steadfastly disregarded the consequences of the taxes on an association whose funds its painting from the reserve fund. The State does not make the rules for the IRS, you should also know that this is an item which is best discussed with your Association's CPA.

It is recommended that the Board of Directors make an informed business decision. If the Board wishes

to view this study as a integral component of the "Reserve Fund" and you wish to place money in this fund which is defined by the IRS as maintenance funds; then you should be prepared to pay the Tax rate provided under IRS 528. Generally, this rate will be 26% (subject to revisions of the tax rates under the new Federal Budget/Tax Plan just approved) versus 16% on the "Non-Exempt Function Income." Generally, "Non-Exempt Function Income" is income other than members assessments. Interest income earned on the associations funds is not exempt from taxation. Some Boards of Directors look at this study as a planning device that takes into account a variety of items; neither capital in nature or maintenance in nature but rather as economic model to meet long term funding requirements. The specific objective of the economic plan is to recognize long term expenses and provide a plan for meeting those needs. An additional objective is to do this with as little impact on the membership as possible. It is not considered appropriate as fiduciaries to collect funds in excess of the Associations needs (California Civil Code 1366.1). Nor is it appropriate to fund the operations through "Special Assessments." Unforeseen expenses should be managed to the minimum. At least one measurement of management is the ability to anticipate events and to plan for meeting them.

State law allows the Board of Directors to barrow funds from the "Capital Reserve Fund" for a variety of purposes; so long as the Board has a reasonable plan for paying it back. This "Cash Flow Plan" and this "Reserve Study" can be viewed as instruments to meet the funding challenges of the Association. Simply, we are making capital contributions. The only monies which are ever "expended" from the Capital Reserve Fund are Capital Expenditures which meet the test of the IRS. This would allow the association to barrow money from the reserve fund for operating fund expenditures for painting and the like and to repay it out of the "cash flow."

Another factor worth noting is the percent funded report. The (Calif. Civil Code 1365) requires that we report the percent funded as of the moment of

the report is prepared. The method used to report the "percent funded" is a calculation for purposes of conveying information to the membership on the health of the association. The means used to calculate this are in substantial dispute among the authorities. At the time of this publication, at least three independent trade organizations (CAI, CACM and ECHO) have registered concern about the methodology of reporting this factor.

Regardless, the law requires we make a report. The common method of calculating is based upon a method which is not altogether consistent with other provisions of the Statutes. Generally the method requires that we divide each components "current replacement cost" by the estimated life of that component. Then to multiply the result of the previous calculation times the number of years since the component was replaced, repaired etc. Finally, adding up the results of all of these calculations gives the amount of "accrued liabilities - on a straight line method." The amount of "cash" which has been accounted for by the Association that has been set aside for the reserves is divided by the accrued liability of all of the items. The result of this division is the percent funded. Again there are inconsistencies in the law because it requires that these calculations be based upon actual amounts for a time in the future, which of course is not actual until the time has occurred. Regardless, we will provide the basis of calculations.

This study was limited to a non visual inspection and since no destructive testing was undertaken, this study does not purport to address any latent and/or patent defects, nor does it address any life expectancies which are abnormally short due to either improper design or installation, or to subsequent improper maintenance. It is assumed that components are to be reasonably maintained for the remainder of their life expectancy.

Recommendation
For
The Glen of Pacific Grove Homeowners Associations

Revenue: The Glen of Pacific Grove Homeowners Association's Reserve Fund requires an annual provision of \$44,179 (\$61.36 per unit per month) for 1996/97. This was determined by doing a Replacement Cost and Component Life Analysis (Table 1) and then using a Cash flow projection to determine the minimum annual provision necessary to ensure that funds will be available when needed (Table 2).

This study indicate that it will be necessary to increase the annual reserve contribution by 3.00% in fiscal years 1997 through 2026. Subsequent increases may not be necessary to keep pace with inflation.

Percentage Funded: California Civil Code 1365(a)(2)(c) requires that the Association Disclose to the membership "Percentage Funded".

The Association's estimated Reserve Fund Balance at the end of this fiscal year August 31, 1996 (Table 2) is \$136,500.00. This starting balance, along with funding plan provided in the thirty (30) year cash flow we will be 100% fully funded based upon these contributions.

Painting - Exterior Wood siding: There is estimated to be 99,280 sq.ft. The siding will require painting on a six (6) year cycle and it is scheduled to be painted during 1996/97 fiscal year. which .

Painting - Wrought Iron Fencing: There is approximately 1,964 sq.ft. This fence was painted in 1994. the normal painting cycle should be every two (2) years and need to be painted as soon as possible.

Entry Gate - Mechanical/ Intercom System: The life expectancy of these components is at least 10 years with good preventive of maintenance. the total area is estimated at 65,440 sq.ft. for purposes of calculating the current replacement cost.

Roofing - Composition Shingle & Gutters Replacement: There is approximately 89,535 sq.ft roof area. It has a life of approximately twenty four (24) years. Current condition appears good.

Street Light Fixtures: There are present 16 street lights. With care and replacement of burned out globes , these lights should last their projected lifespans of thirty(30)years.

Exterior Light Fixtures: There are 99 light fixtures on the buildings throughout the project. With care and replacement of burned out lights, these fixtures should last Twenty (20) years.

Lake Dredging: The lake should be dredged at least every seven (7) years. 1988 is last time that lake was cleaned and it is schedule for 1996/97 to be dredged.

Lake Pump & Motors: The pumps and motors all appear to be in good operating condition and with routine maintenance should last their expected lifespans.

Fencing - Repairs & Replacement: Surrounding the property area there is chain Link and Wrought Iron fencing there is Chain Link fencing around tennis court area. The life of the fence is estimated to be thirty (30)years.

Asphalt Sealing: The general condition of the roadways are standard for the age. There is approximately of 28,500 sq.ft. It is recommended to be resealed in 1996/97. Generally, this will be done three times then an Asphalt Overlay will be performed. Normal life expectancy is five (5) years.

Asphalt Overlay: Provision is made to provide a scoring of the surface and the laying of a two (2) inch lift of asphalt. The normal cycle is twenty (20) years.

Tennis Court: The tennis court is require resealed at least every seven (7) years cycle. The present condition of court is good ant it should last its expected lifespan.

Irrigation System: The irrigation system is controlled by timers and served by valves that have a projected lifesapn of ten (10) years. With routine care and maintenance, these components should last their expected lifespan.

THE GLEN OF PACIFIC GROVE HOA 1996 RESERVE STUDY

TABLE 1. REPLACEMENT COST/LIFE ANALYSIS

Item Description	Quantity	Unit of Measure	Unit Cost	Replacement Costs	Normal Life Expectancy	Last Disbursement	Next Disbursement
Painting - Exterior Wood Siding	99,280	sq. ft.	\$0.80	\$78,995	6	1996	2003
Painting - Wrought Iron Fencing & Pole Lights	1,964	sq. ft.	\$0.64	\$1,250	2	1996	1998
Entry Gate - Mechanical /Intercom System	1	each	\$5,304.50	\$5,305	10	1993	2003
Roofing - Composition & Gutters	89,535	sq. ft.	\$2.55	\$227,970	24	1984	2008
Street Light fixtures	16	each	\$2,121.80	\$33,949	30	1984	2014
Exterior light fixture on buildings	99	each	\$79.57	\$7,877	20	1984	2004
Lake Dredging	1	All	\$31,827.00	\$31,827	8	1988	1997
Lakes Pump & Motors	2	each	\$1,909.62	\$3,819	16	1984	2000
Fencing- Repairs & Replacement	1,026	ln. ft.	\$26.52	\$27,212	30	1984	2014
Bridge - Repairs & Replacement	1	each	\$4,774.05	\$4,774	20	1984	2004
Asphalt - Sealing	28,500	sq. ft.	\$0.16	\$4,535	5	1987	1997
Asphalt - Overlay	28,500	sq. ft.	\$2.09	\$59,591	20	1984	2004
Tennis Court Resurface	7,400	sq. ft.	\$0.42	\$3,140	7	1994	2001
Irrigation System	1	All	\$6,180.00	\$6,180	10	1995	2005
Administration & Contingency	N/A		5.00%	N/A	N/A	N/A	N/A

THE GLEN OF PACIFIC GROVE HOA 1996 RESERVE STUDY

TABLE 2. THIRTY YEAR CASH FLOW ANALYSIS

Date: 12-Jun-96
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Fiscal Year Date	Painting Exterior Wood	Painting W. Iron - Fe /Pole Lights	Entry Gate Mech.	Roofing & Gutters Replacements	Street Lighting Fixtures	Exterior Lighting Fixtures	Lake Dredging	Lake Pumps & Motors	Fencing Repairs/ Replace	Bridge Repairs/ Replace	Asphalt Sealing	Asphalt Overlay	Tennis Court Resurface	Irrigation Valves & Controllers	Admin & Contingenc	Total Annual	Annual Provision	Provision Balance	Assessment Per/Mo.
1996/97	58,347	607	0	0	0	31,827	0	0	0	0	4,535	0	0	0	4,766	100,082	44,179	136,500	61.36
1997/98	0	1,288	0	0	0	0	0	0	0	0	0	0	0	0	64	1,352	45,669	80,597	63.43
1998/99	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	47,039	171,952	65.33
1999/00	0	1,366	0	0	0	0	4,173	0	0	0	0	0	0	0	277	5,816	48,450	214,586	67.29
2000/01	0	0	0	0	0	0	0	0	0	0	0	0	3,534	0	177	3,711	49,903	260,778	69.31
2001/02	0	1,449	0	0	0	0	0	0	0	0	5,258	0	0	0	335	7,042	51,400	305,136	71.39
2002/03	94,324	0	6,334	0	0	0	0	0	0	0	0	0	0	0	5,033	105,690	52,942	252,388	73.53
2003/04	0	1,538	0	0	0	9,688	39,143	0	0	0	0	73,289	0	0	6,519	136,894	54,531	170,024	75.74
2004/05	0	0	0	0	0	0	0	0	0	0	0	0	0	0	500	10,500	56,167	215,691	78.01
2005/06	0	1,631	0	0	0	0	0	0	0	0	0	0	0	82	1,713	17,852	271,830	80.35	
2006/07	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	59,587	331,417	82.76
2007/08	0	1,731	0	315,564	0	0	0	0	0	0	0	0	4,347	0	16,082	337,724	61,375	55,068	85.24
2008/09	112,627	0	0	0	0	0	0	0	0	0	0	0	0	0	5,631	118,259	63,216	25	87.80
2009/10	0	1,835	0	0	0	0	0	0	0	0	0	0	0	92	1,928	1,928	65,112	63,210	90.43
2010/11	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	67,066	130,276	93.15
2011/12	0	1,948	0	0	0	0	49,585	0	0	0	7,066	0	0	0	2,930	61,529	69,078	137,824	95.94
2012/13	0	0	8,512	0	0	0	0	0	0	0	0	0	0	426	8,938	8,938	71,150	200,037	98.82
2013/14	0	2,066	0	0	56,112	0	0	0	44,977	0	0	0	0	0	5,158	108,314	73,285	165,008	101.78
2014/15	134,483	0	0	0	0	0	0	6,697	0	0	0	0	0	0	7,518	157,868	75,483	82,623	104.84
2015/16	0	2,192	0	0	0	0	0	0	0	0	8,191	0	0	444	9,334	9,334	77,748	151,037	107.98
2016/17	0	0	0	0	0	0	0	0	0	0	0	0	0	410	8,601	8,601	80,080	222,516	111.22
2017/18	0	2,326	0	0	0	0	0	0	0	0	0	0	0	116	2,442	2,442	82,483	302,557	114.56
2018/19	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	84,957	387,514	118.00
2019/20	0	2,467	0	0	0	0	62,813	0	0	0	0	0	0	0	3,264	68,545	87,506	406,475	121.54
2020/21	160,580	0	0	0	0	0	0	0	0	0	0	0	0	8,029	168,609	90,131	327,997	125.18	
2021/22	0	2,618	0	0	0	0	0	0	0	0	9,496	0	0	934	19,623	92,835	401,209	128.94	
2022/23	0	0	11,440	0	0	0	0	0	0	0	0	0	0	572	12,012	95,620	484,817	132.81	
2023/24	0	2,777	0	0	17,497	0	0	0	0	17,824	0	132,368	0	0	8,323	178,990	98,488	404,316	136.79
2024/25	0	0	0	0	0	0	0	0	0	0	0	0	0	707	14,846	14,846	101,443	490,913	140.89
2025/26	0	2,946	0	0	0	0	0	0	0	0	0	0	0	147	3,093	3,093	104,486	592,306	145.12
30 Years Annual	560,361	30,785	26,286	315,564	56,112	27,185	183,369	10,870	44,977	24,541	34,546	205,657	19,802	34,660	78,736	1,653,454	2,109,260	7,405,040	246,835
Annual	18,679	1,026	876	10,519	1,870	906	6,112	362	1,499	818	1,152	6,855	660	1,155	2,625	55,115	70,309	246,835	

Expected Annual Reserve Expenditures

Assuming 3% Annual Inflation

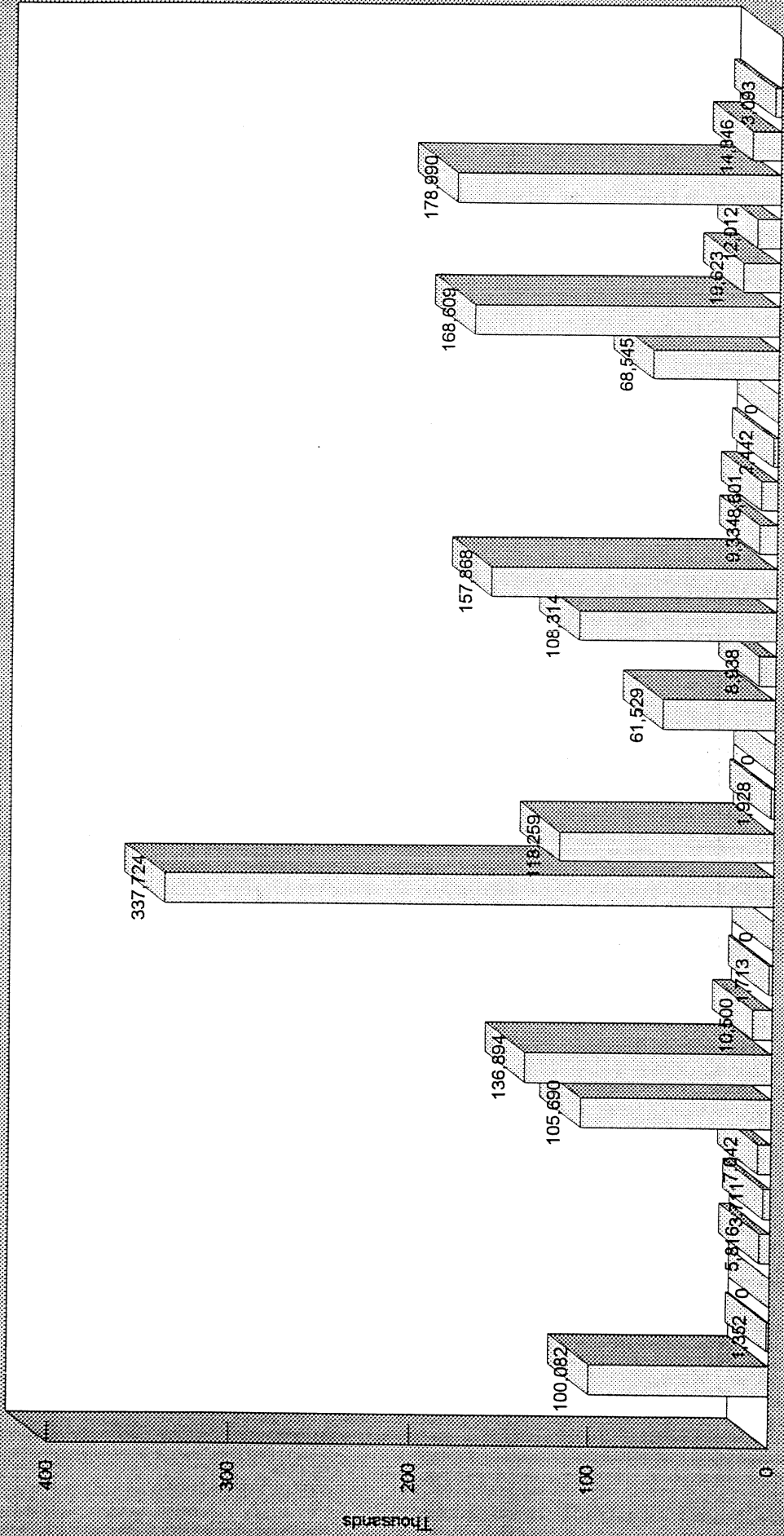


Chart 1

30 Year Cash Flow Projection
 Assuming 3% Annual Inflation

