

ORIENTATION
OF
TOWNHOME MANAGEMENT
PERSPECTIVES

BY



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OVERVIEW OF INDUSTRY

Community Associations (also known as Common Interest Communities and Common Interest Realty Associations) developed in phases over the past 170 years in the United States. Today there are more than 245,000 community associations in the US housing over 50 million people. Approximately one in every six US residents lives under the jurisdiction of a community association. The number of community associations is increasing rapidly and is expected to continue to do so in the future. In fact a significant majority of new home sales throughout the United States today are in community associations.

The Community Associations Institute commissioned the Gallup Organization to conduct a survey, "Inside look at Community Association Homeownership, Fact & Perception", from which it appeared that 89 percent of homeowners agree that living in a community association is a satisfactory housing choice. Sixty-six percent of the respondents reported that their community is "friendly or neighborly." Twenty-six percent find their community to be "distant or private" and only 8 percent "divided and unfriendly."

Research conducted by Dr Barton Smith of the University of Houston Center for Public Policy demonstrated that an effective homeowners association had a direct impact on the value of homes. During the downturn in Houston's economy during the 1980's the price of homes in effectively managed associations declined far less than homes in associations with ineffective management. The differential was as much as 18%.

ORGANIZATIONAL STRUCTURE

The organizational structure of a community association is best demonstrated by defining the basic concept.

The Association: The association of owners in a community association consists of the owners of individual lots that are subject to a Declaration whether or not such owners live on the property.

The Community: The community consists of all the residents in a real estate development – whether or not such residents are owners.

Community Associations have four fundamental things in common –

- ◆ Filing of a Declaration creating mutual obligations
- ◆ Individual Ownership of Real Estate
- ◆ Mandatory membership
- ◆ Right of Assessment

TYPES OF COMMUNITY ASSOCIATIONS

There are three basic types of Community Associations:

- ◆ Cooperatives
- ◆ Condominium
- ◆ Homeowners Association (Planned Unit Development)

Cooperatives

Each purchaser obtains an ownership interest or a share of a cooperative corporation and because of such ownership the owner has an exclusive right to occupy a unit. The entire property is owned by the cooperative corporation.

Condominium

Condominium is a form of ownership in which portions of the property are designated for separate ownership and the remainder of the property is owned in common by all of the owners of the portions. In a condominium development each purchaser acquires exclusive ownership of the interior of the Unit and a shared (undivided) ownership interest in the rest of the property. The Unit consists of separate ownership of the interior within the unfinished surfaces of the perimeter walls floors and ceilings and an undivided interest in the common property. The condominium association typically has no ownership interest in the property.

Homeowners Association

Each purchaser has exclusive ownership of a lot, including the improvements situated on the lot. The common property is typically owned by the association. There are many types of homeowners associations including townhome developments, planned unit developments, property owners associations, and master planned communities.

It is not always possible to determine the form of ownership from the appearance of the property. Garden style apartments could be a condominium, townhome or a commercial apartment development. It is essential that the legal documents be reviewed to determine the form of ownership as there are significant consequences flowing from the form of ownership. The consequences include liability for ad valorem taxation and maintenance. The legal documents may specify who is responsible for maintenance of various parts of the development, but if the documents are unclear, the owner is required to provide the necessary maintenance.

LEGAL FOUNDATION

Federal Statutes that apply to community associations include the following –

The US Constitution
The IRS Code
Fair Housing Amendments Act
Fair Debt Collection Practices Act
1996 Telecommunications Act.

Some chapters of the **Texas Property Code** apply to homeowner associations or planned unit developments. These chapters include 202, Construction and Enforcement of Restrictive Covenants; 203, Enforcement of Land Use Restrictions in a County with Population of more than Two Million; 204, Powers of Property Owners' Association Relating to Restrictive Covenants in certain Subdivisions (which only applies to Harris County); 207, Disclosure Information by Property Owners' Associations; 209 Texas Residential Property Owners Protection Act. Other

Texas statutes that apply to property owners associations include –

Texas Business Corporations Act
Texas Non-Profit Corporations Act.

The documents that form the legal foundation for the property owners association are –

1. The **Plat Map** lay out the property, establishes lot boundaries, and sometimes also defines land use. It is filed in the County courthouse.
2. The **Declaration** is sometimes referred to as deed restrictions or covenants, conditions and restrictions (CC&Rs). This document is also filed in the County courthouse. It creates the community and the interlocking relationships between the owners.
3. The **Articles of Incorporation** create the corporation and are filed in the office of the Secretary of State. The Corporation is created to limit the liability of the property owners and to facilitate dealings with the business community. It is generally created as a Non-Profit Corporation.
4. The **Bylaws** contain the procedures for operating the association such as the election of directors, voting and meetings.
5. The **Rules and Regulations** are promulgated by the Board and generally contain procedures for the use and enjoyment by members of the common property. They may also establish guidelines for the exercise of the association's authority.

The documents are listed in order of their priority. The higher-ranking document has precedence over the lower listed document. In the event of a conflict the provision of the higher-ranking document prevails. Federal and State legislation prevails over the documents and Federal statutes have precedence over State statutes. The US Constitution prevails over all statutes and documents.

There are other documents involved in real estate transactions that are not necessarily part of the governing documents for the association. These include the deed of sale and the deed recorded in the courthouse transferring the property.

Property owners are deemed to have knowledge of the statutes and of the documents filed in the County courthouse or with the Secretary of State. They are not deemed to be aware of or have knowledge of the association's rules, regulations, policies, guidelines, and procedures that are not filed in the County courthouse. It is now required that the Association's rules, regulations and guidelines be filed in the County courthouse.

ROLES AND RESPONSIBILITIES

THE DEVELOPER

The Developer in a community association plays a number of different roles –

1. Developer as Declarant -
 - Conceives and creates the community
 - Causes the legal documents to be prepared and filed of record
 - Markets the Association.

2. Developer as Owner
 - Is subject to the covenants and restrictions the same as any other owner (save for any exceptions or exemptions contained in the Governing Documents)
 - Is a seller of the lots created.

3. Developer as Board Member
 - Is subject to fiduciary obligations to Association
 - Sets policy for the Association.

4. Developer as Manager
 - Implements or causes to be implemented decisions of the Board.

ROLES AND RESPONSIBILITIES

THE HOMEOWNER

Homeowners come from diverse backgrounds and have a variety of individual expectations, Their needs and expectations also change from time-to-time resulting in different considerations being necessary to meet their constantly changing needs and expectations.

The principal **Rights of Homeowners** are –

- ◆ Use and enjoyment of the common facilities
- ◆ Receive the benefits of common services
- ◆ Have association operated in accordance with Governing Documents
- ◆ Inspect Association records
- ◆ Elect (and remove) Board Members

The **Obligations of Homeowners** include –

- ◆ Payment of assessments
- ◆ Compliance with Governing Documents
- ◆ Acceptance of Community Rules and Regulations
- ◆ Support of Association

Homeowners may **Voluntarily Participate** in –

- ◆ Attendance and participate at general and special meetings of members
- ◆ Attendance at Board Meetings (excluding Executive Sessions)
- ◆ Serve on Committees
- ◆ Serve on Board
- ◆ Vote at elections and other decisions requiring member approval.

ROLES AND RESPONSIBILITIES

THE BOARD OF DIRECTORS

The Board of Directors is responsible for the operation of the Association. The Board may delegate functions to committees and management, but is ultimately legally responsible for the functioning of the Association and the fulfillment of its purpose. A community association combines the characteristics of a local government, a business, and a community. The Board has responsibilities in all three areas:

1. Protect, preserve, and enhance the value of the assets of the association and its owners.
2. Policy-making body responsible for maintenance, administration, and financial well being of the association.
3. Community building body responsible for fostering and developing the quality of life in the community.

The **Responsibilities and Duties** of the Board include the following -

◆ **Fiduciary Responsibility**

Position of trust

Exercise care in all matters

Loyalty to association and owners

Must act in the “best interest” of the community

◆ **Must act in accordance with the governing documents**

Perform duties

Exercise discretion

◆ **Must act in “good faith”**

Avoid conflicts of interest

◆ **Must meet test of “business judgment rule”**

Decisions are to be made by Directors on an informed basis, in good faith, and in the honest belief that the decision is in the best interests of the Association.

Decisions must be reasonable

Must meet “reasonable man” test

Must protect against mismanagement

◆ **Scope of Authority**

Permit the Board to act or give it authority to act

The word “may” in the governing documents empowers the Board. The documents may state that the Board may purchase insurance or promulgate rules and guidelines.

Require the Board to act.

The word “shall” obligate the Board to act. For example, the documents may state that the Board shall purchase insurance. If the Board fails to perform the acts it is required to do, the Board and even the individual Board members may be liable.

Prohibit the Board from acting.

The Board does not have the power to amend the Declaration - only the members have this authority. The Telecommunications Act prohibits the Board from restricting satellite dishes of less than one meter in diameter.

◆ **Set Policy**

Adopt policies for the orderly operation of the Association

Adopt policies for the use and enjoyment of the common areas and facilities

◆ **Develop a Business Plan**

Develop short and long term business plans for the Association.

ROLES AND RESPONSIBILITIES

OFFICERS OF THE BOARD

The Officers of the Association are appointed by the Board of Directors at their organizational meeting immediately following the annual general meeting of Owners. Officers serve at the pleasure of the Board. They may be removed from office and replaced by the Board. They serve until the organizational meeting following the next annual general meeting of the Members.

◆ **President**

CEO and representative of the Association

Presides at all meetings of the Board and membership

Sets Agenda (with management)

Executes legal documents on behalf of the Association

◆ **Vice President**

Assumes duties of the president when president is absent

May have specific assigned tasks

◆ **Secretary**

Prepares and distributes – or causes to be prepared and distributed – minutes and other Board material

Maintains – or causes to be maintained – corporate records and minute books

Receives and verifies proxies – or causes proxies to be received and verified

Attests to the legitimacy of certain documents

◆ **Treasurer**

Prepares or causes to be prepared budget and financial records of the Association.

ROLES AND RESPONSIBILITIES

COMMITTEES OF THE BOARD

◆ **Appointment of Committees**

The Board of Directors generally appoints committees. The Board can terminate any committee appointed by it and can remove and replace members of the committee. Committees, like Officers, generally serve for one year.

◆ **Authority of Committee**

Committees act under the authority of the Board of Directors. The Board may delegate authority but not responsibility. Sometimes the governing documents give certain committees independent authority. Examples of committees that sometimes have independent authority are the Nominating Committee and the Architectural Review Committee.

◆ **Responsibilities of Committees**

Sometimes the responsibilities of the committee are set out in the Governing Documents. If not, the Board should provide a job description with clear guidelines for the committee.

◆ **Purpose of Committees**

Committees assist the Board by gathering information, making recommendations and acting when the Board gives them the authority to do so. Committees serve to broaden the community's input in decision making. Recommendations of committees are submitted to the Board of Directors for consideration.

◆ **Types of Committees**

There are essentially two types of committees: Standing and Ad Hoc. Standing committees generally serve from year to year whereas Ad Hoc committees serve to achieve a specific purpose and are then disbanded. Today, Ad Hoc committees are more commonly referred to as task forces.

Typical Standing Committees

Architectural Review

Budget and Finance

Newsletter/Communication

Social/Recreational

Examples of Ad Hoc Committees

Nominating Committee

Document Amendment

Research

Capital Improvement

ROLES AND RESPONSIBILITIES

MANAGEMENT

The role of management is succinctly stated by Wayne Hyatt in “*Condominium and Home Owners Associations: A Guide to the Development Process*” (Shephards/McGraw-Hill 1985 at page 350 as follows:

“(T)he role of management is to implement the decisions and policy established by the board of directors and to have the day-to-day responsibility for the administration of the programs, services, and activities of the association as established in the founding documents and as amplified or clarified by resolution of the board of directors or vote of the members.”

Functions of Management

Perform research as to -

- The obligations of the Association,
- The needs of the community, and
- The preferences of its members and residents.

Perform the functions of the Association, including

- Operation and maintenance of the common areas and facilities
- Monitor personnel performance
- Maintenance of sound financial records
- Effectively communicate with members and residents

Guide and advise the Board in the performance of its functions.

- Prepare all documents for meetings including the agenda and minutes of the meeting
- Report to the Board on the activities of the Association
- Obtaining proposals for consideration by the Board
- Make recommendations to the Board

Implement the decisions and policies of the Board

- Enforcing the provisions of the Governing Documents according to the standards set by the Board
- Publicizing and enforcing Association rules and regulations
- Monitor Contracts entered into by the Board

MAINTENANCE AND REPAIRS

Responsibility for maintenance and repair is generally specified in the Declaration. In the event of any doubt the Owner of the property is generally responsible for its maintenance and repair. The following are extracts from the Declaration of Green Trails Townhomes.

ARTICLE VIII

By the Owners. In addition to all maintenance obligations of Owner set forth in Article X, it shall be the duty, responsibility and obligation of each Owner at his own cost and expense to care for, maintain and repair the Living Unit and all structural elements of the Living Unit including the exterior doors, windows, their respective frames and hardware, and the foundations, and interior of all improvements on his Townhome Site including the fixtures, appliances, equipment and other appurtenances thereto, including any fixtures, appliances, equipment and other appurtenances located outside the Living Unit, but exclusively serving the Living Unit, and any plumbing, electrical, and communication lines exclusively serving the Living Unit from and including the connection from any Common lines excepting only Association-owned improvements located in any easement benefiting the Association, which shall be maintained by the Association and those elements of the Living Unit maintained by the Association in accordance with paragraph (b) of this Article VIII. The Association shall have the right to enforce the requirements of this Section by any means provided for enforcement of this Declaration, including by self-help entry and repairs by the Association at the cost and expense of a Townhome Site owner as a Special Individual Assessment hereunder.

By the Association. The Association, as a common expense of all Owners, shall perpetually care for, maintain and keep in good repair the Common Property, Common Facilities and all parts thereof and all other easements or services related to or devoted to the use and enjoyment of the Common Property and/or the Common Facilities, including but not limited to, Landscape and Irrigation Easements, Private Street Easements, Private Street Facilities, Access Facilities, Service Easement, landscaped lawns, esplanades, parking areas and improvements and facilities owned by the Association. The Association, as a common expense of all Owners, shall perpetually care for, maintain and keep in good repair the exterior building surfaces of the Living Units, including painting, roof maintenance and similar maintenance activities, but expressly excluding doors, windows, and their respective frames and hardware, any fixtures and appliances and any approved additions to or modifications of the exterior of the Living Units which are the responsibility of each individual Owner. The Board has the additional right, but not the obligation, to have the grass or vegetation in readily accessible areas of the lots cut and maintained, in a neat and sanitary manner, on the land that is owned by or dedicated to Harris County Flood Control District or any municipal utility district and that lies within the Properties (or adjacent thereto) if the appropriate county agency's or utility district's maintenance standards are not acceptable to the Board of the Association.

INSURANCE

The Association Management, Inc. group insurance program provides the following coverages -

Property Exposure to Loss. The policy is written on a "blanket" Broad Form Covered Causes of Loss basis with "agreed amount" and "full insurable replacement cost" coverages less the applicable deductible. Total coverage for the building will be equal to 100% of its estimated insurable replacement value. The following is an explanation of these terms in the policy:

1. Blanket Broad Form Covered Loss. The total amount of insurance applies to both the Common Elements and the individual Living Units, including the party walls, fixtures and installations initially installed by the Developer and their replacements, as well as any improvements and betterments made or acquired at an Owner's expense in accordance with the building standards. In short, the Property coverage on the master policy covers the Property that was originally purchased from the Developer (e.g., exterior walls, roofs, interior walls, partitions, ceilings, floors, floor coverings, etc.) excluding custom and special extras installed at an owner's expense that exceed building standards.
2. Agreed Amount. There is no coinsurance (an obligation to contribute for any loss if you are under insured) in the event of loss. There is a deductible per occurrence.
3. Full Insurable Replacement Cost. The building will be insured at 100% of its estimated insurable replacement cost.
4. Replacement Cost. Losses are adjusted without depreciation (except for carpeting), provided the buildings are repaired or replaced to their original condition.
5. Broad Form Covered Causes of Loss. The master policy covers normal risks of loss formerly considered "all risk" coverage, with some common exclusions as listed below:
 - a. Personal property of an individual owner.
 - b. Damage caused by earthquake and flood.
 - c. Other common exclusions in such policies.

In addition to the hazard coverages listed above, the master policy provides the following coverage for the Association:

Liability Exposure to Loss.

1. Commercial General Liability.
 - ◆ Bodily Injury and Property Damage Liability \$1,000,000 per occurrence, with a \$2,000,000 annual aggregate.

- ◆ Personal Injury Liability & Advertising Injury Liability.
 - ◆ Fire Damage Legal Liability: \$100,000 per occurrence.
 - ◆ Non-owned Auto: \$1,000,000 combined single limit.
2. Umbrella Liability Coverage. \$50,000,000 umbrella liability coverage; however, the Association does not provide liability coverage for accidents or occurrences that occur within the individual units.
 3. Directors and Officers' Liability. \$1,000,000 with a \$1,000 deductible per occurrence.
 4. Fidelity Coverage. \$200,000 Employee Dishonesty.
 5. Income Exposure to Loss.
 - ◆ Business Income Insurance
 - ◆ Assessment Fees Receivable Insurance. Lost assessments because of a covered loss to the Property.
 6. Workers Compensation Employers Liability Insurance.

Areas Not Covered. Because of the exclusions in the master policy, Homeowners should consult with their own agent about purchasing a policy to cover the following exposures:

- ◆ Value of the household and personal property.
- ◆ Improvements and betterments to the unit installed by the Owner
- ◆ Additional living expense.
- ◆ Personal injury.
- ◆ Loss assessment coverage.
- ◆ Value of jewelry, furs, silverware, fine art.
- ◆ Business interruptions.
- ◆ Liabilities arising or resulting from occurrences within individual units.

In certain circumstances, an Owner may have liability for all or portions of the insurance deductible of the Association's insurance policy(ies) in accordance with the Declaration, or the Rules and Regulations of the Association in effect and/or amended from time to time. The Association highly recommends that Owners/Occupants purchase insurance for the contents of the Living Unit and for liability within the Living Unit. This Homeowner's policy would provide coverage for personal property and betterments and improvements and the policy can be purchased with an endorsement, HO-382, which will pay up to \$1,000 of any special assessment levied against the Owner.

When an incident is submitted to the Association's insurance carrier for review, an investigation will be performed in determining the cause and origin of the loss. Based on the investigation, the loss will be handled according to the policy's terms, conditions and exclusions.

The following are some of the circumstances that determine the assessment of the deductible:

1. A loss occurs within the Living Unit. In this case, the Owner is responsible for the deductible. A claim should be filed with Management.
2. A loss occurs in a Living Unit as a result of an incident from a neighboring Living Unit. It is recommended that the Owner incurring damage report the loss to Management and his insurance carrier. The Owner of the Living Unit from which the damage resulted is responsible for the deductible.
3. A loss occurs as a result of a Common Facility leak or Common Property related problem. The Association's insurance will provide coverage and the Association will cover the deductible.
4. A loss occurs as a result of the negligence of an Owner, his tenant, or guest. In this case, the Owner is responsible for the deductible.

The Association's insurance policy is subject to a deductible of \$5,000 and is payable pursuant to the following policy:

"In the event that an Owner, his/her tenants, invitees or guests cause the loss or damage, or the loss or damage originates from within or is due to his/her Living Unit, such Owner will be liable for the full amount of any deductible on the Association's policy." (For example, if the icemaker water supply line in your Living Unit ruptures, you would be assessed the entire deductible amount.)