



Do Your Homework

The Complete Three Part Series

by Joel W. Meskin, Esq., CIRMS ♦ Featured in *CondoManagement* (May, July & August 2005)

PART 1:

As a provider of directors and officers liability insurance, I'm often asked about the claims brought against community association boards. The most common claims are non-monetary: challenges to elections, challenges to board member removal, challenges to architectural review board decisions, changes in bylaws, and the inequitable enforcement of association rules.

Most people are incredulous that community associations are beset by such relatively frivolous or silly claims. The next question is, "How can we avoid these claims?"

My response is, "Do your homework." By homework, I mean the general work that a board and its members must do before they conduct any business, as well as preparing for the actual running of meetings and acting on the board's duties and obligations. In this article, I'll discuss the first part, preparation that should take place before the board meets.

Understand your Duties & Obligations as a Board Member

If the association has an orientation book, read it. The board should make sure that the book is up-to-date by hiring a community association attorney or community manager consultant to make sure the book complies with the relevant state statutes.

Have the community manager, if she or he is experienced, hold an orientation meeting to discuss the duties and obligations of board members. If your association doesn't have a community manager, hire a community association attorney or community manager consultant to conduct an orientation. This orientation should be repeated every time the composition of the board changes. The expense is well worth it, and attorneys and consultants who specialize in this area know how to price the service for budget-driven asso-

ciations. Many associations can conduct the training themselves once they have gone through it. The Community Association Institute is always a good resource for this type of information.

Know your Bylaws

Did you ever try to assemble a child's toy or piece of furniture without looking at the instructions? You tell yourself that it only has a few parts, how difficult can it be? The end result is irritation, frustration, and spending far more time than if you followed the instructions in the first place.

Bylaws are your association's operating manual. And as with a toy, it is better to do it right the first time than to have to fix it later. Before a homeowner is elected to a board position, he or she should read the bylaws and understand how the association is managed. (Ideally, all association members should be familiar with how their association is governed.) Invite prospective members to attend a meeting before they accept a position. If you think that will scare them away, you have other issues to deal with.

Make sure your association's bylaws are up-to-date and that the way the association handles issues does not conflict with the bylaws. A deviation from the bylaws may seem innocuous now, but what if someone new moves into the association and moves to invalidate decisions done in contravention of the bylaws? Not only will this create acrimony, it will probably result in an insurance claim. It is a valuable investment to have an attorney who specializes in community associations review the bylaws, comparing them to the association's actual practices to make sure they are in sync. If they are not, the attorney can revise the bylaws as necessary.

Know your Covenants, Conditions, & Restrictions

While the bylaws are the instructions for how to gov-



ern an association, the CC&Rs are the rules that the board is charged with enforcing. Before a person is elected to a board position, he or she should read the CC&Rs. (In fact, even more so than with the bylaws, all association members should be familiar with the CC&Rs. Once people buy into an association, they will be deemed to have fully read and understand the CC&Rs, whether they have read them or not.) All board members should know how the CC&Rs are enforced, what procedures are used and if exceptions to the rules have been allowed that may impact future enforcement.

Prospective board members who understand their duties and obligations, and who are familiar with the association's bylaws and declarations will be prepared to take on the task of being an effective board member. Next month, I'll discuss the homework that's required for the actual operation of a board and its responsibilities.

Parenting & Board Membership

I have experience insuring tens of thousands of community associations, reviewing hundreds of community association director and officer claims, and spending years as a litigator. But my greatest qualification for advising association boards and managers comes from being the father of four.

Like parents, most board members begin with no direct relevant experience. This isn't criticism, just a reality. Not-for-profit community association boards are made up of volunteers, most of whom have the greatest of intentions. Some have prior board or organizational experience, but most do not. Despite this lack of formal experience, such association members should be encouraged to serve. It is their community and the more active the members, the more vibrant the community.

No amount of training, guidelines or manuals will ensure a perfect association board and eliminate all claims against it. But you can take steps to minimize claims and eliminate many potential problems. The steps outlined in this and future articles are not magic. There are no short cuts. (Remember how many times you have said this to your children.) But the steps to running a highly functional association do not have to be difficult and the results will be well worth the effort you put into it.

PART 2: An HOA Board's Homework

In the May issue, we looked at the preparation HOA residents should do before they take on the task of being a board member. In this installment, I'll discuss the "homework" that's required for the actual operation of a board and its responsibilities.

Make Sure Your Employees Are Doing Their Job

Throughout the country, there are between 275,000 and 300,000 community associations. Many are professionally managed and just as many are self-managed by residents of the community. If the association is professionally managed, it's the board's job to make sure the community manager is doing his or her job. Remember, the board is the employer and the manager is the employee. Make sure that the community manager's job is clear and concise, as set forth in a written management agreement. If the community manager balks at doing his or her job, it is time for a new community manager – end of question. On the other hand, when you hire a community manager, assuming they are experienced, you must let them do their job and not micromanage.

One of the board's most important jobs when hiring a manager is to conduct the appropriate due diligence. As part of this process, the board or its hiring committee should:

- Post job openings with the professional associations



that certify community managers

- Obtain a current resume
- Check out the resume and make some phone calls
- Check out references

If the applicant is a management company, the board should speak with other community associations using that company. Just as you would check the references of a nanny who is going to watch your children, you should check the references of a manager or management company that will be watching out for your home and your lifestyle.

Finally, an association must do a criminal check on any prospective community manager. If you hire a management company, anyone who is to work at your association on behalf of the company must have had a criminal check done by them, without exception. We often read stories of someone who is semi-retired, has lived in a community association for years and is a great volunteer. The association decides to hire him or her, thinking they know the person and therefore do not do a background check. This is when such a check is needed the most. Remember, the board has a fiduciary obligation and will be held responsible if this person had a criminal background and it was not discovered.

If the community manager is the one who is hiring other professionals, make sure there is no conflict of interest involved. Remember, although it is perfectly appropriate to delegate this responsibility to a community manager, the manager is still your agent and you will be presumed to have supervised and ratified his or her decision. While there is nothing inherently wrong with a community manager having relationships with lawyers, accountants, or other vendors, you must not sacrifice quality for the sake of such a relationship. The board should demand that any relationships with professionals and vendors be

fully disclosed by the community manager. This is a critical aspect of the board's responsibility to conduct due diligence and allows it to respond to any concerns by the association membership if questioned. As always, the best defense is a good offense. Moreover, the burden of proof is on the board to establish that the appearance of a conflict is not a true problem nor contrary to the association's interests.

Finally, with respect to professionals, make sure you have "express written" engagement agreements that set forth exactly what the professional will do and what the cost will be.

Every community has individuals that specialize in association work and can provide affordable services. By making use of them you won't have to recreate the wheel when every issue is confronted. As with a community manager, ask for a list of the professional's current clients and speak to them about the services they have received.

Deal with Employment & Contract Issues Properly

An association is a business and board members, although volunteers are employers and must handle employment issues appropriately. If your association is large, your legal counsel may determine that you need an employment manual. Most community association employees – as with most employees nationwide – are "at-will" employees, meaning they can be terminated for any reason. Nevertheless, the decision to terminate a manager or other employee should be done with your community association counsel. This is money well spent, as it is generally better to do it right the first time than have to fix it later. Moreover, few boards are experienced in human relations duties and obligations. Unless you have experienced community managers to handle terminations, using legal counsel is wise.



Similarly, significant contracts should be handled with all due seriousness. To begin with, the board must know what is within its authority. If a significant contract is involved, it's wise to obtain the opinion of your legal counsel, who can confirm that your board has the authority to proceed and can guide negotiations in the appropriate terms and conditions.

Conduct Meetings Professionally

Meetings are a critical part of a board's responsibilities. The board is not required to have a vote on every issue by an entire association. On the other hand, by holding meetings in the open and giving non-board members notice of topics and an opportunity to speak, you can avoid many problems. Although some items must be dealt with behind closed doors, all other items should be out in the open.

The board should adopt a clear and concise method for conducting meetings regardless of how big or small the board is. Specifically, if the board always follows the formalities, in those few instances when big issues arise and 50 people show up at the meetings, no one will be able to complain that the rules of the game are being changed due to the specific issue at hand. The board should obtain and follow Robert's Rules of Order. It should prepare an agenda, distribute or post the agenda and stick to it. You can always leave room for new issues, but limit discussion debate. Again, follow the rules religiously, because if you don't, it will come back to haunt you.

Minutes should be taken seriously. A secretary should take minutes and they should be distributed prior to the next meeting to they can be approved and adopted. In the event of a claim or litigation, the board minutes and the procedure for maintaining and approving them will be key evidence.

Handle Finances Carefully

It is crucial that the board understand what its duties

and obligations are with respect to the association and its finances. The board maintains the operating budget, annual reporting and reserve studies. The first priority is to know when these items must be done in the course of the year and who's involved: the community manager, an accountant or association volunteers. Again, the "buck stops here board." Accordingly, homework is key.

As entire separate article could be written on the importance and usefulness of reserves studies (studies of future spending needs for common areas such as roofing or paving, along with a funding plan to pay for them). As in so many other areas, you get what you pay for, so make sure your budget includes fund for a professional reserve study. Once a reputable reserve study is conducted, the cost to update it should be minimal. With a reserve study, a great deal of your financial decisions will be outlined, including: how much you need to save to protect your investment, how much you need for emergencies and what you need to operate on a daily basis.

In part three of this series, we'll examine the final important area of an HOA board's homework, insurance.

PART 3: Insurance

In parts one and two of this series, we examined the preparation HOA residents should do before they become board members, followed by the work involved in the actual operation of a board. A final key responsibility of the HOA board is obtaining and maintaining the proper insurance.

No matter where you live, there are insurance brokers who specialize in community associations. Just as you would choose a brain surgeon to handle brain surgery, you should choose an insurance broker who specializes in community associations. Don't choose a broker simply because they live in the community or



because someone on the board is an insurance agent or has a relative who sells insurance. If the agent specializes in community associations, their relationship to the association doesn't necessarily preclude them from consideration. But the board must always avoid the appearance of impropriety and must conduct due diligence in selecting an agent. The Community Association Institute or other local organizations (such as the California Association of Community Managers) can provide names of several agents to interview in your area.

As with any professional, the chemistry between the association and the professional is critical. Ask the agent how many associations he or she handles, how long they have handled these associations and what organizations they belong to in this field. It is not unusual for an insurance agent specializing in HOAs to have 100 to 1,000 associations as clients. On the other hand, having only 10 clients doesn't mean they are not qualified (your geographical area may not have large numbers of associations). But the agent should clearly know what he or she is talking about. Ask them what the typical claims are and what coverages the association should have. If they can't answer these questions, keep looking.

As with all aspects of board management, surveying other community associations is a great way to obtain insurance agents, as well as to determine what coverages you need. Community Associations are not in competition for the professionals and can learn from other communities' mistakes.

Plan Your Coverage

Every association is different and requires coverage tailored to its own needs and the needs of its members. A high-rise cooperative in Manhattan with \$3MM units may not have the same needs as a 10-home association in Arizona with \$250,000 average unit value.

Among the components of typical coverage are:

- *Property Coverage* – This is a large part of the condominium association's insurance profile. As an HOA board, you must understand – and the policy must specify – what the association's responsibility is and what the individual unit owner's responsibility is.
- *Boiler and Machinery* – Coverage against mechanical or electrical breakdown is critical for most associations.
- *Liability Coverage* – Every association needs liability coverage to protect the association and its members when individuals are injured or suffer property damage.
- *Workers Compensation* – All associations need workers compensation whether they have employees or not, even if it is a minimal policy in the event that someone claims to be an employee.
- *Auto Liability* – This coverage is necessary if the association has any mobile equipment or autos.
- *Directors & Officers Liability Insurance* – This protects the board from allegations of improper conduct committed in the course and scope of its responsibilities. Such conduct includes employment liability exposure, discrimination and general claims of defamation. D&O policies are not a big-ticket item, but are critical in that they protect board members' personal assets as well as those of the association.
- *Fidelity/Crime Coverage* – This coverage protects the association from employees or third parties who might steal amounts held in operating or reserve accounts. It includes forgery and wire and computer fraud.

One area of insurance that is often overlooked is coverage for lessees, vendors or other entities operation within the community. First, it is critical that these entities have the appropriate insurance. Second, the insurance issued to these third parties should name the association and (if appropriate) the board members as being covered. Again, the association's agent can often assist with this, and will often handle it as a value-



added service.

Homework & Discipline

In this three part series, I've outlined the basic homework of an association board. The next step is discipline, which is twofold. First, the association must continue with the homework process; an association is continually changing and the board must continue to do its homework and remain flexible. Second, once the homework has been done, use it. It is not enough to have done the preparation. You have to act on all the preparation you've done.

Managing an association does not have to be difficult. However, to do it correctly and to avoid problems that can give rise to claims, the board needs to know its duties and must operate accordingly.

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