

Association of Condominium,
Townhouse, and
Homeowners Associations



ACTHA NEWS

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and ACTHA Annual Meeting,
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Lots of Programs in May!

For details, visit www.actha.org

"Annual Budgets and Special Assessments"

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In the management and administration of condominium associations, no single issue is more important to each and every unit owner than finances. In fact, meetings related to financial matters usually have the highest attendance levels, and the most common of these relate to annual budgets and special assessments. Therefore, it is extremely important for condominium boards to strictly follow the procedures for adopting annual budgets and special assessments. Moreover, any action taken by a condominium board that is inconsistent with the *Condominium Property Act*, 765 ILCS 605/1 et seq. ("CONDO ACT"), or its own *Declaration of Condominium, By-Laws, or Rules and Regulations* ("GOVERNING DOCUMENTS"), is void as a matter of law. This article will explain the procedures for adopting annual budgets and special assessments, and address many common misconceptions and mistakes made by condominium boards and unit owners alike.

The CONDO ACT and GOVERNING DOCUMENTS

First and foremost, a condominium association must look to the CONDO ACT for guidance as to the procedures required to validly adopt an annual budget or a special assessment. While a condominium association is bound by its own GOVERNING DOCUMENTS, the CONDO ACT always prevails in case of a conflict between the two. This is a common mistake made by condominium boards and unit owners who rely on their GOVERNING DOCUMENTS without first checking to see if the provisions therein comply with

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the CONDO ACT (this is especially true of very old documents or "form" documents drafted by individuals unfamiliar with the CONDO ACT). For this reason, it is always important to review both the GOVERNING DOCUMENTS and the CONDO ACT, or seek the advice of a professional, prior to proceeding with a course of action.

Powers and Duties of Board of Managers

Pursuant to the CONDO ACT, a condominium board has the duty and power: "(a) To provide for the operation, care, upkeep, maintenance, replacement and improvement of the common elements ... (b) To prepare, adopt and distribute the annual budget for the property ... (c) To levy and expend assessments..." It is extremely important to note that almost all decisions regarding these matters are made solely by the board of directors, not by a vote of the unit owners. While a unit owner may voice his/her opinions during the open meeting in which the board adopts a course of action, the actual decision itself is made by the board.

Maintaining the Common Elements

A condominium board has the absolute authority to expend funds to maintain the common elements, and such decisions are made without the need for unit owner approval. However, if the repair, replacement, or restoration, of a common element will result in an "improvement" (i.e. change the original condition of a common element), and the cost of such an "improvement" exceeds 5% of the annual budget, then unit owners with at least 20% of the total votes may (within 14 days of the board's approval of such expenditure) petition the board to "reconsider" said expenditure. This does not apply when an "improvement" is mandated by law or constitutes an emergency. Within 30 days of delivery of such a petition, the board must call a meeting of all unit owners, at which time unit owners with a majority of the total votes can reject said expenditure. Unless all these actions are taken in a timely manner, the board's decision approving such an expenditure is forever ratified by operation of law.

Preparing An Annual Budget

A condominium board may avoid such situations (including the always unpopular special assessment) through the careful and consistent preparation of annual budgets. Pursuant to the CONDO ACT, an annual budget must include all anticipated expenses by category, all anticipated income from assessments and other sources, and reasonable reserves. Usually, the anticipated expenses and the anticipated income can be readily ascertained based upon the previous annual budget (factoring in any additional planned

expenses and inflation). However, it should be noted that an "initial" annual budget prepared by a developer prior to turnover will likely require significant scrutiny and modification since developers have a tendency to understate anticipated expenses to show a more "attractive" monthly assessment to prospective purchasers. At minimum, an annual budget should be drafted so that a condominium association's income meets all its operating expenses, with an additional amount set aside for reserves. Professional property management will be of great help to a condominium board in preparing an annual budget as they usually have significant experience and knowledge regarding these issues.

Reasonable Reserves

While the CONDO ACT provides general guidance as to the amount a condominium association should budget for reserves, the exact amount of reserves will vary greatly based upon the size, age, and location, of a condominium association, and therefore, condominium boards should seek the advice of a qualified professional in making this determination. Engineers or architects can prepare a "reserve study" which outlines anticipated expenses (both short term and long term) related to the maintenance of the common elements. For instance, if a "reserve study" shows that the roof will need to be replaced in 10 years at an estimated cost of \$100,000.00, then the board can include \$10,000.00 in reserves in the annual budget so that in 10 years, the association will have sufficient funds to replace the roof without having to go through a special assessment. It should be noted that, in certain instances, the CONDO ACT allows a condominium association to waive the "reserve requirement," but for the practical reason of having funds readily available for emergency situations, and also to maintain property values (i.e. sales or refinancing), it is recommended that condominium associations maintain a reserve account.

Adopting An Annual Budget

Once an annual budget has been prepared, a condominium board must strictly adhere to the procedures and requirements for its adoption. The CONDO ACT provides a minimum framework for this process which begins with all unit owners receiving a copy of the proposed annual budget at least 30 days before its adoption. The annual budget must be adopted in an open meeting of all unit owners, and all unit owners must receive notice of such meeting at least 10 days, but not more than 30 days, prior thereto. It is very important to note that the board adopts the proposed annual budget: unit owners do not vote. However, if the adopted annual budget would result in a 15%

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assessment increase, then unit owners with at least 20% of the total votes may (within 14 days of adoption) petition the board to "reconsider" the adopted annual budget. Within 30 days of delivery of such a petition, the board must call a meeting of all unit owners, at which time unit owners with a majority of the total votes can reject the adopted annual budget. Unless all these actions are taken in a timely manner, the adopted annual budget is forever ratified by operation of law.

Special Assessments

The CONDO ACT defines a special assessment as "any common expense not set forth in the budget or any increase in assessments over the amount adopted in the budget." In general, there are 3 "types" of special assessments: 1) non-emergency special assessments for the maintenance, repair, or replacement, of common elements ("REGULAR SPECIAL ASSESSMENT"); 2) non-emergency special assessments for additions and/or alterations to the common elements ("ALTERATION SPECIAL ASSESSMENT"); and 3) emergency special assessments ("EMERGENCY SPECIAL ASSESSMENT"). Each type of special assessment has its own procedure for adoption and ratification; but all special assessments must be separately assessed against each unit owner.

REGULAR SPECIAL ASSESSMENT

A REGULAR SPECIAL ASSESSMENT relates to unexpected expenses which do not constitute an "emergency" (as defined below), such as painting or re-carpeting (i.e. work that does not materially alter the common elements). The procedure for adopting a REGULAR SPECIAL ASSESSMENT is similar to adopting an annual budget: it must be adopted in an open meeting of all unit owners, and all unit owners must receive notice of such meeting (along with a copy of the proposed REGULAR SPECIAL ASSESSMENT) at least 10 days, but not more than 30 days, prior thereto. The board adopts the proposed REGULAR SPECIAL ASSESSMENT at the open meeting: unit owners do not vote. However, if the adopted REGULAR SPECIAL ASSESSMENT would result in a 15% assessment increase, then unit owners with at least 20% of the total votes may (within 14 days of adoption) petition the board to "reconsider" the adopted REGULAR SPECIAL ASSESSMENT. Within 30 days of delivery of such a petition, the board must call a meeting of all unit owners, at which time unit owners with a majority of the total votes can reject the adopted REGULAR SPECIAL ASSESSMENT. Unless all these actions are taken in a timely manner, the adopted REGULAR SPECIAL ASSESSMENT is forever ratified by operation of law.

ALTERATION SPECIAL ASSESSMENT

An ALTERATION SPECIAL ASSESSMENT relates to improvement projects such as lobby expansions or garage additions (i.e. work that materially alters the common elements). The procedure for adopting an ALTERATION SPECIAL ASSESSMENT is very different from adopting an annual budget or a REGULAR SPECIAL ASSESSMENT because, while the notice and meeting requirements are the same, a proposed ALTERATION SPECIAL ASSESSMENT must be approved by unit owners with at least 2/3 of the total votes. Uniquely, a proposed ALTERATION SPECIAL ASSESSMENT cannot be adopted by the board without the approval of the unit owners.

EMERGENCY SPECIAL ASSESSMENT

Finally, an EMERGENCY SPECIAL ASSESSMENT relates to expenditures mandated by law or relating to "an immediate danger to the structural integrity of the common elements or to the life, health, safety or property of the unit owners." The procedure for adopting an EMERGENCY SPECIAL ASSESSMENT is similar to adopting an annual budget or a REGULAR SPECIAL ASSESSMENT: it must be adopted in an open meeting of all unit owners, and all unit owners must receive notice of such meeting (along with a copy of the proposed EMERGENCY SPECIAL ASSESSMENT) at least 10 days, but not more than 30 days, prior thereto. The board adopts the proposed EMERGENCY SPECIAL ASSESSMENT at the open meeting: unit owners do not vote. However, unlike adopting an annual budget or a REGULAR SPECIAL ASSESSMENT, an EMERGENCY SPECIAL ASSESSMENT is final and irrevocable, and unit owners do not have a right to petition the board to "reconsider" adoption thereof.

Final Thoughts

Very few decisions by a condominium board are as closely scrutinized or as hotly debated as those relating to finances, and this is especially true in these dire economic times. Moreover, a condominium board has a fiduciary obligation to maintain the financial stability of the association. Therefore, it is extremely important that condominium boards adhere strictly to the requirements of the CONDO ACT and their GOVERNING DOCUMENTS, and seek the advice of experienced professionals in this regard.

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