

Condo Insights

#75 – Adequacy

In the context of condominiums and homeowner associations (HOAs), "adequacy" primarily refers to the financial health and sufficiency of the reserve funds. Specifically, it means the association has enough money in its reserve accounts to cover the anticipated costs of major repairs and replacements of common elements (such as roofs, building exteriors, or elevators) over a long-term period without needing to impose a special assessment on unit owners or significantly raise regular fees.

In New Jersey's Structural Integrity Act, "adequate" or "adequacy" means having enough money in an association's capital reserve fund, as determined by a professional reserve study, so that the fund balance doesn't drop below zero during the next 30 years, ensuring major repairs and replacements can be funded without needing special assessments or loans for those specific items.

Here's a breakdown of the definition. Sufficient funds refer to the amount needed to cover projected costs for common element repairs/replacements over 30 years. New Jersey's Structural Integrity Act (the "Act") requires that an association's reserve fund must be sufficient, so its projected balance never falls below zero within the 30-year window. Adequacy is determined and assessed via a capital reserve study conducted by a licensed architect, engineer, or certified reserve specialist which projects future repair and replacement costs. The primary goal of having "adequate" reserves is to ensure that owners are not hit with large, unexpected special assessments or loans for repairs or replacement of common area components.

Major mortgage entities like [Fannie Mae](#), [Freddie Mac](#), and the [FHA](#) have specific, stringent standards for condo/HOA reserve adequacy, requiring evidence like a minimum 10% annual budget allocation to reserves and a current reserve study to ensure financial health, avoid special assessments, and protect loan collateral, with inadequate reserves often disqualifying projects. The mortgage lender wants to ensure the property is a sound collateral for a mortgage.

Associations generally must budget at least 10% of their annual income for reserves, though a third-party capital reserve study showing adequacy can sometimes substitute. A current, professional capital reserve study is crucial, detailing major components, replacement costs, remaining life, and funding plans. Reserve contribution must be a clearly identified line item in the annual budget, not just a general fund. Lenders look for reserves that can cover future major repairs and replacements (like roofs, exterior waterproofing, paving and elevators) to prevent unexpected special assessments that could hurt homeowners' ability to pay mortgages.

Lenders use reserve data to assess risk, ensuring the community can maintain common elements, which protects the long-term value of the property (the collateral for the loan). Poorly funded or undocumented reserves can make a condo project ineligible for conventional or government-backed loans, impacting marketability. Requirements often must meet or exceed state-specific statutes (like recent NJ laws), with a focus on long-term financial stability.

Lenders will review the annual budget, reserve contribution as part and percentage of the annual budget, and inclusion of adequate insurance deductibles. They will also review the reserve study and potentially other engineering reports or questionnaires, as well as looking for low unit owner delinquency rates and lack of significant pending litigation are also factors.

In New Jersey, a condo board has a strict duty to disclose reserve adequacy under the Act. Boards must conduct capital reserve studies, assess physical conditions, and ensure funds for major repairs, with failure to disclose potentially impacting property values and mortgage approvals, while new communities must fully fund from inception.

A 2025 amendment to the Act states that if an association's reserves are inadequate, boards can temporarily fund at 85% for up to 5 years but must provide a prominent, 20-point bold-font notice to all owners and buyers; as well as the anticipated year and amount of any required special assessment or loan. These disclosures must be given to every buyer before closing, making them legally required for real estate transactions.

In summary, "adequacy" is a measure of a condominium association's financial preparedness to maintain its building and components responsibly over time. Condo boards have a duty to disclose the adequacy (or lack thereof) of the reserve fund to current and prospective owners so they can make informed financial decisions.

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