Condo Insights

#45 – Best Financial Practices for Condominium and Community Associations Part 1

Keeping your association financially sound involves much more than just collecting condo fees and paying bills on time. A realistic financial plan and budget coupled with timely, accurate and logically organized financial recordkeeping are important to the well-being of the association. Poor, inaccurate and disorganized financial management results in unnecessary inefficiencies and can lead to unintended and unwanted consequences for the association and its board. This article will identify many of the best financial practices for condominium, community, and homeowner associations.

The business of the association begins with payments of owner fees, being applied accurately and in a timely manner. All unit owners are members of the association per the Master Deed. Owner fees, also known as maintenance fees, condo fees or HOA fees are paid by all members in a condominium, community, or homeowner's association to cover the ongoing administrative, operating, maintenance, common utilities, and insurance expenses. The individual condo unit fee is typically a percentage of the association's annual budget based on the unit's common interest percentage. The association budget is largely determined by the facility's location, size, the amenities offered, and the annual reserve contribution to replace association assets when they reach the end of their useful service life.

Associations benefit by making it easy for members to pay their fees. Some associations offer their members multiple ways to pay. The most common method has been for owners to pay by check. In recent years fewer owners are hand-writing checks, instead opting for online bill paying services. More recently, associations have offered members automatic online debit of their bank account to pay these recurring fees. From an association perspective, automatic debit is the most efficient, accurate and timely payment method. Some associations even accept credit cards for payment. Systems that allow owners to set up recurring payments automatically are becoming more prevalent. A major advantage of automatic payment is the reduction in delinquency rate or lingering small balances when condo fees change.

Sound financial practices include a collection policy. A collection policy defines the date on which fees and assessments are due, the grace period for payment of the fees, as well as late fees and/or penalties in event a member pays after the grace period or fails to pay. For most associations, fees and assessments are typically due on the first day of the period. The grace period varies by association but is usually ten or fifteen days for associations that require monthly payments. Associations that require quarterly payment may have a thirty-day grace period.

A collection policy will include a surcharge for late payment if fees are not paid before the end of the grace period and may stipulate increasing fees for ongoing delinquency. The collection policy should spell out additional steps the board is authorized to take against delinquent members to collect unpaid fees and assessments. Such actions may include filing liens and imposition of additional collection costs against the delinquent member if an attorney is involved, and possible acceleration of fees. Additionally, delinquent members usually lose their "good standing" status which results in suspension of privileges to use the association's recreational facilities and amenities and loss of voting rights.

When it comes to bill paying, many associations have their treasurer write a check or make electronic payment as bills are received. When it comes to financial recordkeeping, accounting experience is beneficial, but accuracy is essential. Categorizing, classifying, and documenting both income and expenses is important so board members (both current and future) can fully understand what it costs to operate the association.

A chart of accounts is used to categorize, classify and record financial transactions in a meaningful way. Expense categorization leads to better understanding of the association's expenses. Typical association expense categories include administrative expenses, insurance, operating expenses, utilities, and reserve contributions.

Administrative expenses include such items as postage, copying, licenses & inspections and professional fees. Insurance expenses include property, liability, officer's insurance, and flood insurance premiums. Operating expenses include the costs to operate and maintain the building, grounds, pool, and essential equipment such as elevators, fire alarm and suppression systems, domestic water pumps, and swimming pools. Utilities include electricity, gas, cable and internet, water, and sewer. Reserve contributions are the portion of the budget set aside for replacement of association assets and significant maintenance to the building and facilities. The association's chart of accounts should be as specific as possible. Subcategories may require additional effort, but the details and documentation will benefit the association (and future board members) over time.

Accounting/bookkeeping software can facilitate and expedite the financial recordkeeping process so long as it is used consistently and correctly. Some associations are utilizing online accounting. When all accounting activity is in one place it is easier to manage. An online or digital bill approval system allows Board members and key staff to review and approve bills before payment is processed. Since all accounting information is stored securely offsite in a server, there is little chance for loss of information. Even if financial data is stored on a server, duplicate or triplicate backup systems are part of a sound fiscal management program. Financial transactions can be recorded using accounting software, but there should always be written support including contracts, receipts, invoices, and deposit tickets.

There are several accounting methods available, but the accrual method is generally the preferred method for condominium and community associations because it conforms with Generally Accepted Accounting Principles. Under the accrual basis, revenue is recorded when earned and expenses are documented as soon as they are incurred.

Implementation of internal controls includes systems put in place to assure that fees are recorded and accounted for and expended following the budget, and also includes pre-authorization of significant expenses, board authorization of contracts, online bill review and approval. Internal controls serve to make certain that costs billed and paid for services are accurate and safeguards against theft. At least one board member should review and approve operating expenses and two board members should approve reserve expenses.

The second part of this article will discuss financial reporting, annual workplans, budgets and additional fiscal practices for condominium, community, and homeowner's associations.

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