Assessment Increase Q&A

Hot Springs Village faces a major financial challenge that will greatly affect our future. An assessment increase has been recommended and all HSV members in good standing will be asked to vote on this issue. If approved this fall, the new rate would take effect January 1, 2015.

The assessment increase recommendation is a call to action for our future – to restore the financial health of the Village and keep things running properly. This strategy will complement an aggressive marketing approach by the POA to attract new lot and homebuyers as well as developer investment to promote and grow.

The following information reflects answers to questions and concerns raised by Villagers in emails and during the July 16 town hall meetings. The goal of this Q&A is to address these issues in a way that will aid Village members in making an informed choice.

Q&A ADDED 15 SEP 2014:

Q. Are there significant blocks of investors in HSV?

A. No. As of August 15, 2014, there are 70 HSV “investors” (those owning five or more lots in good standing – excluding the POA), and the total number of unimproved lots they own is 1,075. The maximum owned by any one investor is 142, and only two others own more than 72. These investors span 16 states.

The total number of unimproved lots in good standing in HSV is 16,681. The POA owns 2,351 of these lots.

Q. Don’t the draft budgets for 2015-2017 indicate that there’s plenty of cash to avoid a near-term shortfall?

A. No. The draft budget that assumes no assessment increase allows only for a reactionary response to the crisis of the day.

The following is provided by Lesley Nalley, CFO for the POA:

Scenario I = Assessment increase does not pass; Scenario II = Increase Does Pass

With regard to Scenario I, the budget memo states “While this scenario was prepared to safeguard cash as long as possible, as evidenced by the growing outstanding capital
balance, it is not sustainable beyond 2017 without significant cuts to amenities and programs. Under this scenario, such cuts must be discussed by 2016 for implementation in 2017 & beyond”. Scenario I requires immediate decisions on which specific amenities and services we are willing to forgo in order to properly fund those deemed to be core offerings. There are millions of dollars in pending and deferred maintenance awaiting our stewardship, regardless of the path chosen. Since our amenities are costly to maintain, we can either begin closing them, maintaining them at a lower standard, or properly plan their funding at the same or increased standards.

Pointing to one line on a financial statement or budget and declaring either health or insolvency is irresponsible. To be relevant, financial data must be used in its proper context with an eye to the future. When considering the comprehensive information provided, you clearly find a cash flow problem that cannot be solved by cutting routine expenditures. This problem exists because we do not yield enough cash from our operations to fund all current amenities at an appropriate level. Notice in Scenario I that our operating profit hovers between $3.5mil and $4mil. This line reflects only operational spending and does not address the $27mil in capital either budgeted or held as of today, or the additional $300k of paving and $200k of sewer maintenance being deferred annually.

Perhaps the most misunderstood line of the budget is “Total Cash at Year End”. Yes, we arrive at just over $5mil by 2017 under both scenarios, but one offers a proactive path to spending and one is reactionary to the crisis of the day. Over the three-year period shown in Scenario 2, we complete $5.3mil more in backlogged capital projects and $700k more in deferred maintenance than would be completed under Scenario I. Additionally, we are able to reserve/save $600k more to continue catching up. In other words, in Scenario II, we are able to reverse the trend of deferring basic services and maintenance. We still don’t have unlimited cash, but we can proactively plan spending rather than spending in crisis mode, which is always more costly.

For the person that says we will be back at this point in 5 years: I disagree, as long as we recognize that absent savings in the bank (reserves), grants, or intentionally and thoughtfully using bond debt, we can only spend what our operations yield. $3.5mil of operating profit is insufficient to support the amenities offered today. Under budget scenario II, our operations yield approximately $2mil more per year.

Q. What does the POA do to try to collect on delinquent assessments?

A. Accounts delinquent for 120 days are sent to a third-party collection agency. Interest (6% per annum), penalties ($5/month), and collection fees are added to the account balance. Accounts delinquent for another 137 days are sent to a different
third-party collection agency. Interest, penalties, and collection fees continue to be added to the account balance.

HSV’s Declarations state:

If the assessments are not paid on the date when due. . .then such assessment shall become delinquent. . .and shall, upon the election of the Association to declare the entire assessment due and payable, together with such interest thereon and cost of collection. . .thereupon becoming a continuing lien on the property which shall bind such property in the hands of the then owner, his heirs, devisees, personal representatives and assigns. The personal obligation of the Owner to pay such assessment shall remain his personal obligation and shall not pass to his successors in title unless expressly assumed by them.

If the assessment is not paid. . .and the Association shall declare the entire assessment due and payable, the assessment shall bear interest from date of delinquency at the rate of 6% per annum, and the Association may foreclose the lien against said property, or may bring an action at law against the individual(s) or entity personally obligated to pay the same. . .There shall be added to the amount of such assessment the costs of preparing and filing the complaint in such action, and in the event a judgment is obtained, such judgment shall include interest on the assessment. . .and a reasonable attorney’s fee to in fixed by the court together with the costs of the action.

The POA is taking advantage of all available avenues to collect on delinquent accounts. It ceased foreclosing on lots in 2012 due to legal costs involved, and it ended its acceptance of quit claim deeds in May 2014 for all but the most desirable properties.

Q. I pay more to the POA than just my assessment. Why are these fees not factored in to the assessment increase proposal?

A. The assessment increase proposal addresses only those items identified in the HSV Declarations:

The annual assessment. . .shall be used exclusively for the purpose of promoting the recreation, health, safety, and welfare of the Owners in The Properties and in particular for the construction, improvement and maintenance of properties, service and facilities devoted to this purpose and related to the use and enjoyment of the Common Properties and the improvements situated upon The Properties, including, but not limited to, construction of the water system and sewer system, the payment of taxes and insurance on the Common Properties,
and repair, replacement, and additions thereto, and for the cost of labor, equipment, materials, management and supervision thereof.

There are usage-based fees, such as water, garbage collection, golf, etc., which are set by the Board each year and don’t require a membership vote. The Board believes that the case for increased assessment revenue better aligns with the purpose of this revenue as stated in the Declarations. Should the assessment increase proposal not pass, however, the Board will have no choice but to increase some usage-based fees to increase overall revenue.

Q. Isn’t the two-tier system discriminatory? Won’t it create two classes of members? Isn’t it unfair?

A. In 2003, the legitimacy of the two-tier assessment system in Bella Vista was challenged, and eventually upheld by the Arkansas Court of Appeals. The HSV board believes that the Hutchens doctrine applies to HSV.

The following excerpts are verbatim from the court case:

*In applying the reasonableness test, the reviewing court had to determine:

1. whether the decision . . . is arbitrary,
2. whether the decision . . . is applied in an even-handed or discriminatory manner; and
3. whether the decision . . . was made in good faith for the common welfare of the owners and occupants. . . .

Courts will especially consider whether the majority’s action has an unfair or disproportionate impact on only certain . . . owners. The reasonableness test protects against the imposition by a majority of a rule or decision reasonable on its face, in a way that is unreasonable and unfair to the minority because of its effect is to isolate and discriminate against the majority. It provides a safeguard against a tyranny by the majority.

. . . the facts in this case demonstrate the need for limitations on the majority’s authority to change the method of assessments. We hereby adopt the "reasonableness" test and conclude that the power of the governing body of a property owners’ association . . . to make rules, regulations, or amendments to its declaration or bylaws is limited by a determination of whether the action is unreasonable, arbitrary, capricious, or discriminatory.
. . .the declaration does not state that the maximum and minimum must be the same for all lots.

. . .the different assessments did not create different classes of members. The distinction was rationally based on the purpose of the fees, i.e. owners of improved lots are more likely to use and need the benefits of security than owners of unimproved parcels of land. The distinction did not affect the other rights or obligations of the members in any way.

Likewise. . .members are charged varying "usage" fees for use of various POA amenities, but even more significant is the fact that the declaration does not specifically require equal assessment.

Therefore, [the appellate court held] that the creation of a two-tiered assessment scheme by the Bella Vista Village POA’s members was not unreasonable, arbitrary, capricious or discriminatory.

Click here to read the entire case.

PREVIOUSLY PUBLISHED Q&As:

1. Why an assessment increase?

- The overall goal of the recommendation is to raise sufficient money to maintain HSV facilities and services at a high level that will protect property values, attract new, long-term development, and carry the Village into the future.

- HSV faces the reality of infrastructure that is aging, and in many cases, has not been properly maintained due to lack of funds in recent years. Numerous high-ticket items have been deferred far too long.

- In the meantime, decreased assessment revenues because of non-performing lots have placed a significant burden on our budget and our ability to maintain infrastructure and services at the proper level.

The bottom line: As of June 30, 2014, there were 8,822 lots – 25.8 percent of the Village total – no longer generating assessment income for the POA. That number comprises 6,477 lots whose assessment dues are 60 days or more past due, and 2,345 lots in the POA inventory, having already been returned to the
POA. Those lots represent $3.2 million in lost assessment revenues in 2013, and $13.8M in uncollected assessments since 2006.

- When Cooper Communities began developing the Village in the 1970s, facilities and roads were new and maintenance needs were low, so HSV’s financial practices did not include funds for long-term maintenance and capital needs. Now, 44 years later, we need to change that business model by recognizing the need for additional revenue to restore and maintain services and facilities that, in turn, will strengthen property values.

- An assessment increase offers a solution for funding deferred infrastructure repairs and ongoing capital needs. It’s an opportunity to keep the Village functioning properly, protect property values, and build a long-term foundation on which to grow.

2. What will the assessment increase pay for?

- The additional revenue will be used toward deferred and ongoing infrastructure maintenance, ongoing capital needs, and unforeseen emergencies.

Having cash reserves for unforeseen emergencies is good planning for any community. For example, the April 2011 tornadoes cost the Village more than $600,000 in cleanup efforts. Following the December 2012 ice storm, we were fortunate to receive more than $1 million in cleanup funds from FEMA, Saline County and Garland County; however, we cannot count on that type of financial support in the future, which means we’ll need to be ready to respond if necessary.

- Examples of priority infrastructure repairs.

(a) Village roads
   What this means: Maintenance and surfacing of the Village’s 470 miles of paved roads. Projected cost: $6.3 million over five years

(b) Water supply
   What this means: Replace deteriorating water supply lines in the older parts of the Village to prevent service interruptions, water losses, and excessive repair costs.
   Projected cost: $1.25 million over five years

(c) Sewer / rainwater infiltration issues
**Assessment Committee**

**What this means:** Replace broken sewer pipes and repair manholes (primarily in the west end of the Village) that allow excess water to seep into sewer lines resulting in the overloading of our waste water treatment plants, and putting us at risk for fines from the Arkansas Dept. of Environmental Quality.

**Projected cost:** $2.5 million over five years

(d) Rebuilding the Cortez fire station roof

**What this means:** Reconstruct the roof which is currently structurally unstable.

**Projected cost:** $100,000 – $180,000

(e) Culvert replacements

**What this means:** Repair/replace broken drains under Village roadways.

**Projected cost:** $500,000 in 2015; then $250,000 per year for maintenance

(f) A/C units in the Woodlands Auditorium

**What this means:** Continue replacing all inefficient, costly units in the Woodlands, and install a new control system to coordinate all A/C units in the Ponce de Leon complex. (Note: There are A/C units in other POA buildings that will need to be replaced in the future.)

**Projected cost:** $316,000 over three years

(g) Lake management program

**What this means:** Performing basic maintenance on Village lakes.

**Projected cost:** $150,000/year

(h) Replacing high-ticket equipment

**What this means:** Replace rolling stock like fire trucks ($750,000 each), trash trucks ($150,000 each), police cars, dump trucks, mowers, tractors, etc. – all key elements of maintaining our quality of life.

**Projected cost:** $2 million per year

- Funding is also needed for the deferred infrastructure maintenance and repairs on the Village’s 94 buildings and other facilities. Those expenses will be addressed over time depending on the priority of repairs and available funds.

- Capital projects currently in the POA’s five-year plan will be reviewed and voted on individually by the Board to be sure those projects are needed and cost-managed. For example, if golf rounds and revenues continue to decrease, total renovations of the Balboa and Coronado golf courses may be deferred until such time as a significant increase in usage justifies the capital expenditure, or another usage is determined. In the interim, however, minimal repairs on items
like an irrigation system may occur to maintain a course at a basic level.

- Another consideration for continued capital funding may be for general use facilities like the DeSoto Club. The current plan is to fund a Desoto Club/Outdoor Pool Complex using $700,000 previously reserved for pool renovation, $450,000 in insurance proceeds, and an estimated $1.1 million in additional funding.

- **Revenue from an assessment increase will not be spent on new amenities or new programs.**

### 3. What is the plan?

Hot Springs Village is taking a three-pronged approach to financial recovery, strengthened property values, and future growth. The **assessment increase** – which is the **only component Village members in good standing will be voting on in the fall** – is one of those prongs.

**Three-pronged approach for the growth of the Village:**

1. **Assessment increase:**
   - A rate increase is the best action that can be implemented in a timely manner to begin taking care of our most pressing infrastructure and capital needs.

2. **Improved amenity performance:**
   - Going forward, we need to decide how best to lower subsidies without sacrificing quality, and without placing the full burden on our amenity usage fees. For example, increasing golf revenues with more rounds from guests and visitors is but one way to increase that amenity’s performance.

3. **Funding for future growth:**
   - While the other two “prongs” of the plan are aimed at maintaining the current level of facilities and services, this is the long-term component which is aimed at growing the Village and raising funds for its future operation and improvements.

   This component consists of:
   - Outreach efforts to lot owners to reverse or at least slow the trend of abandoned lots;
   - A coordinated marketing campaign to attract new lot and home buyers;
   - A program to attract developers to help finance the growth of HSV;
• The development of a variety of home and lifestyle options to broaden our attraction to more buyers;
• The development of new sources of revenue like a capital buy-in fee on new owners purchasing property in the Village; and,
• A continuing effort to improve the efficiency of our operations.

4. What is the impact of not funding maintenance projects on our infrastructure and capital needs?

• If we continue to defer key infrastructure projects, the cost for repairs or replacements will increase. Further delays will result in much greater expense long-term, and could cause building closures and major breakdowns in services in the short-term.

• A continued decline in our infrastructure will reduce the quality of life in the Village and could contribute to an increase in non-performing lots. We cannot afford to lose our competitive edge in the real-estate marketplace.

• Maintaining the Village will attract new property owners and developer investment to help grow the Village.

• An assessment increase will also help us establish a cash reserve allowing us to respond more quickly to unforeseen emergencies.

5. Is a $65 monthly rate adequate? Will that amount solve our problems?

• The POA and Board believe that $65 per month will sustain our level of services and facilities through 2020 while allowing time for the other two elements of the three-pronged approach (refer to Q&A #3) to position us where we need to be financially.

• The recommended assessment increase is not intended to solve all problems at the expense of current Village members. As our community grows, our revenue will grow, giving us additional resources for infrastructure and capital needs.

• It will be the responsibility of POA management and current and future POA Board members to:
  (a) make prudent decisions on how our money is spent,
  (b) address the most critical infrastructure and capital needs,
  (c) keep our current amenities in good order,
(d) implement an aggressive marketing campaign, and
(e) identify new revenue sources to fund our future growth.

6. Will we continue to subsidize amenities?

- One of the responsibilities of a homeowners association is to provide and maintain basic amenities for the collective whole that could not be done as individual property owners.

- Amenities are a key factor in attracting homeowners to a community and a primary reason why most of us moved to the Village. Some residents don’t play golf; others don’t go to the pool or use the library, the Woodlands or the trails. However, all of the amenities contribute to the total quality of life and property values in the Village.

- For example, an outdoor swimming pool is a basic amenity found in almost all high-quality communities, and one that most people expect to find when considering a move to the Village. In fact, this was one of the first amenities built by John Cooper because he recognized its value when marketing the Village. The cost of repairing our 40+ year-old pool exceeds the cost of replacing it, and we have an option of replacing it with a version which requires less actual maintenance and staffing, while still fulfilling the community’s needs.

- Maintaining a variety of amenities keeps us competitive in the real-estate marketplace. However, we need to carefully review all future subsidies, cost-saving measures, and usage fees to keep our expenses and fees at a reasonable level.

7. Will the assessment increase include funding for new amenities?

- No. The third component of our three-pronged approach to financial recovery, strengthened property values, and future growth (refer to Q&A #3) includes a plan for funding future growth, which is separate and independent from the assessment increase.

- Providing amenities is an important part of creating value and a good quality of life for current and prospective residents. However, it must be done at an appropriate level based on the financial health of the community.

8. Why a two-tier approach to an assessment increase?
A two-tier system is an equitable method of increasing revenues for priority infrastructure and capital needs without accelerating the rate of returned lots.

No system is perfect or equitable in all scenarios. However, having two tiers draws greater revenue from properties that receive the greatest benefit from the services, amenities and overall quality of life provided by the Village. All improved properties receive benefits equally regardless of amenity usage or property values.

The majority of the assessment revenue is coming from owners who don’t use or need what the money pays for. An increase in assessment revenue will not benefit them directly. It has been that way throughout the history of the Village, and it will continue to be that way until either we change our assessment format or we get more than half of the lots developed. Since it is quite likely we will not achieve 50% developed in the next decade or more, it must be time to change our assessment format.

If we implement the $65 assessment on improved lots in January 2015, improved lots will pay 46.1% of the assessment revenue and unimproved lots will pay 53.9%. The unimproved lots would still be paying more than half but we would be moving in the right direction, the fair direction.

9. Why can’t assessments be based on the value of each property? (Sometimes known as “ad valorem”)

This is one of the alternatives considered before settling on the two-tier assessment. It was rejected because:

a. Whereas we have legal advice and an Arkansas court decision saying the two-tier assessment is legal, there has been no legal test of an ad valorem assessment in Arkansas for a private corporation type of community such as ours. Therefore, we would risk a long legal process to defend against any challenge to this approach.

b. An ad valorem assessment would result in not two, but multiple, tiers, resulting in increased internal strife among property owners. The owners of unimproved lots would still have the lowest rate, and the owners of improved lots would be divided into several different rates. The result among improved lot owners would be all would receive the same benefits from the assessment revenue while paying widely varying amounts for those benefits. That would surely be perceived as unfair and would be a motivation for a legal challenge.
c. Because Garland and Saline Counties do not assess real property exactly the same, owners of identical properties could wind up in different assessment tiers, creating another perception of unfairness.

   d. Implementing an ad valorem assessment would be a complicated and burdensome task for the POA staff. Obtaining the assessed values of all properties and establishing a database for that information could take months of manual labor. Then, the database would not be static because owners often appeal their assessments and get changes and counties recalculate the assessed values periodically.

10. When will the ballots be sent out and will the votes representing the non-performing lots be used in the count?

   • Ballots will go out 30 days in advance of the election date, only to Village members in good standing. Once the election date is set by the Board, it will be announced on the POA website and communicated through various print and electronic communications. There will also be instructions about the return date for the ballots and when the final vote count has been determined.

   • The Board must cast the votes representing POA-owned lots. However, those votes must be cast in the exact proportion as the HSV membership votes based on the returned ballots. In other words, the POA votes cannot change the outcome as reflected in the returned ballots; they would have meaning only for purposes of attaining a quorum if needed.

If you have additional questions about the assessment increase topic that are not addressed here, please send them to boardmembers@hsvpoa.org.