

Budget Submittal and Review Summary for Those Required to File With the Department

Regardless of the type of common interest subdivision you are involved with, completing a Duplicate Budget Package (DBP) for Department review is very important. The information necessary for compliance can be found in the application packets RE 624 (Common Interest), RE 635 (Amendment/Renewal), RE 658 (Stock Cooperative or LEHC), or in the Subdivision Public Report Application Guide (SPRAG). The instructions and guide are available at the subdivision offices in Sacramento or Los Angeles.

The general procedures given here will apply to the majority of the projects reviewed by the Department. Completing the budget form (RE 623), including computing various costs, is explained in the remainder of the manual. Other required forms or documents are listed in Parts I and II of the application packets. You may wish to contact the Department's Budget Review Section for additional information.

Plans and Maps

As part of the submittal, a plot or site plan is required. This plan should show the layout of the buildings, streets, recreation facilities, walls and entry structures, if applicable. Also, the plan should be a scale drawing. Large, especially phased, projects may require a separate plot or site plan for each phase. A map showing the phasing plan for the entire project must also be submitted.

The tract map and/or condominium plans should also show legible dimensions and be a scale drawing. All of these are necessary for verification of area calculations and location of the common facilities. A legible and adequately detailed vicinity map is required.

Phase Projects

When submitting DBPs for phased projects, only provide budgets for those phases that are projected to be completed within three years. If the association has been formed, see the Existing Homeowner Associations Section below for procedures. Also, an estimated assessment for the built-out project should be submitted. Budgets are

considered acceptable for 24 months from the date the Special Investigator completes the review. Changes in the offering budget or non-issuance of a Public Report before 24 months expire may be cause for a second review of the budget.

Existing Homeowner Associations

When submitting a DBP for review of an existing homeowner association, the following information should be included in the Duplicate Budget Package:

- The association's current financial statements (audited, if available) for the past two years or from start-up, whichever is less; balance sheet (less than 90 days old at the time of submittal); and a year-to-date statement (current year only).
- A copy of the current or latest reserve study as required by Civil Code section 5550.
- The Assessment and Reserve Funding Disclosure Form required by Civil Code section 5570.
- A copy of the association's current adopted budget. If the HOA has approved the budget for the next fiscal year, also include and indicate the commencement date for the fiscal year.
- A statement from the association showing the dollar amount of past due delinquencies. In particular, the statement should indicate assessments due, if any, from the subdivider.
- A copy of the Association's most current reserve and operating bank account statements (less than 90 days old at the time of submittal).
- A copy of the following information as required to be distributed to the membership under Civil Code section 5300 (a comprehensive reserve study should cover the items listed below):
 - The amount of the total cash reserves of the association currently available for replacement or major repair of common facilities and for contingencies.

- An estimate of the current replacement costs of, and the estimated remaining life of, and the methods of funding used to defray the future repair, replacement or additions to, those major components of the common areas and facilities that the association is obligated to maintain.
- A general statement setting forth the procedures used by the governing body in the calculation and establishment of reserves to defray the costs of repair, replacement, or additions of major components of the common areas and facilities for which the association is responsible.

After the above documents have been reviewed, it may be necessary to request additional information if a clear picture of the financial status of the association is not presented. If the existing association has operating deficiencies and/or underfunded reserves, a special note will be included in the Public Report.

If the subdivider is delinquent in payment of assessments, then the subdivider will be required to pay the delinquent assessment amount prior to the issuance of the Public Report. Also, reserve delinquencies owed by the subdivider must be remedied prior to the issuance of the Public Report, or a special note will be included in the Public Report, depending on the circumstances.

Conversions and Existing Structures (more than 12 months old)

For submittal on buildings converted to, or previously built as, condominiums or stock cooperatives, TICs, a Reserve Study must be completed and included with the DBP. A RE 639 form must also be included in the DBP if the project is a conversion. If a reserve component has been replaced or renovated after the reserve study has been completed, then supporting documentation should be included in the DBP. Reserve amounts in the budget may change depending on the remaining life of the building components and equipment. The costs shown for reserve estimating in this manual are for new building components and equipment. Also, shown in the reserve section is the expected useful life of each item.

Reserve Studies

The Department of Real Estate understands that data provided in a reserve study may not always be a perfect fit with the format provided in the DRE budget form. In addition, the Department will normally accept the data from a competent reserve study, except where errors are found. Aside from this, the information used from the study should match that included in the DRE budget form.

The reserve study must be current (no more than 24 months old) and prepared by a qualified, independent professional company.

Bonds for Completion

When using a bond as security for completion of on-site construction work, RE 611 must be completed and submitted for review and acceptance by the Department. Hard cost and/or in-house estimates must include an additional 20% in the total cost to complete. Items that are subcontracted and are verifiable by executed contracts normally need not include the 20%. Also, an annual inflation factor should be added, prorated on a monthly basis, for the months left until completion.

Although not specifically required, if the completion bond includes the living units, building plans may be requested if the required maps/plans are inadequate for cost verification.

Worksheets

As noted earlier, this manual contains forms and worksheets to assist you in preparing a budget. It is important that all worksheets and forms are completely filled in (if applicable) prior to submittal to the Department of Real Estate.

Cost Centers

The “cost center” term, as used for budget purposes, identifies an area of a project used by only some of the owners within a homeowners’ association. Typically, this may be a guard gate or recreational facility utilized only

by a portion of the association membership. It would be unreasonable in these cases to require all members of the association to contribute to the maintenance of a facility only benefiting a portion of the project.

A cost center may also be used for projects with mixed product types. When a project includes both attached and detached units, a cost center can be created to provide for the exterior maintenance of the attached units. Additional maintenance costs for special benefit facilities/services, or exterior maintenance of certain product types within the project may be managed through a cost center or a sub-association.

Range of Assessments

Defined: Range of Assessments (ROA) is a method or procedure used for setting up an assessment/budgeting program for large projects with multiple builders or one builder with multiple product types. The estimated range is established for the project through review of the proposed assessment program from start-up to build-out. The range is useful for projects with multiple product types and provides flexibility for phases to close out of sequence. The minimum size of a project for use of this procedure is 150 lots/units, and 10 phases, including build-out. The ROA shall commence after Phase 1 and may include additional stand-alone phases prior to the ROA procedure commencing. Any exceptions to these criteria would be considered on a case-by-case basis.

For use of this procedure, the ROA budget package may be submitted to the Supervising Special Investigator for a preliminary review and approval, or it may be submitted at the time of filing the Duplicate Budget Package. Contact the Budget Review Section for more information.

Once the ROA procedure is approved by the Supervising Special Investigator of the Budget Review Section, the budgets are reviewed by staff upon DBP submittal for accuracy, quality, and sufficiency within our minimum cost manual guidelines.

Level Assessment Procedure

Defined: The Level Assessment procedure is a method used for setting up an assessment/budgeting program for large projects with one or more subdividers. Generally, the

Level Assessment selected falls within a range of the actual assessments, which are both above and below the level amount. Also, the level amount can be “stepped,” usually down, as the assessments decline towards build-out.

The estimated Level Assessment or assessments are established for the project through review of the proposed assessment program generally from start-up to build-out. The established level assessment amount cannot be more than 15% above or below the actual estimated assessment for any given phase. Any “step” in the Level Assessment must include a minimum of three phases. The minimum size of a project for use of the procedure is 100 lots/units with 10 or more phases.

By definition, there will be phases where the established level amount is less than the estimated actual expenses or budget. For that reason and in order for this procedure to be viable, some surplus funding of the operating account is necessary in the initial phases of the project. During the life of the Level Assessment Procedure, the cumulative operating surplus, combined with actual assessments, should not drop below three months of funding, or 10% of the current monthly budget, whichever is higher. Any exceptions to these criteria would be considered on a case-by-case basis.

For use of this procedure, a preliminary review and approval should be completed prior to filing with the Department. Contact the Budget Review Section for more information.

Once approved for use by the Supervising Special Investigator of the Budget Review Section, the budgets are reviewed by staff upon DBP submittal for accuracy, quality, and to make sure they meet our minimum cost manual guidelines.

Large Increment Assessment Procedure

Defined: The Large Increment Assessment Procedure is a method of structuring an assessment program for very large projects, normally master-planned communities, with multiple builders and front-loaded amenities. Use of this procedure requires that the number of lots/units per increment (similar to a phase) not be less than 300 and that the minimum size of the overall project not be less than 1200 lots/units.

Each subsequent increment, including construction of the infrastructure, must be contiguous to the first or previous increment annexed to the project. Also, this procedure requires the use of a Deficit Subsidy Agreement which requires the developer to subsidize any excess of expenses over revenue. Builders are required to only pay assessments on unsold lots/units that are subject to a final Public Report.

For use of this procedure, it is recommended that a preliminary review and approval be completed prior to filing with the Department. The minimum documents required for review include: the incremental budgets, including HOA Common Facilities (RE 624A) forms completed for the first three years of the project, plus build-out; a phasing map that depicts all of the increments; a draft deficit subsidy agreement; a range of assessment; spreadsheet for each increment; and a current marketing study. The marketing study should be prepared by a third-party professional not related to the developer and must include the projected sales absorption rates from start-up to build-out.

Once the procedure is approved by the Supervising Special Investigator of the Budget Review Section and the filing for a final Public Report is received, the budgets will be reviewed upon DBP submittal by staff for accuracy, quality and to make sure they meet DRE minimum cost manual guidelines.

Ratio Utility Billing System (RUBS)

Using a RUBS for allocating various commonly metered utility expenses (typically water) based on unit size so they can be excluded from the association budget is not acceptable under DRE guidelines. Liability for these common expenses still lies with the homeowners' association and must be included in the budget. When applicable, allocation of common utilities based on unit size can be done by using the Proration Schedule Worksheet part of the Budget Worksheet (RE 623) included in this manual.

Note: Specific management and budget guidelines are available and must be adhered to in order to utilize these procedures.