



Alliance of Reston Clusters and Homeowners
Supporting Homeowner Groups in All of Reston's Neighborhoods

ISSUES BULLETIN 2005-4

October 10, 2005

RESTON ASSOCIATION GOVERNING DOCUMENTS:

Summary of Changes Contained in the Sept. 15 Drafts

The September 15 drafts restore certain aspects of the balance between Board authority and Member oversight that exist in the current RA Deed, and address certain concerns that the earlier drafts materially altered the existing Board-Cluster relationship. In addition to other changes the RA Board may determine are needed, ARCH believes:

- A 10-year projection of RA's revenue needs and expenses, and explanation of how the drafts' proposed changes specifically address those needs, would aid in greater understanding of the drafts' financial provisions. It generally has been stated that "additional revenues" are required to "maintain RA's aging infrastructure." We believe many RA Members want, and the "Reston Yes" campaign would benefit from, something more specific.
- A guide summarizing the changes from the existing Deed -- and why -- would be of significant benefit in assessing the merits of the proposed drafts. While a "redline" of the existing Deed is neither necessary nor practical, we believe an easy-to-understand summary of the changes and their rationale (perhaps by general subject matter) would prove helpful in getting to "yes."
- Even with a summary, the documents remain long, complex, and difficult for the average person to read and understand. To be sure these are legal documents. Still, streamlining the documents and making them more "readable" for the Membership would, we think, aid in gaining the required participation and support.
- A new timeline that allows additional time to make and digest further changes, and to educate the Members on those changes, would also seem prudent.

It is important to emphasize that ARCH is not at this time taking a position with respect to the drafts. Instead, this Issues Bulletin is a response to the RA Board's continuing and commendable efforts to reach out for community input. The ARCH Board, through its Issues Committee, has sought to identify what we believe to be the most "material" or "meaningful" questions/comments within our organization concerning the latest drafts. We believe that at this stage -- where the RA Board continues to solicit input on the drafts -- providing this kind of objective information is the best service we can provide our Members and the community at large on this critically important issue for RA's future.

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ARCH SUMMARY: Governance Changes as set forth in the Sept. 15 Drafts

For each of the three topics ARCH has been monitoring during the drafting process – RA Finance/Governance, Cluster Governance/Services, and DRB/Covenants Committee – a summary of the key changes (as compared to the previous, July 19 drafts) is set forth first, and then a matrix identifying key remaining issues that the ARCH Board believes to be of particular interest to our membership is provided.

TOPIC: RA FINANCE/GOVERNANCE		
KEY CHANGES TO JULY 19 DRAFT: MODIFIED CAP ON ANNUAL ASSESSMENTS RESTORED (BASELINE ASSESSMENT INCREASED \$69 TO \$514, WITH ANNUAL INCREASES CAPPED AT GREATER OF 4% OR ECI); REDUCES FROM \$500K TO \$365K THE THRESHOLD FOR A CAPITAL PROJECTS REFERENDUM (CONSISTENT WITH CURRENT BASE LINE); ELIMINATES BOARD'S ABILITY TO APPROVE ADDITIONAL ASSESSMENTS WITHOUT MEMBER APPROVAL; BOARD MAY NOT ADOPT, WITHOUT MEMBER APPROVAL, SPECIAL ASSESSMENTS THAT, WHEN ADDED TO THE ANNUAL ASSESSMENT, WOULD EXCEED THE CAP FOR THAT YEAR; PROPOSED \$250 RESALE FEE CANNOT BE USED FOR CAPITAL PROJECTS; IF ANNUAL BUDGET NOT TIMELY ADOPTED, PREVIOUS YEAR'S ASSESSMENT CARRIES OVER; ALL MORTGAGEE PROVISIONS DELETED.		
ISSUE	SUMMARY	QUESTION/COMMENT
Financial Projections	To date the RA Board has not presented financial projections identifying RA's anticipated revenue and expense needs and explaining how the savings and new revenues that could be realized under the drafts would meet those needs.	ARCH believes one of the most meaningful steps the Board could take to build support for the proposed changes is to detail the Association's anticipated revenue/expense needs for the next 10 years and explain how the drafts <u>specifically</u> address those needs.
Cap on the Annual Assessment	The proposal would increase the Maximum Annual Assessment by \$69 to \$514. The July 19 draft had eliminated this cap. The \$69 increase equals the current annual per-member cost of pool maintenance. RA assumed this expense in 1991, when the annual per-member cost was \$50; adjusted for inflation it now stands at \$69. Since pool maintenance is a recurring cost, this \$50 per member arguably should have been added to the base-line assessment in 1991, but it was not.	<ol style="list-style-type: none"> 1. How the \$69 increase was calculated is clear. 2. Less clear is why \$69 (rather than some other number) remains the relevant number today by which the Maximum Assessment should be increased (note: 14 years after assuming pool maintenance the current Assessment is still @ \$20 below the maximum allowed). 3. The principal justification articulated to date for this proposed cap increase is that additional revenue is needed to maintain the aging infrastructure. Will additional and <u>specific</u> information be provided so Members can determine if the proposed \$69 increase is adequate or inadequate to meet RA's future needs?

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<p>Annual Increase to the Cap</p>	<p>Annual increases to the Maximum Assessment are capped at the greater of 4% or ECI (§ 8.2(i)). This is a change from the existing Deed's cap, which uses the CPI only. Generally, the ECI rises at a slightly higher rate than the CPI. RA's Board believes the ECI is more appropriate than the current CPI accelerator, since personnel costs comprise a significant percent of RA costs. ECI does not include Federal government salaries.</p> <p>The cap may be exceeded upon a majority vote of the Members at referendum with a 10% quorum. This is unchanged from the existing deed.</p>	<ol style="list-style-type: none"> 1. Some believe the existing CPI accelerator should be maintained; RA Board has articulated its rationale for ECI. 2. Presumably the need for an accelerator is to protect against inflation. Given that, why isn't the accelerator simply an inflation index (whether ECI or CPI)? If the 4% is retained, why then isn't it the lesser of 4% or the chosen inflation index? 3. Why does the Board perceive a need to guaranty a 4% increase option? 4. Under the drafts, "material amendments" require a 25% quorum and 2/3 vote. While this admittedly would be a change from the current Deed, is there reason to treat the cap differently from other "material amendments"?
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<p>Budget Process</p>	<ol style="list-style-type: none"> 1. § 8.2(f) allows operating surpluses to be placed in a reserve account or, at the Board's discretion, expended "for the general welfare of the Owners." 2. Current Resolution IV.5 limits Member input and visibility into budgeting to "budget suggestion forms" prior to two public hearings on the proposed budget. There is no provision to provide Members year-to-date financial performance. 3. Unlike many corporations (public or private), there currently is no Audit Committee empowered to work independently with the outside auditors to review financial performance and internal controls. 4. The current Deed § V.6 limits Special Assessments to costs related to capital improvements, subject to majority vote of those Lot owners subject to the assessment. § 8.2(b) in the draft Declaration does not limit Special Assessments to capital improvements; allows the Board to approve Special Assessments without need of Member approval up to the Maximum Assessment rate for that year; and while "notice" of any Special Assessment is required, it is unclear whether that is <u>prior</u> notice <u>and</u> hearing. 	<ol style="list-style-type: none"> 1. Changing this process could help promote greater Member involvement and confidence in the budget. Some ideas: <ul style="list-style-type: none"> • Requiring in § 8.2(f)(1) that any operating surplus be applied only to the next year's operating budget and/or appropriate reserve; • Creating a Budget Committee of qualified Members or expanding the Fiscal Committee charter to: (a) work with RA staff during the budget formulation phase; (b) produce an independent summary of the budget that Board and RA Members may use to understand the proposed budget and comment effectively; and (c) review quarterly financial actuals vs. budget and produce year-to-date fiscal summaries; • Creating an independent Audit Committee comprised of qualified Members that have financial experience and are conversant with Generally Accepted Accounting Procedures; • Including the Fiscal (and/or Budget) and Audit Committee charters in the Declaration (such as the Legal Committee), underscoring the importance of the financial function; and • Clarifying in § 8.2(b) that Special Assessments may be adopted only upon <u>prior</u> notice <u>and</u> hearing. 2. Given that four new reserves are proposed, what is the need to utilize Special Assessments beyond unforeseen, non-recurring expenses?
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<p>Capital Projects</p>	<ol style="list-style-type: none"> 1. § 9.4 restores the capital referendum threshold to the current \$365K, with projects above that number subject to majority Member approval at referendum with a 10% quorum (all unchanged from current Deed). The annual accelerator, however, has been changed from the CPI to ECI. 2. As with the July drafts, donated capital facilities are excepted from the referendum requirements. This is a change from the existing Deed. 3. § 9.4 excludes replacement costs and depreciation from the required 5-year operating costs proposal to be presented to the Members. 	<p>Restoration of the existing threshold has been well received. Remaining issues:</p> <ol style="list-style-type: none"> 1. Significant community disagreements over proposed capital projects have, in recent years, centered largely on projected or actual use of the facilities by significant numbers of non-Members. Few contest the good of allowing non-Members to use such facilities (often at increased user fee rates). But concerns arise when the majority of users are non-Members, who are benefiting from RA's initial capital expenditure without truly contributing to the capital outlay. Would the Board consider adding language to the effect that "Any proposed capital project must be designed principally for the benefit and use of RA Members and only incidentally for the benefit and use of non-Members, not the reverse"? 2. Why was the accelerator changed from CPI to ECI, given this is a capital- and not labor-intensive item? 3. The presumed rationale for excepting donated facilities from the referendum requirement is that, because no significant capital outlay is required, there is no need for Member review. However, the impact on operating expenses of undertaking management/maintenance for a major capital facility can be significant and could impact Members' interests in accepting such a donation. Why should donated capital facilities be exempted from the referendum requirement? 4. While the Board would presumably meet its fiduciary duty by holding public hearings and the like before taking on such expenses, is there value in specifically requiring such to eliminate any ambiguity on the point (perhaps in § 17.3)? 5. Given that replacement costs and depreciation are an essential component of making a decision on capital projects, why are these exempted from the 5-year projected costs?
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<p>\$250 transfer (resale) fee</p>	<p>Imposed on the sale of any residential Lot within RA. Important change from the July 19 draft: language added preventing use of this money for capital projects.</p> <p>With the current average of @ 1,500 home sales per year, this would generate @ \$375,000 (which would equate to @ \$19/household in assessments).</p>	<ol style="list-style-type: none"> 1. Why is this needed (particularly in light of the \$69 increase to the Maximum Assessment), and what will it be used for? Is the implication the Board would seek a higher cap without this fee? 2. The capital reserve study suggests @ \$250,000 in new annual contributions are needed. That amount is more than covered by this new resale fee. The need, therefore, for both this new fee and an increase to the Maximum Assessment needs elaboration. 3. RA's CFO stated at the July ARCH Forum this money would be applied to general revenues. The new capital exclusion is helpful, but is there any reason why the draft can't simply state that "proceeds will be added solely to General Revenues to mitigate any need for increased assessments"? 4. Applies as well to Members moving within RA. If the justification is to gain a contribution from new residents who haven't paid for the existing infrastructure, it is unfair to ask existing members moving within RA to pay this fee. One way to deal with this is to cancel or rebate the fee for such internal moves. 5. Any consideration given to voting on this separately at referendum?
<p>Category C (Commercial) Members</p>	<p>This new category of possible membership remains, but important changes have been made:</p> <ol style="list-style-type: none"> 1. There will be no Category C seat on the RA Board unless at least 25 Category C Members have joined RA; and there will be at most one such seat. 2. Category C voting rights have been limited to: (a) one vote for each @ \$400K of assessed value of the commercial lot when voting for the Category C Board seat; and (b) one vote per commercial lot (regardless of value) on all other referenda. 	<p>We understand the Board has voted to eliminate this item. If reinserted:</p> <ol style="list-style-type: none"> 1. The principal concern is that this potential for new revenue may not be worth the price of diluting the Board strength of the residential Members. For one thing, this would change the character of RA from a homeowners association to a property-owners association. 2. Conversely, a single Board seat for Category C – regardless of the percent of overall revenue generated from commercial assessments – may prove inadequate incentive for Category C members to join.

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<p>Owners to Assume some responsibility for RA Common Area</p>	<p>§ 9.2(a) requires individual Lot owners to maintain leadways, sidewalks, and utility aprons adjacent to or serving his/her Lot <i>even if</i> such is on RA Common Area (to include shoveling snow on RA Common Area sidewalks adjacent Lots). Under the existing Deed, RA is responsible for all RA Common Area.</p>	<ol style="list-style-type: none"> 1. This provision shifts responsibility, <i>and thus liability for injury</i>, to the individual Lot owner for accidents occurring on certain RA Common Area. What is the rationale for this shift of responsibility/liability? 2. Can this be legally accomplished, given that each Lot Owner has only a share in RA Common Area? 3. How would this be monitored?
<p>Enforcing County and State regulations</p>	<p>§ 12.2(b) authorizes RA Board to enforce county and state law. This express authority is not in the existing Deed.</p>	<ol style="list-style-type: none"> 1. What is the rationale for taking on this authority, and is the RA legally permitted to take on this authority? 2. Would it be moving the Board into areas beyond its competency/expertise? 3. If the Board needs to reserve this right in specific instances (towing?), should it be more narrowly tailored?
<p>Quorum</p>	<p>The quorum required for material amendments to the Declaration has been reduced from 40% to 25% (unchanged from July 19 draft).</p>	<ol style="list-style-type: none"> 1. There are essentially two purposes of a quorum requirement: (a) to ensure that turnout is adequate to constitute a reliable sampling of the community and (b) to prevent a small but organized minority from controlling material issues affecting RA. The hurdle of getting 2/3 support from at least 40% of the Members on referenda questions helps ensure (for better or worse) that change is incremental and consensus-driven, but many accept that a smaller quorum requirement is adequate. The point involving the possibility that a minority could hijack a referendum, however, continues to raises concern about any meaningful reduction to the quorum requirement. 2. What is the Board's rationale for reducing the quorum requirement? 3. If cost is part of that rationale, are there data to support the conclusion that having a lower quorum requirement will reduce the costs of a referendum? 4. Does this introduce a concern that a small, organized minority could either promote <u>or</u> prevent change?

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<p>Pledging Assets or revenue, mortgaging property, and conveying property</p>	<p>Unchanged from the July 19 draft – the draft Declaration provides the RA Board considerable flexibility in each area without need of Member approval. This is an aspect of the drafts that is very difficult to parse, partly because multiple provisions must be compared; e.g., compare § 4.1(11) (giving Board wide discretion) with § 20.3 (which, while difficult to digest, suggests certain of these decisions could be subject to Member approval).</p> <p>The current Deed is silent on the question of incurring debt. While there is some ambiguity on pledging assets or conveying property, the current Deed – or interpretation of the Deed by past Boards – has required Member referenda on these questions.</p>	<ol style="list-style-type: none"> 1. These changes are generating significant attention. Why does the RA Board feel the need to change the current requirement/interpretation of prior Member approval on pledging assets or conveying property? 2. The document needs to explain more simply and carefully exactly what changes are being suggested here. 3. One change does appear clear: under § 20.3 conveying property to a non-profit or government entity (e.g., the Southgate project) would no longer require Member approval. Why? Among concerns expressed, this could allow the RA Board to convey Common Area to non-profits or government agencies for significant capital projects that would otherwise be subject to the capital referendum requirement. 4. It is unclear from § 20.3 whether conveyances to private developers are exempt from the referenda requirements. 5. § 20.3 is an example where readability needs to be improved; it is very difficult to figure out what is and is not subject to the material amendments referenda requirement.
<p>Dissolving RA</p>	<p>No change from July 19 draft. § 21.1 requires 80% approval of Members, but then says it is subject to § 20.3. That section requires a two-thirds vote with a 25% quorum on “material amendments.” It is not clear, therefore, if a quorum requirement applies and/or if/how/why the 80% modifies the two-thirds requirement.</p>	<p>We understand this may have been changed to a 66.7 % threshold. The following questions still apply:</p> <ol style="list-style-type: none"> 1. Under Deed Art. VIII.1, an absolute majority of Members is required to vacate the Deed. Why does the Board perceive a need to increase/change that requirement and/or make it different from other material amendments? 2. Given the importance of this issue, does there need to be a significant quorum requirement? 3. As currently written, what conditions or requirements do the drafts place on becoming a town? 4. Should the ambiguity between this provision and it being subject to § 20.3 be addressed? 5. Does this supersede any requirements in POAA?

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<p>Incorporation by Reference</p>	<p>Last sentence of §13.1(b) continues to incorporate by reference all existing RA guidelines.</p>	<p>There remains concern this incorporation clause could require a Member referendum to change existing agency guidelines (since they are made part of the Declaration). All understand that is not the intent (which presumably is to ensure that nothing in the drafts invalidates validly adopted existing regulations not inconsistent with the new Declaration). Still, given the confusion this language has created, is it necessary and, if so, shouldn't it be rewritten to more closely match its intended purpose?</p>
<p>Timing/Schedule for Documents Referendum</p>	<p>The revised schedule has the Board voting on the final documents October 20; ballots would be mailed October 31; December 16 is the ballot deadline.</p>	<ol style="list-style-type: none"> 1. ARCH believes the Board should take whatever time it feels is necessary to create a thoughtful and approvable document. Substance should dictate timing, not the reverse. 2. Concern remains that the current time-line may not be adequate to digest changes in new drafts.
<p>Readability</p>	<p>Reflecting the Board's commendable effort to solicit and understand community input over the summer, the September 15 draft has made a number of meaningful changes. The draft remains lengthy, however, and is not easily read/understood.</p>	<p>ARCH believes a meaningful hurdle to winning approval will exist until the document is significantly streamlined and made easier to read/understand.</p>

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TOPIC: CLUSTER GOVERNANCE/SERVICES

KEY CHANGES TO JULY 19 DRAFT: THE TERMS "CARE AND OPERATION" HAVE BEEN ELIMINATED FROM THE DEFINITION OF UPKEEP; THE DEFINITIONS HAVE BEEN TIGHTENED TO MAKE CLEARER CLUSTER COMMON AREA IS NOT PART OF LOTS OR COMMON AREA; LANGUAGE HAS BEEN ADDED PROHIBITING THE RA BOARD FROM REQUIRING ANY CLUSTER TO CONTRACT WITH AN RA OR RA-MANDATED MANAGEMENT AGENCY; DELETED THE NEWLY ADDED REQUIREMENT PROHIBITING USE OF GARAGES IN WAYS THAT PREVENT PARKING IN THAT SPACE; CLARIFIED THAT THE RA BOARD GENERALLY WILL NOT COME UPON CLUSTER PROPERTY (E.G., FOR TOWING) UNLESS REQUESTED TO DO SO; AND IT HAS BEEN MADE CLEARER THAT THE RA BOARD WILL INVOKE SELF-HELP TO ADDRESS CLUSTER DEFICIENCIES ONLY AFTER A CLUSTER HAS BEEN GIVEN NOTICE AND AN OPPORTUNITY TO CURE. THESE CHANGES HAVE ALL MADE CLEARER THE RA BOARD'S EXPRESSED INTENT OF NOT CHANGING THE CURRENT BOARD-CLUSTER RELATIONSHIP.

ISSUE	SUMMARY	QUESTION/COMMENT
Summary Guide	There currently is no succinct summary of each specific change proposed on cluster governance/services and why.	Rather than requiring Members to parse through a nearly 80-page legal document, ARCH believes a clear summary of the specific changes in this area and why they are proposed would aid in generating support for the changes.
Definitions	Some changes have been made to the definitions of Lots, Common Area, and Cluster Common Area to address concerns that definitional changes were altering the existing definitions and/or practices.	These definitions, while improved, remain lengthy and substantially changed from the existing Deed. Are there reasons these definitions cannot more simply state that Lot means any homeowner lot (townhouse, condo, single family, or multi-dwelling), Common Area means only RA Common Area, and Cluster Common Area means exactly that?

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<p>Upkeep and Maintenance Standards</p>	<p>Key changes to the July 19 draft include deleting new Board authority to regulate trash <u>collection</u>, in addition to storage, and deletion of the new regulation prohibiting use of garages in ways that prevent parking for the number of vehicles intended. The principal new addition to the existing Upkeep and Maintenance Standards is the express regulation of home offices (unchanged from July 19).</p>	<ol style="list-style-type: none"> 1. RA's Board has said it does not intend by these drafts to alter the existing relationship with clusters, which currently have authority to regulate home offices. Given that, why does the RA Board feel the need to regulate home offices (and thus, indirectly, parking) for its HOA Members? 2. As for RA Members that are not part of an HOA, why does RA's Board feel the need to assert this authority? Are existing Fairfax County regulations on home office thought to be inadequate? 3. Some suspect this is in fact a parking issue. In that case, there are home activities that could generate more stress to local parking than certain home office situations. Therefore, it could appear that home offices are in effect being "singled out" when the issue is much larger. 4. If kept, the proposed regulations are fairly specific. Did the Board consider including general authority to regulate home offices in the Declaration, but then leaving particular definition of any regulation to the normal regulation process – with notice and hearing and an opportunity for home office stakeholders to provide input?
<p>Insurance</p>	<p>Changed some since July 19. § 8.4(b) now requires Clusters to maintain products (added since July 19) and commercial liability insurance in minimum amounts of \$1 million per incident and \$2 million in aggregate (added); D&O insurance in the minimum amount of \$1 million (note that under § 6.3(c) RA is not required to obtain D&O coverage in a specific amount); and list RA as an additional named insured under a Cluster policy. The stated rationales are that when Clusters don't have these coverages, the other members of the Association may be sued if injury occurs (pursuing the "deep pocket"), and the Board believes that is unfair to Clusters who have bought insurance. The provision allowing the RA Board to purchase coverage if none exists at a cluster has been eliminated.</p> <p>Clusters must also indemnify RA when it comes onto Cluster property; language has been added stating RA will indemnify clusters for acts and omissions of RA agents.</p>	<p>These requirements continue to generate significant concern among ARCH members.</p> <ol style="list-style-type: none"> 1. What is the benefit to RA Members (as distinct from cluster members) of requiring cluster boards to obtain D&O coverage? 2. If these requirements are to be retained, does a "one size fits all" requirement make the most sense? Does calibrating those requirements based on Cluster size have any merit, or is that impractical? 3. While language indemnifying Clusters for RA actions has been added, this does not seem to override the Cluster requirement to indemnify RA any time RA comes on Cluster property. Why should Clusters ever be required to indemnify RA when RA comes onto Cluster property? 4. Has the Board identified the financial impact (both likely and worst-case) on cluster associations of imposing these new insurance requirements?

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TOPIC: DRB/COVENANTS COMMITTEE ISSUES		
<p>KEY CHANGES TO JULY 19 DRAFT: THE TERMS "CARE AND OPERATION" HAVE BEEN ELIMINATED FROM THE DEFINITION OF UPKEEP, MITIGATING CONCERN THAT DRB'S JURISDICTION WOULD EXTEND BEYOND TRADITIONAL AREAS OF EXTERIOR ADDITIONS, MODIFICATIONS, AND ALTERATIONS; THE NEW AUTHORITY TO IMPOSE APPLICATION FEES HAS BEEN LIMITED TO NON-MEMBER APPLICATIONS.</p>		
ISSUE	SUMMARY	QUESTION/COMMENT
Summary Guide	No summary of DRB changes has yet been created.	As with the previous topics of RA finance/governance and Cluster governance/services, ARCH believes a summary of the <u>specific</u> changes to the existing DRB provisions and rationale for them would be helpful in generating greater understanding and support for the drafts.
Consistency in Decisions	The changes to the DRB provisions have significantly improved the documents. There remains some concern that some decisions seem inconsistent with past precedent.	This is an admittedly difficult area. There is wide agreement that requiring DRB to be bound by past precedent is probably not good policy (it may be bad precedent). To aid in transparency in decision-making, ARCH had offered the idea that DRB be required to distinguish past precedent, or say why it was not following it, when making decisions on factually similar cases. RA Board representatives at the July ARCH Forum said they believe that kind of requirement would impose an undue burden on DRB.
Affected Parties	Currently, in certain cases, a DRB petitioner must get a cluster board member and two neighbors to sign the petition. Under § 13.5(b) of the current draft, RA is now required to notify the appropriate cluster of <u>any</u> DRB application.	Why is RA changing the current procedure to take on a burden that will likely be difficult to meet?