Community Associations – A Budget FAQ

1. **What is a budget?** Budgets are estimates of income and expenses calculated on an annual basis, and are based on reasonable fiscal assumptions – they are not a guarantee of money in the bank, fiscal soundness, or responsibility.
2. **Is a budget required?** Unfortunately, Oklahoma law provides community association no guidance on budgets. The governing documents to the association may require an annual budget to be formulated and given to each member. However, most association boards are left to set annual assessments and budgets on their own.
3. **What is the purpose of a budget?** There are two main purposes to a budget.
   3.1. First, the budget is a financial document that outlines the goals and purpose of the association. The budget should reflect where the membership wants the association to go in terms of the goods and services it provides. This might also be described as identifying the association's needs and wants.
   3.2. Second, the budget is a tool to help the board price out the needs and wants of the association in order to set the annual dues amount for each member.
4. **How does an association develop a budget?**
   4.1. **When to begin**. The budget formulation and approval process should begin in September, assuming the association has an annual meeting in December. Conducting a budget analysis over several months allows for adequate review and response, and notice to the members.
   4.2. **Member involvement**. The association board should strive to get input from the association's customer: the members. This may be done through committees, surveys, and comments gathered at board meetings.
   4.3. **Data**. Generally, a budget begins as an outline of income sources to the association and regular expense items expected by the association. Each income and expense item is listed in plain language with a corresponding figure borrowed from last year's actual income or expenses. Then, the income and expense items are adjusted according to any anticipated items of income or expense for the upcoming year. The figures under each item are then analyzed as compared to the goals set by the board for the association. Once all assumptions and modifications to the budget are finalized, the board modifies the annual assessment amount accordingly.
   4.4. **Approval**. Some governing documents require the members to approve the annual budget. If so, the board must follow the adoption procedures outlined within the governing documents. If the documents are silent on budget approval, a board generally adopts the budget itself, after a period of notice and comment to the members.
5. **Are there additional considerations?**
   5.1. **Realism**. Be realistic and understand that there will be errors both on the high and low side as to certain budget lines. Part of the budget process is to minimize surprises as much as possible, but we all know that in the real world budgets are affected by cost-overruns, supply and demand, windfalls, and unexpected events.

Being realistic also involves recognizing that physical items deteriorate and a dollar will buy less in five years than it will right now. This means that keeping annual assessments at the same rate year after year only buys artificial happiness.

5.2. **Assumptions**. All budgets incorporate assumptions to a certain degree. Any assumptions and their basis should be noted within the budget so that next year's board or budget committee does not reinvent the wheel.

5.3. **Deductibles**. An association should budget for insurance deductibles instead of taking the money from reserve or making a special assessment.

6. **How should the budget be presented?** Because the budget reflects the goals and values of a community association, the budget presentation shouldn't simply recite items and figures. A board would work to present the budget so that the budget becomes one more document that explains the association's strategic plan. Because people process information differently, the budget should be presented both in text and graphic formats.
7. **What is cash flow and is it important?** Cash flow projects whether the money should be in the bank when you need it. For example, an association makes an assessment in January for annual dues, and allows monthly payment on that assessment. It is possible that by August, the HOA will run out of funds due to the expenses of a swimming pool and landscaping in the summer. This HOA needs to consider cash flow in setting its fiscal policies.
8. **What are reserves and are they important?** Just like budgets, Oklahoma does not require even condominium associations to reserve for capital improvements. The lack of legislation in this area belies the importance of responsible reserve funding. A reserve fund is a capital improvements savings account. Most associations establish a reserve based on a reserve study, which outlines the capital improvements over which the association is responsible and attempts to establish a funding plan for the periodic repair and replacement of those improvements. Unfortunately, many associations look to special assessments for their capital improvement funding, which may not be economically feasible when needed, and is always patently inequitable.

This FAQ is presented as a service from Matthew L. Winton, Esq.

VAUGHN & WINTON PLLC
2801 East Memorial Road, Suite 110
Edmond, Oklahoma 73013
405.478.4818 telephone
405.478.4819 facsimile
www.vaughnandwinton.com
www.okhoa.blogs.com