Cameron Station Community Association – Financial Advisory Committee (FAC)

19 February 2015 – Meeting Minutes

- **Meeting Called to Order:** 7:02 p.m. by FAC Chairman Jeff Gathers.
- **Members Present:** Joe Chesney, Aldo D'Ottavio, Harry Glenos, Mahl Avila, Ted Pickett, and Tim McLaughlin
- **Board Liaison Present:** Megan Brock (Treasurer)
- **Members Absent:** NA

- **Approval of Agenda:** Motion passed unanimously

- **Approval of Minutes from 20 November 2014 meeting:** Meeting minutes approved.

- **Resident Open Forum:** No residents in attendance

- **Review of Financial Reports:**

  - **December 31, 2014 Financials**

    Members discussed the 2014 year-end financial report in detail. Numerous questions were raised about the significant change in year-to-date net surplus from the November 30 position of ($1,045) to an “adjusted” year-end result of ($51,206). The Chairman had earlier provided e-mail commentary on these issues in several categories as follows:

    - **The Bottom Line(s)**
      
      The appearance of the word "Adjusted" for YTD Expense and YTD Net Income in the Executive Summary is unusual. No adjustments are normally required in this table. The "adjustment" reflects subtraction of $5,405.66 from YTD expense and addition of the same amount to net income. This is essentially a “footnote” correction of a coding error by CMC corporate accounting. Because the error was discovered only after the books were closed for 2014, the overstated expense will remain on CSCA’s 2014 books until later in 2015 – certainly no later than late summer when any other auditing corrections are typically reflected in an adjustment to Owners' Equity. All of the detailed reports in the financial package reflect "unadjusted" expenses and a full-year net loss of $56,611.16.

      The 2014 "Loss Note" observes that the $50K+ adjusted variance is "directly attributable" to the excess expenditure for snow removal in the first quarter of 2014. This is accurate in the sense that the (uncontrollable) snow variance of $48K is close in value to the total net loss for the year, which in turn implies that "controllable" expenses were managed to only a very small variance. However, as recently as the November 30 financial report, the YTD net variance was only ($1,045) **including** the excess snow removal expense. Several other “anomalies” contributed significantly to the $50K swing in the final month.
• **Use of Prior Year Income/Deficit**
  In the middle of page 2, Colleen attributes nearly half ($23,650) of the December swing to the accounting reversal of the year’s transfers of prior years’ Owners’ Equity (OE) into Operating Income. In the budgeting process for both 2013 and 2014 (but not 2015), OE transfers were used to offset a portion of the assessment increase that would otherwise have been required. As the report points out, the decision to preserve or reverse these transfers does not affect the CSCA’s ultimate financial position – only the years in which net income/loss is nominally incurred. For 2014, the reversal of the transfers creates a technical deficit in income of $13,180 where a surplus of $10,470 (from non-assessment income items) would otherwise have appeared.

• **Reclassifications**
  The Loss Note also refers to $15,100 in accounting “reclassifications” that were effected in December 2014. Roughly 10 expenditures that had been charged earlier in the year to the Replacement Reserve were “reclassified” into regular 2014 operating expense accounts. The decision to reclassify these expenses emerged from a December meeting of the FAC Chairman with the Community Manager. The primary subject of the meeting was the large gap between the $240,000 that was projected in the reserve study “funding plan” to be spent on 2014 reserve items and the roughly $110,000 that had been spent through November. A review of the accounting records showed that several expected major cost items (street and sidewalk repairs, new security system, replacement light poles) had not (yet) been addressed. A major reason for the delay in addressing these issues had clearly been the effect of turnover on the staff’s ability to manage such significant projects, but planning to catch up in 2015 will begin promptly.

The same review also identified a number of relatively minor expenditures that had been charged to the reserve but that did not correspond to any of the cost categories that the reserve explicitly covers. Colleen acknowledged that a practice has evolved of charging some "non-routine" maintenance expenses (often $500-$1,500) against the reserve rather than to the otherwise applicable operating account. This practice has the "benefit" of making operating expenses appear lower, because reserve charges affect only the balance sheet -- that is, until reserve contribution levels need to be increased in subsequent budgets. In the 2014 case, however, the primary motivation seems to have been a difference of opinion about what the Reserve Study should include, rather than what it actually does include. The reclassifications put these charges into operating expenses immediately.

It is a clear that both the FAC and Management need to be more thorough in the planned 2016 reserve study update than was possible in the 2013 study – specifically in discussing the types of expenses to be included by the contractor. These reclassification issues are additional examples of the same problem that put “tree & shrub maintenance” way over budget in 2014: i.e., not enough categories in the reserve study to support established management coding practice. It remains to be determined whether correcting these shortcomings will necessitate an increase in reserve funding requirements for 2017.
- **Administrative Salaries**
  Even after the error correction, the 2014 salary account was more than $9,000 over budget for the year. This overage has been attributed primarily to temporary “double staffing” of some positions, i.e., departing incumbents staying on to train replacements. This was especially important in regard to the Covenants Administrator transition.

- Concerns from the committee members were also discussed in the general area of budgetary control.
  - A specific question was raised in regard to the snow removal contract: Insofar as the contract has been expanded to clear and treat more sidewalks, was the cost impact fully considered by the Board?
    - While all agreed that safe sidewalks are desirable, any service change with a budget impact is potentially problematic if implemented in the middle of a budget cycle. The operating budget is only changed once per year.
    - The committee is concerned generally about “mission creep” and its effect of the budget and adequacy of assessment income.

  [Ed. Note: Subsequent to this meeting, the Community Manager explained to the FAC Chairman that, in fact, the scope of the snow removal contract was not expanded – only the approved methods for clearing sidewalks. It is expected that this change will have no effect on net cost, but this will be closely monitored by Management and the Board. See Board minutes of 12/9/14]

- A review of statistics comparing actual and budgeted expenditures in 2014 showed greater than expected dispersion:
  - Expenditures exceeded budget by more than 10 percent for 23 accounts.
  - Expenditures were within 10 percent of budget for 26 accounts.
  - Expenditures were more than 10 percent under budget for 32 accounts

  The committee took particular notice of the accounts with expenditures significantly over budget. Members with experience managing budgets in other settings expressed concern about the adequacy of oversight that might have prevented some of these overruns, or at least more thoroughly documented their justification.
  - What members see is a current process that relies primarily on the monthly financial reports. These explain income and expenses in great detail but – by definition – only “after the fact.”
  - What members have not seen is a process by which line item budgets actually constrain CMC’s spending.
  - FAC members seek to understand better the process whereby Management makes day-to-day and month-to-month spending decisions against the backdrop of a detailed, but frozen, annual budget.
  - Members are also sensitive to the risks of “micro-management” by any party to spending decisions: loss of timeliness in addressing maintenance needs, extra demands on management staff already stretched thin – perhaps for little or no net improvement.
Members also understand that $300-$400K in Owners’ Equity provides significant margin to cover unanticipated operating expenses. This is of considerable comfort – most obviously in the case of uncontrollable expenses like snow removal. (History suggests that there really are no uninsured exposures that are “like snow removal.”) We are sure that the Board does not intend this margin to reduce the importance of reasonable discipline in spending decisions.

[Ed. Note: Subsequent to this meeting, the Chairman invited the Community Manager to attend the next (March 26) FAC meeting. The hope is to advance this discussion on the basis of a more thorough common understanding of the current budget management process.]

- **January 31, 2015 Financials**
  - Discussion deferred due to the late distribution of data from CMC.

- **Old Business**
  - **Investment Manager/Banker Solicitation Process**
    - Waiting for response from CMC regarding proposal language and viability of a routine banking arrangement with other than Pacific Premier Bank.
  - **Irrigation System Expansion**
    - Lancaster Landscapes had expressed a commitment from Cameron Station by mid-March to go ahead with the work on Phase 1 of the proposal presented by the Common Area Committee chair at the November FAC meeting.
      - Reason given by contractor was to ensure adequate time to source materials and manpower.
      - Would require transfer from Owner’s Equity to fund the effort as a Capital Improvement.
      - FAC Chairman proposed a motion to seek Board approval at its February 24 meeting to agree conditionally to the Lancaster proposal for Phase 1— that is, with a Board option to defer a final decision until March 15 to weigh the effect of additional snowfall on available funds. If additional snowfall was significant, Cameron Station would not go ahead with Phase 1 until midyear at the earliest.
      - FAC members discussed and agreed there was no compelling reason (certainly not encouragement from the contractor) not to defer any decision until after the snow season is completely behind us. The FAC will revisit in April.

- **Replacement Reserve Issues**
  - See December 31, 2014 Financials discussion above.

- **New Business**
  - None

- **Adjournment:** The chairman adjourned the meeting at 9:04 p.m.