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HOA

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ANDY JACOBSOHN FOR WSJ The U.S. is home to about 373,000 community associations.

Check the HOA Risks Before You Buy House

A homeowners association means going into business with neighbors

BY VERONICA DAGHER

The stakes of buying into a homeowners association are rising, with aging buildings and soaring insurance costs threatening to strain community finances.

Note

A growing number of people are buying homes in community associations, which can include condos, co-ops or single-family homes where residents share costs to maintain common spaces. Roughly 373,000 U.S. community associations include about 78 million Americans, according to the Foundation for Community Association Research. That figure is set to rise as more homeowners band together to cover public upkeep costs as local governments grapple with budget shortfalls.

Note

With monthly dues surging, it is important to check an HOA's finances. Once you buy the home, you take on shared responsibility for maintenance costs and the consequences of past board decisions.

Here are four ways to evaluate the financial health of a community and decide if it is the right fit for you:

1. Improvement projects

Boards typically have a three-tofive- year view of planned improvements. It is important to understand how the projects will be funded and the disruption they might cause, said David Diestel, chief executive of property-management company FirstService Residential.

A pool-deck renovation that sounds routine might mean a full season without pool access. Ask the board what projects have been completed recently and what's coming. A strong track record of upgrades is often a sign of good governance, Diestel said.

Unless state law or HOA documents specifically require disclosure, prospective buyers usually don't have a legal right to any records directly from the association, said Scott Weiss, a condo association lawyer in Nashville, Tenn. But, he said, a buyer can request a contract contingency from the seller that gives them a brief due-diligence period to review HOA documents that the seller obtains— such as board minutes—before the purchase agreement becomes binding.

2. Reserves

Prospective buyers can request to see the community's reserve study, a report evaluating the HOA's financial health.

In the report, look for the "Percent Funded" level. It shows how prepared the HOA's reserve is for major repairs such as a roof replacement. A level above 70% indicates strength, while anything below 30% increases the likelihood that special assessments will be needed to deal with surprise costs, said Jim Talaga, president of Association Reserves—Washington, a firm that evaluates HOAs' financial health.

The study also should include a recommended reserve funding level. Compare that with how much is actually being budgeted for reserves each year. A shortfall often signals that the board is pushing today's repair costs onto future owners, Talaga said.

The study you're given shouldn't be older than 36 months.

Mortgage lenders apply stricter standards for applicants buying in to condo associations, which expose homeowners to more shared risk. If you're buying into a condo association, the reserves could affect your ability to get a mortgage. Updated Fannie Mae and Freddie Mac requirements for lenders are increasing scrutiny of the finances of condo associations, and insufficient reserves could be a reason to deny a loan.

3. Claims

Insurance claims can reveal hidden operational problems, said Kevin Davis, president of Kevin Davis Insurance Services, in Los Angeles, which insures HOAs.

"One dispute may not mean much, but a pattern reveals the association's true culture," said Davis.

Red flags include repeated claims over water leaks, construction disputes or harassment. Associations rarely share full claims reports with prospective buyers, but you can ask the seller or board about significant claims, pending lawsuits or insurancepremium increases from the past five years.

For someone buying a singlefamily home, a CLUE (Comprehensive Loss Underwriting Exchange) report contains information about insurance claims associated with the home in question generally going back up to seven years, said Loretta Worters, vice president at the Insurance Information Institute, a trade group. The current homeowner can request a copy and share it with a prospective buyer.

4. Vibe

Every association has its own personality, with some operating like easygoing golden retrievers, and others tightly wound like pit bulls, said Julie Adamen, an HOA consultant in Saddlebrooke, Ariz.

"Drop a golden retriever owner into a pit bull neighborhood, and they'll face constant stress," Adamen said.

To get a better feel for a community, hang around after checking out the home you are considering.

Join local social-media groups, call board officers directly, or use personal connections to get information before making an offer, said Dave Amis, a private investigator in Austin.

You can also speak with other residents to get a sense of how responsive the board members are, he said.

But even with careful vetting, it is possible to be hit with surprises.

Weiss, the Nashville lawyer, knows of a case where a buyer intended to live in her unit for one year before converting it into a rental. Nine months after her purchase, the HOA voted to require a two-year owner-occupancy period before leasing.

She sued to keep the rule the same, but a court ruled in favor of the association.

"You can't expect the HOA's governing documents will always remain the same," said Weiss.

