01 Botanica Presidents Letter

Fellow Owners,

The proposed 2023 budget has been completed and sent out. What follows is an explanation of the causes of the significant increases for owners that did not attend our budget meetings.

Before jumping into that, a brief explanation of our two budgets may be helpful.

* We have an Operating Budget, which covers the expenses of running our Association day-to-day. This includes numerous expenses including payroll and benefits for our employees, insurance, landscaping maintenance, pool cleaning, professional services, and supplies for repairing and maintaining our building and grounds.
* We also have a Reserve Budget, which covers the cost of repairing and replacing the most crucial and expensive structural aspects of our property including our roofs and infrastructure, hallways, swimming pool, gym, party room, office, security and access technology, and more.
* The Operating Budget is set by the Finance Committee and the Board with our Manager and professional advisors.
* The Reserve Budget is largely set by a licensed, professional Reserve Specialist based on the repair and replacement costs of the structural items that are legally required to be in the Reserves of a condo in Florida as well as other expensive items that the Board and owners want to have in Reserves for prudent long-term budgeting.

There is some additional context that I believe is necessary before launching into an explanation of our 2023 proposed budget. I want to be very clear on this point: as a lifelong community volunteer, serving in leadership for my church, yacht club, my kids' schools, other local organizations, and this condo for many years, I honor and respect the efforts of fellow volunteer leaders that have served before me. I know first-hand the challenges of trying to understand complicated problems, the pressures of making difficult decisions with other people's money, and doing that amidst the requirement to reach consensus to accomplish anything. I believe that all volunteer leaders try to do their very best. I also know that there tends to be a cycle in organizations. A team comes in and makes investments, likely needed and perhaps somewhat inefficient. This team is often followed by another that makes cuts, also likely needed and perhaps somewhat shortsighted. Sometimes budget cuts are deliberate and thoughtful and sometimes not. The leaders of our Association over the past few years made significant cuts to maintenance, especially landscaping, underestimated insurance and utility costs, underpaid many of our employees which drove high turnover, and failed to update our reserves with current costs. The current team was therefore put in the position to address and overcome all this.

The Association's Finance Committee and Board of Directors, in conjunction with our Manager, put significant time and energy into our responsibilities over the past couple months. We met perhaps a dozen times with our accountant, insurance agent, attorney, and others. While I am proud of our efforts, I am frustrated with the result. Our 2023 budget unfortunately includes large increases to both our Operating Budget and our Reserve Budget. The full budget has been sent out to every owner and additional copies can be requested from the management office.

For 2023, our proposed Operating Budget is 19% bigger than the 2022 budget and the 2023 Reserve Budget is a 78% increase over 2022. The biggest driver of our budgetary increases, both to Operating and Reserves, is insurance. Let me explain . . .

Insurance premiums are an Operating expense. Our insurance premium, primarily for coverage from hurricanes and the damage they can cause, increased by 50% year over year -- or by more than $350,000 since 2022. This is consistent with a trend across condos and other waterfront properties in Florida due to significant storm-related insurance claims this year and over the past few years. For those that will assume that we can simply shop around for a lower rate, as with auto insurance, please understand that it doesn't work that way for a large condo near the water in South Florida. There are only a couple insurance providers that will even consider covering a building like ours and we are with the best by far on cost and quality, QBE. Losing coverage from QBE and having to go with an alternative is estimated to cost us $600,000 to as much as $1 million more per year, every year. This must be avoided.

QBE, as part of their renewal process, inspected our roof recently and gave it a failing grade -- meaning that they notified us it must be replaced prior to renewing our policy in May 2023. Roof replacement and major repair is a Reserve expense and our roof is in our Reserves. However, the Reserve Specialist estimated several years ago that our roof would last until 2030. This means that our reserve funding model does not account for outgoing funds for the roof for another seven years. But, if we don't replace the roof now, we will lose coverage from QBE and see a much higher premium from another insurance company. What this means is that while we currently have about $2.4 million in reserves, we need more and we need it right away to replace our roof. The cost of replacing our roof is estimated to be as high, including contingencies, as $4 million. So that accounts for the large increase in the 2023 Reserve Budget.

We have two options to fund the gap in Reserves for 2023: increase the monthly contribution for owners for 2023 to fully-fund Reserves or partially-fund Reserves through the monthly contribution and close the bulk of the gap with a Special Assessment. This is a choice that, by law, only the owners can make by voting. To be clear, here are the two options:

1. Option A: Partially-fund Reserves through the monthly condo fee but use a one-time Special Assessment to fund the big gap in 2023 reserves caused primarily by the need to accelerate the roof replacement. Using my unit, 176, as an example and including everything -- the KC4 Operating and Reserve contributions plus the KCHOA contribution -- my monthly fee would go from $1,364.27 today to $1,683.64 in 2023. This is an increase from 2022 of $319.37 or 23%. Plus I would have a one-time Special Assessment of an estimated $13,000 which I could pay in a lump sum or finance it over five years for an estimated $253.14 per month based on the loan terms we have been quoted of 6.3% over five years. (Please see note below regarding the Special Assessment amount being a preliminary estimate for discussion purposes only.)
2. Option B: Fully-fund Reserves through an increase to the monthly condo fee. Again using my unit, 176, as an example, this would increase my monthly payment, inclusive of KC4 Operating and Reserve Budget contributions and the contribution to the KCHOA Master Association, from $1,364.27 today to $2,223.89 in 2023. This is an increase from 2022 of $869.62 or 63%.

EXAMPLE BASED ON UNIT 176
2022 | 2023 Option A | 2023 Option B
Monthly Condo Fee (KC4 Operating & Reserves & HOA): $1,364.27 | $1,683.64 | $2,208.34
One-Time Special Assessment (estimate): N/A | $13,000 | $0

Financed Monthly Special Assessment (estimate -- 5 years @ 6.3%): N/A | $253.14 | N/A
Total Monthly Fee with Financed Special Assessment (estimate): N/A | $1,936.78 | N/A

Please Note: the Special Assessment amount has not been determined yet. We are working with an engineer and getting multiple quotes to replace the roof in order to try to minimize the size of the Special Assessment as much as possible. The $13,000 per unit mentioned above is an estimate, that is probably on the high side, for discussion purposes only.

So most of you are probably asking, what's the practical difference between these two options (of course aside from the difference, assuming the Special Assessment is financed in Option A, of $271.56 per month)? As I see it, the main difference is this: when someone is looking to buy a condo, they incorporate the monthly condo fee into what they can justify or afford to spend. So keeping the monthly condo fee lower and using a Special Assessment to address a specific, short-term funding gap is generally wiser as it preserves higher unit sale value. That's my opinion and it's shared by the experts I've spoken with and so Option A is the way I'll personally be voting my unit's share. Obviously every owner is entitled to their own opinion and vote on which approach they prefer.

There are few other aspects of our 2023 budget that I want to touch on. Regarding the Operating Budget, the simple reality is that everything has gotten more expensive over the past year -- driven by inflation (up about 9% over the past 12 months), higher energy costs (higher by 8% over the past 12 months), supply chain challenges, and the increased cost and decreased availability of labor. In addition to these factors, the proposed 2023 Operating Budget includes a significant increase for landscaping improvement and maintenance. Our landscaping budget was dramatically cut over the past few years and the Board was unanimous that this needed to be reversed. Regarding the Reserve Budget, in addition to the acceleration of the roof replacement by seven years, the replacement costs of all the items in the Reserve Budget had not been updated for three years. Given what's happened to the cost of construction materials and labor, we saw increases across the board to the replacement cost of the items in our Reserves.

That summarizes the 2023 budget increases and the contents of perhaps a dozen meetings this Fall. If you've read this far, thanks for being an engaged owner. I am personally very concerned and frustrated with the situation described above. I made the decision to ask the Board to make me the President of our Association at the end of September of this year in order to decisively take every prudent action to address all this in the best possible way. As soon as our budget is finalized in December, I am leading a top-to-bottom review of our building, grounds, staff, contractors, and suppliers to identify opportunities to lower costs and improve performance. If we identify meaningful savings, I look forward to proposing an amended budget at some point in 2023. Thank you and please feel free to email or call me directly at mbramson@keycolony4.org or (786) 972-4580 to discuss any questions or concerns regarding our Association.

Sincerely, Matt Bramson

President, Key Colony IV Condo Association

Fellow Owners,

About three weeks go, on September Xth, I was named President of our Association by a majority of the Board of Directors. I accepted this responsibility in order to provide leadership though a significant and immediate set of challenges. I will do my best herein to briefly summarize these challenges, provide context, and outline potential actions we can take. This letter is not intended to offer an exhaustive explanation of the recent past nor the foreseeable future. Every owner is encouraged to contact me, our Manager, other Board members, plus attend Board and Committee meetings for more information and/or visit the Association office for access to all our records.

The first challenge we face is that we must, by state law, complete and submit a proposed 2023 Operating and Reserve budget to the ownership by November 15, 2022. For various reasons, we did not commence our budgeting process as far in advance of this deadline as best practices recommend.

The second challenge is that, given our circumstance - an older building on a barrier island vulnerable to hurricanes, the cost of insurance, especially from storm damage, is a major component of our annual Operating expenses. In 2022 we spent $600,000 on insurance for our Property, Liability, Wind, and Umbrella coverage. For 2023 we are estimated to spend $769,000. Please note that we are insured by QBE, which is the best and most affordable option available to us. Remember this fact because it will be important.

The third and biggest immediate challenge is our roof. Our Reserve Study, prepared by a licensed reserve specialist, estimated as recently as two years ago that our roof would not need to be replaced until 2030. We accrue reserves using the "cash flow method" which is one of two methods allowed under state law. This method is preferable in some respects as it offers greater flexibility. Recently, as part of the process of renewing our policy, our insurance company, QBE, asked for a roof condition report from a licensed inspector. Our roof received a poor grade and has less than two years of life remaining. It was determined to need immediate replacement to retain QBE as our insurance company. Here are some details on this challenge:

* We have $2.3MM in our Reserve Account right now. We can expend those funds on any Reserve Item that requires replacement or significant repair. Our roof is a Reserve Item.
* We have estimates to repair the roof ranging from $XMM to $Xmillion. Our plan is to engage our engineer to create a RFP and get multiple quotes. But we need to move quickly as QBE has conditioned their renewal of our coverage on having the roof replacement well underway by May 2023. In addition, qualified roofing companies in our area, especially after Hurricane Ian, are in high demand.
* The estimated cost of losing QBE and going to the only other option, Citizens, is at least $XXXX per year more. Plus, Citizens coverage includes the possibility of an assessment based on a loss in their portfolio unrelated to our property so, for example, a building that was destroyed by Ian in Ft. Myers could end up costing us extra money beyond our premium. There is no way to accurately budget for this open-ended financial risk. This is a situation we must do everything reasonable to avoid.
* The revised Reserve Report, updated by our reserve specialist this week, calls for $2.9MM in funding in 2023. For the past few years we have been funding $640,000 per year, so this is a huge increase. This increase is driven by two factors: the acceleration of the roof replacement by seven years and the required updates to the replacement cost of all the other Reserve Items. Inflation, increased cost of construction materials, labor cost increases, supply chain issues, higher fuel costs, and other economic factors have driven up the cost of replacing nearly everything. When our Reserve Report was updated, so were all these costs. Having updated and accurate reserves is a legal requirement. New laws will make it mandatory that

condos fully fund reserves starting in 2024.

The fourth challenge is our Operating Budget. As a result of two primary factors, the underestimation of our insurance premiums and utility costs for 2022 and the increasing cost of everything mentioned above due to inflation and other economic factors, we are needing to consider an increase to our 2023 Operating Budget of about 15% or look at reducing services and deferring maintenance. Neither of these options are desirable and could even be financially counterproductive as less service and maintenance can affect property values and rents. It's always tempting to say, "find waste to cut", and this effort is underway but, I need to be honest, we don't have much to consider unless we look at cutting employees and service providers like landscaping and property maintenance.

So it's not a pretty picture. We are all more or less equal owners so I am simply being direct and presenting the facts. Whatever we decide to do it will be borne by all of us equally based on our share of ownership. Before getting into our potential courses of action, let me provide some guardrails that we need to adhere to or at least fully understand.

* We have the option to not fully fund our reserves in 2023 but this option does not exist, due to changes in state law spurred by the Surfside disaster, for 2024 and beyond. So waiting a year will only make next year even tougher.
* We don't have to replace the roof right now. The inspection was not favorable but we can repair the biggest issues for about $40,000 and expect at least a couple more years of service from our current roof. We will, however, definitely be dropped by QBE if we don't replace the roof in 2023. This will cost us at least $XXXXX more per year and maybe much more due to assessments from the insurer of last resort, Citizens.
* If we decide to fully fund our Reserves in 2023, we have three options:
* Monthly payments - approximately $833 per unit per month ($2.9MM / 293 units / 12 months)
* One-time Special Assessment - approximately $10,000 ($2.9MM / 293 units)
* Line of credit - $2.9MM at 6% on a 10-year term would cost about $110 per unit for 10 years - but keep in mind, this only addresses the 2023 Reserve Budget shortfall and would not fully fund our reserve needs for the next 10 years

So the decisions facing the Board of Directors within the next few weeks are . . .
* How to address our 2023 Reserve Budget increase of $2.9MM?
* How to address the increased costs driving our 2023 Operating Budget up?

The Association Board and Finance Committtee have been working hard and meeting frequently over the past couple weeks. As our decisions will affect every owner, we welcome and encourage engagement. Now is the time for that. Changing decisions and revising budgets after the fact is not impossible, but neither is it optimal. If you want to know the best way to get engaged, it's to come to meetings. They are posted and blasted out via email at least two days in advance. You can always call the office to know when the next meeting is being held. They are always in the same place: our party room as well as on Zoom.

If you've gotten this far, thanks for being an engaged owner. I am personally very concerned and frustrated with the situation described above. I made the decision to ask the Board to make me the President in order to decisively take every prudent action to address this in the best possible way. But there appears to be no easy path. Please feel free to email or call me directly at mbramson@keycolony4.org or (786) 972-4580 to discuss any of this.

Sincerely, Matt Bramson

President, Key Colony IV Condo Association