

# UNCERTAINTY & RISK – HOW ARE THEY DIFFERENT?



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April 2013

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The stock market is climbing back up to pre-2008 levels. Because you don't know how the economy is going to behave in the next few months (uncertainty), does that mean you are financially at risk? If you are traveling in a big city and are uncertain of how to get to your destination, you may be at risk of missing the meeting. Aren't uncertainty and risk kind of the same thing, where more uncertainty means more risk? Not necessarily!



Uncertainty and risk are often used interchangeably, but they really shouldn't be. Uncertainty is the state of not knowing something, whereas risk is an undesirable consequence. In the stock market illustration, if I don't have money invested in an uncertain stock market, I have little financial risk if the Dow falls. If I am fumbling my way through a big city to a meeting that I am leading, there is no risk of missing it... the meeting will start when I arrive.

So what does all this have to do with budgets and Reserve Studies? The business of predicting the future is fundamentally uncertain. In our line of work we can observe very predictable trends... how fast different roof types decay, how long it takes paint to dry out and crack, how mechanical equipment deteriorates at a different rate in the desert compared to an oceanfront environment, etc. But exactly how fast, well, that's something no one can be certain about.

Now consider two unnamed Associations, with the same building style & materials, located across the street from each other, built by the same developer, about 20 years ago. One Association has always been guided by a Board of Directors with a high level of financial responsibility. They have been following the Funding Plan outlined in their Reserve Study and are close to being fully-funded. Their monthly assessments are slightly (3%) higher than the

second association, due to higher Reserve funding contributions. Both Associations face exactly the same “uncertain” future, but the first Association is well-maintained and has almost no risk of a Special Assessment. The same cannot be said for the second Association, which has ignored their Reserve Study’s Funding Plan and have been chronically underfunding reserves. As a

result, the Owners have been burdened with three Special Assessments in the past ten years. Unless the Board passes another Special Assessment to accomplish the next repainting project in a timely manner, the property will suffer the consequences of unsightly deferred maintenance.



Uncertainty affects us all. But not all uncertainty exposes you to risk. My advice: minimize your uncertainty, and take action to reduce your risk of Special Assessments, deferred maintenance, and declining property values by getting a current, credible Reserve Study and start properly funding your reserves. Living in an Association-governed community will always involve uncertainties, but that doesn’t mean you have to be at risk!