

Dear Preserve Owner,

Over the last several months, KICA staff has responded to various questions regarding the increase in the Preserve segment assessment. We have had these conversations in person, over the phone, and by email. In some instances, members have posed questions about the authority of KICA to levy the assessment. Others have wanted to better understand the expenses attributed to the assessment. On the following pages, a letter from KICA's attorney addresses both of these issues.

As it relates to expenses, members have requested a variety of documents. A recent request essentially asked for all financial records in the Preserve over a multi-year period. While time consuming to compile, this proved to be a helpful exercise for two reasons. First, it allowed a full year review of actual expenses as opposed to the partial year numbers available at budget time last fall (actuals turned out higher than our original estimate), and it highlighted the fact that direct vendor costs total \$163,500 of the \$165,000 billed to the Preserve. These invoices are available for inspection by any KICA member.

The \$163,500 direct vendor costs do not include any KICA labor costs for mowing, trimming or other maintenance work. It is clear the overall costs will exceed \$165,000. Because the direct and verifiable expenses essentially equal the total assessment, differences of opinion over the appropriate allocation of labor and other costs are diminished.

An example of these direct costs includes the actual 2018 water bills from Kiawah Island Utility for irrigation lines along the roadways throughout the Preserve. These KIU bills total \$91,920, and are only associated with maintaining the right of way landscaping. The Cinder Creek pavilion property has its own water meter and none of the expense for that facility - water or otherwise - is included in the segment assessment. It's important to reiterate that there are no charges to the Preserve for maintenance of the roads, drainage, leisure trails, docks, viewing tower, boat landing, etc. These expenses are shared with the entire Kiawah community. The segment assessment is focused solely on expenses associated with the fencing and landscape maintenance along the road rights of way within the Preserve.

We hope that the letter will answer any remaining questions about authority and allocation of expenses.

Sincerely,

The Kiawah Island Community Association

G. TRENHOLM WALKER
Direct: 843.727.2208
Email: Walker@WGFLAW.com

March 4, 2019

U.S.MAIL[] EMAIL[X]

Jimmy Bailey
Chief Operating Officer
Kiawah Island Community Association
23 Beachwalker Drive
Kiawah Island, SC 29455

Re: Kiawah Island Community Association – Preserve Segment Assessment
WGFL File No. 2560-003

Dear Jimmy:

I am writing at your request to discuss the legal basis for KICA's imposition of the Preserve segment assessment and to respond to several other questions posed by some of the property owners in the Preserve. These owners assert that KICA has no legitimate authority to impose the segment assessment, that KICA is unable to substantiate the amount of the segment assessment, and that they are being treated unfairly in comparison to other KICA owners outside the Preserve. You have asked that I address the letter to you, understanding that you intend to provide it to the members who have raised these questions.

In discussing these issues in this letter, neither this firm nor KICA is waiving the attorney-client privilege on these subjects. KICA is using this letter to respond to several of the assertions that have been made by the challengers to the segment assessment.

BACKGROUND

KICA's typical neighborhood maintenance generally includes routine pickup of large debris, line of sight pruning, pruning for vehicular clearance, blowing of roads, routine maintenance of neighborhood entrance landscape beds and cul de sac plantings (if in existence), and basic mowing/edging of the rights of way in front of unimproved lots.

Unlike most neighborhoods on Kiawah Island where the lot owner is responsible for the landscaping and maintenance of the landscaping up to the KICA right of way, the Preserve has a split rail wooden fence separating the area maintained by the lot owner and that by KICA. KICA maintains the split rail fence and landscape improvements along the rights of way. The grass and other landscaping along the shoulder is irrigated. KICA oversees all the needed care and maintenance for the fence, shoulders, and other roadway landscaping, and pays for all the water

and electricity for the irrigation that are separately metered. Due to the physical configuration of the Preserve, there are approximately 5 miles of fence and landscaping that KICA maintains that are unique to the Preserve.

The documentation that KICA has provided to substantiate the community segment assessment in the total amount of \$165,000 includes the following direct vendor costs:

KIU (Water):	\$91,920
BEC (Irrigation Electric):	\$5,759
Replacement Sod:	\$2,100
Replacement Plant Beds:	\$13,933
Straw and Straw Install Labor:	\$35,862
Fence Repairs:	<u>\$13,976</u>
Total out of pocket direct costs:	\$163,550

These figures are based on actual 2018 invoices, with the exception of Pine Straw, which is based on a 2019 contract price. They do not include any allocation of labor as well as any other estimates for known expenses unique to the Preserve. Those costs would include the KICA labor costs for mowing, trimming, and other work performed in the Preserve. KICA has estimated its labor costs in the Preserve, but because direct vendor costs are within \$1500 of the total assessment, KICA has not undertaken the additional exercise of tracking employee time exclusive to the Preserve. It is clear that the overall costs well exceed \$165,000.

Many neighborhoods on the island have their respective HOA or condominium regime directly assume the responsibility for maintaining their individual landscaping and other community improvements, taking over the equivalent of the services KICA provides and expenses that KICA pays in the Preserve. The following neighborhood associations and regimes impose separate assessments on their owners to cover these costs:

West Beach:

- Beach Townhomes
- Courtside Villas
- Duneside Villas
- Fairway Oaks Villas
- Greenslake Cottages (Cottage Owners HOA)
- Inlet Cove Cottages
- Oceanwoods Villas
- The Pointe
- Riverview
- Seascape Villas
- Shipwatch Villas
- Sparrow Pond Cottages (Cottage Owners HOA)

East Beach:

- Cypress Point
- The Enclave (Turtle Beach Ln)
- Mariners Watch Villas
- Maritime Villas
- Night Heron Cottages
- Parkside Villas
- Tennis Club Villas
- Turtle Cove Villas
- Turtle Point Villas
- The Village at Turtle Beach (Atlantic Beach Ct & Muirfield Ln)
- Windswept Villas

Vanderhorst:

- Indigo Park (Halona Ln)
- Marsh Cottages (Club, Osprey & Marsh)
- Ocean Green (Ocean Green & Silver Moss)
- Ocean Oaks
- Ocean Palms
- Settlement
- Summer Islands
- Terrapin Island

Several of these neighborhoods have private access gates, but most do not. My understanding is that KICA would gladly transition to the Preserve HOA everything that it is now doing and paying in the Preserve that is beyond the basic level of KICA services. The Preserve would then have full control over the degree of installation and maintenance it desired in its neighborhood and their associated costs. However, under the Preserve Covenants, the Preserve Association is to remain dormant until the Declarant conveys an interest in the Preserve Common Properties to it. I have not undertaken to determine if a transfer satisfying this requirement has occurred.

ANALYSIS

KICA's authority to levy a segment assessment in this instance arises from both the KICA Covenants and the Preserve Covenants. The KICA Covenants provide that the board has discretion in the interpretation and application of the KICA Covenants, which of course would include the provisions dealing with segment assessments. KICA has presented proof of direct costs that, combined with any reasonable allocation of its own labor and equipment costs, fully substantiate the reasonableness and fairness of the Preserve segment assessment. The Preserve Covenants go so far as to bar Preserve owners from challenging KICA's authority to impose the segment assessment by containing an express waiver by each Preserve owner of waging such a challenge. Finally, the Preserve Covenants include extensive dispute resolution procedures that

may apply to this controversy if some of the Preserve owners pursue a claim against KICA as they have indicated they may do.

Turning first to the legal authority of KICA to impose the segment assessment, Article 5, Section 5, of the KICA Covenants empowers KICA to implement segment assessments as follows:

- (a) **Segment Assessments.** In addition to the Annual Assessments and Special Assessments authorized in Sections 3 and 4 of this Article, the Board of Directors of the Association is hereby empowered to levy assessments to be used for the benefit and/or operation of a particular portion or segment of Kiawah Island, the payment of which assessment shall be borne by the Owners with such segment only; such assessment being herein referred to as "Segment Assessments". A Segment Assessment can only be levied by the Board of Directors of the Association after a determination that the affected segment of the Island has such need of a particular addition or improvement as would justify the expenditure therefor by the Owners who would be assessed and who would enjoy the benefits of such improvement or addition and/or the operation thereof. In cases where such a determination is made by the said Board the levy of the applicable Segment Assessment by the Board of Directors of the Association shall be final and not subject to approval by either the whole body of Members or by those Members who would be subject to the assessment. Any one Segment Assessment may not exceed a sum equal to one-half of the amount of the Maximum Annual Assessment in any one assessment year. The proportion of each Segment Assessment to be paid by the affected Owners of the various classifications of assessable property shall be in proportion to the payment of Annual Assessments.

If a Segment Assessment is made for an improvement or addition which requires a continuing assessment for maintenance and/or operational costs, then those Owners subject to the levy of the Segment Assessment may discontinue and abolish such Segment Assessment if such Owners so vote in a Referendum held during the second or any subsequent year of such a continuing Segment Assessment. Should any costs result from the removal of any addition or improvement where a particular Segment Assessment is discontinued, such costs shall be funded by the Segment Assessment before its discontinuance.

The additions or improvements that warrant the segment assessment in this case include the fences, landscaping, and irrigation system. There can be little doubt that the Preserve owners enjoy the benefits of such additions and improvements that would justify the expenditure by KICA for the operation, maintenance, and repair of them. As the second paragraph of this section makes clear, the segment assessment may be "a continuing assessment for maintenance and/or operational costs."

Contrary to what has been suggested, this section of the KICA Covenants does not require that KICA pay for the initial installation of the improvement or addition as a prerequisite to

implementing a segment assessment. All that is required is for the KICA board to make “a determination that the affected segment of the Island has such need of a particular addition or improvement as would justify the expenditure therefor by the Owners who would be assessed and who would enjoy the benefits of such improvement or addition and/or the operation thereof.” As stated, the segment assessment can be entirely for “the operation thereof.” Moreover, “[i]n cases where such a determination is made by the said Board the levy of the applicable Segment Assessment by the Board of Directors of the Association shall be final and not subject to approval by either the whole body of Members or by those Members who would be subject to the assessment.”

The boards of homeowners’ associations are afforded considerable latitude in determining the amount of assessments that are based on the costs of certain services to the community. Six months ago the Supreme Court of Vermont decided a similar case in an appeal involving a POA where a member claimed the amount of the assessment for those services was greater than the actual costs, just as in this case. Alpine Haven Property Owners’ Association, Inc. v. Brewen, 2018 VT 88, 198 A.3d 533 (2018). The Supreme Court of Vermont held the association’s determination of the assessment must be upheld in the absence of a showing that the amount was entirely unreasonable and, therefore, in violation of the implied covenant of good faith and fair dealing. The Court took the additional step of ruling that it was error for the trial court to determine the actual costs because the board’s determination was entitled to judicial deference in the absence of a violation of the implied covenant of good faith and fair dealing.

To the extent that a challenge to this segment assessment is based on an argument that somehow the landscaping, fencing, and irrigation are not “improvements” or “additions,” the KICA Covenants vest the KICA board with the discretion to interpret these terms and such interpretation is binding, provided that it has some reasonable basis.¹ Article 8, Section 4 of the KICA Covenants specifies the following:

Interpretation, The Board of Directors of the Association shall have the right to determine all questions arising in connection with this Declaration of Covenants and Restrictions and to construe and interpret its provisions. And its determination, construction or interpretation, shall be final and binding. In all cases, the provisions of this Declaration of Covenants and Restrictions shall be given that interpretation or construction that will best tend toward the consummation of the general plan of improvements.

¹ South Carolina’s appellate courts have considered fences, landscaping, sod, and irrigation to constitute a land improvement. First Eq. Inv. Corp. v. United Serv. Corp. of Anderson, 299 S.C. 491, 493, 386 S.E.2d 245, 247 (S.C. 1989)(landscaping and split rail fence are improvements); Thornton v. Thornton, 2007-UP-336, 2007 WL 8327919, at *2 (S.C. App. June 28, 2007)(landscaping, sodding, and a watering system are improvements).

All owners within the Preserve took title to their respective properties subject to The Preserve Covenants and are bound by its provisions. These community covenants contain extensive provisions that gave full notice of the segment assessment that some owners are now challenging and go so far as to include their de facto agreement to segment assessment. The Preserve Covenants provide a second independent basis for KICA's authority to levy a segment assessment on the Preserve owners.

The paragraphs within the Preserve Covenants discussing the KICA segment assessment are extensive. I repeat the text of Section 3.01(i) (ii) through (iv) below verbatim to communicate the detail with which this segment assessment was fully disclosed and explained to the Preserve owners:

(ii) Any fences and/or landscaping installed or replaced by the Declarant and/or KICA adjacent to the Lots, *either within the road rights-of-way or within the easement reserved by Declarant in Section 3.02(a) hereof*, shall be maintained and replaced as required by KICA, and shall not be materially altered, damaged, or destroyed by any Owner, their guests, invitees, tenants, permittees, employees, heirs, successors, and assigns.

(iii) Upon the acquisition of a Lot in The Preserve from Declarant, each Owner shall pay to Declarant, a "Capital Reserve Fee" in the amount of \$150.00, which fee shall be delivered by Declarant to KICA, to be held by KICA in an account and administered by KICA for the sole purpose of maintaining and replacing the fences and/or any special landscaping installed by Declarant and/or KICA as set forth in Section 3.01(i) above. Such fee shall be paid by the initial Lot purchaser only, and shall be used by KICA, its successors and/or assigns, solely for the uses and purposes set forth herein.

(iv) *KICA also has the right under Article V, Section 5(a) of the KICA Master Covenants to impose upon the Owners, a segment assessment for the maintenance and replacement of the aforesaid fences and special landscaping.* Once the funds from the "Capital Reserve Fee" established in Section 3.01(i)(iii) above have been depleted, and the KICA board of directors, *in its sole discretion*, determines that the continued maintenance and/or replacement of said fences and/or landscaping *to ensure the high standards of quality and distinction befitting the Lots, streets, rights-of-way, residual areas, and other properties within The Preserve*, cannot be accomplished absent the imposition of a segment assessment, *the KICA board of directors may*, pursuant to the powers thereunto enabling as set forth in Article V, Section 5(a) of the KICA Master Covenants as aforesaid, *levy upon the Owners, such a segment assessment for the purpose of maintaining, repairing, and/or replacing such fences and special landscaping. Further, in the event the KICA Board determines that such segment assessment must be a continuing segment assessment, each Owner, by the acceptance of a deed of conveyance to a Lot or Homesite in The Preserve, shall be deemed to have*

unilaterally, unconditionally, and permanently waived the right under Article V, Section 5(a) the KICA Master Covenants to discontinue and abolish such segment assessment during the second or any subsequent year.

Based on the last sentence, the Preserve owners waived any right to challenge the authority of KICA to impose the segment assessment when they accepted the deeds of conveyance for their respective properties. There is no legal basis for asserting that this conclusive waiver is not binding.

While the terms of the Preserve Covenants prevent the Preserve owners from litigating the authority of KICA to impose the segment assessment, and the law prevents them from overturning the board's determination in the absence of bad faith, they are entitled to make reasonable requests of KICA to provide documentation of the cost basis for the segment assessment as some of them have done.

Neither the law, nor the KICA Covenants, nor the Preserve Covenants require that the amount of the segment assessment must exactly reflect the precise dollar amount of the direct costs and allocated costs. Consistent with the law, the KICA Covenants grant the KICA board discretion in both the specific section dealing with segment assessments and in the general provision that states that the board's interpretation and application of a provision of the KICA Covenants is final and binding.

It should also be noted that neither the KICA Covenants nor the Preserve Covenants impose on KICA the burden of determining the exact level of services in other neighborhoods and the exact costs of these services to demonstrate that the segment assessment is entirely for services above this "baseline." Rather, the KICA board has the discretion to make a reasonable determination of the costs associated with the operation, maintenance and repair of the particular improvements and additions, without determining what it normally does and spends in other neighborhoods on the island.

Even though KICA is not required to perform a baseline analysis, subsection (iv) of the Preserve Covenants previously quoted is directly responsive to assertions that there is nothing unusual about the landscaping along the roads in the Preserve. This subsection recognizes that the roadside landscaping in the Preserve is superior to the common landscaping in the other communities on the island. In its words, the segment assessment is "to ensure the high standards of quality and distinction befitting the Lots, streets, rights-of-way, residual areas, and other properties within The Preserve...."

Considering the direct vendor costs being incurred by KICA as well as what the allocated costs of labor and equipment would be, the KICA board's current annual segment assessment appears reasonable and fair and in no way a violation of the implied covenant of good faith and fair dealing. Even if there were a legitimate question as to the fairness of the amount, the provisions

in both the KICA Covenants and Preserve Covenants conclusively bind the Preserve owners to the KICA board's decision as to the appropriate amount.

Because litigation against KICA has been discussed, it is worth mentioning that Article VIII of the Preserve Covenants includes extensive terms that govern disputes. KICA has the option of agreeing to be bound by these dispute resolution sections. Among its other provisions, these sections require that 75% of the owners must approve initiating a claim and that the prevailing party is entitled to recover its attorneys' fees and costs from the losing party.

CONCLUSION

For these reasons, the KICA board has the authority to impose the segment assessment on the Preserve owners and the Preserve owners have waived the right to challenge this authority. Further, the KICA board's calculation of the amount of the segment assessment is binding on the Preserve owners and in an entirely reasonable amount, given KICA's actual costs. If there is litigation or arbitration and KICA prevails, KICA shall be entitled to collect its attorneys' fees and costs from the adverse party.

Sincerely yours,

WALKER GRESSETTE FREEMAN & LINTON, LLC



G. Trenholm Walker