Reserve Fund Planning

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With So Many Reports, Why are Depreciation Reports Crucial?

What costing and reporting are we to use for long-term planning? Too often renewal projects end up costing more or a different amount than anticipated.

Some say that quotes, engineer reports, and/or maintenance plans are the closest we have to reality – and all that stakeholders need for long-term planning. Yet strata councils vary: some picking low, and others high bids; some doing the work after careful prior planification along with no-surprise 50 percent special contributions, other relying on last minute stressful ¾ special levies.

Each development's renewal history is different because councils – made up of volunteers with varying backgrounds and agendas – are themselves renewed every fiscal-year over the life of the development. The cumulative history of their decisions determines the condition of a development's common assets.

Final renewal project costs often vary from quoted or estimated costs. Recording actual costs; historical costs; renewal costs is a must to gauge the condition of a development. Only Real Estate Institute of Canada (REIC) Certified Reserve-fund Planner (CRP) compliant Depreciation Reports (DRs) record the actual history of final renewal costs, and rely on the history of scheduled expenditures for realistic reserve fund planning.

The focus on depreciation is crucial. Problems with relying on 25 percent of the last fiscal-year's operating budget for setting the reserve fund floor have led to requiring DRs. Over the life of a development – and with attention to the lifecycles of components – strata corporations are responsible for maintaining shared common assets with operating budget regular and required maintenance, and major repairs and replacements renewals from the reserve fund.

Based on performance in the field, common assets managed through the reserve fund are subject to expenditures that are less frequent than once a year – or every two (2) fiscal-years or more – with some components having full or partial replacements several fiscal-years in the future, often after current Owners are gone.

Good and fair reserve fund planning has strata councils input a development's actual renewal costs, and anticipates future costs based on this history. DRs are renewed every three to five years – depending on the legislation – REIC CRP compliant DRs are in fact standardized reporting that accurately represent a development's past, present and future. This is the fairest way to ensure up-to-date fiscal-year based allocations to the reserve fund.

Standardized reserve fund planning has a strata council input their expected costs – based on inspections and acquired quotes, opinions of probable costs, and asset plan costs acquired at the right time – at least for the next three to five fiscal-years. These estimates are used to propose motions for resolutions at AGMs so that Owners can be on top of the tendering process at any time and over the long-term; so that final costs are minimised, and so that regular contributions to the reserve fund are planned to reflect Owners' use of depreciating common assets, one fiscal-year at a time.

Only reserve fund planning provides a fiscal-year based measure of what is due by owners and needed to prepare for the development's common asset major repairs and replacements. While a maintenance plan or engineer report will detail what, at which quantity surveyor estimated cost, and when a major repair or replacement is to occur, only DRs break down the costing into a fiscal-year share of development specific costs, based on the remaining life of the common assets, adjusted one fiscal-year at-a-time.

Without standard DRs it is hard for strata councils that sit one year at a time to stay on top of the process of scheduling inspections, quotations, contributions. These are all needed to determine what is to be operating budget minor repairs; reserve fund major repairs, and reserve fund replacements.

Only DRs allow Owners to gauge their fair-share of contributions each fiscal-year regardless of when renewal projects are to occur over the life of a development. While a Long Term Maintenance Plan (LTMP) or a Capital asset Plan (CAP) tell us that replacing common assets today will likely cost $4,000,000 – and that in year 2030 $900,000 will be needed for a particular project – only a DR – by adjusting the current requirements from fiscal-year to fiscal-year – determines that future fiscal-year's share of that anticipated repair for Owners, regardless of their occupancy tenure.

REIC CRP compliant DRs measure a reserve fund's current requirements based on an analysis of all common assets' defined-age depreciation – very roughly, if roof shingles last twenty five years, then each fiscal-year's Owners are to pay for 1/25 of the cost to replace the shingles. Owners contributions are based on current requirements over the life of the development – 80 and more fiscal-years – not on their ownership tenure.

Having strata councils determine that Owners are to allocate regular contributions to the reserve fund based on $1,200,000 of next fiscal-year' current requirements ceiling is very different than having buyers calculate their return on investment based on capital costs of $4,000,000; or from having Owners contribute to the reserve fund based on the $4,000,000 estimated to replace all common assets now.

Only REIC CRP DRs calculate a benchmark of current requirements based on actual renewal costs for all common assets, adjusted from fiscal-year to fiscal-year. Other approaches focus on national or book current costs – relevant for taxation issues; for insurance purposes in the even of an earthquake, or for a developer wanting to know where to put their money.

Strata councils are responsible for the fiscal-year to fiscal-year management of a strata corporation over the life of a development. Sitting council members must ensure that the next strata council members have all the information they need to make the best decisions. Having the decision process open by overlapping several fiscal-years is the best way to guarantee sound management. The full disclosure of information to all stakeholders is in the best interest of all parties.

If you focus on the product only – the type of report – you partly miss the point. Warranty Reviews, Building Envelope Condition Assessment (BECA) reports, LTMPs, CAPs, etc. all come with their own type of costing, suited to their particular needs and short-term outlook.

Only DRs allow all stakeholders to have a historical perspective on the actual physical and financial performance of common assets; the actual renewal costs for projects undertaken and planned; the current requirements of a development, and the allocation of monies to sections, if any.

While councils' reserve fund planning can vary greatly, only REIC CRP DRs provide a comparable way too review a development's common asset inventory and renewal history across phases, sections and developments. Without measuring current requirements, the allocation of monies to each entity can only be arbitrary.

Without DRs, councils are prone to rely on the operating budget Repair and Maintenance line item to undertake renewals that are actually to be managed through the reserve fund. That is because without a DR, expenditures from the reserve fund require ¾ votes. Once Owners acquire their first DR and reserve fund plan accordingly, both operating budget expenses and reserve fund expenditures require 50 percent votes. Having all monies on the same footing facilitates decision-making.

Expenses and expenditures can actually be routed through their respective funds, making it much easier for councils to manage both funds, and Owners to know what is actually going on. With DRs and active reserve fund planning councils can now schedule inspections and expenditures for three to five fiscal-years until the next mandated DR, as well as manage the investment of the monies in the reserve fund – monies that are not required liquid for undertaken expenditures can be invested in vehicles that mature up to five fiscal-years in the future.

The REIC CRP reserve fund planning approach and its standardized reporting have been followed since the 1990s across Canada, and is recognized by BC Engineers and Architects in their guidelines. Having a development with several DRs done with the same approach is highly beneficial. Having two developments with DRs done the same way makes deciding where to buy a lot that much easier. ■

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J.-F. is active in the REIC CRP'S Task Force – reviewing Standards, and chairing the Education and Experience committee. He is IREM trained as REIC faculty for teaching reserve fund planning and reporting to professionals across Canada – he will be in Toronto in October co-teaching.

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