

# 7 Things To Know Before Your Next Reserve Study

Community associations are charged with the responsibility of maintaining the property value of their common elements. To do this properly, the association must develop a funding plan for future repairs and/or replacements of major common-area components. A reserve study is a professional budget-planning tool involving both a physical and a financial analysis that does just that. After determining the estimated remaining useful lives of the association's components and identifying the current status of the association's reserve fund, the reserve study report establishes a stable and equitable funding plan to offset the anticipated future major common-area expenditures.

In addition to providing a specific plan for the replacement of major items, reserve studies meet legal, fiduciary and professional requirements. Reserve studies also minimize the need for special assessments and enhance resale values.

**Before obtaining your next reserve study, you should know the following:**

## **1. All Reserve Study Preparers are Not Equal.**

Although a reserve schedule could be prepared by anyone, Reserve Specialists and Professional Engineers undoubtedly have the expertise and experience to compose more accurate and effective studies. The Reserve Specialist designation is awarded by the Community Associations Institute(CAI) to those who have a bachelor's degree in construction management, engineering or architecture and have prepared at least 30 reserve studies in the past three years. By obtaining this designation, the individual has proven through a combination of education and experience that they are qualified to perform a reserve study in conformance with the National Reserve Study Standards of the CAI. Since a significant portion of a reserve study is based on the condition of the individual components included within the study (such as roofs and roads), it is important that they be evaluated by someone with extensive field evaluation experience and knowledge. Being a licensed Professional Engineer confirms that the person has been trained and educated in performing this type of evaluation.

*With 25 years of expertise in providing reserve studies, Kipcon can provide the expertise, experience and accessibility to meet all of your needs. All of our reserve studies are performed under the direction of and are reviewed by both a Reserve Specialist (RS) and a licensed Professional Engineer (PE).*

## **2. All Reserve Studies are Not Equal.**

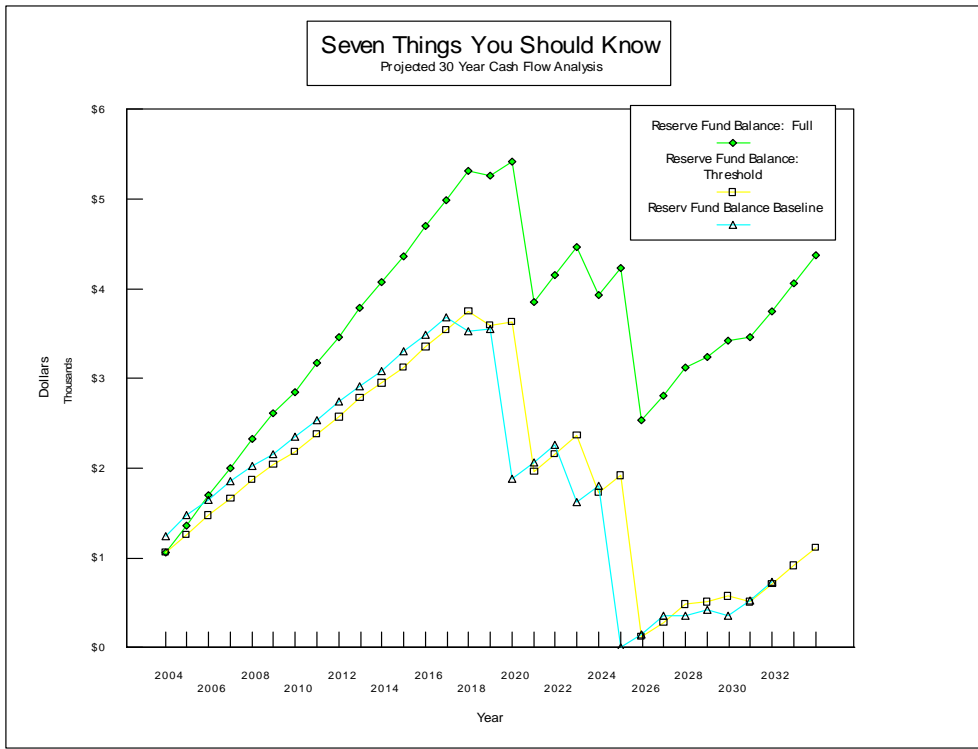
Years ago, most reserve studies included a list of all of the association's components, their replacement costs and remaining useful lives in order to determine what the next year's funding should be. To avoid being short sighted and focusing on only the next year's replacement items, the CAI developed national standards that consider long term planning decisions. According to the CAI's National Reserve Study Standards, all reserve studies require both a physical and a comprehensive financial analysis. The physical analysis determines the existing condition of the common elements. The financial analysis includes a 20 to 30 year cash flow projection of the reserve fund and focuses on the planning and budgeting of replacing these common elements. By providing this projection, the association is able to make an informed decision in regards to how much money should be set into the reserve fund each year to feel comfortable that a special assessment will not be required over the life of the projection.

*All Kipcon reserve studies are prepared in conformance with the National Reserve Study Standards of the Community Associations Institute. In fact, Kipcon's president, Mitchell H. Frumkin, was chairman of CAI's National's Reserve Professionals Committee when it developed these standards as well as the Reserve Specialist designation. In 1998, he was awarded the National Presidents Award for these efforts.*

## **3. Full Funding May Mean Over Funding.**

The National Reserve Study Standards of the Community Associations Institute recommends four different funding goals to choose from as a basis for an association's future reserve fund planning. Baseline funding allows for the cash flow to reach \$0 at some time over the projection period. Full funding is based on keeping each individual component 100% funded and in most instances results in having a significant amount of money stored without use for long periods of time. Threshold funding aims to maintain a pre-determined amount of money in the fund throughout the cash flow projection period. This amount is generally more than baseline funding and less than full funding. Lastly, statutory funding is when the amount to be funded is dictated by the local state requirements.

*At Kipcon, we work with the client to establish the funding goal ahead of time and then concentrate on strategies to achieve that objective. We also present multiple projections so the association can immediately see the result of continuing their present funding as well as the range of funding plans which can be selected.*



#### 4. Replacement Costs Must Be Accurate.

Replacement Costs should not always be based upon a replacement with the exact same component. In many instances the original component may not be available or has become outdated since it was first installed. By making recommendations for alternatives to the initial installation, the Association may be able to install a replacement with a significantly longer life such as a new type of roofing system, or something which is more energy efficient such as a new HVAC system. Smart replacements can result in a reduction to the recommended contributions to the Reserve Fund and/or a reduction in the client's energy costs.

*At Kipcon, all Reserve Studies are prepared under the direction of licensed Professional Engineers whose expertise in not only estimated life valuations and cost estimating but also in design. Kipcon also provides alternative recommendations and the required design services when the replacements become necessary.*

#### 5. A Reserve Study Has Many Uses.

In addition to estimating the Associations contributions to the Reserve Fund, a Reserve Study cash flow analysis can be used as a tool for determining how the Association's reserve funds can be invested. They give the Association the ability to plan for actual replacements, therefore making it easier to negotiate more effectively with contractors. The cash flow analysis will show how much money will be in the Reserve Fund and over what period of time. By reviewing this information with the Association's investment advisor, an investment plan

can be established to maximize the return on these funds based upon when they will be needed. Furthermore, by reviewing the anticipated replacements in the coming year, the Association can plan to have the required work performed before the actual conditions deteriorate to the point that remedial work will be required as part of the replacement, which can cause a significant increase in the actual cost of doing the work. For example, if the application of the seal coating on pavement is not performed on the recommended schedule, even if the concrete looks good, it can result in additional deterioration of the pavement which must be corrected prior to the application of an overlay. This can reduce the anticipated time period before the overlay is needed and increase the cost of the work.

*At Kipcon our expertise in both the analysis of existing conditions and the ability to answer technical questions specifically related to the conditions at your site can help prevent this from occurring.*

#### **6. A Reserve Study is Not a Maintenance Schedule.**

A reserve study is not the only funding an Association will need for the upkeep of its common elements. The reserve study is only for the major repair or replacement of the common and limited common elements that are the Association's responsibility. In all cases the cost of ongoing maintenance should also be budgeted separately, as this is not included within the reserve study. If the proper maintenance is not performed, it can result in a significant loss of useful life for the reserve components. This will result in their replacement occurring sooner than anticipated when adequate funds have not yet been accumulated.

*At Kipcon, we can also provide the Association with a recommended maintenance schedule and budget to help prevent this situation from occurring.*

#### **7. Reserve Studies are Budgeting Tools.**

Because a reserve study is only a budgeting tool it must be recognized that the actual cost of performing replacement work when it occurs will generally vary from the costs included within the study. In preparing the reserve study, replacement costs are based upon both estimating standards as well as the actual cost of similar projects. The replacement costs are typically based upon current dollars and are not based upon the preparation of specifications and bidding of the work to actual contractors. It is intended to be used as a budget-planning tool. In order to keep the replacement costs as well as the anticipated useful lives current, the reserve study should be updated (including a site visit) on a regular basis.

*At Kipcon, our expertise in the preparation of Reserve Studies and the implications of the different funding plans, allows us to make recommendations on how often the Study should be updated and what may happen if it is not. All studies include a comprehensive section outlining these recommendations.*