

Best Practices for Using Reserve Studies

(You have your Reserve Study. NOW WHAT?)

The Basics

1. **Agree to do something:** see “Consequences of Just Guessing”
2. Time reserve funding and capital planning to coincide with your budget process.
3. Select the kind of help that’s best suited to your Board and Association:
 - a. Do-it-yourself for minimally challenging or well-understood situations.
 - b. Full-feature Modeling tool customized for your association.
(recommended – especially for first-time data-based planning)
 - c. Turn-key consulting incorporating a customized funding modeler
(minimal involvement required from Board members).

Guidelines for Funding Reserves and Capital Projects

1. Start with an up-to-date reserve study
 - a. Use a study that’s no more than 3 years old for the first full funding plan.
 - b. Review and adjust the urgency and timing of capital projects based on expert input from the chief engineer, property manager, treasurer, and/or other knowledgeable individuals.
 - c. Add any projects that may not be included in the reserve study. Request rough estimates from contractors who may later be asked for bids.
 - d. Be sure to include inflation (35 – 5% minimum)
2. Incorporate any existing inflows/outflows that may affect reserves:
 - a. Anticipated interest on reserves
 - b. Anticipated income from any existing Special Assessments or Chargebacks
 - c. Anticipated Association loan payments scheduled
 - d. Sale of Association-owned units, etc.
3. Discuss with the Board the pros and cons of the basic funding mechanisms, answer their questions, understand their concerns, work to gain consensus:
 - a. Increase reserve contributions (to increase a low balance or save for upcoming projects)
 - b. Association Loan
 - c. Special Assessment (based on percent of owner equity)
 - d. Chargeback (based on percent of owner limited common element use)
 - e. Combinations of the above
4. Use a robust, data-based funding modeling tool that considers all factors
 - a. Reserve Study (capital expenditures and reserve balances by year)
 - b. Ability to easily shift planned project timelines and update cost estimates.
 - c. Basic condo data (number of units, etc.) and year-end financials to calculate important averages and metrics.
 - d. Uses graphic output to model and refine different strategies.

5. Don't strive to keep reserve balances consistent from year to year. They should vary.
6. Try out several possible funding strategies to understand the effect on future reserves:
 - a. Adjusting annual contributions to reserves
 - b. Getting an association loan
 - c. Levying a special assessment or chargeback
 - d. Using the above in various combinations
7. Fine-tune the optimal funding strategy by adjusting the variables:
 - a. Loan amount, interest rate, interest-only rate, first disbursement date, credit line period (disbursements) fees, repayment term, etc.
 - b. Special assessment amount, start date, repayment terms, etc.

Implementing the Funding Plan

1. Incorporate the results into next year's budget:
 - a. Adjust the budgeted regular monthly reserves (increase or decrease) by the amount planned as next year's contribution to reserves.
 - b. Include all planned capital projects.
 - c. Include any desired placeholder amounts for unexpected repairs.
2. Communicate fully and transparently to owners
 - a. Present the big picture and the details.
 - b. Make percentage increases come-to-life by providing average amounts.
 - c. Consider using an outside professional to do presentations.
3. Begin discussions with legal counsel regarding any planned special assessment or chargeback (state condo law, declarations and bylaws, etc.).
4. Discuss upcoming major projects with contractors to get fresh rough estimates.
5. Begin negotiations with lenders and get pre-qualified BEFORE signing any contractor agreements for any loan-dependent projects.
6. Assess and redistribute your reserve fund investments (and determine how long money can be tied up in higher-earning fixed-term CDs or Treasuries).
7. Commit to updating your reserve study at the end of each year to reflect actual versus projected balance and project costs.

Consequences of Just Guessing

1. Sharp increases to reserve contribution
2. Inability to get insurance (insufficient reserves to pay the deductible or worse)
3. Unanticipated special assessments
4. Not having enough in reserves to qualify for a loan
5. Deferring projects is always more expensive
6. Deconversion
7. Failure of structural components or expensive to remediate damage (water intrusion)