



WHAT MAKES A GOOD RESERVE STUDY?



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Everyone wants a good reserve study. What does that imply, though?

Here's a list:

1. All the “right” components on your Reserve Component List (none missing that should be on the list, and none on the list that should be handled in the Operating Budget)
2. Accurate estimates of Useful Life (UL) and Remaining Useful Life (RUL)
3. Accurate estimates of Repair/Replacement costs (\$)
4. An accurate projection of the starting Reserve balance (\$)
5. A Funding Plan that allows for the timely repair & replacement of all the items on the Component List

Component Selection: National Reserve Study Standards

If you've had a Reserve Study prepared by an independent, credentialed Reserve professional (a “RS” or Reserve Specialist), your Reserve Component List should only need minor adjustments annually.

Even so, review that Component List in light of the following National Reserve Study Standards 4-part test. Make sure that every component on the list is:

1. A common area maintenance responsibility
2. With a limited Useful Life
3. With a predictable Remaining Useful Life, and
4. With a repair or replacement cost above a minimum threshold of significance

This will be your best way to make sure you are Reserving for all the “right” components.

Inform Your Reserve Provider of Completed Projects

Any recent Reserve projects that the Association has completed should be acknowledged in your Reserve Study.

Receipts and proposals can be filed in a "Reserve Projects" folder that is kept by some associations. Estimates for Useful Life, Remaining Useful Life, and especially current Repair/Replacement costs are more accurate with this information.

Your current Reserve Study ought to reflect your actual costs if a roof was replaced for \$100,000 earlier in the year. Your reserve study won't accurately reflect the community if your reserve specialist notices the new roof, but is forced to use their estimated replacement cost of \$80,000.

Inaccurate information about components will have an impact on the Percent Funded and recommended monthly reserve funding. The best way to improve the accuracy of your reserve study is to use learn from project experience at your association and use actual Useful Life, Remaining Useful Life, and Replacement Cost values, not estimates.

Provide Vendor Information to Your Reserve Study Provider

By providing your Reserve Specialist with a list of the Association's vendors, your reserve study provider will gain access to important information from those service professionals. The state of various components, as well as the price of replacing them, are regularly provided by these vendors.

A pool vendor, for instance, might be able to provide information regarding a pool filter that, despite not leaking or rusting, is simply not functioning properly and requires replacement. The Reserve Specialist could be informed by the pool vendor that a different kind of filter is required at this time, and how much it would cost to replace it.

An asphalt vendor could also provide information such as the state of the current seal-coat, and how much longer before a more significant (costly) resurface project will be required.

Your End-of-Year Reserve Fund Balance

Estimating your end-of year Reserve Balance requires the involvement of the Board and management. Management typically has the most recent bank statements, knowledge of any outstanding payments needed to be made from the Reserve Fund, and a realistic expectation of whether budgeted Reserve transfers will actually be made through the end of the year.

It is that combination of actual balance, projected expenses, and projected income to the Reserve Fund that will ensure a realistic and accurate projection of Fiscal Year End Reserve balance. The accuracy of this computation is essential, as it will affect the Percent Funded calculation and possibly the ongoing Reserve funding requirement.

Timing is also an important factor in the Reserve Study process. Ideally, the recommended Monthly Reserve funding should be incorporated into the budget for the upcoming year. The study should therefore be completed before the draft budget is completed. For communities with a December 31 Fiscal Year End, bids for preparation of the Reserve Study should be obtained in early summer and the process started in July or August. The best case schedule

scenario is shown below:

- Jun-Jul Obtain bid for Reserve Study
- Sep- Oct Reserve Study is completed
- Oct-Nov Budget is approved
- Nov State Disclosures are sent out (as req'd)

This schedule allows the management and board to review the study and request possible revisions. The worst case scenario is that the association needs a Reserve Study and is frantically seeking bids in early November. That situation will lead to the Reserve Study being expensive, rushed, too late to be used in the budgeting process.

Reserve Study Funding Plans: National Reserve Study Standards

Finally, what makes a great Funding Plan? National Reserve Study Standards require a Funding Plan be based on four principles:

- Providing adequate funds when needed
- Providing budget stability from year to year
- A fair distribution of Reserve funding among the owners, over the years, and
- that it be fiscally responsible.

These principles ensure that the Funding Plan offsets ongoing deterioration, not burdening future owners with “more than their fair share” of ongoing funding, or special assessments to replace assets that deteriorated well before they became owners in the association. That also means that a great Funding Plan does not under-reserve in the short term, favoring current owners.

Ideally, Reserve funding should offset the ongoing deterioration of Reserve assets. In this way, all owners pay their fair share of the deterioration of the common areas they are “using up” during the time they own a home at the association.

There should be an anticipation that the Reserve funding rates will increase annually. The desire not to increase dues is understandable, but should not be confused with the reality of inflationary trends and the needs of the association.

Unfortunately, \$300 a month is not worth what it was 15 years ago. If increases have not been made over that 15-year period, the association has been taking steps backward as the value of the dollar decreases. Further, historically low interest rates earned on Reserve funds will never offset inflation.

The above principles require the involvement of the experienced Reserve Study professional, the Association Board, and management. A “great” Reserve Study is the result of refinements year after year, so that it accurately reflects the current physical and financial state of the association, providing accurate budget guidance to the Board and management.