

CAI National Reserve Study Standards

Rolled out in early 1998, CAI's National Reserve Study Standards provided a greatly needed framework for the community association industry which paved the way for the future of Common Interest Communities nationwide. Providing consistent terminology, basic disclosures within the Reserve Study, defining the three "Levels of Service" provided, and a credentialing program for professional providers (the "Reserve Specialist" designation), CAI's minimum reserve study standards brought order to this relatively new industry.

Reserve Study

A Reserve Study is made up of two parts:

- the information about the physical status and repair/replacement cost of the major common area components the association is obligated to maintain (Physical Analysis), and
- the evaluation and analysis of the association's Reserve balance, income, and expenses (Financial Analysis).

The Physical Analysis is comprised of the Component Inventory, Condition Assessment, and Life and Valuation Estimates. The Component Inventory should be relatively "stable" from year to year, while the Condition Assessment and Life and Valuation Estimates will necessarily change from year to year.

The Financial Analysis is made up of a *finding* of the client's current Reserve Fund status (measured in cash or as Percent Funded) and a *recommendation* for an appropriate Reserve contribution rate (Funding Plan).

Reserve Study

Physical Analysis

Component Inventory
Condition Assessment
Life and Valuation Estimates

Financial Analysis

Fund Status
Funding Plan

Levels of Service

The following three categories describe the various types of Reserve Studies, from exhaustive to minimal.

Full: A Reserve Study in which the following five Reserve Study "Tasks" are performed:

- Component Inventory
- Condition Assessment (based upon on-site visual observations)
- Life and Valuation Estimates
- Fund Status
- Funding Plan

Update, With-Site-Visit/On-Site Review: A Reserve Study update in which the following five Reserve Study "Tasks" are performed:

- Component Inventory (verification only, not quantification)
- Condition Assessment (based on on-site visual observations)
- Life and Valuation Estimates
- Fund Status
- Funding Plan

Update, No-Site-Visit/Off Site Review: A Reserve Study update with no on-site visual observations in which the following three Reserve Study "Tasks" are performed:

- Life and Valuation Estimates
- Fund Status
- Funding Plan

Terms and Definitions

CASH FLOW METHOD: A method of developing a Reserve Funding Plan where contributions to the Reserve fund are designed to offset the variable annual expenditures from the Reserve fund. Different Reserve Funding Plans are tested against the anticipated schedule of Reserve expenses until the desired Funding Goal is achieved

COMPONENT: The individual line items in the Reserve Study, developed or updated in the Physical Analysis. These elements form the building blocks for the Reserve Study. Components typically are: 1) Association responsibility, 2) with limited Useful Life expectancies, 3) predictable Remaining Useful Life expectancies, 4) above a minimum threshold cost, and 5) as required by local codes.

COMPONENT INVENTORY: The task of selecting and quantifying Reserve Components. This task can be accomplished through on-site visual observations, review of association design and organizational documents, a review of established association precedents, and discussion with appropriate association representative(s).

COMPONENT METHOD: A method of developing a Reserve Funding Plan where the total contribution is based on the sum of contributions for individual components. See "Cash Flow Method".

CONDITION ASSESSMENT: The task of evaluating the current condition of the component based on observed or reported characteristics.

CURRENT REPLACEMENT COST: See "Replacement Cost".

DEFICIT: An actual (or projected) Reserve Balance less than the Fully Funded Balance. The opposite would be a Surplus.

EFFECTIVE AGE: The difference between Useful Life and Remaining Useful Life. Not always equivalent to chronological age, since some components age irregularly. Used primarily in computations.

FINANCIAL ANALYSIS: The portion of a Reserve Study where current status of the Reserves (measured as cash or Percent Funded) and a recommended Reserve contribution rate (Reserve Funding Plan) are derived, and the projected Reserve income and expense over time is presented. The Financial Analysis is one of the two parts of a Reserve Study.

FULLY FUNDED: 100% Funded. When the actual (or projected) Reserve balance is equal to the Fully Funded Balance.

FULLY FUNDED BALANCE (FFB): *Total Accrued Depreciation*. An indicator against which Actual (or projected) Reserve balance can be compared. The Reserve balance that is in direct proportion to the fraction of life "used up" of the current Repair or Replacement cost. This number is calculated for each component, then summed together for an association total. Two formulae can be utilized, depending on the provider's sensitivity to interest and inflation effects. Note: both yield identical results when interest and inflation are equivalent.

$$\text{FFB} = \text{Current Cost} \times \text{Effective Age} / \text{Useful Life}.$$

or

$$\text{FFB} = (\text{Current Cost} \times \text{Effective Age} / \text{Useful Life}) + ((\text{Current Cost} \times \text{Effective Age} / \text{Useful Life}) / (1 + \text{Interest Rate}) ^ \text{Remaining Life}) - ((\text{Current Cost} \times \text{Effective Age} / \text{Useful Life}) / (1 + \text{Inflation Rate}) ^ \text{Remaining Life})$$

FUND STATUS: The status of the reserve fund as compared to as established benchmark such as percent funding.

FUNDING GOALS: Independent of methodology utilized, the following represent the basic categories of Funding Plan goals:

BASELINE FUNDING: Establishing a Reserve funding goal of keeping the Reserve cash balance above zero.

FULLY FUNDING: Setting a Reserve funding *goal of attaining and maintaining* Reserves at or near 100% funded.

STATUTORY FUNDING: Establishing a Reserve funding goal of setting aside the specific minimum amount of Reserves required by local statutes.

THRESHOLD FUNDING: Establishing a Reserve funding goal of keeping the Reserve balance above a specified dollar or Percent Funded amount. Depending on the threshold, this may be more or less conservative than "Fully Funding".

FUNDING PLAN: An Association's plan to provide income to a Reserve fund to offset anticipated expenditures from that fund.

FUNDING PRINCIPLES: In the development of a Funding Plan, the following four principles are to be considered:

- Sufficient Funds when Required (adequate)
- Stable Contribution Rate over the Years (smooth annual transitions)
- Equitably Distributed Contributions over the Years (fairness)
- Fiscally Responsible

LIFE AND VALUATION ESTIMATES: The task of estimating Useful Life, Remaining Useful Life, and Repair or Replacement Costs for the Reserve components.

PERCENT FUNDED: The ratio, at a particular point of time (typically the beginning of the Fiscal Year), of the actual (or projected) Reserve Balance to the Fully Funded Balance, expressed as a percentage.

PHYSICAL ANALYSIS: The portion of the Reserve Study where the Component Inventory, Condition Assessment, and Life and Valuation Estimate tasks are performed. This represents one of the two parts of the Reserve Study.

REMAINING USEFUL LIFE (RUL): Also referred to as "Remaining Life" (RL). The estimated time, in years, that a reserve component can be expected to continue to serve its intended function. Projects anticipated to occur in the initial year have "zero" Remaining Useful Life.

REPLACEMENT COST: The cost of replacing, repairing, or restoring a Reserve Component to its original functional condition. The Current Replacement Cost would be the cost to replace, repair, or restore the component during that particular year.

RESERVE BALANCE: Actual or projected funds as of a particular point in time that the association has identified for use to defray the future repair or replacement of those major components which the association is obligated to maintain. Also known as Reserves, Reserve Accounts, Cash Reserves.

RESERVE PROVIDER: An individual that prepares Reserve Studies.

RESERVE STUDY: A budget planning tool which identifies the current status of the Reserve fund and a stable and equitable Funding Plan to offset the anticipated future major common area expenditures. The Reserve Study consists of two parts: the Physical Analysis and the Financial Analysis. "Our budget and finance committee is soliciting proposals to update our Reserve Study for next year's budget."

RESPONSIBLE CHARGE: a Reserve Specialist in responsible charge of a Reserve Study shall render regular and effective supervision to those individuals performing services which directly and materially affect the quality and competence rendered by the Reserve Specialist. A Reserve Specialist shall maintain such records as are reasonably necessary to establish that the Reserve Specialist exercised regular and effective supervision of a Reserve Study of which he was in responsible charge. A Reserve Specialist engaged in any of the following acts or practices shall be deemed to not have rendered the regular and effective supervision required herein:

- The regular and continuous absence from principal office premises from which professional services are rendered; except for performance of field work or presence in a field office maintained exclusively for a specific project;
- The failure to personally inspect or review the work of subordinates where necessary and appropriate;
- The rendering of a limited, cursory or perfunctory review of plans or projects in lieu of an appropriate detailed review;
- The failure to personally be available on a reasonable basis or with adequate advance notice for consultation and inspection where circumstances require personal availability.

SPECIAL ASSESSMENT: An assessment levied on the members of an association in addition to regular assessments. Special Assessments are often regulated by Governing Documents or local statutes.

SURPLUS: An actual (or projected) Reserve Balance greater than the Fully Funded Balance. See "Deficit".

USEFUL LIFE (UL): Total Useful Life or Depreciable Life. The estimated time, in years, that a reserve component can be expected to serve its intended function if properly constructed in its present application or installation.

CAI's Professional Designation - RS

The following is an outline of the designation application. The RS designation is intended for individuals, and is designed to demonstrate a basic level of competency within the industry. The application is comprised of four parts: Background, Experience and Sample Work Product, References, and Continuing Experience. All four parts must be completed and submitted to apply for the credential via the Reserve Specialist (RS) Application.

QUALIFICATION GUIDELINES:

I. Background:

- College bachelor level degree in construction management, architecture, or engineering;
Or
- Four years prior related experience (prior to and in addition to direct Reserve Study experience) in a field servicing community associations (accounting, association management, construction, etc.);
Or
- Trade school diploma and two years prior related experience (prior to and in addition to prior Reserve Study experience).

II. Experience and Sample Work Product:

- Must certify preparation of or be in responsible charge for preparing at least 50 Reserve Studies within the past three calendar years.
- Must submit one study of the applicant's original work using format on application, including all five tasks as described within for a "Full" study.
- One sample work product must have been submitted to demonstrate that minimum Report requirements and disclosures have been met.

III. References:

- Two references from community association industry professionals.
- Five references from different clients.

IV. Continuing Experience:

Must continue to prepare or be in responsible charge for the preparation of at least 10 Reserve Studies for Community Associations based on visual on-site observations. Renewal applications, required every third year, will require documentation of this experience.

Reserve Study Contents

The following is a list of the minimum contents to be included in the Reserve Study.

- A summary of the association's number of units, physical description, and Reserve Fund financial condition.
- A projection of Reserve Starting Balance, recommended Reserve contributions, projected Reserve expenses, and projected ending Reserve Fund Balance for a minimum of 20 years.
- A tabular listing of the Component Inventory, component quantity or identifying descriptions, Useful Life, Remaining Useful Life, and Current Replacement Cost.
- A description of methods and objectives utilized in computing the Fund Status and development of the Funding Plan.
- Source(s) utilized to obtain component Repair or Replacement cost estimates.
- A description of the Level of Service by which the Reserve Study was prepared.
- Fiscal Year for which the Reserve Study is prepared.

Disclosures

The following are the *minimum disclosures* to be included in the Reserve Study.

- **General:** Description of other involvement(s) with the association which could result in actual or perceived conflicts of interest.
- **Physical Analysis:** Description of how thorough the on-site observations were performed: representative sampling vs. all common areas, destructive testing or not, field measurements vs. drawing take-offs, etc.
- **Financial Analysis:** Description of assumptions utilized for interest and inflation, tax, and other outside factors.
- **Personnel Credentials:** State or organizational licenses or credentials carried by the individual responsible for Reserve Study preparation or oversight.
- **Update Reports:** Disclosure of how the current work is reliant on the validity of prior Reserve Studies.
- **Completeness:** Material issues which, if not disclosed, would cause a distortion of the association's situation.
- **Reliance on Client Data:** Information provided by the official representative of the association regarding financial, physical, quantity, or historical issues will be deemed reliable by the consultant. The Reserve Study will be a reflection of information provided to the consultant and assembled for the association's use, not for the purpose of performing an audit, quality/forensic analyses, or background checks of historical records.
- **Reserve Balance:** The actual or projected total presented in the Reserve Study is based upon information provided and was not audited.
- **Component Quantities:** For Update With-Site-Visit and Update No-Site-Visit Levels of Service, the client is considered to have deemed previously developed component quantities as accurate and reliable.
- **Reserve Projects:** Information provided about Reserve projects will be considered reliable. Any on-site inspection (visual examination) should not be considered a project audit or quality inspection.