Realistic Reserves

for

Today's Economy

August 16, 2012

Hosted By: **SOUTH CAROLINA CHAPTER**
COMMUNITY ASSOCIATIONS INSTITUTE

Presented By: millerdodson ASSOCIATES | Capital Reserve Consultants

Today's Presentation Overview

1. **Four Funding Challenges**
   in Today's Economic Climate

2. **Understanding the Reserve Study**
   Where do the numbers come from?

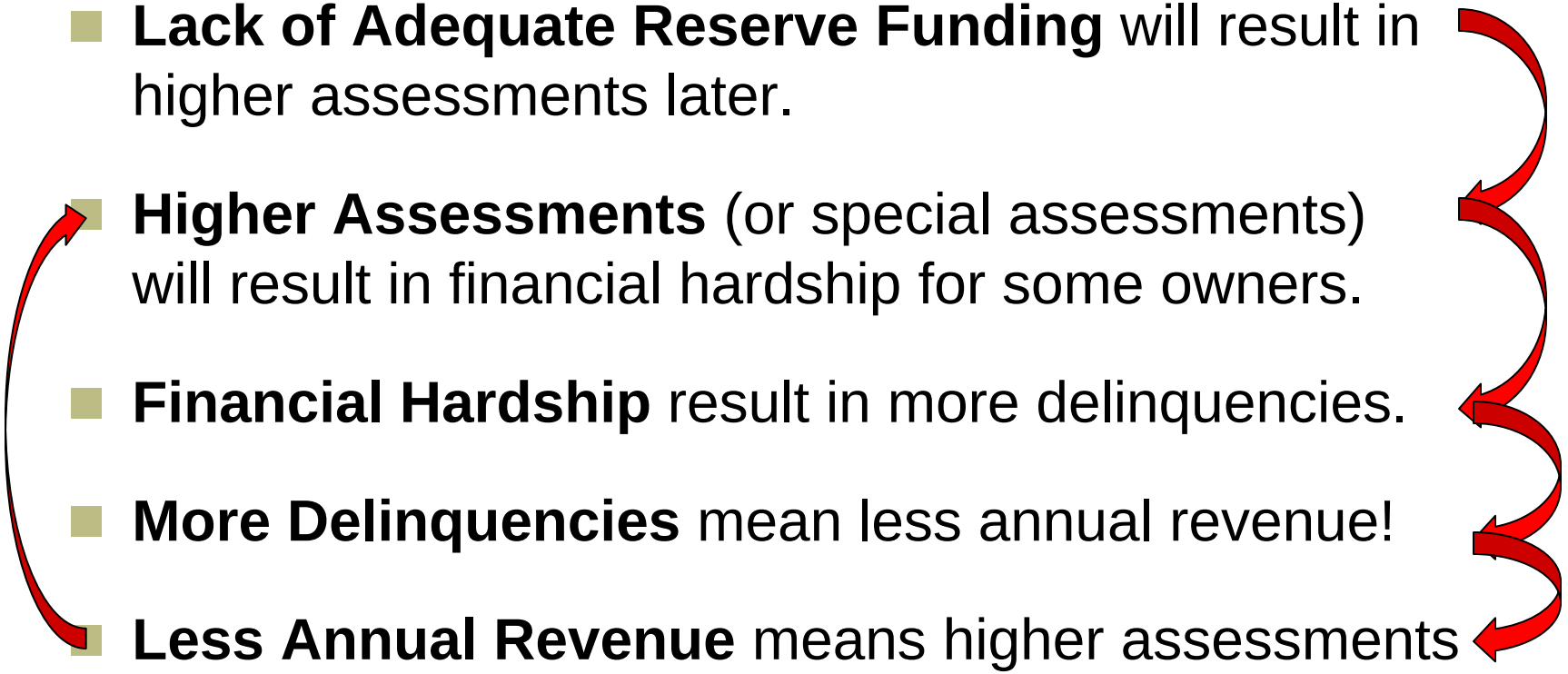
3. **Strategic Funding Solutions**
   Funding Methods – Pros & Cons
   Roadmap to your Funding Objective

Core Ideas:

- Market Conditions Have Changed since December 2007 housing downturn!
- Adequate Funding of Reserves more of a challenge then ever before!
- In today's economy, delinquencies and foreclosures may be triggered by:
  - Large increase in assessments
  - Large special assessments
- New Market and Economic Conditions Require New Strategies

Reserve Funding Cycle Pitfall

- **Lack of Adequate Reserve Funding** will result in higher assessments later.
- **Higher Assessments** (or special assessments) will result in financial hardship for some owners.
- **Financial Hardship** result in more delinquencies.
- **More Delinquencies** mean less annual revenue!
- **Less Annual Revenue** means higher assessments for others!



FOUR CHALLENGES TO RESERVE FUNDING

Funding Challenge 1

Adequate Funding

- Adequately fund “long-term” financial obligations, i.e. Replacement Reserves…
- Without triggering “short-term” financial crisis, i.e. delinquencies or foreclosures.

Funding Challenge 2

Keep Property Values High
While Still Staying Competitive!

- Aesthetic Quality / Curb Appeal
- Amenities and Facilities Up-to-Date
- Reasonable Normal Assessments
- Without History of Special Assessments

Funding Challenge 3

Limitations on Delinquency Level

- **FHA** (Freddie Mac & Fannie Mae similar)
  - 15% delinquency will disqualify Condominium from FHA approval for financing guarantee.
- **Commercial Bank Loans**
  - 8% to 10% delinquency will disqualify community from commercial bank loans.
- Also: Remember Reduced Revenue Stream

Funding Challenge 4

Today's Housing & Economic Climate

- Residential Sales **DOWN**
- Home Foreclosures **UP**
- Family Income **DOWN**
- Delinquencies **UP**
- Assessment Receipts **Down**
- Replacement Costs **UP**

More on cost inflation later

Issues Affecting Assessments

1. **Individual loss of jobs/income**
2. **Decline in Home Value**
3. **Underwater (upside-down) mortgages**
4. **Rising delinquencies and foreclosures**
5. **Inflation in replacement costs**

1. Decline in Household Income

- The Median Household Income has fallen 8.3% since the end of 2007 from $49,600 to $45,800 in 2010. * Lowest level since1996. * **
- Ave. Family Net Worth dropped from $126,400 in 2007 to $77,300 in 2010. Wiped out 2 decades of prosperity!
- Number of people living below the Poverty Line (below $22,314 annual income) at historic high level of 15.1%. (Almost 1 of 6 Americans - Highest since 1983)*
- Unemployment at 8.2% ***

* Federal Reserve/US Census.

** **New York Times** /Business Day Economy / June 11, 2012

*** US Bureau of Labor Statistics / May 2012

2. Declining Property Values

- Average Home Price in US have fallen 34.4% since the 2006 peak.**
- Zillow estimates an additional 3.7% fall in home value (nat'l average) by the end of 2012. *
- Lack of confidence has potential buyers on the fence until market bottom is reached and turnaround is underway.
- Experts calculate between 1.6 million and 5 million homes in "Shadow Inventory". ***

Sources: * Zillow ** CNN Money, May27, 2011 *** Miami Herald October 18, 2011

3. Underwater Mortgages

- Roughly 16 million homes had negative equity as of the 1st quarter of 2012.

  = 31.4% of all residential home loans

- Down slightly from 32.4% one year previously.

- That means that virtually **3 out of 10** homes have no financial value to their owners**!**

Source: **CNN Money** May 24, 2012

4. Rising Delinquencies & Foreclosures

- Reports indicate that ~ 4 million U.S. home-owners are 90 days or more delinquent on their loans. * (This figure decreased slightly in 1Q12)
- July 2010 highest foreclosure month in US history. *
- 3.5 Million Foreclosure filings in 2010 **
- 2.8 Million Foreclosure filings in 2011 **

Sources: * RealtyTrac
** Zillow

4.1 Rising Foreclosures

- **Foreclosures rose in 3rd Qtr 2011 due to corrections in paperwork & process problems.**
- **Previous declines due to delays; NOT due to robust recovery in housing market!**
  - Robo-signing scandal forced postponement and delay of filings at end of 2010.
  - Processing delays in 2010 include court approvals in states that require judicial process.
  - Foreclosure prevention efforts –state & federal

Source: CNNMoney 11/17/2011

4.2 Expert Forecasts

- Short-term interventions will extend the current housing market woes into 2012 and beyond. *
- Zillow estimates housing prices will likely bottom out in early 2013. *
- 7.4 million homes foreclosed since 2007.**
- Another 7.4 million foreclosures through 2016.**

Sources: * Zillow
** RealtyTrac

4.3.1 List of Hardest Hit States

Source: RealtyTrac

State	Foreclosure Rate 2011	Decline in Home Value
1. Florida	11.9%	-49.0%
2. New Jersey	6.4%	-22.6%
3. Illinois	5.4%	-29.0%
4. Nevada	5.3%	-59.3%
5. New York	4.6%	-13.6%

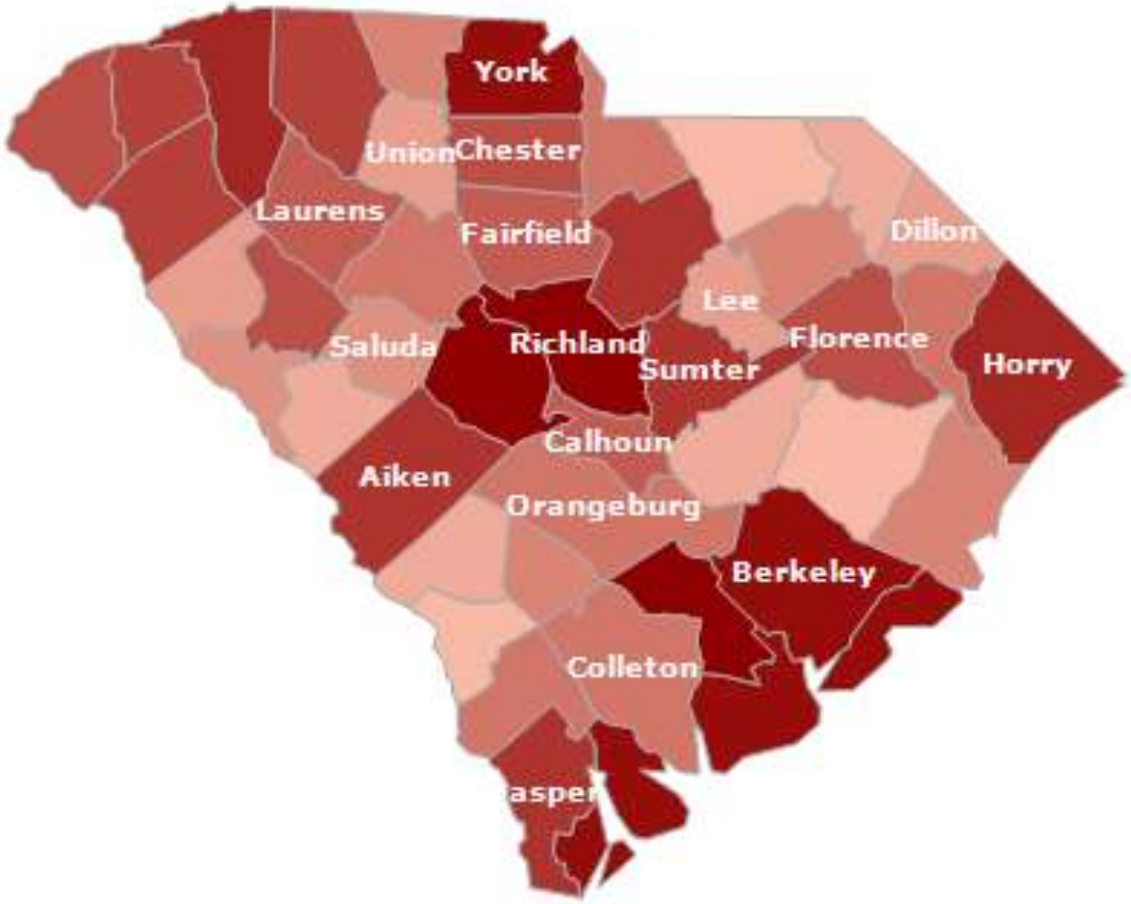
4.3.2 List of Hardest Hit States

Source: RealtyTrac

State	Foreclosure Rate 2011	Decline in Home Value
6. Maine	4.2%	-6.0%
7. Connecticut	4.1%	-16.6%
8. Hawaii	3.8%	-22.2%
9. **South Carolina**	3.7%	-10.2%
10. Ohio	3.5%	-14.1%

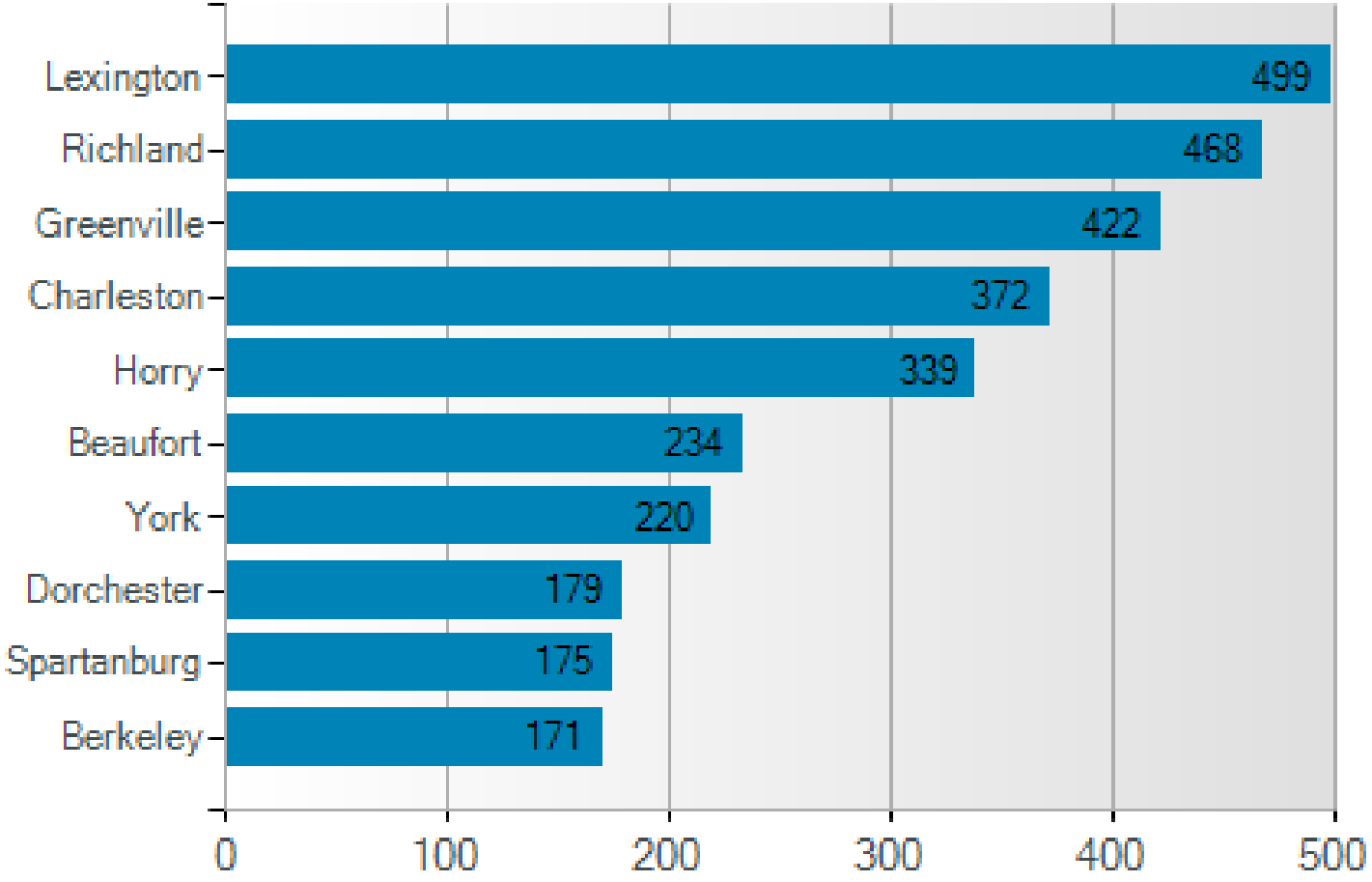
4.3.3 Hardest Hit Counties in SC

Source: RealtyTrac



4.3.4 List of Hardest Hit Counties

Source: RealtyTrac



5. Inflation is High!

Yes, Very High!

Inflation Confusion
CPI versus PPI

- **Consumer Price Index (CPI)** gauges:
  - Food Costs
  - Fuel Costs
  - Electricity Costs
  - Housing Costs (meaning rent)
- **Producer Price Index (PPI)** gauges
  - Manufacturing costs
  - Construction costs

Percentage Changes in Producer Price Indexes (PPIs) for

Construction Materials & Components, (2003 - 2012)

BLS Series ID		12 months through December--						to May 2012 since--			
		2006	2007	2008	2009	2010	2011	4/12	2/12	5/11	12/03
Table 1: Changes in Consumer, Producer & Construction Prices											
CUUR0000SA0	Consumer price index (CPI-U)	2.5	4.1	0.1	2.7	1.5	3.0	-0.1	0.9	1.7	24.7
WPUSOP3000	Producer price index (PPI) for finished goods	1.1	6.2	-0.9	4.3	3.8	4.7	-0.6	0.6	0.7	34.2
PCUBCON	PPI for inputs to construction industries	4.6	4.8	2.8	0.4	5.3	5.2	-0.5	0.9	1.0	51.4
PCUBHWY	Highway and street construction	6.2	10.1	-0.6	3.9			discontinued after June 2010			
PCUBHVY	Other heavy construction	5.5	6.9	1.3	-0.1			discontinued after June 2010			
PCUBBLD	Nonresidential buildings	4.0	4.8	2.2	0.3			discontinued after June 2010			
PCUBNON	PPI for inputs to nonresidential construction						5.7	-0.6	1.0	0.6	
PCUBNCS	Commercial structures						4.9	-0.3	1.0	1.2	
PCUBNIS	Industrial structures						5.2	-0.5	0.8	1.1	
PCUBONS	Other nonresidential (highway, other heavy)						6.1	-0.7	1.0	0.5	
PCUBRSM	PPI for inputs to multi-unit residential	4.9	3.8	3.0	-0.5			discontinued after June 2010			
PCUBRES	PPI for inputs to residential (formerly single-unit)	4.2	2.5	5.0	-0.6	4.3	4.8	-0.3	0.9	1.9	42.6

Updated 6/18/12 Source: Bureau of Labor Statistics (BLS): www.bls.gov/cpi for CPI, www.bls.gov/ppi for PPIs

Compiled by Ken Simonson (simonsonk@agc.org), Chief Economist, Associated General Contractors of America, www.agc.org

Changes in Producer Price Indexes

Percentage Change in Producer Price Indexes (PPIs) for Construction Materials, Structure Types & Subcontractors, 2003-2012

BLS Series ID		12 months through December--						to May 2012 since--			
		2006	2007	2008	2009	2010	2011	4/12	2/12	5/11	12/03
Table 3: Changes in PPIs for Specific Construction Inputs											
WPU057303	#2 diesel fuel	2.3	33.9	-38.2	22.1	26.4	20.0	-3.6	-1.1	-0.2	234.0
WPU139401	Asphalt paving mixtures and blocks	27.6	1.6	34.3	-9.3	4.4	8.4	0.0	1.3	6.2	124.7
WPU136	Asphalt felts and coatings	5.0	1.4	57.8	-7.5	1.8	5.8	1.5	-0.8	-2.0	95.7
WPU1361	Prepared asphalt & tar roofing & siding products	5.2	2.3	57.5	-5.5	1.9	2.5	1.8	-0.7	-4.5	95.2
WPU133	Concrete products	8.1	3.8	4.1	-1.4	-0.4	0.9	-0.4	-0.2	1.3	37.8
WPU1331	Concrete block and brick	6.8	3.3	4.2	0.2	-1.1	1.1	-0.6	-0.3	0.7	31.3
WPU1332	Concrete pipe	2.5	10.0	4.2	-6.5	0.4	1.4	-0.1	0.1	0.6	27.8
WPU1333	Ready-mixed concrete	10.1	3.1	4.2	-1.1	-1.2	0.5	-0.7	-0.6	1.2	40.4
WPU1334	Precast concrete products	4.7	4.7	4.3	1.6	1.0	2.9	-0.3	0.8	2.2	37.3
WPU1335	Prestressed concrete products	4.9	2.2	2.8	-10.6	4.7	-3.1	2.0	1.2	1.0	25.1
WPU1342	Brick and structural clay tile	6.0	0.0	0.3	-0.9	-0.3	-2.6	-0.6	0.1	-2.9	11.9
WPU072106	Plastic construction products	-0.7	0.4	4.1	-0.7	3.3	3.6	-0.7	1.1	3.6	48.9
WPU137	Gypsum products	5.5	-22.1	7.2	-10.2	3.2	-1.6	1.2	1.5	13.6	29.6
WPU1392	Insulation materials	2.1	-3.5	0.8	-0.7	4.6	5.4	0.5	0.5	5.2	25.8
WPUSI004011	Lumber and plywood	-10.2	-0.7	-6.8	0.1	5.7	-0.7	2.2	5.3	7.0	-2.8
WPU062101	Architectural coatings	6.3	4.2	16.6	-0.5	-0.1	4.2	0.0	-0.1	11.8	69.8
WPU1017	Steel mill products	11.6	0.9	4.8	-9.8	12.5	12.2	-0.9	-1.3	-3.0	92.2
WPU101704	Hot-rolled bars, plates, & structural shapes	7.5	8.1	3.3	-13.4	18.4	13.2	-1.6	-1.5	-1.5	108.7
WPU101706	Steel pipe and tube	5.5	-1.3	28.6	-19.5	19.6	13.7	-1.4	-1.0	2.6	151.9
WPU102502	Copper and brass mill shapes	44.4	-3.0	-23.3	41.3	11.8	-9.3	-1.6	-3.8	-8.3	163.8
WPU102501	Aluminum mill shapes	12.7	-1.7	-4.0	-8.1	11.6	0.6	-1.9	-1.7	-9.0	25.0
WPU1073	Sheet metal products	6.5	0.2	7.4	-4.2	4.0	3.7	-0.2	-0.5	-1.3	36.1
WPU107405	Fabricated structural metal	3.6	5.3	11.8	-13.5	1.9	3.8	-0.3	2.8	4.8	49.2
WPU1074051	Fabricated structural metal bar joists & rebar	3.3	4.7	9.4	-10.2	-0.3	1.6	0.2	1.6	2.7	37.6
WPU107408	Architectural and ornamental metalwork	4.9	2.0	21.8	-5.8	1.6	4.5	0.2	0.1	2.0	66.7
WPU1076	Fabricated steel plate	8.6	5.7	21.8	-11.1	3.2	3.0	-0.1	-0.1	0.1	43.9
WPU1079	Prefabricated metal buildings	5.5	2.0	25.5	-14.8	8.4	9.8	0.1	0.0	-0.7	90.2

Updated 6/18/12 Source: Bureau of Labor Statistics (BLS): www.bls.gov/cpi for CPI, www.bls.gov/ppi for PPIs

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Table 4: Changes in PPIs for Basic Inputs Important to Construction											
WPU056	Crude petroleum (domestic production)	0.1	51.7	-57.7	87.0	24.8	16.2	-7.6	-6.8	-5.5	229.2
WPU05810212	Asphalt (at refinery)	34.9	-0.2	48.3	5.6	-5.1	32.1	2.1	8.3	16.3	320.3
WPU066	Plastic resins and materials	-7.8	9.7	-8.3	3.4	5.9	9.0	0.6	1.3	0.7	67.5
WPU1321	Construction sand/gravel/crushed stone	9.3	8.4	6.7	2.6	1.7	1.3	-0.3	1.1	2.9	53.7
WPU1322	Cement	10.5	4.4	-0.9	-3.7	-6.0	-1.8	-0.3	-0.3	1.1	26.7
WPU1011	Iron ore	7.5	1.3	12.1	0.5	3.8	22.9			22.8	101.7
WPU1012	Iron and steel scrap	2.9	29.4	-35.2	52.9	38.9	8.7	-1.0	-1.8	-4.8	160.8
WPU101212	Stainless and alloy steel scrap		-7.8	-39.8	97.5	29.0	-8.4	-8.0	-17.7	-21.0	
WPU102102	Copper ores	53.1	-1.7	-46.6	84.4	28.8	-15.6	-3.9	-1.9	-10.2	293.0
WPU102301	Copper base scrap	50.0	3.1	-48.2	101.5	19.2	0.6	-0.7	-0.8	-4.2	314.4

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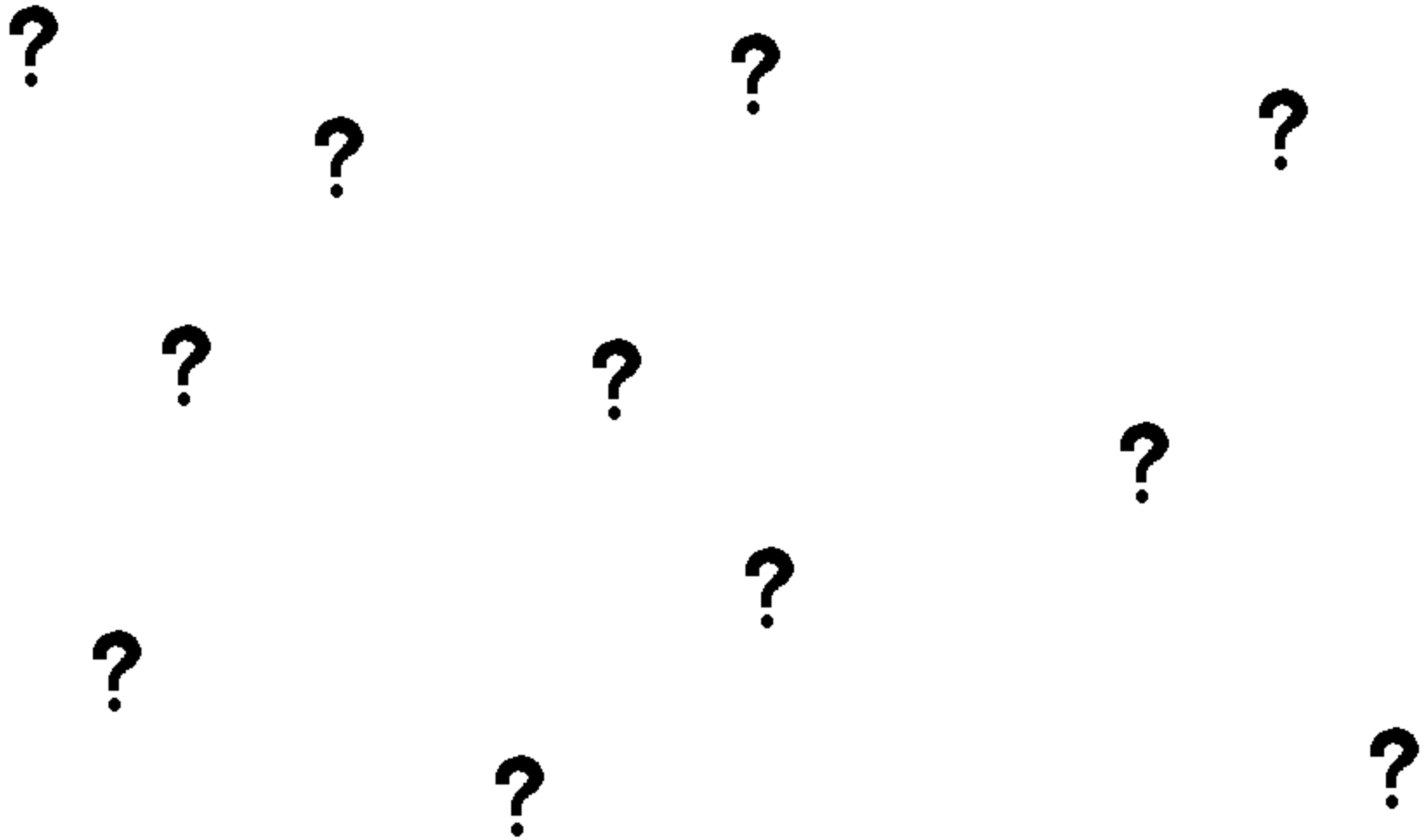
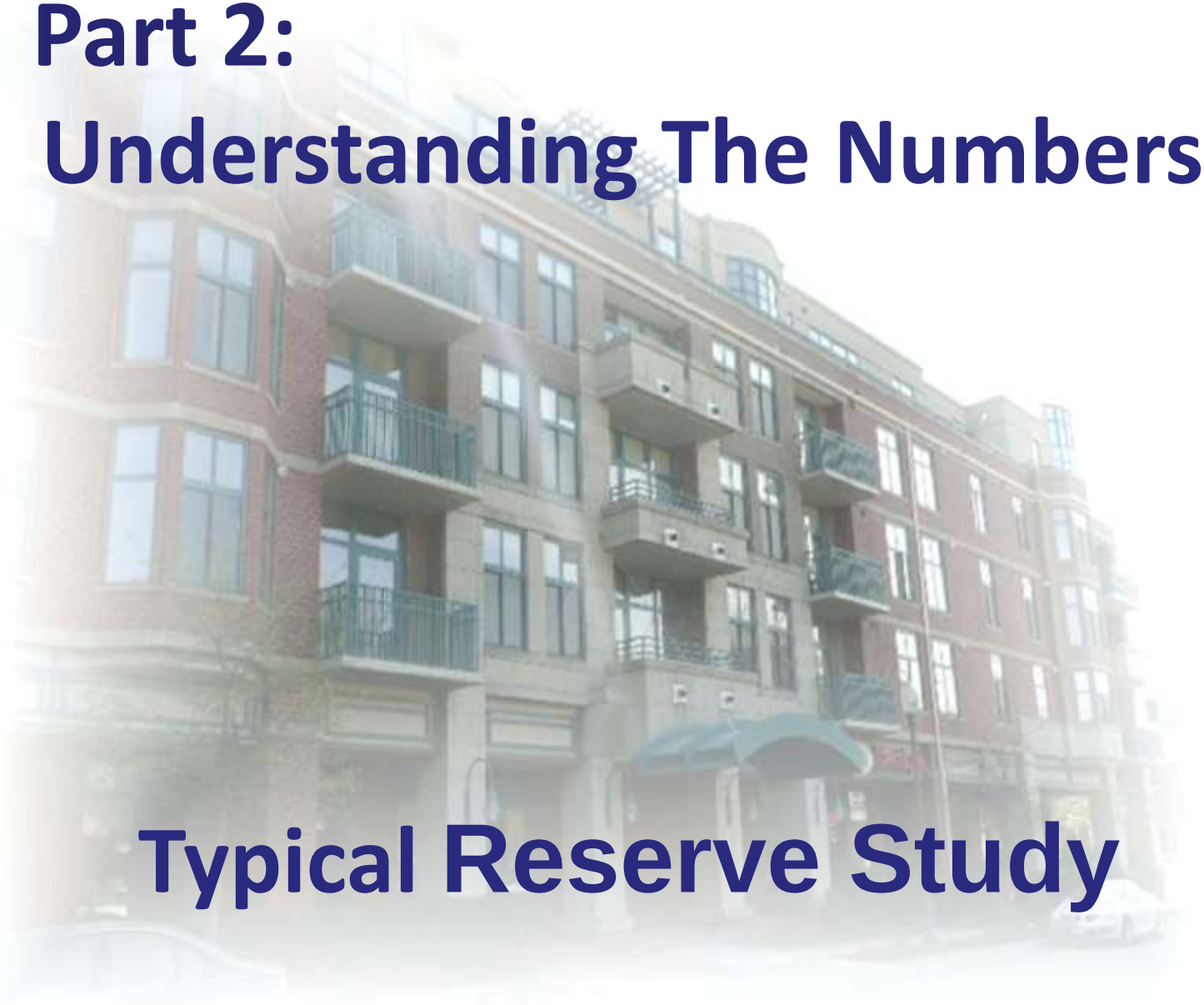
Funding Challenges Recap

1. Adequately fund reserves without triggering short-term crisis.
2. Keep property values high
3. Limit delinquencies.
4. All of above in today's housing market & economy.

Questions…



Part 2:
Understanding The Numbers



Typical Reserve Study

Sample Condominium

- Mid-rise Condominium
- Five Years Old
- 80 “Upscale” units
- Board transitioning from Declarant control.
- Concerned about staying “competitive” in tight real estate market!

Exterior elevation

Courtyard elevation

Courtyard elevation

Exterior elevation

SITE IMPROVEMENTS

Courtyard Elements. A courtyard provides outdoor seating areas. The courtyard elements include a water fountain, hard surface walkways, lighting, and outdoor furniture. An irrigation system provides water for grass and plantings.

Courtyard

Paver walkways are located throughout the courtyard and sidewalk adjacent to the building. Pavers have been set in sand or mortar. The pavers are in very good condition, and some of the pavers are long life items. However, funds should be set aside to periodically repair the base for the pavers as needed, and to replace broken pavers. Areas that collect water during rainstorms indicate localized settlement of the base and pose a potential trip hazard. We have provided funds to reset sand-set pavers every six years, to re-point grouted pavers every 18 years, and to replace the entire paver system (sand-set and grout) after 36 years of service.

The water fountain structure was replaced in 2009 as a result of faulty construction by the developer. The new fountain should last 20 years or longer. Periodic repairs and maintenance should be funded from the operating budget. We have provided funds for major repairs to the structure after 20 years of use, and a new motor pump every 10 years.

Pavers and flagstone in grout

Water fountain; recently replaced

SITE COMPONENT

PROJECTED REPLACEMENTS AND EXCLUDED ITEMS

ITEM #	ITEM DESCRIPTION	UNIT	NUMBER OF UNITS	UNIT REPLACEMENT COST ($)	NORMAL ECONOMIC LIFE (YRS)	REMAINING ECONOMIC LIFE (YRS)	REPLACEMENT COST ($)
1	Brick step, replace	ft	470	$150.00	25	18	$70,500
2	Concrete planters, 2' x 10'	ea	13	$750.00	30	23	$9,750
3	Reset paver, sand set	sf	9,555	$3.00	18	14	$28,665
4	Repoint paver, grouted	sf	2,810	$5.00	24	17	$14,050
5	Paver sand set, replace	sf	9,555	$12.00	36	29	$114,660
6	Paver grouted, replace	sf	330	$13.00	36	29	$4,290
7	Flagstone paver, replace	sf	1,710	$20.00	36	29	$34,200
8	Paver landscape border, mortar, replace	ft	770	$21.00	36	29	$16,170
9	Aluminum handrail, stairs	ft	140	$26.00	45	38	$3,640
10	Aluminum guardrail, stairs	ft	145	$65.00	45	38	$9,425
11	Aluminum guardrail, parking	ft	240	$45.00	45	38	$10,800
	Metal gates, courtyard	ea	2				EXCLUDED
	Light poles, parking	ea	2				EXCLUDED
	Landscape lights, perimeter courtyard	ea	12				EXCLUDED
	Landscape floodlights, courtyard	ea	15				EXCLUDED
	Fountain motor	ea	1				EXCLUDED
	Fountain structure, repairs	ls	1				EXCLUDED
12	Wood benches, courtyard	ea	6	$1,000.00	15	8	$6,000
13	Cedar furniture, courtyard	ls	1	$13,700.00	20	13	$13,700
				SITE COMPONENT - Replacement Costs - Subtotal			$335,850

GARAGE AND PARKING

PROJECTED REPLACEMENTS AND EXCLUDED ITEMS

ITEM #	ITEM DESCRIPTION	UNIT	NUMBER OF UNITS	UNIT REPLACEMENT COST ($)	NORMAL ECONOMIC LIFE (YRS)	REMAINING ECONOMIC LIFE (YRS)	REPLACEMENT COST ($)
14	Concrete surface parking-exposed, 10%	sf	1,027	$9.80	60	6	$10,065
15	Concrete surface parking-exposed, 10%	sf	1,027	$9.80	60	12	$10,065
16	Concrete surface parking-exposed, 10%	sf	1,027	$9.80	60	18	$10,065
17	Concrete surface parking-exposed, 10%	sf	1,027	$9.80	60	24	$10,065
18	Concrete surface parking-exposed, 10%	sf	1,027	$9.80	60	30	$10,065
19	Concrete surface parking-exposed, 10%	sf	1,027	$9.80	60	36	$10,065
	Concrete curb	ft	60				EXCLUDED
20	Concrete parking repairs, 5%	sf	1,846	$15.00	60	10	$27,690
21	Concrete parking repairs, 5%	sf	1,846	$15.00	60	20	$27,690
22	Concrete parking repairs, 5%	sf	1,846	$15.00	60	30	$27,690
23	Concrete waterproofing repairs, allow	ls	1	$95,000.00	25	none	$95,000
24	Slab heating system, electric	coil	4	$13,500.00	20	13	$54,000
25	Slab heating system, electric	coil	1	$13,500.00	20	20	$13,500
26	Metal halide lights, garage	ea	76	$225.00	25	18	$17,100
27	Overhead garage doors	ea	2	$9,500.00	20	13	$19,000
28	Garage fans, 12k-15k cfm	ea	6	$1,350.00	20	13	$8,100
	Storage exhaust fan, 4700 cfm	ea	1				EXCLUDED
29	CO detector system	ls	1	$3,500.00	20	13	$3,500
				GARAGE AND PARKING - Replacement Costs - Subtotal			$353,658

BUILDING INTERIOR

PROJECTED REPLACEMENTS AND EXCLUDED ITEMS

ITEM #	ITEM DESCRIPTION	UNIT	NUMBER OF UNITS	UNIT REPLACEMENT COST ($)	NORMAL ECONOMIC LIFE (YRS)	REMAINING ECONOMIC LIFE (YRS)	REPLACEMENT COST ($)
48	Marble flooring, lobbies and restrooms	sf	1,850	$49.00	42	35	$90,650
49	Marble flooring, refinish	sf	1,850	$2.50	3	1	$4,625
	Carpet, lobby	sf	280				EXCLUDED
50	Wall covering, lobby	sf	3,910	$5.00	15	9	$19,550
51	Mailboxes, lobby	ea	82	$110.00	40	33	$9,020
52	Furnishings, lobby, 50%	ls	1	$5,250.00	20	13	$5,250
53	Management office furniture	ls	1	$3,750.00	20	14	$3,750
54	Management office equipment	ea	2	$2,500.00	5	none	$5,000
55	Millwork, work area first floor	ls	1	$5,500.00	30	23	$5,500
	Reception desk counter, p.lam	ls	1				EXCLUDED
56	Window treatments, first floor	ea	11	$1,500.00	15	8	$16,500
	Rest room ceramic wall tile	sf	90				EXCLUDED
	Rest room wallcovering	sf	630				EXCLUDED
57	Rest room fixtures	ls	1	$9,000.00	30	24	$9,000
58	Corridor carpet	sf	15,400	$5.00	8	2	$77,000
59	Wall mounted lights, corridors	ea	108	$110.00	24	18	$11,880
60	Ceiling mounted lights, corridors	ea	36	$175.00	24	18	$6,300
61	Exit lights	ea	30	$145.00	24	18	$4,350
	Trash chute doors	ea	4				EXCLUDED
				BUILDING INTERIOR - Replacement Costs - Subtotal			$268,375

PROJECTED REPLACEMENTS - YEARS 1 TO 6

Item	2011	$
23	Concrete waterproofing repa	$95,000
54	Management office equipme	$5,000
66	Furniture, Club Room, 25%	$5,400
70	Fitness room, treadmills	$13,000
	Total Scheduled Replacements	$118,400

Item	2012	$
49	Marble flooring, refinish	$4,625
	Total Scheduled Replacements	$4,625

Item	2013	$
58	Corridor carpet	$77,000
85	Security system upgrade, 7	$6,250
	Total Scheduled Replacements	$83,250

Item	2014	$
43	EIFS/stucco coating	$50,575
44	EIFS repairs (10%)	$14,450
65	Carpet, Club Room	$3,600
	Total Scheduled Replacements	$68,625

Item	2015	$
36	Concrete balcony coating	$27,375
49	Marble flooring, refinish	$4,625
	Total Scheduled Replacements	$32,000

Item	2016	$
54	Management office equipme	$5,000
66	Furniture, Club Room, 25%	$5,400
88	Corridor HVAC, 2.5-ton con	$15,625
90	Fitness/corridor HVAC, 3-to	$15,000
92	Club room/library HVAC, 5-t	$6,250
94	Lobby HVAC, 5-ton condens	$6,250
	Total Scheduled Replacements	$53,525

PROJECTED REPLACEMENTS - YEARS 7 TO 12

Item	2017	$
14	Concrete surface parking-ex	$10,065
70	Fitness room, treadmills	$13,000
	Total Scheduled Replacements	$23,065

Item	2018	$
49	Marble flooring, refinish	$4,625
	Total Scheduled Replacements	$4,625

Item	2019	$
12	Wood benches, courtyard	$6,000
46	Exterior facade caulking	$40,000
56	Window treatments, first floc	$16,500
74	Fitness room, rubber flooring	$4,640
96	Duplex sump pump system	$7,500
	Total Scheduled Replacements	$74,640

Item	2020	$
50	Wall covering, lobby	$19,550
71	Fitness room, Total Body Tr	$6,500
72	Fitness room, bicycles	$5,000
75	Elevator cab & door, passen	$15,800
	Total Scheduled Replacements	$46,850

Item	2021	$
20	Concrete parking repairs, 5%	$27,690
49	Marble flooring, refinish	$4,625
54	Management office equipme	$5,000
58	Corridor carpet	$77,000
66	Furniture, Club Room, 25%	$5,400
85	Security system upgrade, 7	$6,250
	Total Scheduled Replacements	$125,965

Item	2022	$
	No Scheduled Replacements	

PROJECTED REPLACEMENTS - YEARS 13 TO 18

Item	2023	$
15	Concrete surface parking-ex	$10,065
63	Furniture, Library, 25%	$6,250
70	Fitness room, treadmills	$13,000
79	Trash compactor	$13,500
95	Elevator room HVAC unit, M	$4,200
	Total Scheduled Replacements	$47,015

Item	2024	$
13	Cedar furniture, courtyard	$13,700
24	Slab heating system, electri	$54,000
27	Overhead garage doors	$19,000
28	Garage fans, 12k-15k cfm	$8,100
29	CO detector system	$3,500
43	EIFS/stucco coating	$50,575
44	EIFS repairs (10%)	$14,450
49	Marble flooring, refinish	$4,625
52	Furnishings, lobby, 50%	$5,250
65	Carpet, Club Room	$3,600
	Total Scheduled Replacements	$176,800

Item	2025	$
3	Reset paver, sand set	$28,665
36	Concrete balcony coating	$27,375
37	Concrete balcony repairs, 1(	$32,850
53	Management office furniture	$3,750
73	Fitness room, nautilus statio	$4,000
76	Elevator, hydraulic psngr, cc	$59,000
	Total Scheduled Replacements	$155,640

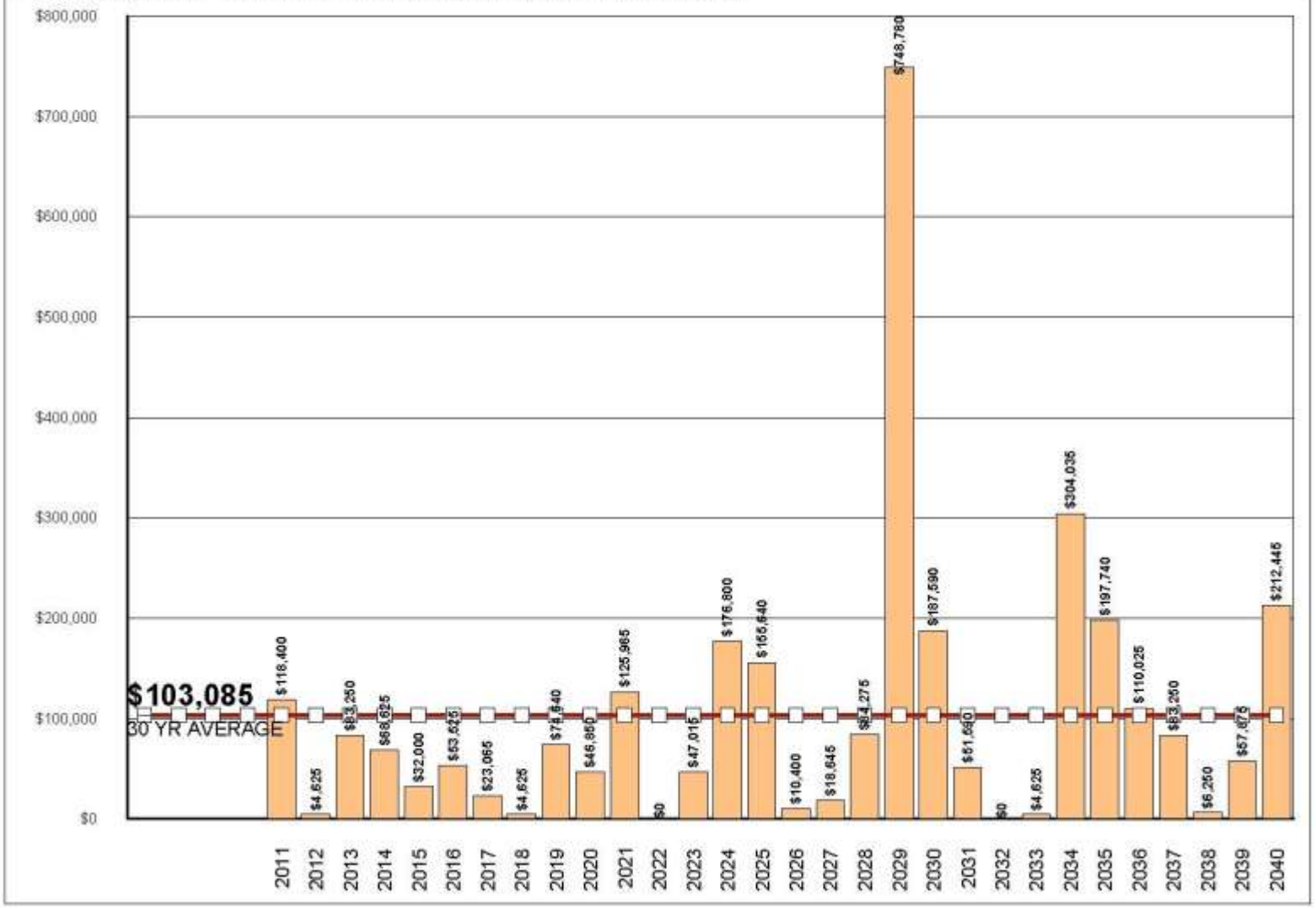
Item	2026	$
54	Management office equipme	$5,000
66	Furniture, Club Room, 25%	$5,400
	Total Scheduled Replacements	$10,400

Item	2027	$
47	Exterior lights, arched decor	$4,500
49	Marble flooring, refinish	$4,625
62	Wood flooring, replace, Libr	$3,640
64	Wood flooring, replace, Clut	$5,880
	Total Scheduled Replacements	$18,645

Item	2028	$
4	Repoint paver, grouted	$14,050
87	Corridor HVAC, 2.5-ton AHL	$10,500
88	Corridor HVAC, 2.5-ton con	$15,625
89	Fitness/corridor HVAC, 3-to	$9,000
90	Fitness/corridor HVAC, 3-to	$15,000
91	Club room/library HVAC, 5-t	$3,800
92	Club room/library HVAC, 5-t	$6,250
93	Lobby HVAC, 5-ton AHU	$3,800
94	Lobby HVAC, 5-ton condens	$6,250
	Total Scheduled Replacements	$84,275

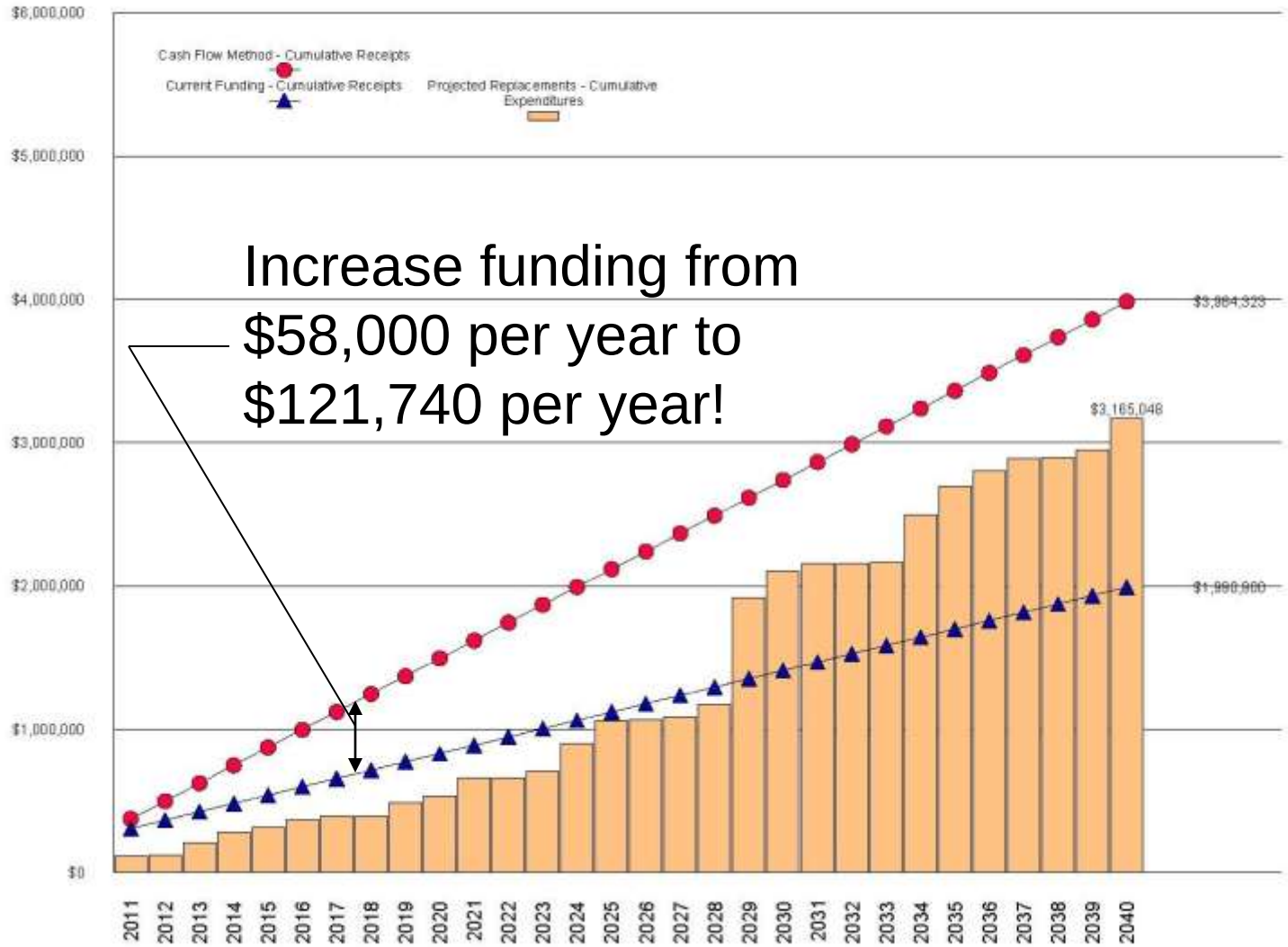
Graph #1. Annual Expenditures for Projected Replacements

This bar graph summarizes annual expenditures for the $3,092,548 of Projected Replacements identified in the Replacement Reserve Inventory over the 30-year Study Period. The red line shows the average annual expenditure of $103,085.



Graph #2. Comparison of Cumulative Replacement Reserve Funding and Expenditures

The line graph shows Replacement Reserves - Cumulative Receipts over the 30-year Study Period by the Cash Flow Method (red circles) and the Current Funding Plan as reported by the Association (blue triangles). The bar graph shows the Cumulative Expenditures necessary to fund the Project Replacements listed in the Replacement Reserve Inventory (Section B) and summarized in Graph #1.



EXECUTIVE SUMMARY

The Replacement Reserve Inventory identifies 97 Projected Replacements for funding from Replacement Reserves, with an estimated one-time replacement cost of $3,125,108.

The Replacement Reserve Analysis calculates recommended funding of Replacement Reserves by the two generally accepted methods, the Cash Flow Method and the Component Method. The Analysis also evaluates current funding of Replacement Reserves, as reported by the Association. The calculations and evaluation are summarized below:

$121,740 **CASH FLOW METHOD MINIMUM ANNUAL FUNDING OF REPLACEMENT RESERVES IN THE STUDY YEAR, 2011.**

$125.25 Per unit (average), minimum monthly funding of Replacement Reserves

The Cash Flow Method (CFM) calculates Minimum Annual Funding of Replacement Reserves that will fund Projected Replacements identified in the Replacement Reserve Inventory from a common pool of Replacement Reserves and prevent Replacement Reserves from dropping below a Minimum Recommended Balance.

CFM - Minimum Annual Funding remains the same between peaks in cumulative expenditures called Peak Years.

The first Peak Year occurs in 2050 which is outside of the 30-year Study Period. The Cash Flow Method - Minimum Annual Funding of Replacement Reserves remains constant at $121,740 throughout the entire 30-year Study Period.

$250,318 **COMPONENT METHOD RECOMMENDED ANNUAL FUNDING OF REPLACEMENT RESERVES IN THE STUDY YEAR, 2011.**

$257.53 Per unit (average), recommended monthly funding of Replacement Reserves

The Component Method is a time tested and very conservative funding model developed by HUD in the early 1980's.

The Component Method treats each projected replacement in the Replacement Reserve Inventory as a separate account. Deposits are made to each individual account, where funds are held for exclusive use by that item.

Based on this funding model, the Association has a Current Funding Objective of $812,859.

The Association reports having $250,900 on deposit, which is 30.9% funded.

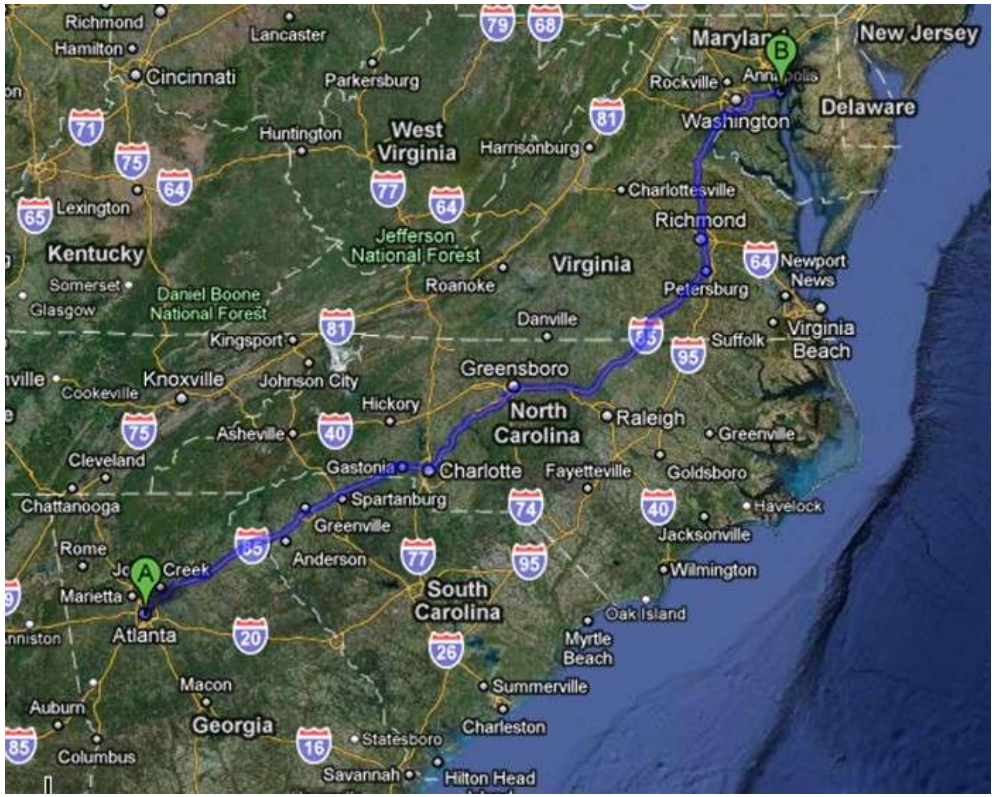
$58,000 **CURRENT ANNUAL FUNDING OF REPLACEMENT RESERVES (as reported by the Association).**

$59.67 Per unit (average), reported current monthly funding of Replacement Reserves

The evaluation of Current Funding, as reported by the Association, has calculated that if the Association continues to fund Replacement Reserves at the current level, there will NOT be adequate funds for Projected Replacements in 12 years of the 30-year Study Period, and a maximum shortfall of $-1,101,648 occurs in 2040.

Part 3: Strategic Funding Plans:

Developing A Reserve Funding Roadmap



Once the Reserve Study is Completed :

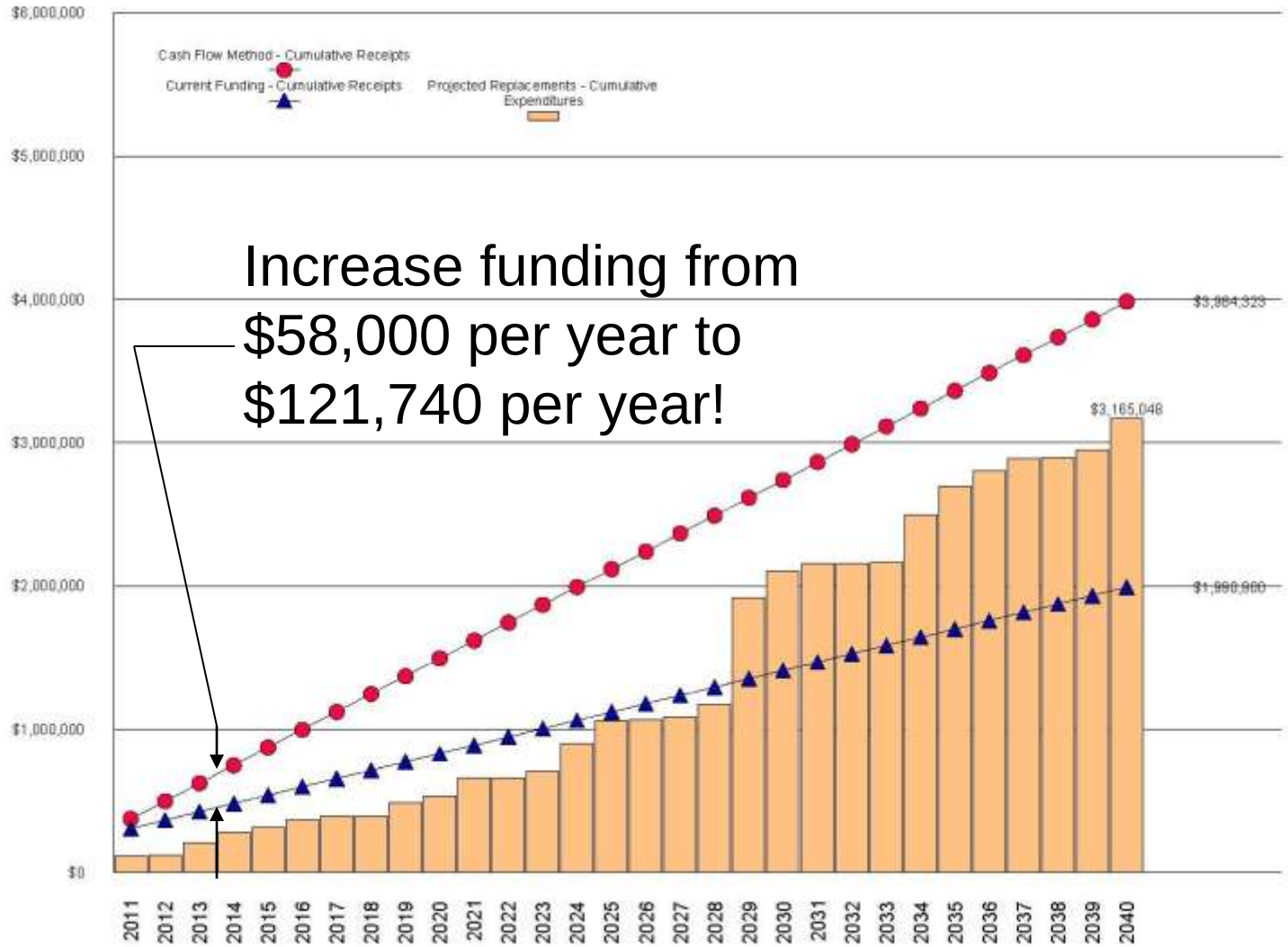
- What is your next step?
- What tools do you have available?
- How do you get from where you are to where it is you should be?

The Next Step…

- Look at Cash Flow Situation in Study
- Use next 3 to 5 years to establish funding plan for the next 30 years.
- Develop a Strategic Funding Solution that:
  - Adequately Funds Reserves
    - Near-Term
    - Long Term
  - Works for the association as a whole.

Graph #2. Comparison of Cumulative Replacement Reserve Funding and Expenditures

The line graph shows Replacement Reserves - Cumulative Receipts over the 30-year Study Period by the Cash Flow Method (red circles) and the Current Funding Plan as reported by the Association (blue triangles). The bar graph shows the Cumulative Expenditures necessary to fund the Project Replacements listed in the Replacement Reserve Inventory (Section B) and summarized in Graph #1.



What Tools Are at Your Disposal?

- **Increase Normal Assessments**
  - Ramp Up over 3 to 5 years if possible
- **Institute a Special Assessment**

  (Caution!)
- **Secure a Commercial Bank Loan**

Special Issues: Delinquencies

- **FHA backed mortgages – NEW GUIDELINES**
  - No more “spot approvals” for condos
  - Each condo community must pre-qualify.
  - Delinquencies over 30 days capped at 15%

- **Capital Improvement Loans**
  - Loans collateralize revenue stream
  - Delinquencies capped at 8% - 10%

Increase Normal Assessments

PROS:

- No Interest

CONS:

- Will increase monthly assessments.
- A vote may be required to pass increase.
- There may be an assessment increase cap.
- It may take time to build up Reserves.
- May hurt property values.
- May trigger more delinquencies and foreclosures!

Special Assessment

PROS:

- No Interest
- Can be done quickly

CONS:

- May be very unpopular.
- A vote may be required to pass increase.
- May hurt property values.
- May trigger more delinquencies and foreclosures!

Commercial Bank Loan

PROS:

- Needed repairs/improvements are completed quickly.
- Everyone benefits from improvements at same time.
- Reduced financial impact on homeowners.
- Interest Rate may be lower than Inflation Rate.

CONS:

- May increase monthly assessments
- Interest costs incurred may be high
- Association may not qualify!

Strategic Funding Solutions

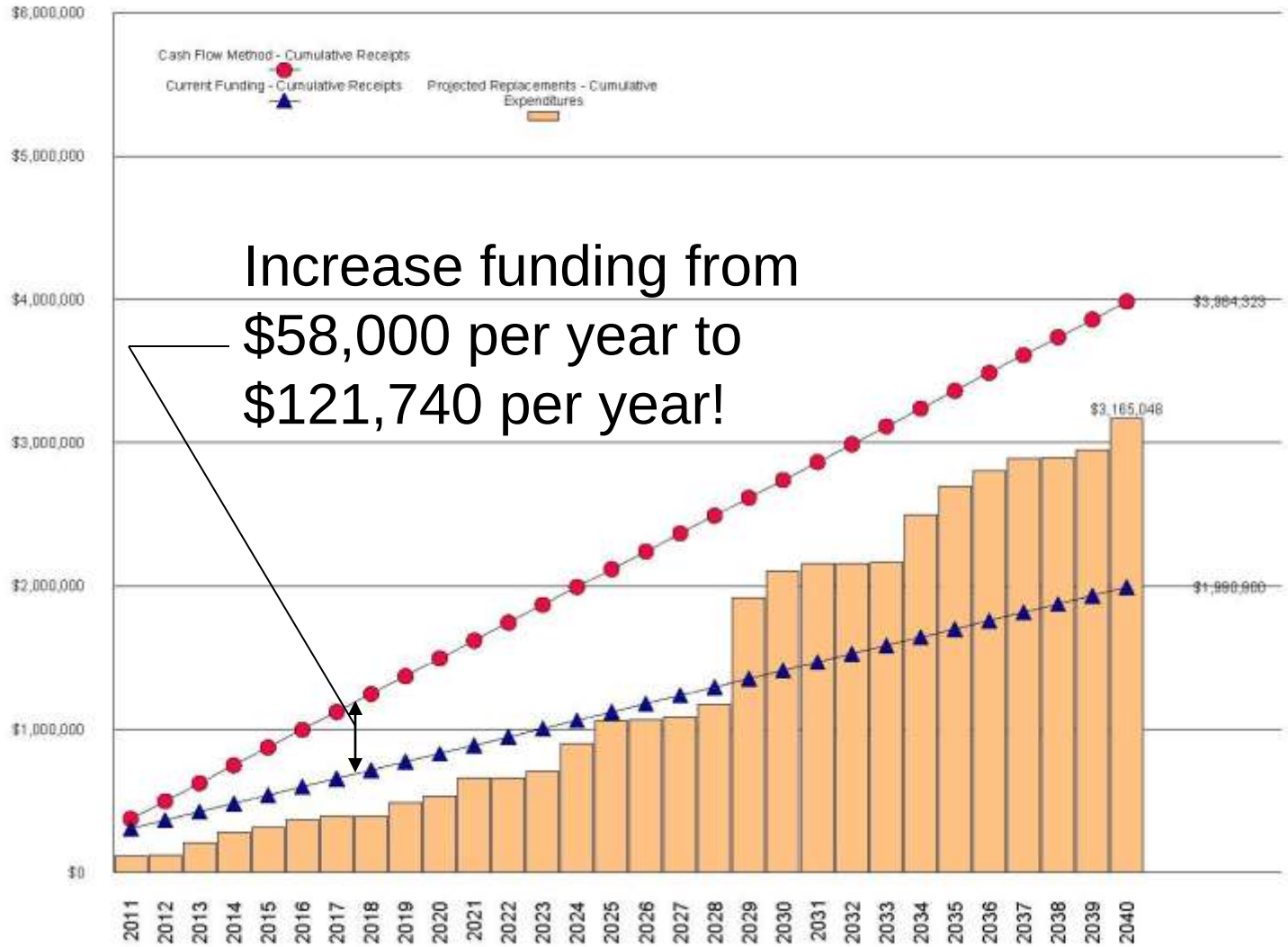
- Understand the intricacies of each funding tool so as to avoid inadvertent consequences and pitfalls.
- Use full range of funding tools in order to minimize the adverse financial impact of large increases to reserve funding levels.
- Empower community board to select and implement “best tools” for their association’s unique needs and abilities.
- “Roadmap” to arrive at funding goals.

Example: **Ramp Up Assessments**
Mid-Rise Condominium

- Mid-rise Condominium
- Five Years Old
- 80 units
- Saturated condominium sales market
- Concerned about “competitive” assessments

Graph #2. Comparison of Cumulative Replacement Reserve Funding and Expenditures

The line graph shows Replacement Reserves - Cumulative Receipts over the 30-year Study Period by the Cash Flow Method (red circles) and the Current Funding Plan as reported by the Association (blue triangles). The bar graph shows the Cumulative Expenditures necessary to fund the Project Replacements listed in the Replacement Reserve Inventory (Section B) and summarized in Graph #1.



EXECUTIVE SUMMARY

The V2 Replacement Reserve Inventory identifies 91 Projected Replacements for funding from Replacement Reserves, with an estimated one-time replacement cost of $2,886,793.

The Replacement Reserve Analysis calculates recommended funding of Replacement Reserves by the Cash Flow Method. The Analysis also evaluates current funding of Replacement Reserves, as reported by the Association, as well as providing a Proposed Funding Plan. The calculations and evaluation are summarized below:

$109,508 **CASH FLOW METHOD: ANNUAL FUNDING OF REPLACEMENT RESERVES IN THE STUDY YEAR, 2011.**

$112.66 Per unit (average), minimum monthly funding of Replacement Reserves

The Cash Flow Method (CFM) calculates Annual Funding of Replacement Reserves that will fund Projected Replacements identified in the Replacement Reserve Inventory from a common pool of Replacement Reserves and prevent Replacement Reserves from dropping below a Minimum Recommended Balance.

The Cash Flow Method - Annual Funding of Replacement Reserves remains constant at $109,508 throughout the 30-year Study Period. The first Peak Year occurs in 2045. The Cash Flow Method requires an 88.8% increase in Reserve Funding over the Current Annual Funding level. The Proposed Funding Plan shown below has been developed to mitigate the issues presented by a large, single increase to the Reserve Funding.

$65,000 **PROPOSED ANNUAL FUNDING OF REPLACEMENT RESERVES IN THE STUDY YEAR, 2011 Increases each year until 2015**

See Page A5 for the Proposed Funding Plan Annual Data

The Propsed Funding Plan increases the Annual Funding as follows: $58,000 in 2010, $65,000 in 2011 $75,000 in 2012, $85,000 in 2013, $95,000 in 2014, and $100,000 from 2015 through the end of the Study in 2040.

It is important to note that these numbers need to be adjusted each year for inflation (Use PPI from BLS.Gov)

$58,000 **CURRENT ANNUAL FUNDING OF REPLACEMENT RESERVES (as reported by the Association).**

See Table 2 Page A7 for funding details.

The evaluation of Current Funding, as reported by the Association, has calculated that if the Association continues to fund Replacement Reserves at the current level, there will NOT be adequate funds for Projected Replacements in 12 years of the 30-year Study Period, and a maximum shortfall of $-979,283 occurs in 2040.

Pages A2 and A3 explain the Study Year, Study Period, Adjustments (interest & inflation), Beginning Balance, and Projected Replacements. Pages A4 to A9 explain in more detail the calculations associated with the Cash Flow Method, Component Method, and Current Funding.

Proposed Funding Plan

Increase Normal Assessments over 5 years:

2010 - Increase from $58,000 to $65,000

2011 - Increase from $65,000 to $75,000

2012 - Increase from $75,000 to $85,000

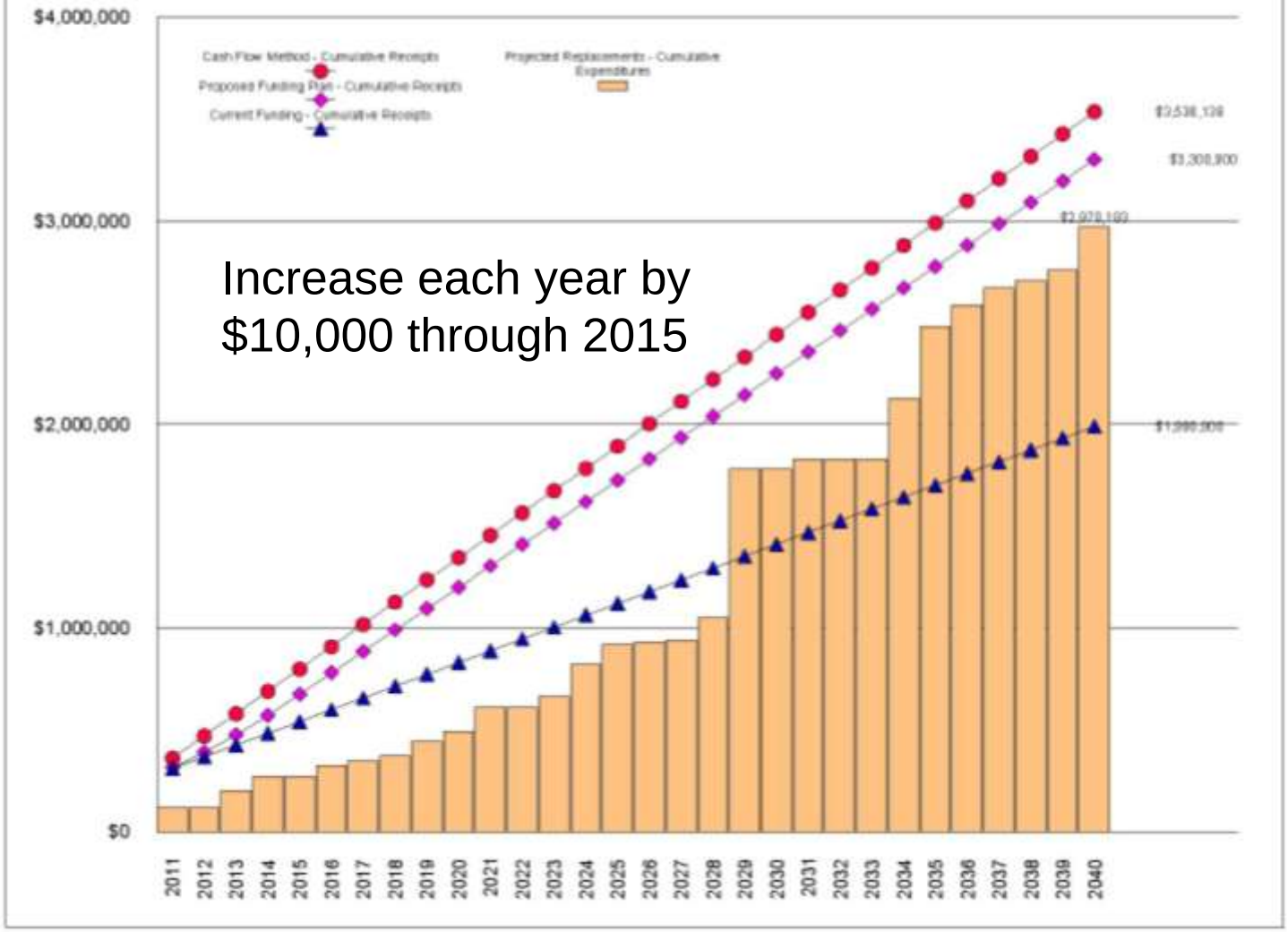
2013 - Increase from $85,000 to $95,000

2014 - Increase from $95,000 to $105,000

2015 - Update Reserve Study

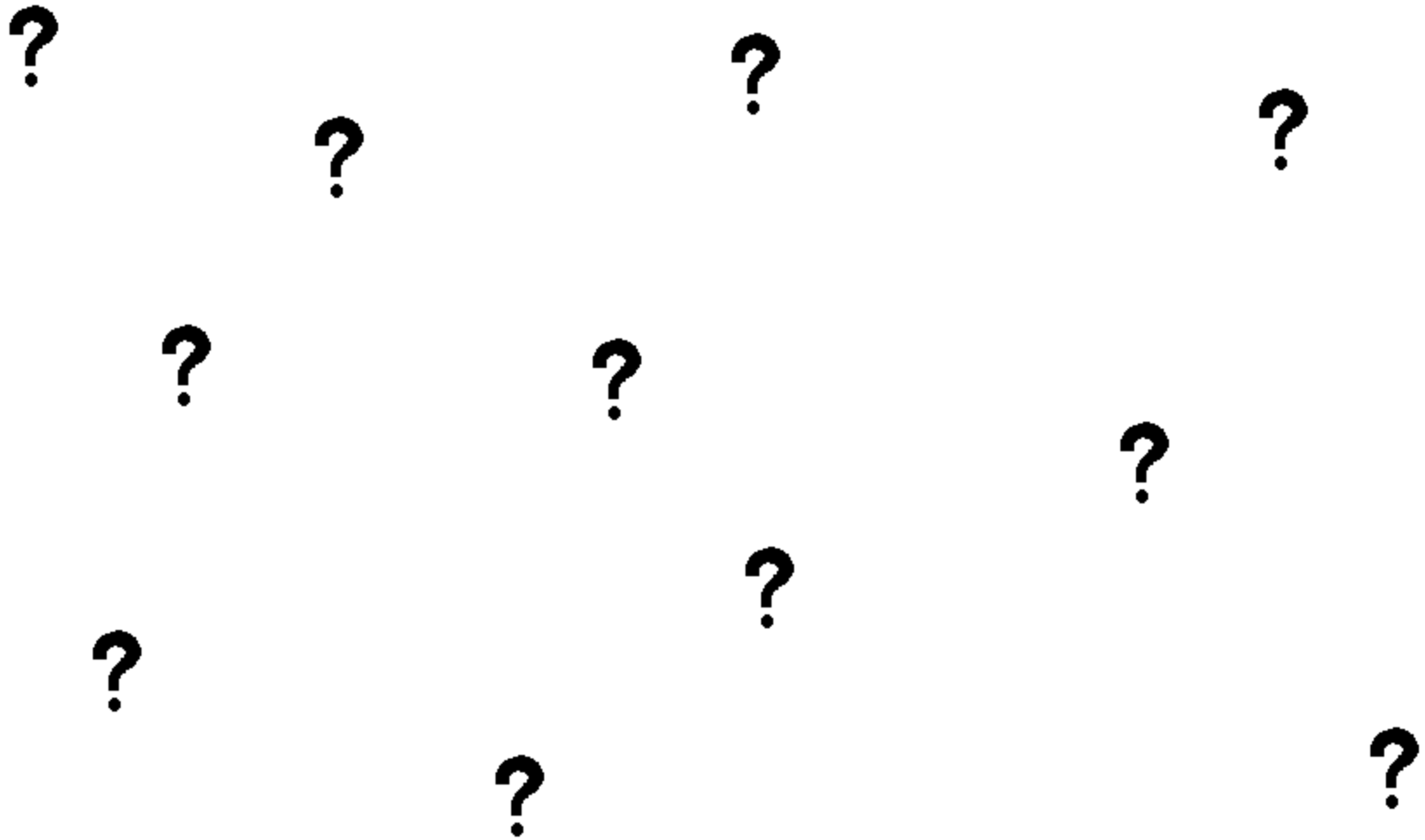
Graph #2. Comparison of Cumulative Replacement Reserve Funding and Expenditures

The line graph shows Replacement Reserves - Cumulative Receipts over the 30-year Study Period by the Cash Flow Method (red circles), Proposed Funding Plan (purple diamonds), and the Current Funding Level as reported by the Association (blue triangles). The bar graph shows the Cumulative Expenditures necessary to fund the Project Replacements listed in the Replacement Reserve Inventory (Section B) and summarized in Graph #1.



Increase each year by $10,000 through 2015

Questions…



Thank you for your time!

Presentation is available as a PDF

Please feel free to download and share with your Managers and Board/Committee members!

www.MDAreserves.com/resources