

Definition of Terms Used

A reserve study contains a number of industry-related terms and phrases. To help you better understand the reserve study process and reports, we've provided definitions for the most commonly used terms.

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, 5) as required by local codes.

Component Assessment and Valuation - The task of estimating useful life, remaining useful life, and repair or replacement costs for the reserve components. This task is accomplished either with or without on-site visual observations, based on the level of service selected by the client.

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, review of established association precedents and discussion with appropriate association representative(s) of the association or cooperative.

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.

Field Inspection - A site visit which includes a visual inspection of all components. In cases where plans of the property are unavailable, it would also include the quantity survey.

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 and 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.

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

or

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

Fund Status - The status of the reserve fund as compared to an 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.

Full 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:

- Sufficient Funds When Required
- Stable Contribution Rate over the Years
- Evenly Distributed Contributions over the Years
- 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. Based upon information provided and not audited.

Reserve Study 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.

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 not to have rendered the regular and effective supervision required herein:

1. 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;
2. The failure to personally inspect or review the work of subordinates where necessary and appropriate;
3. The rendering of a limited, cursory or perfunctory review of plans or projects in lieu of an appropriate detailed review;
4. 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.