Reserve Fund Planning
Best-practice Report
Component Classification

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How about Having Developments, Their Components and Stakeholders on the Same Page?

This Article Answers the Following Questions:

- Why is it important to classify components?
- What are a component's types?

Knowing your Components

Stakeholders and Developments: When it comes to condos and strata lots in multi-owner single land-title developments, stakeholders – owners, buyers, agents, appraisers, lenders, property managers, developers, architects, trades, engineers, reserve fund planners, accountants etc. – have their particular understanding of what are a development's components.

Reviewing how reserve fund planners classify components for remediation and renewal projects is an effective way to bring stakeholders to 'see' the same things. By using reserve fund planning lenses we can demonstrate why it is important to have all stakeholders 'look' at common assets in a standardised way.

Present Classification of Components: Canadian provincial legislations do not currently provide exacting direction on how to classify common asset components. The REIC does promote the Construction Specification Institute (CSI)'s functional construction assembly classification – the Uniformat II component system – that details over 550 component elements, and counting.

Functional Component Types

Types of Components: Not all components are created equal. From a functional perspective, there are four types of components. Some are typical – roof shingles requiring a 'full replacement'. Others require 'updates' – the electrical distribution system rarely has all of its wiring replaced, but breakers, switches, wall plates will be replaced.

Other components are altered before their life reaches their expected end – a code change may trigger the partial replacement of some of the elements of a component – an 'upgrade' to the fire-safety system comes to mind.

Focus on Allowances: And finally, an 'allowance' can be made for a partial replacement – major repairs to concrete foundations cannot be ignored. Establishing when a major concrete repair will occur is less important than knowing that it is expected and financially prudent to plan for.

However, what is the time-horizon for an allowance? While full replacements, updates and upgrades have defined lives and are construction-failure focused items, an allowance tilts the focus towards market forces.

New buildings could be built on the existing foundations, as these typically last longer than the development. But most legislations set the life of a development at its termination date. It is thus common-sense to have an allowance last as long as the life of the development.

Isn't an allowance the same as a contingency? The latter is typically a general percentage amount and not a component. A component allowance is part of long-term financial planning – this is crucial as it has legal implications and affects the cost of renewal projects.

IMPACT ON RISK-MANAGEMENT:

In British Columbia for example, if the need for a component expenditure arises and the work is not defined as a component in a reserve study | depreciation report, then a 75 percent – rather than a 50 percent vote – is required at a General Meeting (GM). A component inventory has serious financial and management consequences.

Full Disclosure: Disclosing uncertainties helps to qualify and manage risk. Is it not better to divulge assumptions so that boards | councils can plan for them and not come back and ask why a component or part of one wasn't properly detailed?

With all stakeholders having the same historical information on developments and their components, it is easier to tackle maintenance, replacements and major repairs.

Understanding how to 'look' at components ensures that developments have the monies they need over their economic life, reduces complexity and limits legal action.

When it comes to developments and their components, all stakeholders benefit from being on the same page.

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