



Depreciation Reports, Contingency Reserve Funds and Special Levies

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Depreciation Reports

On December 14, 2011, new requirements came into effect for Depreciation Reports.

A depreciation report helps strata corporations plan for the repair, maintenance and replacement of common property, limited common property and common assets. The report must contain:

- A physical inventory of the common property including building systems.
- Anticipated maintenance, repair and replacement costs for common expenses projected over 30 years.
- A financial forecasting section that contains at least three cash flow funding models for the contingency reserve fund (CRF).

Depreciation reports provide useful information to strata lot owners and can help prospective purchasers, mortgage providers and insurance companies. Depreciation reports are also known as reserve fund studies in other jurisdictions.

Strata corporations are required to obtain depreciation reports by December 14, 2013 (two years from the effective date of the new requirement) or hold a $\frac{3}{4}$ vote to waive the requirement.

Strata corporations that do not need depreciation reports:

- a) Strata corporations with four or fewer units
- b) Strata corporations that exempt themselves by passing an annual $\frac{3}{4}$ vote. If a strata corporation fails to pass another waiver the following year, they would be required to obtain a report within 18 months of the previously passed waiver. Thus, if the votes were being held at the annual general meeting, there would still be six months left to arrange for a depreciation report to be performed.

Updates

Depreciation reports must be renewed every three years. If a strata corporation has already obtained a depreciation report, which meets the new requirements, it will have three years to obtain another report.

How much do depreciation reports cost to prepare?

The cost would vary depending on the size of the strata corporation, the complexity of the development and who is hired to do the report – there are too many variables to estimate the costs with any certainty. The initial depreciation report usually costs more than subsequent updates. The cost, relative to the assets, is low and provides real value for owners and purchasers.

What must be included in a depreciation report?

- A physical component inventory and evaluation of applicable components as outlined in the Strata Property Regulation 6.2. Examples of the components that are to be reviewed for the depreciation report. (This is not a complete list and not all strata corporations will have all the components listed):
 - the building structure;
 - the building exterior including roofs, decks, doors and windows;
 - building systems such as electrical, plumbing, heating, fire, protection and security;
 - common amenities and facilities. (For example, a pool, exercise room, guest house);
 - parking facilities and roadways;
 - utilities, including water and sewage;
 - landscaping, including paths, sidewalks, fencing and irrigation;
 - interior finishes including floor covering and furnishings;
 - green building components; and
 - balconies and patios.
- A financial forecasting section that includes:
 - a projection of the anticipated maintenance, repair and replacement costs for the next 30 years and the factors and assumptions used, including interest rates and inflation rates;
 - at least 3 cash-flow funding models over 30 years;
 - the current balance of the contingency reserve fund (CRF) and how it is funded.
- A summary of the repair and maintenance work to be done (other than on an annual basis) over the next 30 years;
- The date of the report, the qualifications of the author(s) of the report, their relationship, if any, to the strata corporation and information on any errors and omissions insurance.
- Any other appropriate information or analysis.
- The report must also identify those parts of the common property and limited common property, if any, that individual owners are responsible to repair and maintain.

How to prepare for a depreciation report

The person, or team, preparing the depreciation report must conduct an on-site visual inspection of the strata corporation's building(s) and components; review both the common and limited common property; as well as any part of the strata lots that the strata corporation, by bylaw, is responsible to repair and maintain.

Strata corporations may want to consider the following steps:

Prepare Basic Information: Initially you will need to provide information on total units, year built, floors, and general building systems information – such as elevators, etc.

Do some research: Talk to other strata corporations similar to yours, review best practices and materials from strata owner associations and websites. (*See Resources Section at the end of this guide*). Write down all the questions you want to ask prospective firms or individuals. You can also check if the depreciation report will be available electronically and thus easier to update.

Gather relevant documents: You will need to provide documents that include those related to repair, maintenance, inspection, agreements with owners about repairs to strata lots, common property or limited common property, as well as financial records and the strata's bylaws.

Who is qualified to prepare the depreciation report?

The Strata Property Regulation does not specify who must prepare a depreciation report. The knowledge and expertise required to prepare a depreciation report for a six-plex may be considerably different than the qualifications and expertise required to prepare a depreciation report for a highrise residential tower with its own power generating plant, airspace parcel and underground parkade.

The person (or team) preparing the depreciation report must have the expertise to:

- understand the scope and complexity of the common property, limited common property, and common assets including individual components and their condition and life expectancy;
- provide the financial forecasting required; and
- understand the strata corporation's bylaws and any agreements entered into with owners respecting common property and strata lots.

It is possible that for some strata corporations, the expertise and knowledge may exist among the strata lot owners to prepare the depreciation report or assist the qualified person or team in preparing the report. The strata lot owners and strata council should carefully consider the responsibilities and risks involved in having a strata lot owner(s) prepare a depreciation report.

To find the right person or team to prepare your report, start by consulting with your Strata Property Manager, if your building has one. You can also ask for recommendations from other Strata Corporations similar to yours and look online at best practice guides offered by strata organizations. Make a list of qualified individuals firms and invite bids or proposals. Don't forget to check for references.

Recordkeeping

Depreciation Reports and Form B (the Information Certificate):

The most recent depreciation report, if any, must be attached to the Form B.

Retaining Depreciation Reports and other related materials

Under section 35 of the Strata Property Act the strata corporation must retain:

- any depreciation reports obtained by the strata corporation under section;
- any reports obtained by the strata corporation respecting repair or maintenance of major items in the strata corporation, including, without limitation, engineers' reports, risk management reports, sanitation reports and reports respecting any items for which information is, under section 94, required to be contained in a depreciation report;
- the records and documents referred to in section 20 or 23 obtained by the strata corporation. These are documents provided to the strata corporation by the owner developer.

Contingency Reserve Fund

Strata corporations must have a contingency reserve fund (“CRF”) to pay for common expenses that:

- usually occur less often than once a year; or
- do not usually occur.

The funds must be accounted for separately from other monies held by the strata corporation or separate section;

- must include any interest or income earned on the CRF; and
- can be used to secure a strata corporation loan by approval of a $\frac{3}{4}$ vote.

Funds from the CRF can be lent to the operating fund to cover temporary shortages as a result of expenses becoming payable before contributions to the operating have been collected. If a temporary loan is made:

- it must be repaid to the CRF by the end of that fiscal year; and
- the strata council must inform owners as soon as feasible of the amount and purpose of the loan.

Contributions to the CRF

Contributions from strata owners to the CRF should be included in every budget approved at an annual general meeting. CRF contributions will usually appear as a single expense line item in the budget, without any specific detail.

Usually CRF contributions are based on the unit entitlement of each strata lot in the strata corporation. Contributions to the CRF are approved in the annual budget and collected through strata fees. The following may also be added to the CRF:

- surplus funds from the previous year’s operating fund; and
- surplus funds from a special levy, as long as the surplus funds owing to each strata lot is \$100 or less.

Minimum Contributions

The CRF must have a minimum balance of 25% of the operating fund for the fiscal year. If the amount in the CRF is less, the strata corporation must contribute at least 10% of the total contribution to the operating fund for the current year until the 25% minimum is reached.

Please NOTE: This statutory minimum level for the CRF has no relationship to repair and maintenance costs over the longer term. These costs are reflected in a depreciation report; not the operating budget.

Strata owners may now make contributions to the CRF (above the minimum) by simple majority vote as part of the budget approval process and with consideration to the depreciation report. (Previously a $\frac{3}{4}$ vote was required to make contributions to the CRF if the balance in the CRF was above 100% of the operating budget).

Sections and CRFs

Separate sections within a strata corporation have a duty to establish their own operating fund and CRF for common expenses that relate exclusively to the section. (For more information on sections, please see *Guide 28: Sections: www.housing.gov.bc.ca/strata/guides.htm*).

Strata corporations with separate sections will usually have separate section budgets, a CRF for section expenses, a strata corporation budget and a CRF for expenses common to strata lots in all sections.

Common expenses shared by different sections cannot be included in section budgets. They must be included in the strata corporation budget as a common strata corporation expense.

If the strata corporation has separate section budgets, CRF contributions for that section are usually based on the unit entitlement of each strata lot in the section. Contributions to the separate section CRF are approved in the separate section annual budget and collected through separate section strata fees.

Strata lots that are differentiated as different types of strata lots in a bylaw do not have the power to establish their own operating fund and CRF.

Expenditures from the CRF

Expenditures from the CRF must be:

- approved by a $\frac{3}{4}$ vote at an annual or special general meeting; and
- consistent with the purpose of the CRF.

An unapproved expenditure from the CRF will only be permitted:

- if the expenditure is necessary to ensure safety or prevent significant loss or damage; and
- if the expenditure does not exceed what is required to ensure safety or prevent loss or damage; or
- if the expenditure is for the purpose of paying an insurance deductible required to repair or replace damaged property.

If an unapproved expenditure occurs a strata council must inform owners as soon as possible about the expenditure unless the expenditure was to pay for an insurance deductible.

Investing and Managing the CRF

The CRF can be invested or held:

- in insured accounts with savings institutions in British Columbia
- in those investments permitted by Strata Property Regulation 6.11.

When the sale of a strata lot occurs, the seller is not entitled to a return of contributions to the CRF.

Special Levy

A special levy is money collected from strata lots for a specific purpose. It is in addition to the strata fee. Strata lot owners may be required to pay special levies when:

- the expenditure has not been included in the annual budget because it was either not anticipated or because of the infrequency of the expense;
- there are insufficient funds in the CRF; or
- a decision is made not to use monies from the CRF.

Approving and Contributing to a Special Levy

A resolution for a special levy must be developed and submitted for approval at a general meeting. A resolution approving a special levy must state:

- the purpose of the levy;
- the total amount of the levy;
- the method for determining each strata lot's share of the levy;
- the amount each strata lot must pay; and
- the date(s) by which the levy must be paid.

A $\frac{3}{4}$ vote is necessary to approve a special levy if contributions to the levy are apportioned in the same way as strata fees are apportioned, which is usually by unit entitlement. However, a unanimous vote is required if contributions to the levy are apportioned by a fair division of the particular expense rather than in the same way that strata fees are apportioned.

When a strata lot is sold: if a special levy is approved before the strata lot is conveyed to the purchaser:

- the seller will owe the strata corporation the portion of the levy that is payable before the date the strata lot is conveyed to the purchaser; and
- the purchaser will owe the strata corporation the portion of the levy that is payable on or after the date the strata lot is conveyed.

Expenditures and Uses of a Special Levy

- Monies collected for a special levy must only be spent for the purpose of the special levy. The strata council must also inform owners on how monies raised from a special levy have been spent.
- The special levy can be used to secure a strata corporation loan by approval of a $\frac{3}{4}$ vote.

Excess Funds

The strata corporation must return excess funds from a special levy to each owner of the strata lot proportional to the contribution made to the special levy in respect of that strata lot, if there is at least one owner entitled to more than \$100. If no owner is entitled to more than \$100, the strata corporation may deposit the excess funds in the CRF.

Investing and Managing the Special Levy

Similar to the CRF, the special levy can be invested or held:

- in insured accounts with savings institutions in British Columbia
- in those investments permitted by Strata Property Regulation 6.11

The special levy must be accounted for separately from other monies held by the strata corporation or separate section and include any interest or income earned on the special levy.

Charging Interest on Late Payment of a Special Levy

A strata corporation may, by bylaw or by a resolution approving a special levy establish a rate of interest not to exceed the rate set out in the regulations, to be paid if the owner is late in paying his or her strata lot's share of the special levy.

The interest payable is not a fine and forms part of the special levy.

Additional Resources

Links to additional resources on Preparing Depreciation Reports

- www.housing.gov.bc.ca/strata/regs

Other Strata Property Act Resources

- Guides: www.housing.gov.bc.ca/strata/guides.htm
- Strata Property Act: www.bclaws.ca/EPLibraries/bclaws_new/document/ID/freeside/98043_00
- Strata Property Regulation: www.bclaws.ca/EPLibraries/bclaws_new/document/ID/freeside/12_43_2000

Strata Organizations in British Columbia

- Condominium Home Owners' Association (CHOA): www.choa.bc.ca
- Vancouver Island Strata Owners Association: visoa.bc.ca
- Canadian Condominium Institute, Vancouver Chapter: www.ccivancouver.ca

Additional References:

Sections of the Act referenced in this Guide: 1, 35, 59, 91-96, 98-101, 103, 105, 108, 109, 111, 158, 194, 195

Sections of the Regulations referenced in this Guide: 6.1-6.6, 6.11, 11.1-11.3

Other Relevant Strata Property Guides:

- Guide 10: What to Know about Budgeting and the Collection of Strata Fees"
- Guide 20: Who is Responsible for Repairs" for more information about who is responsible to maintain and repair various parts of the strata development.
- Guide 23: the Information Certificate (Form B)