



M&R/CRR/Reinvestment Account Guidance

ODASA- IH&P



DEFINITIONS & DISTINCTIONS

- To ensure sustainability and marketability over life of project:
- M&R – Maintenance & Repair – Routine, funded from operating expense; pays for day-to-day maintenance
- Change of Occupancy Maintenance – May have some CRR; some M&R components
- CRR – Capital Repair & Replacement - Funds replacement of items when they reach the end of their useful lives (i.e. appliances, roofing, countertops, street signs, paving); CRR are not day-to-day expenses and are not included in initial or out-year development plans; typically a four-part test is applied:
 - Common area
 - Limited Useful Life
 - Predictable Life Limit
 - Cost must be significant
- Reinvestment Account – funds initial and out-year development projects as identified in the CDMP or OYDP



BACKGROUND CRR INFORMATION

- **Original desire to maximize debt led CRR accounts to be minimally funded during CDMP development**
- **Portfolio was benchmarked against IREM data which did not accurately reflect product type or condition**
- **As development scope was reduced in many projects, CRR needs increased**
- **Challenges currently seen across Portfolio:**
 - **Lack of transparency into project's guidelines for classification of expenses**
 - **Blurred distinction and inconsistent classification of CRR expenses, OpEx, and development expenses**
 - **Project legal docs are vague wrt CR&R definitions**



WHO DOES THE WORK?

- **Property Managers should be capable of executing OpEx and most CRR work; exceptions should be agreed upon by the owners**
- **For work that is jointly determined to be beyond the skill set of the Property Manager, partners should identify who should execute the work and negotiate the fees accordingly**
- **Projects should not pay PM/AM AND DM/DB fees on CRR work**
 - **Since PM and AM fees are typically revenue based, most PMs and AMs are indifferent to OpEx/CRR work classification**
 - **At projects where CRR falls below the line and fees are based on NOI, AM is incentivized to classify more work as CRR**
 - **Currently none of the PM Incentive Performance Management Plans include metrics that address management of CRR**



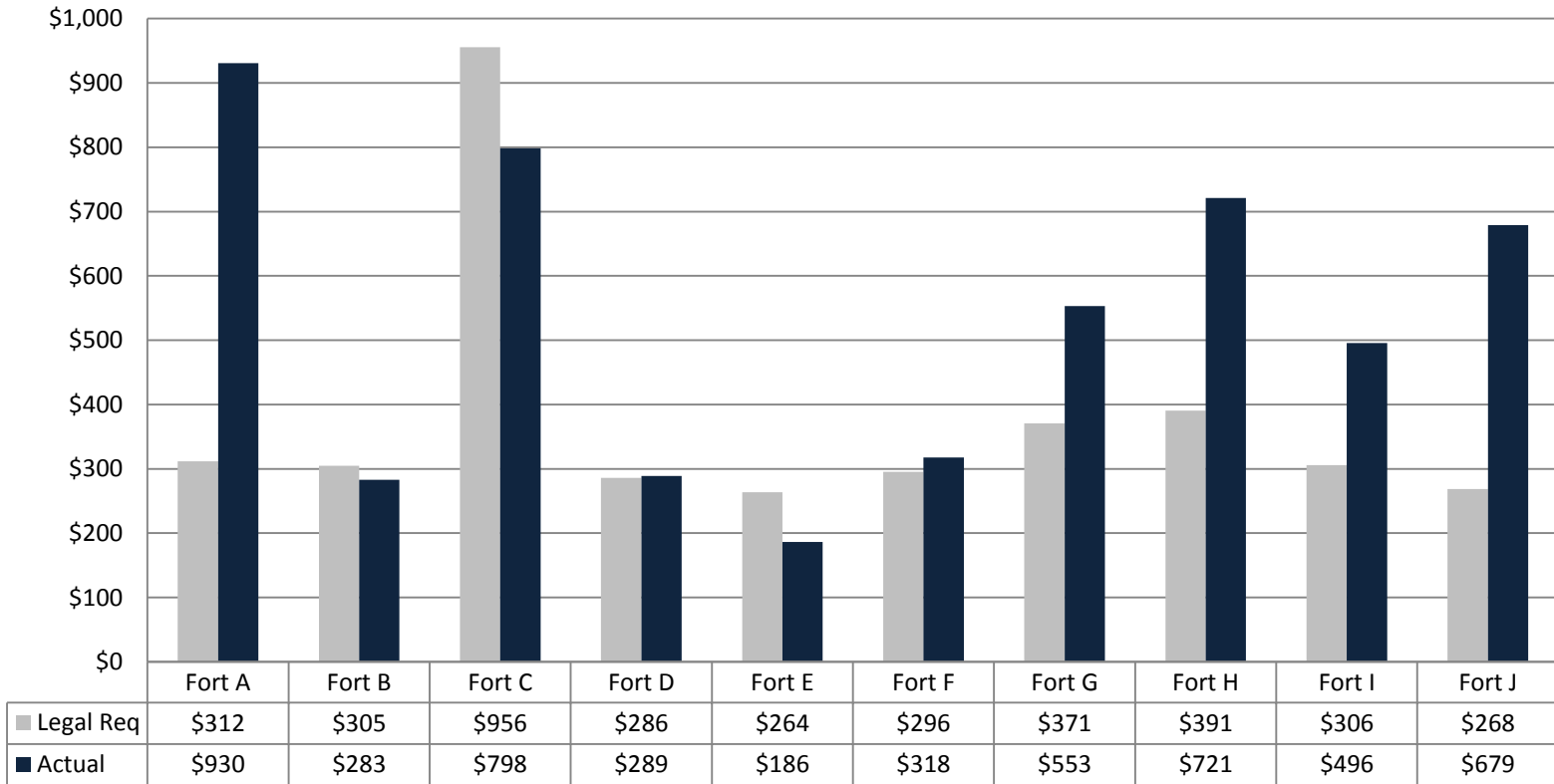
CRR vs. OpEx vs. Reinvestment

- **Army surveyed 10 existing RCI projects**
 - Review of legal documents; required CRR funding levels are clearly defined but definitions are vague
 - CRR reserves are largely insufficient to meet CRR needs
 - Analysis of actual spending and funding practices; CRR needs are being subsidized with excess cash flows, approved through the annual budget process
 - Guidelines vary by partner with “exceptions” at each project and uneven application
- **Difference in philosophy between Army and Partners**
 - Partners not incentivized to increase CR&R deposits due to potential negative impact to partnership splits as well as fee income
 - No project currently includes PM metrics that specifically address CRR
 - Partners indicate that CRR reserves were never intended to cover all sustainment expenses; Army believes that OpEx/CRR should cover all except OYDP renovations/replacements



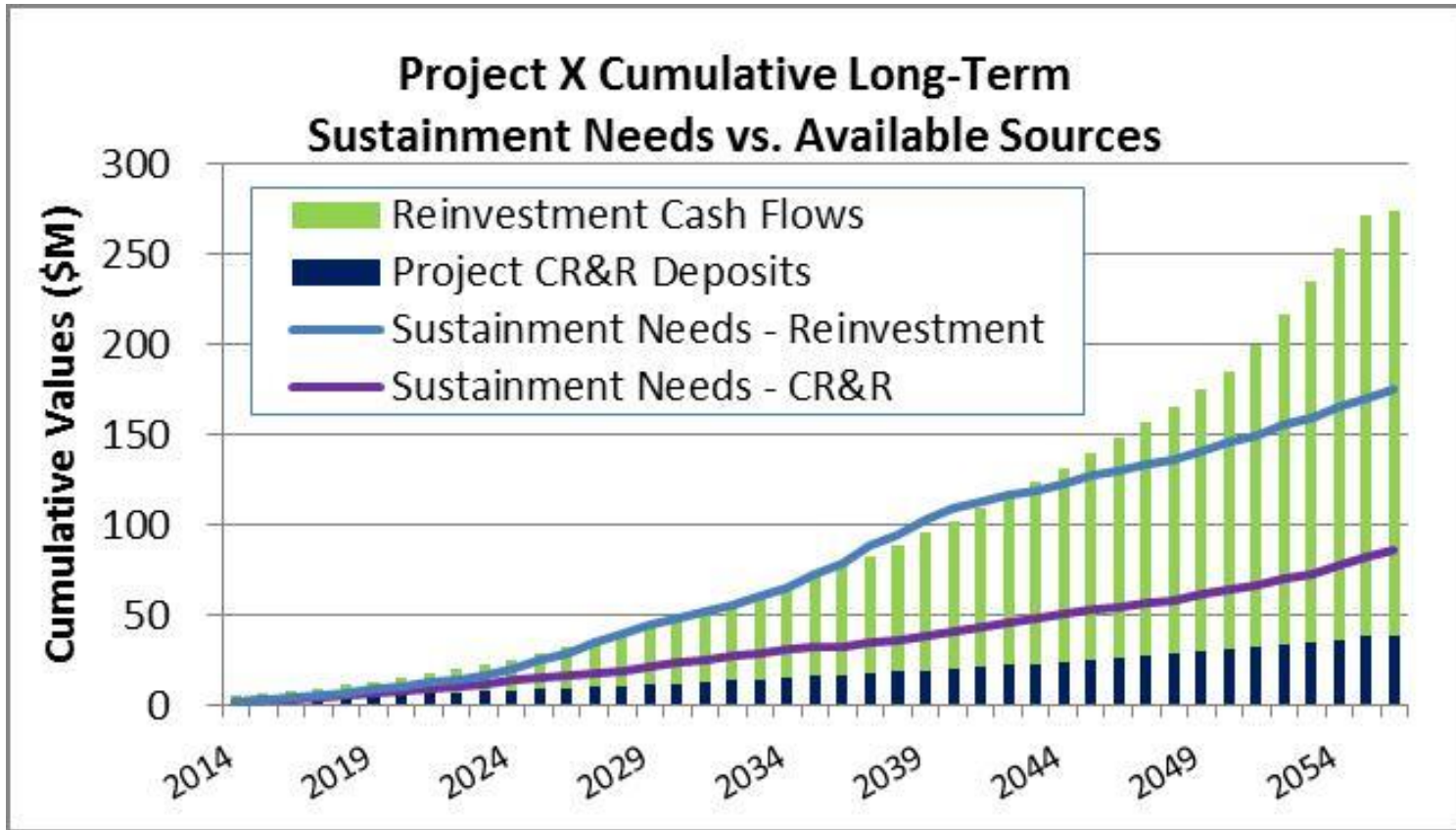
CRR AT TEN LOCATIONS

2012 Legal Requirement vs. Actual



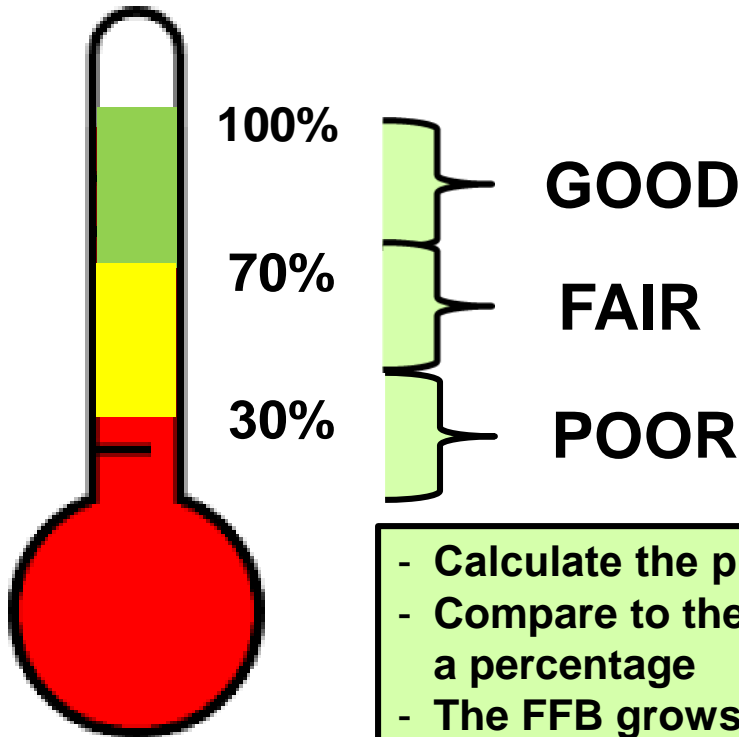


CRR DATA FROM ONE INSTALLATION





CRR Adequate Funding Levels



- Calculate the project's Fully Funded Balance (FFB)
- Compare to the CRR Fund Balance and express as a percentage
- The FFB grows as assets age and shrinks as projects are accomplished
- While 100% is ideal, a CRR fund in the 70-130% range is considered strong
- Funding below 30% will result in deferred maintenance and special funding needs



CAPITALIZED EXPENSES

CAPITALIZED ASSETS

The following represent examples of assets that are expected to be capitalized when utilizing the accompanying decision tree to differentiate from Operating expenses.

Note that no distinction is made at this time between capitalized expenses funded from CR&R vs. the Project Reinvestment Account.

Admin/Misc.

Vehicles
Maintenance Equipment
Boom Lifts
Office Equipment

Computers (desktops, laptops, monitors, dock stations)
Copiers
Fax machines
Servers
Phones
Office Furniture

Building Interiors

Appliances
Refrigerators
Stoves
Ranges
Ovens
Dishwashers
Washer/Dryer
Garbage Disposals
Microwave Ovens
Air Handlers
Water Heaters
Heat Pumps
Vertical blinds
Flooring - full replacement
Carpet
Vinyl Plank
Tile
Interior Painting
Furniture/Fixtures
Countertops
Cabinets
Sinks/faucets/fixtures
Bathtub surrounds
Bathroom vanities
Medicine Cabinets
Bathroom exhaust fans
Exterior Doors
Storm Doors
Smoke & CO2 Detectors/Sprinklers
Air Conditioning - central air or window units
Plumbing
Boilers
Insulation/duct replacements

Common Facilities

Playground Equipment
Tot Lot Ground Buffer
Swimming Pool plaster, equipment, deck
Sport Courts

Sport Courts
Fitness Equipment
Gazebos/Picnic Tables
Clubhouses and Furnishings
Model homes/Hospitality Suites
Common Areas/Fields
Running Trail Resurfacing
Mail Kiosks
Bus Shelters

Building Exterior

Windows
Painting/siding/stucco repair
Exterior Wood Trim Repair
Roofing
Garage Doors
Garage Door Openers
Patios
Chimneys
Sewer Laterals
Hand Rails
Lead-based Paint Abatement
Waterproofing
Slab/Basement Floor Repair
Shutters
Driveways-Paving/Sealing
Pressure Washing
Exterior lighting
Foundation Settlement Repair
Fascia
Soffits
Gutters/downspouts

Utilities

HVAC
Fire Safety
Water/electrical meters
Backflow Prevention

Sewer Laterals
Lift Stations/wetwell
Water mains/laterals/hydrants
Storm Drains
Electrical feeders
Transformers
Gas Distribution

Sitework/Site Structures

Fencing
Streetlights
Trash Enclosures
Parking Lots
Curbs
Sidewalks
Gutters
Guard rails
Landscaping
Tree Removal
Drainage
Irrigation Systems
Signage
Road Resurfacing
Pest Control
Pavement Overlay, Repairs & Sealing
Block Retaining Wall Repairs



STEPS TO CREATING A CRR BUDGET

- **Develop a policy with appropriate guidelines for the establishment of a capital repair/ replacement fund.**
- **Determine specific asset categories which will be funded.**
- **Inventory all assets into these categories.**
- **Determine guidelines for the useful life of each asset.**
- **Determine current replacement or repair costs for each asset category.**
- **Apply the useful life and unit costs to each asset to develop a series of annual costs.**
- **Place the cost of each asset into a 10-year schedule by category and facility.**
- **Summarize the use of funds by category and facility to determine annual requirements.**
- **Determine options available for funding sources and methods.**
- **Balance income with annual cost requirements.**
- **Review, rearrange, and upgrade costs on an annual basis.**



Capital Component Details

| <u>Component</u> | <u>Quantity</u> | <u>Useful Life</u> | <u>Rem. Useful Life</u> | <u>Current Cost (ea)</u> | <u>Future Cost (ea)</u> |
|---------------------|------------------|--------------------|-------------------------|--------------------------|-------------------------|
| HVAC Units | 25 | 15 | 0 | \$7,000 | \$9,000 |
| Kitchen appliances | | | | | |
| Dishwasher | 25 | 12 | 5 | \$600 | \$660 |
| Stove | 25 | 12 | 5 | \$700 | \$770 |
| Refrigerator | 25 | 12 | 5 | \$1,000 | \$1,100 |
| Hot Water Heaters | | | | | |
| | 90 | 12 | 1 | \$800 | |
| | 44 | 12 | 4 | | \$880 |
| Carpet & Tile | | | | | |
| Kitchen Tile | 25 @ 200 sq. ft. | 20 | 5 | \$1,000 | \$1,100 |
| Carpet | 46 | 7 | 3 | \$1,000 | \$1,100 |
| Replace Pool Equip. | 1 | 15 | 6 | \$26,000 | \$27,535 |
| Office Computers | | | | | |
| | 5 | 5 | 2 | \$2,000 | \$2,240 |
| Kitchen Cabinets | | | | | |
| | 25 | 20 | 5 | \$3,500 | \$4,000 |
| Roofs | | | | | |
| | 45 | 25 | 8 | \$6,500 | \$7,455 |



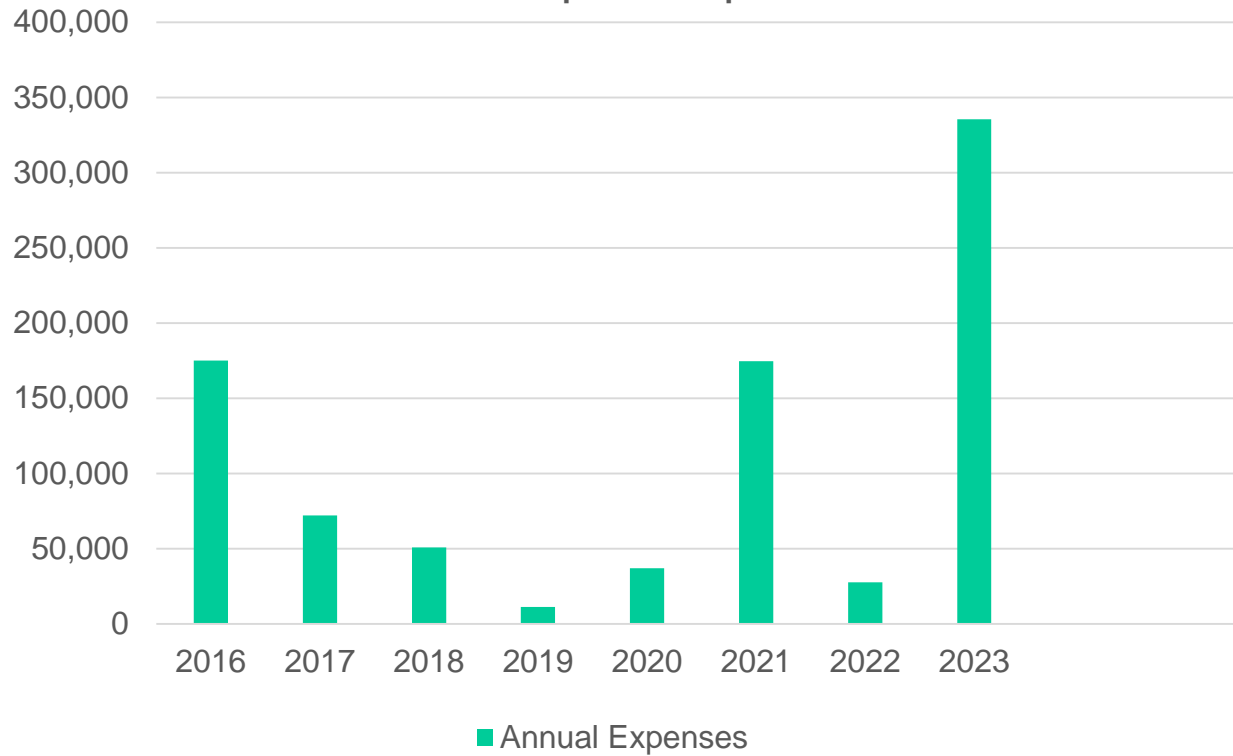
SAMPLE CRR BUDGET

| Fiscal Year | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 |
|-------------------------------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|
| Starting Capital Acct Balance | \$450,000 | \$339,052 | \$333,014 | \$350,188 | \$408,882 | \$443,937 | \$518,131 | \$567,015 |
| Annual Capital Contribution | \$64,000 | \$65,920 | \$67,898 | \$69,935 | \$72,033 | \$74,194 | \$76,419 | \$78,712 |
| Planned Special Funding | \$0 | \$0 | \$0 | \$0 | \$0 | \$190,750 | \$0 | \$0 |
| Subtotal | \$514,000 | \$404,972 | \$400,912 | \$420,123 | \$480,915 | \$518,131 | \$594,550 | \$645,727 |
| Planned Expenditures | \$174,948 | \$71,958 | \$50,724 | \$11,241 | \$36,978 | \$190,750 | \$27,535 | \$335,433 |
| Ending Capital Acct Balance | \$339,052 | \$333,014 | \$350,188 | \$408,882 | \$443,937 | \$518,131 | \$567,015 | \$310,294 |
| Component | | | | | | | | |
| HVAC Units | \$174,948 | \$0 | \$0 | \$0 | \$0 | \$0 | \$0 | \$0 |
| Kitchen Appliances | | | | | | | | |
| Dishwasher | \$0 | \$0 | \$0 | \$0 | \$0 | \$16,500 | \$0 | \$0 |
| Stove | \$0 | \$0 | \$0 | \$0 | \$0 | \$19,250 | \$0 | \$0 |
| Refrigerator | \$0 | \$0 | \$0 | \$0 | \$0 | \$27,500 | \$0 | \$0 |
| Hot Water Heaters | \$0 | \$71,958 | \$0 | \$0 | \$36,978 | \$0 | \$0 | \$0 |
| Carpet & Tile | \$0 | \$0 | \$0 | \$0 | \$0 | \$27,500 | \$0 | \$0 |
| Kitchen Tile | | | | | | | | |
| Carpet | \$0 | \$0 | \$50,724 | \$0 | \$0 | \$0 | \$0 | \$0 |
| Replace Pool Equip. | \$0 | \$0 | \$0 | \$0 | \$0 | \$0 | \$27,535 | \$0 |
| Office Computers | \$0 | \$0 | \$0 | \$11,241 | \$0 | \$0 | \$0 | \$0 |
| Kitchen Cabinets | \$0 | \$0 | \$0 | \$0 | \$0 | \$100,000 | \$0 | \$0 |
| Roofs | \$0 | \$0 | \$0 | \$0 | \$0 | \$0 | \$0 | \$335,433 |



Cycle of a CRR Budget

Annual Capital Expenses





WHAT'S WRONG WITH THIS?

Capital Repair and Replacement Budget

| Acct No. | Account Name | Jan-16 | Feb-16 | Mar-16 | Apr-16 | May-16 | Jun-16 | Jul-16 | Aug-16 | Sep-16 | Oct-16 | Nov-16 | Dec-16 | Total | EXPLANATIONS |
|--|---|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|--------------------|---|
| Capital Repair and Replacement Assumption | | | | | | | | | | | | | | | |
| | Annual Reserve Deposit Per Online Unit | | | | | | | | | | | | | \$280.27 | |
| | Inflation (per year) | | | | | | | | | | | | | 2.000% | |
| | Annual Reserve Deposit Per Online Unit Adjusted for Inflation | | | | | | | | | | | | | \$285.88 | |
| | Beginning of Year Balance | | | | | | | | | | | | | \$1,072,800 | |
| | Total Units Online | 3,000 | 3,000 | 3,000 | 3,000 | 3,000 | 3,000 | 3,000 | 3,000 | 3,000 | 3,000 | 3,000 | 3,000 | | |
| | Capital Repair and Replacement Reserve Deposit | | | | | | | | | | | | | | |
| | Restricted cash - repair and replacement | 70,068 | 71,469 | 71,469 | 71,469 | 71,469 | 71,469 | 71,469 | 71,469 | 71,469 | 71,469 | 71,469 | 71,469 | 856,225 | |
| | Total Reserve Deposit | \$70,068 | \$71,469 | \$71,469 | \$71,469 | \$71,469 | \$71,469 | \$71,469 | \$71,469 | \$71,469 | \$71,469 | \$71,469 | \$71,469 | \$856,225 | |
| | Capital Expenses | | | | | | | | | | | | | | |
| | Carpet & tile | 25,940 | 27,450 | 27,450 | 27,500 | 27,500 | 27,500 | 32,500 | 32,500 | 32,500 | 32,500 | 32,500 | 32,500 | 358,340 | average of 10-13 carpet/tile replacements each month @ 2500 a cost per month |
| | Pool/hot tub | | | | | | | | | | | | | | |
| | Recreational courts | | | | | | | | | | | | | | |
| | Parking lot | | | | | | | | | | | | | | |
| | Carpentry | | | | | | | | | | | | | | |
| | Painting | | | | | | | | | | | | | | |
| | Electrical | | | | | | | | | | | | | | |
| | Plumbing | 5,200 | 5,200 | 13,400 | 13,400 | 13,400 | 13,400 | 13,400 | 13,400 | 13,400 | 13,400 | 13,400 | 13,400 | 144,400 | includes 20 hot water heaters replacements per month at a cost 400 per unit |
| | Roof | | | | | | | | | | | | | | |
| | Fencing | | | | | | | | | | | | | | |
| | HVAC | 13,500 | 13,500 | 13,500 | 13,500 | 13,500 | 13,500 | 13,500 | 13,500 | 13,500 | 13,500 | 13,500 | 13,500 | 162,000 | replacement of 5 HVAC systems per month at 2.5k |
| | Appliance replacement | 31,894 | 31,894 | 31,894 | 31,800 | 31,800 | 31,800 | 31,800 | 31,800 | 31,800 | 31,800 | 31,800 | 31,800 | 381,882 | average replacement of 65 appliances per month at an average cost of 524 per appliance, which can include dishwasher, refrigerator, microwave, digital dishwasher |
| | Windows/screens/blinds/curtains | | | | | | | | | | | | | | |
| | Total Capital Expenses | \$76,534 | \$78,044 | \$86,244 | \$86,200 | \$86,200 | \$86,200 | \$91,200 | \$91,200 | \$91,200 | \$91,200 | \$91,200 | \$91,200 | \$1,046,622 | |



SUMMARY

- **The CRR Account is a vital key to the project's long term sustainability**
- **The Reinvestment Account will not be used to fund CRR work unless it is part of a multi-trade renovation, approved by Major Decision.**
- **CRR work may be strictly contractual – no development or DB fee is earned**
- **Requirements vary from year to year, but deposits should be constant with an inflator**
- **Needs will always exceed funding; what can you put at risk?**
- **Larger contributions to CRR will diminish the amount contributed to reinvestment accounts for renovations/replacement**
- **Establish a comprehensive CRR budget ASAP**