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Major Legislative Changes and Repairs

Elaine T. McCormack, Strata Lawyer
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There have been recent amendments made to the *Strata Property Act* ("Act") that will allow many strata corporations to approve large scale repair projects. In some circumstances, the required voting threshold at a general meeting has been changed from a $\frac{3}{4}$ vote to a majority vote for decisions related to planning for repairs and proceeding with them. This article will review the legislative amendments that will undoubtedly result in many repair projects moving forward in the coming months.

Funding Depreciation Reports

Amendments to the *Act* have clarified that a majority vote is sufficient to approve funding a depreciation report, either from the operating fund or from the contingency reserve fund.

The cost of obtaining a depreciation report may be quite significant on a per strata lot basis, especially for smaller strata corporations. One of the practical considerations of obtaining a depreciation report is how to obtain approval of the owners to pay for it. Since depreciation reports became mandatory (with certain exemptions and waivers that are beyond the scope of this article), one of the questions has always been how to fund the cost of obtaining the report. Given that depreciation reports are only required every three years, it certainly could have been argued that the reports should not be funded out of the operating fund,

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but should be funded by way of an expenditure from the contingency reserve fund or by special levy, both of which required a $\frac{3}{4}$ vote resolution. This put strata corporations who could not obtain a consensus amongst owners about whether to obtain a depreciation report in a "Catch 22." Some strata corporations could not obtain a $\frac{3}{4}$ vote resolution to waive the requirement to obtain a depreciation report and could not obtain a $\frac{3}{4}$ vote resolution to fund the depreciation report through the contingency reserve fund or by way of a special levy.

As of April 9, 2014 an amendment came into effect to section 92 of the *Act* that provides that an operating expense is not only for common expenses that usually occur either once a year or more often than once a year, but also for common expenses that are necessary to obtain a depreciation report. On the same date another amendment came into effect that allows strata corporations to approve by majority vote at a general meeting an expenditure out of the contingency reserve fund necessary to obtain a depreciation report under section 94 of the *Act*.

These amendments will allow more strata corporations to obtain depreciation reports, which should result in increased preventative maintenance and also allow for better planning of large scale repairs, including increased funding into the contingency reserve fund.

Using Contingency Reserve Funds to Finance Maintenance and Repairs

Amendments have now been made to the *Act* which allow expenditures out of the contingency reserve fund to be approved by a majority vote at a general meeting for certain repair, maintenance and replacement.

Under the *Act*, the general rule is that expenditures from the contingency reserve fund must be approved by a $\frac{3}{4}$ vote resolution of the owners. There have always been two exceptions to this general rule under the *Act*. The first exception is under section 98(3) of the *Act* whereby "... expenditures may be made out of the operating fund or contingency reserve fund if there are reasonable grounds to believe that an immediate expenditure is necessary to ensure safety or prevent significant loss or damage, whether physical or otherwise." The second exception allows an insurance deductible to be paid by special levy or out of the contingency reserve fund without a $\frac{3}{4}$ vote if the strata corporation is required to pay it to repair or replace damaged property. As we have just reviewed, there is now a third exception that allows depreciation reports to be paid for out of the contingency reserve fund with approval of the expenditure by majority vote.

We also now have a fourth exception to the general rule. This new exception allows owners to approve by majority vote the cost of repair, maintenance or replacement that is recommended in the depreciation report.

As of April 9, 2014 a majority vote is sufficient to approve or authorize expenditures from the contingency reserve fund if the expenditure is "... related to the repair, maintenance or replacement, as recommended in the most current depreciation report obtained under section 94, of common property, common assets or the portions of a strata lot for which the strata corporation has taken responsibility under section 72(3)..."

As a result, a strata corporation can now use a majority vote to fund a depreciation report from the contingency reserve fund and pay for the recommended work from the contingency reserve fund.

Court Application for Repairs

Another example of the expanding scope of majority votes and increased access to repairs is evidenced by an amendment made to section 173 of the *Act* which came into effect on December 12, 2013.

Prior to this amendment, if a strata corporation failed to approve maintenance, repairs or replacements and owner(s) felt strongly about having the work performed, one or more owners could commence a Petition in the Supreme Court of British Columbia to obtain an order deeming that a $\frac{3}{4}$ vote resolution was passed to fund the repairs. This meant that the burden of commencing the Petition was on one or more owners, who rarely were able to obtain reimbursement from the strata corporation for all of the legal fees expended for the court proceedings.

Now, section 173(2) to 173(4) provide as follows:

173 (2) If, under section 108 (2) (a),

(a) a resolution is proposed to approve a special levy to raise money for the maintenance or repair of common property or common assets that is necessary to ensure safety or to prevent significant loss or damage, whether physical or otherwise, and

(b) the number of votes cast in favour of the resolution is more than $\frac{1}{2}$ of the votes cast on the resolution but less than the $\frac{3}{4}$ vote required under section 108 (2) (a), the strata corporation may apply to the Supreme Court, on such notice as the court may require, for an order under subsection (4) of this section.

(3) An application under subsection (2) must be made within 90 days after the vote referred to in that subsection.

(4) On an application under subsection (2), the court may make an order approving the resolution and, in that event, the strata corporation may proceed as if the resolution had been passed under section 108 (2) (a).

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As a result, if at a general meeting a $\frac{3}{4}$ vote resolution to approve a special levy fails to meet the $\frac{3}{4}$ vote resolution threshold, but the majority of votes cast are in favour of the resolution, then the council can choose to apply to the Supreme Court of British Columbia for an order approving the resolution and the Strata Corporation can proceed as if the resolution had been passed.

The writer envisions depreciation reports being used as evidence in these applications regarding the necessity and urgency of the work required. It may be that in the future, strata corporations will plan on the possibility of needing to rely on the depreciation report as evidence in an application to have a Supreme Court Judge approve a $\frac{3}{4}$ vote resolution for a special levy and will require the qualified person preparing the report to draft the report in a manner so that it can be relied on as an expert report under the BC Supreme Court Rules.

As a result of this new amendment, if a special levy for urgent repairs is approved by enough owners to pass a majority vote, but not a $\frac{3}{4}$ vote, then the council can make an application to the Supreme Court of British Columbia and the voice of those owners will be heard.

How is a Majority Vote Obtained?

Under the *Act*, a “majority vote” is defined as follows:

“**majority vote**” means a vote in favour of a resolution by more than $\frac{1}{2}$ of the votes cast by eligible voters who are present in person or by proxy at the time the vote is taken and who have not abstained from voting.

Under section 48, unless otherwise provided for in the bylaws, quorum is $\frac{1}{3}$ of the strata corporation’s votes, present in person or by proxy. As a result, a strata corporation with a hundred strata lots could meet the quorum

requirements by having 33 strata lots represented. If all strata lots represented vote at the meeting, only 17 “yes” votes would be required to meet the majority threshold. Many strata corporations have bylaws that lower quorum requirements even further, such as providing that $\frac{1}{2}$ hour after the scheduled time for the meeting has passed, those present in person or by proxy constitute quorum. Given these parameters, decisions made by majority vote can be made by a very small percentage of individuals in a strata community.

Section 51 of the *Act* requires that a strata corporation cannot take any action to implement a $\frac{3}{4}$ vote resolution for one week following the vote if it is passed at an annual or special general meeting by persons holding less than 50% of the votes, unless there are reasonable grounds to believe that immediate action is necessary to ensure safety or prevent significant loss or damage. There is no similar provision for majority votes and the council can implement the results of the votes immediately, for instance by signing a contract for major repairs right after the general meeting is held.

Unlike $\frac{3}{4}$ votes, there is no legislative impediment to amending a majority vote at a general meeting. So, not only can a small percentage of the owners constitute quorum, that same small percentage of owners may also be able to amend the majority resolution that was put on the agenda as well. Only time will tell whether majority vote resolutions are amended in a significantly unfair way to those that choose not to attend the general meeting in person or are unable to instruct a proxy properly. For instance, can a majority vote resolution to expend funds from the contingency reserve fund to pay for repairs recommended in the depreciation report be amended at the meeting to greatly increase the amount to be expended? Is that significantly unfair to those that failed to attend the meeting after reviewing the notice of the meeting?

Moving Forward

The recent amendments to the *Act* will allow more strata corporations to move forward with planning and following through with repair, maintenance and replacement, including repairs to major building systems which may have been delayed for many years due to lack of consensus amongst the owners. The use of majority votes for repair decisions makes it very important for owners to attend general meetings.

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Editorial: Pitfalls of Change

Cora D. Wilson, Editor

STRATA-SPHERE CONDOMINIUM SERVICES INC.

E laine T. McCormack, high profile strata lawyer, adeptly summarizes the recent legislative changes to the *Strata Property Act* that substitute a majority vote of owners at a general meeting for the previous $\frac{3}{4}$ vote threshold when addressing the funding of a depreciation report, approval of recommended repairs set out in a depreciation report and repair litigation approval. These are welcome changes.

However, as Michael Wilson, senior engineer, and Gerry Fanaken, veteran strata manager, author and educator, point out, the legislation and the depreciation report do not currently go far enough.

A depreciation report is viewed as a long term planning tool. Michael J. Wilson believes that a strata corporation faces practical problems when implementing the depreciation report, since the actual repair costs may not reflect the cost estimates set out in the report. “The biggest hurdle to overcome may be recalling that the plan is an initial plan based on a number of assumptions including fairly low-level cost estimates.” He indicates that there could be additional costs to those set out in the depreciation report related to consequential work (eg. landscaping), concealed damages from water penetration or previous installation deficiencies that require correction. Mr. Wilson strongly recommends that a Design Study be prepared to assess existing conditions before finalizing the repair cost estimates and implementing the repair approval process. In my view, this course of action should be viewed as a best practice.

Once the cost estimate has been finalized, there are 4 options available to the strata corporation to raise money to pay for the repairs including: a special levy, expenditures out of the contingency reserve fund (“CRF”), strata corporation financing (borrowing) or a combination.

Mr. Fanaken raises a very legitimate concern: “Unlike other provinces which mandate depreciation reports and funding models, BC does not *mandate actual funding* once a depreciation report has been completed ...”. Some strata corporations raise money by increasing strata fees to beef up

the CRF, while other stratas keep contributions the same or implement modest increases. He raises the concern that this different approach to funding could create an “uneven playing field” leading to potential lawsuits, confusion and misunderstandings. He argues that, “The statute must, therefore, be fixed.” It is hoped that the legislature acts on this recommendation before this vision becomes a reality.

If a strata corporation does not increase strata fees by making larger contributions to the CRF, then the remaining funding options include strata corporation financing (borrowing), a lump sum payment (special levy) or a combination.

Trevor Palmquist, VP Commercial, BMO, is promoting financing as a viable option to fund repairs either alone or in combination with the special levy. He addresses the terms for such loans generally and provides the following rule of thumb: “Although no specific guidelines exist on this topic, as a rule of thumb historical evidence has shown that an increase of up to 100% of existing monthly strata fees as a result of the proposed loan is often considered acceptable.”

Tony Gioventu, Executive Director for CHOA, discusses the implementation of the depreciation report and stresses: “It is important that your strata council and manager have the authority they require to expend their funds for the renewal and projects, if approved by a majority vote.”

In my Article, I highlight that funding authority is imbedded in the resolution. This underscores the importance of drafting a proper resolution. The resolution forms “the foundation for funding repairs, paying contractors, financing the repairs and collecting arrears. If the resolution falls, then the owners’ legal obligation to pay also falls. The process could become a house of cards.”

This article provides a non-exhaustive summary of best practices when drafting the resolution and recommends that a qualified strata lawyer be retained to address the resolution.

The changes in the legislation are welcome; however, additional changes are required. Also, more planning is necessary before strata corporations implement the repair process in order to ensure that minimum standards are met.



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Written by Cora D. Wilson,
Strata Lawyer
and Tony Gioventu

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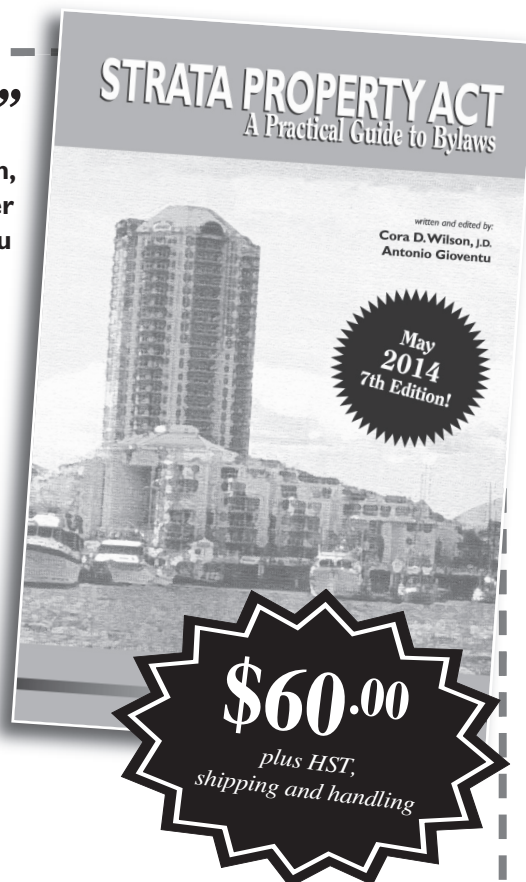
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Major Legislative Changes Impacting Repairs and Best Practices

Cora D. Wilson, J.D.

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Recent amendments to the *Strata Property Act* (“*Act*”) will make it easier for a strata corporation to repair and maintain their buildings. The first legislative amendment changes the voting threshold at a general meeting of owners from a $\frac{3}{4}$ vote to a majority vote when funding a depreciation report or approving repairs recommended by a depreciation report from the contingency reserve fund (the CRF).

The second legislative amendment permits a strata corporation to proceed with a court application to obtain an order for repairs in the situation where a $\frac{3}{4}$ vote resolution for a special levy fails but more than 50% of the votes cast were in favour of the resolution. It is important to remember the strata corporation must approve the funding to proceed with court action. It is recommended that the strata corporation obtain advice from a qualified strata lawyer to verify that this amendment applies to the strata corporation in question.

Recent reviews of resolutions approved by strata corporations reveal major flaws which could result in resolutions being struck down if challenged. The consequences could be catastrophic since the resolution forms the foundation for funding repairs, paying contractors, financing the repairs and collecting arrears. If the resolution falls, then the owners’ legal obligation to pay also falls. The process could become a house of cards.

The following discussion reviews the new legislation in a summary fashion, addresses some of the pitfalls and outlines the process for a strata corporation to follow as a best practice.

Summary of Legislative Amendments

As of April 9, 2014, section 92 of the *Strata Property Act* (the “*Act*”) was amended to clarify that the cost of a depreciation report can be an operating expense. This means the cost to obtain a depreciation report may be included in the annual budget, which is approved by a majority vote.

Also effective April 9, 2014, the cost to obtain a depreciation

report can be paid out of the CRF by a majority vote (s. 96(b)(i)(A)(I), *Act*).

This creates an exception to the general rule that a $\frac{3}{4}$ vote resolution is required to approve expenditures from the CRF. Owners are now permitted to approve funding for repairs, maintenance or replacement recommended in the most recent depreciation report by a majority vote (s. 96(b)(i)(A)(II), *Act*).

By way of summary, a strata corporation can now use a majority vote to fund both a depreciation report and the work recommended in the depreciation report from the CRF.

It is anticipated that these changes will result in more strata corporations proceeding with depreciation reports and addressing major repair programs in a planned, reasonable and timely fashion to meet the mandatory statutory duty to repair imposed by the *Act*.

The team approach comprising appropriate qualified certifying professionals, qualified contractors, a strata lawyer, a strata manager and other qualified persons is recommended to ensure that the strata corporation meets the minimum standards. They safe guard the process by ensuring that the strata corporation acts within the scope of its statutory authority, both substantively and procedurally, adheres to due process, provides transparency and complies with the mandate provided by the approved resolutions.

Special levy resolutions still require a $\frac{3}{4}$ vote of owners at a general meeting (s. 108, *Act*). Effective December 12, 2013, the strata corporation may apply to the Supreme Court for an order approving a special levy to address maintenance or repairs defeated by the owners at a general meeting provided that more than $\frac{1}{2}$ of the votes cast favoured the resolution (ss. 173(2) & (4), *Act*). Previously, a $\frac{3}{4}$ vote was required to authorize the strata corporation to engage in such litigation. Although it is now easier to proceed to the Supreme Court, many obstacles still remain. This process tends to be political, cumbersome, expensive and uncertain.

Since the funding for such litigation still requires a $\frac{3}{4}$ vote, I recommend that sufficient monies for legal costs be

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approved as part of the annual budget. This will allow the council to conduct business, while minimizing the probability of time consuming and often difficult political battles to obtain expenditure approval.

The legislation encourages the use of the CRF as a long term planning tool. Special levies will likely be used less often given the higher voting threshold required for approval. Clearly it is easier to obtain a majority vote approving monies already available in the CRF than it is to approve a special levy ($\frac{3}{4}$ vote). It is envisioned that more strata corporations will investigate financing options available to them to minimize the burden of a huge repair levy. Both special levies and strata corporation financing (borrowing) require a $\frac{3}{4}$ vote for approval (ss. 108 & 111, *Act*). If the CRF

is exhausted or insufficient, owners may view financing (borrowing) as a palatable option in appropriate cases. For example, a repair levy of \$50,000.00 per strata lot amortized over 15 years costs about \$394.00 per month assuming a 5% interest rate (prime plus 2%). It is easier for some owners to pay \$394.00 per month as opposed to coming up with \$50,000.00 all at once.

One of the objectives should be to ensure that owners do not lose their home if they cannot afford to pay the special levy. When the strata corporation acts as the borrower it gives everyone a fighting chance by minimizing the owner subsidy if some owners default, ensuring that funding is available to pay the contractor when due and providing those owners who are least able to pay with an opportunity to hold onto their investment.

The Train Wreck Resolution:

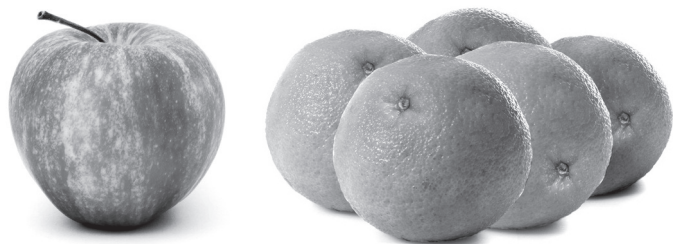
It is not unusual to find a poorly worded resolution such as the following:

Resolved: Contingency reserve fund expenditure by majority vote not to exceed \$3,000,000.00 to replace up to 30 roofs with cedar shakes in 2014, 30 roofs in 2015 and the remaining roofs in 2016. Approved.

The major problems with this poorly worded resolution include the following:

- the strata corporation only has \$500,000.00 in the CRF;
- the depreciation report did not require all of the roofs to be replaced over a 3 year period; and,
- a $\frac{3}{4}$ vote is required to approve significant changes in the use or appearance of common property (s. 71, *Act*).

The failure to comply with substantive provisions of the *Act* is fatal. If a portion of the resolution cannot legally be approved by majority vote, then the whole of the resolution is in jeopardy of being struck down in the event of a challenge. The Courts do not have the power to save fatal resolutions - hence, approving a defective resolution in this case is akin to approving expenditures out of a bank account containing insufficient funds. The



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contractor will rely on this resolution as evidence that there are sufficient funds available to pay its accounts as they fall due. In fact, the funding is grossly inadequate.

There are other problems with this resolution. For example, the scope of authorized work is vague and uncertain and the phasing order of the work is not addressed.

The question is whether a strata corporation should act upon an approved resolution which fails to meet minimum legal standards. The council should seek legal advice from a qualified strata lawyer. As a matter of practice, the political process should always be exhausted before commencing legal proceedings. It could be that the resolution may be revised and ratified by a further vote of owners at a general meeting. This course of action is always recommended over proceeding with major repairs that rely on a flawed resolution.

The strata corporation should not proceed with the project for the following reasons:

- a. There are insufficient monies in the CRF (short by \$2,500,000.00) to pay for the roofing project which requires an estimated amount of \$3,000,000.00 to complete.
- b. Awarding the contract or a tender to a contractor for the complete scope of work (\$3,000,000.00) could place the strata corporation in a potential breach of contract situation if funding is not available as the project proceeds.
- c. Approval of the CRF resolution is predicated upon the approval of a further special levy resolution to provide the balance of the funding required to pay for the entire project. Since this has not occurred and there is no guarantee that it will occur, then moving forward creates the potential for unquantifiable, but avoidable, legal exposure to liability.
- d. The wording of resolution is vague and confusing creating uncertainty such that the resolution could be struck down on this basis.
- e. The failure to obtain a $\frac{3}{4}$ vote pursuant to section 71 of the *Act*, if required, is fatal to the validity of the resolution.

The strata manager's professional liability insurance does not cover work performed outside of that manager's scope

of expertise. For example, resolution drafting is not only an art, it likely qualifies as the provision of a legal service. Strata managers are neither qualified nor licenced to provide legal services. Further, such services by a strata manager are not covered by their errors and omissions insurance. In the event of a loss to the strata corporation due to the negligent drafting of the resolution by the agent, there would be no recourse against the agent's insurance.

It is envisioned that brokerages in the future will exercise prudence and caution when addressing services which qualify as legal services and ensure that services are only provided within the scope of their expertise and licencing requirements and are covered by appropriate insurance.

Practice Tips

The process for addressing major repairs and approving the related expenditures is summarized as follows (this list is not exhaustive):

1. investigate the background of the professionals and contractors;
2. hire a qualified engineer, building envelope or other professional to assist with the process, as required;
3. ensure that appropriate professional insurance coverage is available;
4. retain an experienced strata lawyer;
5. obtain an estimate of probable costs for the repairs from a qualified certifying professional or obtain a reasonable number of quotes from qualified contractors for smaller projects;
6. determine whether the proposed repair is recommended in the most current depreciation report,
 - a. if yes, those repairs may be approved out of the CRF by majority vote subject to the availability of funds;
 - b. if no, a $\frac{3}{4}$ vote resolution is required to approve:
 - i. a special levy;
 - ii. expenditures out of the CRF for repairs which are not recommended in the depreciation report; or,
 - iii. strata corporation financing (borrowing);
7. consider preparing two resolutions for owner approval if there is a concern that the $\frac{3}{4}$ vote may not be approved to permit a partial repair;



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8. address the options for funding the project:
 - a. strata corporation financing (borrowing);
 - b. special levy;
 - c. contingency reserve fund; or,
 - d. combination;
9. keep the owners informed regarding the project throughout including:
 - a. information meetings with the professionals, including the strata lawyer, as required;
 - b. newsletters;
 - c. web-site; and/or,
 - d. other means;
10. address any political, legal or construction obstacles or concerns in a reasonable and in a timely fashion;
11. instruct a qualified strata lawyer to prepare the resolution(s) addressing the following:
 - a. ensure that the repair authorization is tailor made to address all required work including, but not limited to, the scope of work set out in the professional's report and any additional work recommended by qualified professionals during the course of the work;
 - b. ensure that the expenditure authorization is broad enough to capture all expenses such as, the remedial work, warranty, landscaping, permit costs, professional costs, legal costs, collection costs, change work orders, etc.;
 - c. include a reasonable contingency to minimize the possibility of an additional $\frac{3}{4}$ vote of owners to approve additional funding;
 - d. authorize the council to approve change work orders;
 - e. delegate decision making authority, including the power to make expenditures, to the council;
 - f. approve significant changes to the use or appearance of common property by $\frac{3}{4}$ vote;
 - g. insert a provision requiring the strata corporation to report to the owners upon completion of the work (eg. 6 months after completion of the work);
 - h. if the funding amount is paid by a combination of special levy and the CRF, indicate where the expenditures will be applied from first and how any excess funds will be addressed; and,
 - i. address any other clauses that may be required given the nature of the project; and,
 - j. if a special levy is proposed, then the following must be addressed (s. 108, *Act*):
 - i. state the purpose of the levy;
 - ii. state the total amount of the repair special levy;
 - iii. state the method used to determine each strata lot's share of the special levy (e.g. unit entitlement);
 - iv. attach a schedule indicating the amount payable by each strata lot on account of the special levy;
 - v. state the date by which the special levy is to be paid, or, if payable in installments, the dates by which the installments are to be paid; and,
 - vi. draft an interest provision in the event of any default in payment of the special levy, including the commencement date (7 days after approval at a minimum).

The implementation of the major repair project is beyond the scope of this article.

Strata corporations are advised to seek legal advice from a qualified strata lawyer when addressing repair projects to provide input and advice throughout the process. This includes drafting the resolution.

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Trevor Palmquist, Vice President Commercial
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Strata corporations facing large unforeseen costs related to major restorative work and long-term maintenance is not new to strata's across B.C. What remains lesser known is that various financing options for common element repairs exist in the market which means that strata's no longer have to defer often much needed building maintenance. Financing can also be a suitable alternative or compliment to raising funds for repairs via special levy alone. BMO Bank of Montreal has been providing financing in this active market segment for over a decade with increased interest as of late due to recent changes to the B.C. *Strata Property Act*. Below I will outline some of these options as well as highlight some considerations to aid you in your financing decision.

First let's talk about what types of projects are typically financed. The most common are roof repairs and replacements as well as full or partial building rainscreening. Lesser known projects we finance at BMO include improvements to both the exterior (fence repair and maintenance, parkade membrane repair and driveway repaving) and interior (building lobbies and furniture, HVAC systems) of your building.

The second consideration is what loan amortization is appropriate for the project type. Typically longer-life assets such as roof replacements (which often come with a 15 year warranty) and envelope repairs such as rainscreening will warrant a longer amortization of an average of 10 years, while smaller projects, such as the improvements referred to above, will require a shorter amortization of 3 to 7 years. A deciding factor on which amortization you choose will depend on the increase to existing monthly strata fees (discussed further in a later paragraph). To relieve some of the increased cost to the strata corporation during the maintenance or repair period, we'll typically provide an interest only loan period whereby the strata can draw down on the loan as funds are needed rather than advancing the entire loan at the outset of the project.

A third variable for your strata to consider is whether a fixed or variable rate loan is appropriate. Each has its own merits.

Trevor Palmquist has worked for BMO for nearly seven years and recently relocated to Nanaimo to lead the north and central Vancouver Island commercial banking team. Trevor is excited about continuing to build his team's brand both in Nanaimo and surrounding communities. Particular areas of interest for his team include strata financing, agriculture and professionals. When not at the office, Trevor enjoys the vast outdoor playground that is Vancouver Island by hiking, rock climbing, running and camping.

One question I often get asked is whether lump sum payments are allowed throughout the duration of the loan. The short answer is "yes" if a variable rate loan is chosen and "it depends" if a fixed rate option is chosen. Where we can be creative with fixed rate facilities is dividing up your loan into two separate loans, one variable and one fixed. In this scenario, your strata can make lump sum payments to the variable rate loan at any time throughout the year and without penalty, while the fixed rate loan protects your strata from rising interest rates. In our current environmental where interest rates are at historically low levels, it may be appropriate to lock in a portion of the loan today to hedge against increasing interest rates tomorrow.

Finally and most importantly your strata will need to determine what size of loan payments each strata owner could individually support. That is to say that although the level of financing can be as high as 100% of total project costs, with average financing levels between 70 and 80%, what matters most is that each strata owner can support the increased debt load through increased individual strata fees based on unit entitlement. Another way of putting this is that while your strata may have approved financing up to a maximum of 100% of costs via a borrowing resolution, this may not be the most prudent option for all unitholders if the proposed strata fee increase elevates the risk of default to both the strata corporation and to the bank. Although no specific guidelines exist on this topic, as a rule of thumb historical evidence has shown that an increase of up to 100% of existing monthly strata fees as a result of the proposed loan is often considered acceptable.

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Financing options exist at BMO... *continued from page 11*

Loan features aside, let's discuss more generally a couple of other considerations and benefits that might accrue to individual strata owners. Most importantly, through a strata loan the individual strata units are not pledged as security. This means a mortgage charge over individual properties is not taken as collateral but rather a blanket General Security Agreement ("GSA") is taken over the strata corporation as a whole. This means the unitholders individual homes are not encumbered by the loan but rather the strata corporation

assumes the liability. Second, by moving with haste to approve a loan and commence improvements today, your strata is no longer deferring much needed repairs which in turn ensures that the value of your unit is maintained going forward.

As indicated above, your strata council has a number of matters to consider in putting together a financing proposal to the individual unitholders. These include, but are not limited to, size of the loan, term and amortization of the loan, whether to hedge interest rate risk with fixed rates loan facilities and most importantly consideration of whether the corresponding debt burden to individual strata owners once the loan repayments begin are feasible and realistic. Once a collective decision has been made by your strata to repair your building, obtain the necessary borrowing resolutions and secure the requisite financing, the project work can commence in earnest with the ultimate goal being to protect the value of your home today and well into the future.



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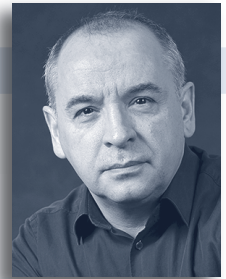
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Implementing Your Depreciation Report

Tony Gioventu, Executive Director

CONDOMINIUM HOME OWNERS ASSOCIATION OF BC

How does your strata corporation get the best value out of the information in your depreciation report?

The depreciation report is in many ways the beginning of a base operations plan to help your strata council and manager to understand your inventory of common property and common assets. Take a look at the major components and the operational assets and summarize them into a short planning schedule that your council can review annually. The list will include: Annual Maintenance and Inspections, Long Term Maintenance Schedules and Renewals.

Annual Maintenance is often related to long term projects; however, the implementation of annual maintenance schedules and inspections will provide better performance of your assets and a better understanding of how to prolong the life of major components, such as roofing, deck and balcony surfaces, exterior cladding, doors and windows and heating and ventilation equipment.

With the introduction of a majority vote to approve expenses from the Contingency Reserve Fund where recommended in the Depreciation Report, the strata corporation also has the ability to now plan for the funding requirements and prepare for the resolutions required in the notice packages to seek the approval of the owners at general meetings. It is important that your strata council and manager have the authority they require to expend the funds for the renewals

Antonio (Tony) Gioventu, is the Executive Director and Strata Property Advisor for the Condominium Home Owners' Association of B.C. (CHOA). He brings 25 years' experience in management, real estate development, construction, building operations, and strata property legislation to this position.

and projects, if approved by a majority vote. The particulars of the project should be included in the resolution to ensure your strata council can implement the scope of work required.

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Depreciation Report

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Implementing ... continued from page 13

The following is a short summary of a depreciation report estimate for major components in a 51 unit - 4 floor wood construction building in Victoria that is 18 years old. The building has 1 elevator and an underground parking garage.

Depreciation Renewals Estimates

Asset	Target Date	Projected Cost
Roof	2020	\$ 178,000
Balconies	2018	163,000
Doors & Windows	2026	408,000
Siding upgrade	2038	561,000
Elevator	2021	56,000
Water piping	2027	382,500

Depreciation Long Term Maintenance

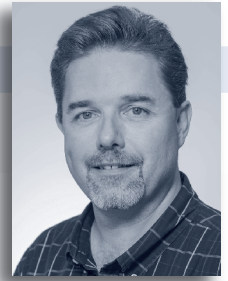
Yard Fencing	2015	\$ 30,600
Trim Painting	2014	15,000
Parking garage	2018	20,000
Fire System Upgrade	2020	10,000

Annual Budget - Maintenance & Inspections

Fire Safety System	\$ 1,800
Elevator Servicing	3,800
HVAC Service Contract	6,400
Roofing & Gutters	5,000
Deck membranes and drainage	3,000
Sewer/Drainage flushing	2,500
Sump pump servicing	500

The roof renewal projected for 2020 is a good example of planning. A detailed inspection is best undertaken in 2-3 years (2017), before the projected renewal date. This gives the strata corporation and owners time to plan for the funding, engage a professional to set up the scope of work and a bidding process, plan meetings to approve resolutions or special levies and address scheduling to ensure that the roofing project proceeds during good weather. This is an essential part of effective budget planning. Don't be a victim of costly unplanned disasters that may be 30-50% higher.

The fall session of the CHOA seminars in 2014 includes a detailed session on the use and implementation of your depreciation report. Go to www.choa.bc.ca for more information on fall seminars in your area.



Depreciation Report Replacement Cost Estimate vs. Project Budgeting

Michael J. Wilson, M.Eng., P.Eng., FEC
RDH BUILDING ENGINEERING

Legislation and the hard work of many Strata's throughout our province has greatly increased the awareness and need for Contingency Reserve Fund financial planning. Strata's that are compliant with current legislation related to Depreciation Reports are now armed with an initial financial plan for a series of predicted activities associated with the renewal and major maintenance of the Strata's physical and commonly owned assets (roofs, boilers, windows etc.).

The hard work is however not over and now these same Strata need to work with the plan that they have been given. The biggest hurdle to overcome may be recalling that the plan is an initial plan based on a number of assumptions including fairly low-level cost estimates.

The cost estimates are considered low-level because they were based on an initial review, estimated quantities, like-for-like replacement, with no consideration for betterment or the impact of consequential work. The cost estimates are also exclusive of any project related costs such as improvements to rectify non-compliant construction (building code issues), repairs to hidden or concealed damage, access costs, design and engineering services, project management, contract administration or legal consultation.

How will the Strata with a Depreciation Report work their initial plan? Ideally each year the upcoming predicted renewal and major maintenance activities contained within a tactical timeframe will be reviewed and updated. A reasonable tactical timeframe may be five years, but a Strata with less tolerance for risk may wish to look further into the future and choose a ten year timeframe. Since the key factor for determining when to implement any of the predicted renewal or major maintenance activities is ultimately likely to be unacceptable performance, continued visual review is essential.

Each year when the review is complete the Strata will be in a position to seek approval to implement some of the

Michael Wilson is a structural engineer and senior building science specialist at RDH Building Engineering. RDH is a firm that focuses on Making Buildings Better (www.rdh.com) with over 150 staff in offices in Vancouver, Victoria, Courtenay, Seattle, Portland and San Francisco. Mike manages RDH's Victoria office and is the firm's managing principal responsible for the services on Vancouver Island.

predicted renewal or major maintenance activities during the next fiscal operating year. Timing for the review and reporting is important so that information can be managed concurrent with the Strata's yearly management timeline.

The Depreciation Report is based on observations and predicted performance and deterioration of materials and equipment. It is unlikely that every prediction will be perfect and the actual timeline for implementing any particular renewal or major maintenance activity is likely to be accelerated or delayed. The act of ongoing review and updating of the Strata's renewal and major maintenance activities will improve the accuracy and usefulness of the Depreciation Report as a financial planning tool, but work is still needed if the Strata is to successfully implement any of the renewal or major maintenance activities.

As described in other articles there are ways to achieve approval for implementing renewal or major maintenance activities that are described in a Depreciation Report by virtual of a majority vote as opposed to a $\frac{3}{4}$ vote. Regardless of the margin of approval, the Strata will need to describe the renewal or major maintenance activity in the form of a "resolution." The resolution will need to be of sufficient detail that the Strata is comfortable providing approval.

The description and detail related to the renewal or major maintenance activity will need to be developed beyond that initially described in the Depreciation Report. The resolution will also require a detailed project budget, which will need to be developed since the cost estimate in the Depreciation Report was only related to the asset's replacement cost and

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Depreciation Report Replacement Cost Estimate... *continued from page 15*

not project needs. An example of an asset that is commonly found in a typical Depreciation Report is a membrane on a balcony. A balcony membrane renewal project is however likely to impact other related assets such as railings, portions of cladding, balcony doors and cause additional consequential work. The project budget for a balcony renewal project will also need to address the potential for structural repairs, consultant costs, access costs etc. This is discussed in more detail later on.

The transition from a renewal or major maintenance activity cost estimate for an asset, as found in a Depreciation Report, to a project budget, that a Strata can consider as a basis for raising funds, is significant and requires a high degree of planning and assessment. The additional planning required can be summarized in what is typically referred to in the industry as a “Design Study,” Design/Cost Study,” “Design Report” or “Design Brief.”

In the case of any significant renewal or major maintenance activity the need for and relevance of a “Design Study” should be identified within the tactical period to provide time to complete the study. There is no sense waiting for the roof to leak before considering what renewal options are available (analogies exist for hot water boilers, roof top air handling equipment, elevators, etc.).

An added twist to consider for enclosure renewals is whether they alter the appearance of the building. If the original appearance of the building is altered the approval margin (majority vs $\frac{3}{4}$) may be impacted. It is always advisable to have questions like this reviewed by legal counsel experienced with BC’s *Strata Property Act* well in advance of the proposed vote.

As a means of demonstrating the need and value of a “Design Brief,” consider the following typical scenario. A Strata with a 20 year old building obtains a Depreciation Report. The balcony membrane data provided in the Depreciation Report was accurately recorded. The membrane age was reported to be 20 years and the remaining service life was estimated at 1 year based on experience and observed conditions. An estimate of replacement costs was provided based on historical or local square foot values for the membrane asset. A reasonable estimate of the quantities was made and the estimated cost of renewal of the membrane asset was identified in the Depreciation Report as an activity recommended for the following year.

The actual age of the membrane was beyond its predicted service life, however in the absence of any significant reported problems (leaks) the Strata elected to defer implementing the renewal activity. The limited and initial observations made during completion of the Depreciation Report (worn looking seams and deteriorated surface condition) while sufficient to support an estimate of remaining service life, but were not compelling enough to move the Strata in the direction of a membrane renewal project. In a prudent manner the Strata did however approve the completion of a “Design Study” to further assess existing conditions, identify renewal options and develop project budget estimates. The Strata seeing the inevitability of membrane renewal in the future took the next step in working their initial plan. They are getting more information and advancing the plan!

During the course of completing a Design Study for a balcony membrane asset, additional field observations can be obtained by destructive testing to reveal concealed condition within balcony soffit spaces, base of wall locations, drain locations and at railing attachments. These conditions are seldom evident when a Depreciation Report is completed and Strata’s are often unaware of the conditions. It is therefore important for the initial work in a Design Study to closely resemble a detailed condition assessment of the building asset in question.

In the case of the balcony membrane renewal scenario, the additional fieldwork undertaken during the Design Study can and typically does identify a number of design issues requiring Strata input and additional consequential work that significantly adds costs to the project budget. Some of the more typical issues that can arise during the replacement of a balcony membrane include:

Balcony surfaces improperly sloped and ponding water on the balconies becomes a condition the Strata owners want rectified when the membrane was replaced. Corrections to the drainage issue become a design issue that results in additional framing, sheathing and plumbing costs that add to the project budget.

Door thresholds are often too close to the balcony surface and proper detailing of the membrane termination and/or correction of a balcony drainage issue results in the need to remove the doors and/or raise the door thresholds which adds costs to the project budget.

When balcony doors are removed or the door threshold is raised (over all door height is reduced), the Strata will need to consider options for either new doors built to fit the new door opening size, or modifications to the existing door opening to suite the existing door size. Either option will add costs to the project budget.

Water leakage through penetrations in the membrane at railing attachment points typically causes damage to the concealed wood sheathing and framing. The need for an alternate method of railing attachment is often identified even though the railings may not be at the end of their service life. Options to either modify the existing railings, or replace the existing railings can be considered but both result in additional costs added to the project budget.

Water ingress at the base of a balcony wall, where the membrane terminates, either at a membrane penetration or improper saddle detail can cause concealed conditions of wood decay. These problems can result in significant additional repairs to the exterior walls with added costs to the project budget.

In the presence of existing conditions such as poor drainage, improper membrane terminations and water leakage at improper drain and railing penetrations; it is easy to appreciate how a relatively simple sounding “membrane renewal” activity quickly builds into a larger “balcony renewal” project. The initial Depreciation Report may have drawn attention to the balcony membrane as the asset with the least service life remaining. It is however a “Design Study” that is needed to identify all the consequential work to address existing conditions, concealed damages, identify options for Strata consideration and develop project budgets suitable for the Strata to approval a project scope and raise funds.


The consequential work examples provided in this article are not meant to be exhaustive, or is the article intended to be used as a guide for planning balcony membrane renewal. There are also issues related to aesthetics that can be equally important to some Strata. While improving building appearance may not be the driving factor in a renewal project, the Strata should be aware of any opportunity to improve the appearance and value of the building when undertaking a significant renewal activity.

Will a balcony membrane renewal always be so

complicated? Not for the Strata in the above scenario. When balcony membrane renewal is required in the future the door thresholds will already be raised, railings will not interfere with membrane replacement and drainage will not be a problem. The future Design Study will be able to focus on developing a project budget for a much simpler project.

There is however no short cut to proper project planning and budgeting. Although every project will be different they all require similar steps that starting with high level planning used to identify broad timelines and costs (Depreciation Report) and moving to a variety of project specific reports (Design brief and then Construction Documents) that are used to more closely define scope and project costs.

More on the need and significance of Construction Documents later.



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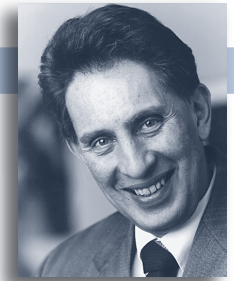
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The Case Against Formal Depreciation Reports

Gerry Fanaken, former CEO

VANCOUVER CONDOMINIUM SERVICES LTD.

I will admit at the outset of this article that it is a very difficult task to argue that strata corporations should not properly and adequately prepare sound financial plans for their future. Having been a strata property manager for some three decades, as well as being the CEO of a very large strata management company in Vancouver, I am all too aware of the absolute need to sock away large amounts of money to support predictable repair and maintenance requirements for a strata corporation. Indeed, many strata buildings constructed from the mid-1960s to the early 2000s were not very well built so not only are these properties going to need “normal” life-cycle repairs and replacement, they will also need to address design and original construction deficiencies. A lot of money is needed. I just am not so sure, however, that the highly-touted depreciation report pursuant to the current legislation is such a great solution.

First, a little background. Strata corporations came to life in British Columbia in 1966 under the first legislation, the *Strata Titles Act of BC*. The original legislation and the subsequent *Condominium Act of BC* in 1979 required that the Contingency Reserve Fund be calculated on the basis of 5% of an annual budget. It became clearly evident to strata councils and property managers that this level of allocation would be inadequate to address the long-term requirements of strata corporations. In fact, not only was such a percentage allocation inadequate in the first place, but also most corporations would use some of the CRF money from time to time for various special projects (some of which were not even in respect of long-term repair/replacement requirements). The net effect, therefore, was that the Fund never grew substantially and, when a major R&M project had to be done, the much maligned special levy was utilized to raise money. The provincial government was aware of this problem and when the *Strata Property Act* became law in July 2000, the allocation in the annual operating budget to the CRF was raised from the 5% level to 10%. Knowledgeable strata council members and property managers applauded the change.

The government, however, in the 1990s was also aware that

Gerry Fanaken is a 35 year condo owner, former CEO of Vancouver Condominium Services and author of *Understanding the Condominium Concept: An Insightful Guide to the Strata Property Act*.

a long-term reserve concept had benefits and would be extremely desirable but then came the horrendous leaky condo crisis which sucked vast sums of money out of the condo owners' wallets. Clearly, this was the wrong time to insist on mandatory reserve studies and resulting funding models. Accordingly, depreciation reports were merely a suggestion to strata corporations, not a mandatory requirement. Subsequently the July 2000 *Act* was further amended to mandate depreciation reports but strata corporations could opt-out by passing a $\frac{3}{4}$ vote resolution.

Notwithstanding the opt-out provision, many strata corporations have, over the past five years, undertaken depreciation reports. Not surprisingly, the numbers coming back from qualified professionals (such as engineering firms) have been staggering. Unlike other provinces which mandate depreciation reports **and** funding models, BC does not mandate actual funding once a depreciation report has been completed (although the Regulation to the *Act* provides an excellent model for any strata corporation that would wish to embark down that avenue). No statistics or other data is available to illustrate how many strata corporations actually advance beyond the initial depreciation report to a full funding model – a “30-year plan.” My guess is that only a small percentage of strata corporations do in fact proceed with such a financial plan, the reason being, simply, that the monthly strata fees would have to increase so significantly that it would be difficult to obtain owner approval at budget time (a majority vote) or at an SGM to raise money to supplement the CRF (a $\frac{3}{4}$ vote for a special resolution for a special levy). It would be most interesting and instructive to obtain empirical data on the outcome of these strata corporations leading the way.

And here then is the problem of depreciation reports as currently legislated. Sure, it is an excellent concept to require strata corporations to identify their future requirements but

since on-going funding is not mandatory, it is reasonably foreseeable that many strata corporations will not advance beyond step one to actually double, triple or quadruple their strata fees to generate funding. Ultimately, the reality will be that long-term major repair and replacement projects in most strata corporations will be funded by a combination of charges against the Contingency Reserve Fund and special levies, mostly the latter. The only way to avoid this scenario is to legislate mandatory funding and that seems to be an unlikely prospect.

Virtually all the publicity and discussion about depreciation reports over the past few years has been positive if not glowing. Nevertheless, many strata corporations are choosing not to do them, often with reasonable positions. They are quite costly and inevitably produce future cost estimates in staggering amounts. Once a depreciation report has been obtained by a strata corporation, it must be made available to prospective purchasers who request Section 59 Information Certificates, whether or not the owners decide to fund the long-term plan recommended by the report. It is quite conceivable that prospective purchasers will be scared away once they see either the huge strata fees (if funding of the plan has been approved) or the huge future liability (if funding of the plan has not been approved). Buyers will also be confused once they figure out that some strata corporations have depreciation reports while others do not. Which option is more appealing to a buyer: strata fees of \$800 per month in a strata corporation that has done a report and has implemented a funding regime or strata fees of \$300 per month in a strata corporation that has not done the report?

Notwithstanding the fact that the *Strata Property Act* is an excellent piece of legislation, the wishy-washy requirements in respect of depreciation reports is surely going to create chaos down the road. It is unlikely that the government will address the problem at this time by “standardizing” the requirements so that all strata corporations play by the same rules. In the meantime, real estate agents and prospective purchasers will be confused, unnecessary lawsuits might arise and an unlevel playing field will create frustration and misunderstandings. The statute must, therefore, be fixed.



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