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condominium **owners**

Timely ideas, insight, inspiration and information of particular interest to condominium owners

Cover Story

Why Are My Fees Going Up?

Understanding Your Condo Fees is a Crucial Part of Condominium Ownership

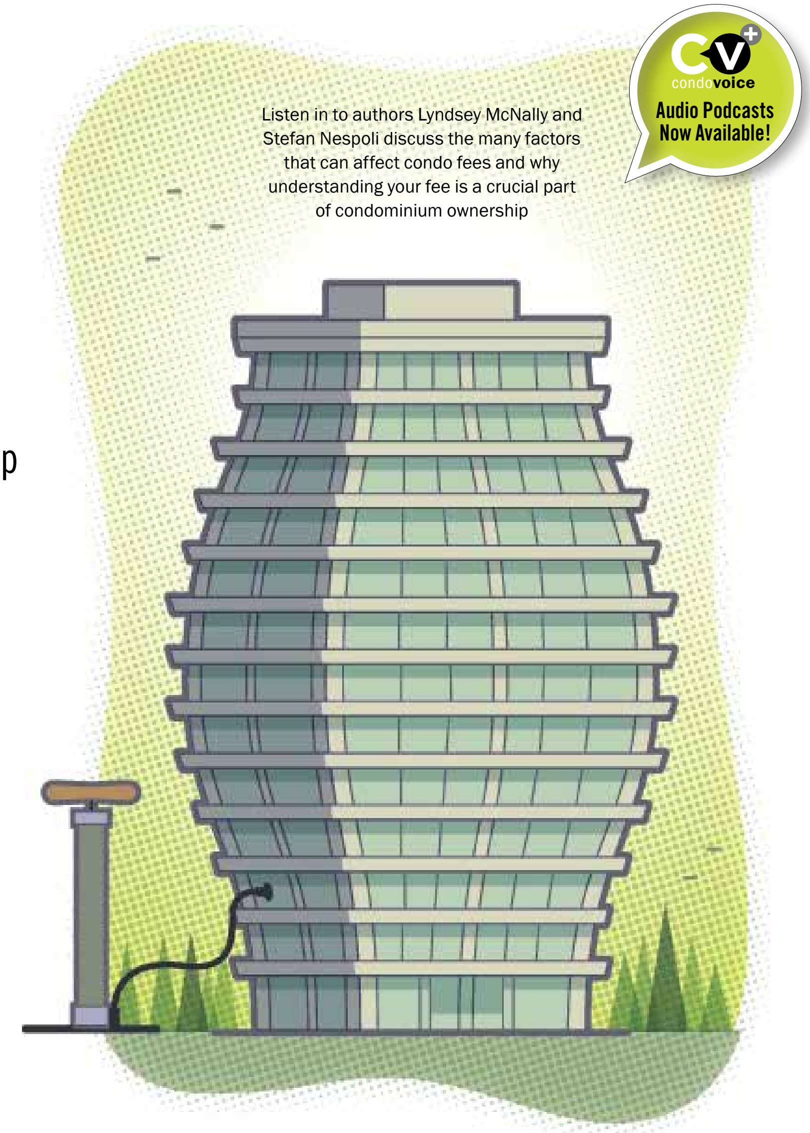

ILLUSTRATION BY CARL WIENS

Of This I Can Be Certain

In this ever-changing, uncertain world, it's impossible to be sure of anything – except death and condo fees. And of course – condo fee increases. But why do my fees keep increasing, sometimes substantially in just one year?

Understanding your condo fees is a crucial part of condominium ownership. It empowers owners with knowledge to make informed decisions, supports the building of a healthy and vibrant community, and sets a course for long-term stability for your Corporation.

What are Contributions made of?

The annual budget for a condominium corporation can be classified using two different funds – the operating fund for day-to-day expenses and the reserve fund for major repairs and replacements of the common elements.

The amount required for each fund varies significantly for different buildings based on social habits of residents, staffing levels, amenities, services provided by the corporation, construction style & materials, mechanical needs, building age, current fund balances, level of finishes, and the expectations of residents.

Factors Affecting the Operating Fund

It is challenging for condominium communities to keep fee increases low. It is important to be sure that in cutting costs, the Board of Directors isn't also reducing services for owners and residents or compromising on the quality of service being provided to the corporation.

Many Boards will try to aim to keep fee increases in line with inflation annually. This is a good goal, but sometimes not a realistic one. In fact, many costs associated with the operation of a property are rising at a rate much greater than that – let's look at some examples.

Legislative changes

We hope that all readers are aware of the changes to the Condominium Act, 1998 which took effect November 1, 2017. There are several more changes to be implemented in the future contemplated in the Protecting Condominium Owners Act, 2015. Additionally, the Condominium Management Services Act, 2015 is increasing costs for property management companies.

Consumer protection legislation such as this is important in our society – but readers should be aware of hidden costs. A good example is the rising administrative costs associated with greater communication requirements (i.e. PICs, NOICs & ICUs).

Increases in Service Contractor Rates

The condominium industry was hit hard when minimum wage increased in the recent past. This is because many service providers (security, cleaning, etc.) had to increase their rates to compensate. Staffing costs can represent a large portion of an operating budget, especially in a residential hi-rise with multiple full-time and 24/7 personnel.

Addition of Services

Many communities are becoming more mindful of safety and security, especially with the current rising gun violence in the City of Toronto. The addition of extra security (cameras, equipment, or staff) can play a big role in increasing fees and no, these "new" items cannot be expensed from the Reserve Fund!

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There may also be other services which are added to the operating budget increasing the overall fees. It is important to note, however, that with these increasing costs there is a direct benefit to owners – the addition of services.

Boards should consult their legal team prior to making a substantial addition however as there may be notice and/or voting rights for owners under Section 97 of the Condominium Act, 1998 (the "Act").

Insurance

At the time of writing this article insurance is a hot topic. It is said that for many years the insurers tried to keep the cost of premiums in the condominium market low. As a result, insurers were not making money due to a high level of claims. Now a market correction is happening. Even with no claims history, many condos are seeing large increases in both premiums and deductibles.

A large increase in rates surely gives sticker shock and can be difficult at budget time, but the increasing deductibles shouldn't be ignored as a cause for financial concern. Let's say a small corporation has a $100,000 deductible and more than one claim in a year. That would likely result in a special assessment or a large common expense fee increase to absorb the deficit it would cause.

Utilities

Carbon tax, government rebates, delivery charges, submetering, retrofits, incentives, rate tiers, time of use, EWRB, benchmarking?!?!?!?

Very few people can be called experts at forecasting utility rates. The reality is that utilities in recent years have increased at a rate much higher than inflation. Your typical high rise might have 10-25% of the total budget being utility consumption. Even minor increases can have a major impact.

There are some strategies that can be used to reduce consumption, reorganize your billing structure, and lock in rates. An expert in utilities can provide guidance and calculate returns on investment as many utility changes come with upfront capital cost.

Factors Affecting the Reserve Fund

Like with the Operating Fund, Boards face pressure to keep Reserve Fund contributions low as well. Ironically, the oft-feared "Special Assessment" becomes more likely when Corporations have artificially low contribution levels, and don't have money available to fund required repairs. Underfunded condos are becoming such a widespread issue that it's given rise to a condominium loans industry and has been identified as a priority for the Ontario Government to review – with CCI input – in 2020.

All condo corporations must collect funds one way or another. Understanding why Reserve costs have increased will help Boards improve their communication with owners and allow them to work together to maintain your shared home. Below are some examples.

New Corporations

Minimum contributions for new Condominiums are set by the Act and are typically around 10% of anticipated first year operating expenses. This minimum is too low and requires increases to establish an adequately funded reserve. Industry norm Reserve Contributions are typically 20-30% of operating costs or higher depending on the type of building, number of amenities, and size of units. The adjustment from 10% to above 20% typically takes place in Year 1, following completion of the first Reserve Fund Study.

Term of Study

The Act currently stipulates that Reserve Fund Studies provide a recommended funding plan projected over 30 years. Although 30 years may seem like a long time ("I won't still be living here 30 years from now!"), contributions for newer Corporations are often driven by major repair projects beyond 30 years including windows, exterior cladding, and some mechanical systems.

These projects can have massive costs relative to other component replacements, and result in Reserve Fund Studies that recommend very high and increasing closing balances over the entire 30-year study period. Understanding what you're saving for will help you communicate with your owners.

Unfortunately, some Reserve Fund Planners may not even anticipate for funding of costs beyond the 30-year report term. As a result, these future costs will creep into your study with future updates and require fee increases. Who doesn't like surprises?

Inflation and Interest Assumptions

Inflation and interest rate assumptions are updated with each Reserve Fund Study update. Historically, interest rates have typically been higher than inflation rates, however, over the past several years interest rates have been very low while construction inflation remains relatively high.

Review the spread between these assumptions regularly. If the assumed inflation rate is higher than the assumed interest rate, higher contributions are required. Conversely, if the interest rate is assumed to be higher than the inflation rate, then lower contributions are required.

Changes in Planned Repair or Replacement Cost

Repair and Replacement costs largely consist of materials and labour. Unfortunately, the cost of both are rising faster than typical consumer price index inflation that we hear about on the news. Inflation cost increases for materials including asphalt (e.g. pavement, shingles), glass & aluminum (e.g. windows, doors), and vinyl (e.g. siding, windows) contribute to rising condo fees. Similarly, provincially legislated increases in minimum wage and high demand for skilled labour have resulted in rising labour costs. Your Engineer should be tracking and updating cost estimates based on actual recent repair and replacement projects.

Changes in Planned Repair or Replacement Timing

Useful Life is established by your Engineer's experience, adjusted by assumptions for quality, rate of wear and tear, expected normal maintenance and exposure. Remaining Useful Life is established primarily by the component's current observed condition and performance. This observed age may not be equal to the chronological age of the components, due to accelerated wear or low usage. For components requiring specialist expertise, or where age characteristics are not visible, your Engineer will typically interview the Corporation's service contractors and obtain their assessment to help establish Useful and Remaining Useful Life. In some instances, additional review is required to clearly define scope and budgets.

Changing Legislation

Legislative changes are expected to address some of the items above, including a realistic Reserve Fund contribution level for new condos, an extended 45-year report period, and clarity on how Reserve Fund Studies are conducted and how contribution increases are established. Reviewing these items and soliciting stakeholder input is a stated priority of the Ontario Government in 2020, although the implementation timing of these changes is not known at the time of writing.

How can we keep our contributions low?

Although most of the items listed above are outside of the Board's control, here are a few items you can control that will help keep your contributions low.

Operating Fund

- Tender Service Contracts: Soliciting quotes every 3-5 years helps keep your contractors sharp and engaged in earning your business.
- Review Goals Together: If high condo fees are a topic of discussion at your AGMs (or even if they're not), review your Operating Budget as a community to identify opportunities for savings.
- Actively Look for Savings Opportunities: Don't take the stance that "this is how we've always done it". Can you save costs by leveraging technology? Are there rebates or incentives for projects that would save operating costs?

Reserve Fund

- Be Proactive: Perform regular preventative maintenance and proactive repairs at your property to help defer major repairs or replacements. For example, have your roofing system reviewed and repaired annually.
- Adjust Expectations: Some communities want their building to look brand new, even if it's 25 years old. Sometimes a repair or retrofit (i.e. for windows or asphalt pavements) can make more sense than a full replacement. Repaired components won't look as nice or perform as well, but despite what some owners may think, they can't have it all.
- Review Long Term Financial Impact: Before investing in large repair or replacement projects run a few funding scenarios to check the impact on fees over the long term. For example, before investing in a major window refurbishment program check out if replacement would be a better long-term strategy. It may make sense to not spend any money now and plan replacement sooner.

What is the Right Contribution Rate?

Work with your Property Manager and Engineer to set condo fees just right – setting them too low presents a high risk for special assessments, while setting them too high can negatively impact property values. Your annual budget is prepared by combining planned Operating and Reserve expenditures, and should strive to provide:

1. Sufficient Cash to meet your planned expenditures;
2. A Healthy Operating Surplus to ensure that you can rise above unexpected costs;
3. Stable and Evenly Distributed Contributions to assist with financial planning and making sure current and future owners all pay their fair share; and
4. A Fiscally Responsible Plan, meeting the requirements of the Act and in the best interests of the Corporation. CV