

**Reserve Fund  
Whizdom  
BY  
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You can be a “whiz” with reserve fund issues — whether you’re a Board Member, Property Manager, Reserve Fund Specialist or Accountant. Read our short articles, think about what we’re saying, agree with us and adopt the advice, or debate and argue another viewpoint. You’re sure to end up better for it.

Today’s Whizdom is all about —

**Your Reserve Fund’s  
Shock-Absorbers**

Most of the time we think of a reserve fund as a cache of money to be used, when required, to handle major repairs and replacements. Not a bad description really, but perhaps it would be more accurate to see it more as three caches of money that are in place for three eventualities.

Let’s call them three “shock-absorbers”.

The first one — and it’s one that almost everyone would think of right away — is a shock-absorber to even out the “bumps in the road” when the big bills come in. A good reserve fund plan shows relatively smooth owners’ contributions, even though the expenditures from the fund are bumpy — more volatile. Thus, by planning carefully, a few years of high costs would not result in high fees, because the high costs were anticipated. They were “saved for” earlier so they wouldn’t be unduly burdensome when they occurred.

That’s the shock-absorber effect at work in a well-managed fund. It’s sensible, and it works.

But there are two more shock-absorbers that should be in your plan.

One of these addresses the problem of expenditures almost never being quite what they were expected to be. Even the most experienced and professional Reserve Fund Specialist would admit that histories of actual payouts versus the costs that were forecast will show that expected-to-actual variances were normal, throughout any period you chose to examine.

We all know why. Costs come in at levels that simply were not the levels you expected. More work was necessary to do a job than the planner predicted. Happens all the time. Or repairs planned for 2009 became necessary in 2006.

Doesn’t mean the plan was “no good”. It’s a fact of life that forecasts are always wrong. Luckily, most of the time they’re wrong by tolerable differences, (and sometimes they’re not), but they’re wrong just the same. Hence the need for Buffer Number Two — another shock-absorber.

What this means in practice is that you should not plan your reserve fund balances “too close to the line”. In other words, if you could rely 100% on the fact that all the estimates of costs — their level, and their timing — were correct, you

could literally run you balances in some years at close to zero. You'd "know" that going over estimate was not going to happen, so you'd "know" you'd be safe from going in the hole.

But in reality you cannot know this, so you have a shock-absorber to, essentially, take care of the forecast-to-actual variances that are sure to occur.

Now for your third and final shock-absorber. It's a bit like the last one, but, if anything, bigger. It's the shock absorber you might want to have to handle occurrences that are totally unexpected. At least in the second example just above, you did expect a repair cost, it's just that the amount of it and the timing of it was off. In this case you are blind-sided by a driveway that caves in due to an underground stream you didn't know was there, or the discovery that inferior metal was used in the stress rods for the garage floor and they have all rusted. Or that winds reached a velocity never before experienced in your area and badly damaged the roof.

Yes, we know, you can't just have a couple of hundred thousand dollars lying around just in case of a highly improbable contingency. But these kind of events usually call for at least some emergency work and a few thousand dollars would be just the ticket to get it done fast, before a loan or special assessment or even an insurance payment were arranged for.

Our lessons for today. Don't rely, more than you should, on the exactness of your expenditure predictions. Don't plan for a reserve fund that runs its balances too close to the line. Don't dismiss the idea of having a little extra put away for the true emergency situation, should it ever arise.

There's a related question, of course. It's ... given the principles above, how do we calculate the right amounts to keep our reserve funds consistently healthy? We've tackled that in a companion article called ... "Reserve Fund Balances — What Does 'Adequate' Mean?" Take a look at it. We're sure you'll enjoy it as much as this one!

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Graham Oliver is President of Oliver Interactive, Inc. the developer and supplier of RFund: The Reserve Fund Manager. He invites you to read other Whizdom articles on the RFund website, and he encourages you to let him have your views on his writings. Visit [oliver-goup.com/rfund](http://oliver-goup.com/rfund) anytime.