



Reserve for Replacement

OHCS Asset Management & Compliance File

CDM Memorandum 8.T1

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8.T1.01_ Overview

This memorandum covers Department administration of restricted financial resources that are required to be held in reserve by the property owner for the purpose of covering capital replacement and/or and other extraordinary costs connected with a given property.

8.T1.02_ Authority

1. Authority through Loan Documents and HUD
Oregon Housing and Community Services (OHCS) (the “Department”) Loan Documents, and HUD 4350.3, HUD 4350.1 (where applicable).
2. Authority through OHCS Finance Committee
The Finance Committee is a sub-group of the Department’s Executive Team that includes managers and program managers and functions in an advisory capacity. The Committee is responsible for reviewing policies as they pertain to OHCS’ lending practices, financial analysis of grants or loans and tax credit allocations, awarding of real estate loans or grants, and recommendations pertaining to underwriting criteria and approval limits, as well as other matters as determined by the Executive Director. Members act as advisors to the Executive Director in an effort to protect the assets of the Department as it pertains to affordable rental housing transactions and portfolio issues.

8.T1.03_ Applicable Programs

All multi-family rental housing projects financed solely through the Department, except for the Conduit Pass-Through Revenue Bond Program, are required, as outlined in loan documents, to allocate and maintain a specified amount of funding reserved for planned long-term major repairs, replacements, and unexpected expenses necessary to maintain the physical asset.

8.T1.04_ Purpose of Reserve for Replacement (RFR)

A Reserve for Replacement (RFR) ensures sufficient funds are available to pay for operating expenses, debt repayment, and other obligations, including the maintenance of required reserve and escrow accounts before Break-Even Occupancy and to fund extraordinary maintenance or repair and the planned replacement of capital items. The RFR is funded through property rent and other property revenues. The RFR resource is expected to be used to maintain the condition of the property throughout the affordability period and therefore cannot be used for anything other than to benefit the residents by supporting the property’s needs.

8.T1.05_ Definitions

Break-Even Occupancy:

A property’s breakeven Occupancy Rate is the minimum occupancy rate threshold of a property to ensure its operating expenses and debt service obligations are met, expressed as a percentage.

Capital items: Capital Outlay shall include any purchase that will add to the value of improvements or extend the life of a capital asset, including, but not limited to, additional structures, improved fixtures, energy efficiency

improvements, innovative technology, machinery, appliances, stock, or furniture, unless otherwise defined in the Loan Documents.

Capital Assets shall include purchases with an initial life beyond a year and an initial cost of at least \$5,000. If Capital Items are not defined in the Loan Documents, the above definition shall be used.

Extraordinary Repair or Maintenance: Extraordinary repair or maintenance is the maintenance or repair that will result in extending the item's life for five years or longer.

Loan Documents: Loan Documents shall include the Project's loan documents, including, but not limited to, the Promissory Note, Trust Deed, Regulatory Agreement, Loan Agreement, Management Agreement, Commitment Letter, Side Letter (if any), and State Housing Council Write-Up.

Management Agreement: Management Agreement shall mean a management agreement between the Borrower and a management agent, as approved by the Department, or between Borrower and the Department, if Borrower is acting as the management agent for the Project. The agreement will identify the terms, conditions, and covenants that must be adhered to in a reasonable and prudent business manner.

Reserve for Replacement "Account": Reserve for Replacement Account (RFR Account) is a dedicated account established upon the first mortgage payment and under the authority of the Department, or in a depository designated by the Department. The Borrower must maintain a specified level of reserves in the RFR Account as defined by the loan documents, by making deposits as prescribed in the Loan Documents. Disbursements from the RFR Account can only be made with the written approval of the Department.

Reserve for Replacement "Job": A reserve for replacement "Job" refers to the replacement of a combination of item(s) that would not individually qualify for reimbursement under the RFR Account. This combination of item replacement would need to be completed within 30-days for the same unit, which would allow the item(s) to qualify for reimbursement.

Example: Unit 1 had a mini blind, dishwasher, and toilet replaced. Individually these items would not likely qualify for reimbursement, but as a "Job" the combined cost may be eligible.

Reserve for Replacement "Project": A reserve for replacement "Project" includes replacement of a combination of item(s) that would not individually qualify for reimbursement from the Account but are covered under one contract or invoice within a 90-day period. When combined, the item(s) would qualify as a project, making it eligible for reimbursement.

Example: Units 1, 3, 5, 6, and 9 received replacement dishwashers. Individually the dishwashers may not qualify for reimbursement, but as a "Project," they provide adequate replacement costs to be eligible.

8.T1.06_ Minimum Balance Requirement

Borrowers have five (5) years to establish a two-year balance in the replacement reserve account, determined by the initial deposit amount x 24 months (only 12 months for Elderly and Disabled Bond funded properties).

The annual replacement reserve amount for each property will be evaluated during the Department annual financial review for consideration of a 3% increase each year.

No maximum account balance shall be determined unless a limit is established in the property's loan documents.

8.T1.06__Acceptable Use of Account Funds

The acceptable use of the Account is, unless otherwise defined in the Loan Documents, outlined in Exhibit A, and includes:

- Replacement of Capital Items.
- Replacement of parts if:
 - (a) The part increases the original estimated life of the fixture or appliance by at least five years; or
 - (b) The part qualifies for replacement as described in the Loan Documents; or
 - (c) It is more cost-effective to repair the fixture or appliance than it is to replace it and it meets the requirements of the Loan Documents.
- Extraordinary repairs or maintenance (as identified in Section 5).
- Replacement qualifies as a reserve for replacement “job” or “project.”

8.T1.07__Extraordinary Repairs and Maintenance

Extraordinary maintenance or repair is an expense that is expected to result in extending the useful life of the property and its items for at least five years or, improvements to enhance livability or, to increase the project’s value or, to improve the marketability of the development, such as the following:

- Purchase of a van to make transportation more readily available to the residents.
- Purchase and installation of energy-efficient improvements (i.e., heat pump)
- Addition of a solarium or activity room to an existing facility.
- Purchase or addition to playground equipment.
- Improvement of the security system.
- Construction of a greenhouse for the residents.
- Remodeling of units to increase their livability and marketability; and
- Improvement of the access to the development or its visibility to make the development more marketable (i.e., new signs, etc.).

Repairs or maintenance of items necessary for the upkeep of property and equipment. Repairs are considered routine and do not qualify as extraordinary, as described in Exhibit A-2.

8.T1.08__Emergency Repair

If the repair is an emergency, the Department may grant verbal approval (i.e., over the telephone or via e-mail). An emergency replacement or repair item must relate to the following:

- (a) Requires immediate action to remedy.
- (b) Threatens the safety or well-being of the tenant(s) or the property; and
- (c) The cause could not have been foreseen by an industry professional in the same or similar situation, such as a tree blowing over in a strong wind crushing a roof; a pipe burst and causes flooding; the failure of a heating system, etc.

Use of the RFR for an emergency repair will be made at the Department’s discretion, upon receipt of supporting documentation. The Department may also request additional documentation indicating what portion, if any, of the repair will be covered by insurance.

8.T1.09__Request to release Funds General Information

1. Compliance with Loan Documents

The request to release funds must comply with all regulatory documents including the Loan Agreement, Regulatory Agreement, and the Management Agreement. The Management Agreement defines the expense authority given to the management agent. If the request exceeds this authority, written approval from the designated owner must accompany the request for reimbursement.

2. Requests in Excess of \$10,000

All contract and/or invoices for which reserves are requested that are individually, as a job, or as a project, in excess of \$10,000 must include three bids/estimates, unless otherwise approved by a Senior Asset Management Analyst from the Department who may request alternative estimates from third parties if the cost appears inconsistent with comparable costs. The Department will review the bids prior to submission to Management for authorization to issue written approval/denial of the request.

3. Planned Improvement Projects: Structural, Construction and/or Capital Improvements

Requests for projects that involve investment in structural modifications/additions, accessibility, building envelope, or restoration require review and approval by a Senior Asset Management Analyst from the Department prior to issuing approval. This approval is expected to be obtained in advance of project initiation to avoid unnecessary inspections or costly changes that may be required to ensure regulatory requirements are met.

4. Account Balance Below the Minimum

If the request to release reserve funds will decrease the Account balance below the required minimum balance, a Senior Asset Management Analyst from the Department may consider approval upon review of a Capital Needs Assessment (CNA), a Capital Improvement Plan, or other property assessment tool, as well as an analysis of the financial performance of the property with regard to its ability to re-establish the minimum required balance.

5. Timeline to Review and Respond to Request for Reimbursement

All completed requests for the release of Account funds shall be reviewed and responded to by the Department within 30 days of receipt of a completed request. Exceptions to this include requests that require in-depth analysis due to the technical nature of the request or the volume of the request. Incomplete requests may be returned to Owner and/or Agent for resubmission.

8.T1.10 Process to Request Release of Funds

All requests must be submitted by the Owner and/or Agent through the Reserve for Replacement **Portal** using the following link: [Reserve for Replacement Request Portal](#).

The following list includes the necessary documents required to release funds:

- (a) Reserve for Replacement Request **Form** using the following link: [Reserve for Replacement Request Form](#)
- (b) Invoices dated within the most recent 12-month period.
- (c) A complete description of the Capital Item, extraordinary repair or maintenance, or improvement item.
- (d) An itemized cost of the Capital Item(s), extraordinary repair or maintenance, or improvement, as well as request total (after applying insurance proceeds or expected insurance proceeds, when applicable).
- (e) Specific unit numbers, when applicable; and
- (f) Justification that the item is either an extraordinary repair or a maintenance replacement of a Capital Item (or is an improvement item).

8.T1.11 Increases to the Account or Establishment of Additional Reserve Accounts

In addition to the provisions in this Policy under Section 3, account deposits may be increased as provided for in the Loan Documents, or only upon financial review by the Department's Asset Management.

Owner and/or Agent is expected to perform an analysis at least annually of the Account and consider the adequacy of the balance and contribution on an ongoing basis. Any increase in contribution must be approved by the Department's Asset Management in advance of implementing an increase establishing a new deposit amount.

8.T1.12_Suspension of Monthly Deposits

Requests to suspend deposits to the Account may be made by the Owner when the balance has reached the amount stated in the Loan Documents. Once the balance drops below that amount, the Borrower shall resume monthly deposits until the balance again equals the amount stated in the Loan Documents.

8.T1.13_Investment of Account Funds

Account funds must be fully insured by the FDIC or invested in direct obligations of the federal government satisfactory to the Department. When the balance in the Account exceeds the minimum level required by the Loan Documents or \$250,000, whichever is less, the Borrower may direct the Servicer to invest a portion of the funds, subject to the Servicer's approval. For further information concerning the investment of funds, the Department's Servicer should be contacted.

EXHIBIT A – RESERVE FOR REPLACEMENT ITEMS

Section A-1: Eligible Replacement Items

When submitting for reimbursement, the total cost of the following items may include labor and must meet or exceed a minimum of \$5000.00, or an amount specified in the Loan Documents, with the exception that the Department may waive the minimum at its sole discretion. These submissions may have items batched together if the submission is for a single “Job” or “Project” (see Definitions), and not a collection of randomly completed repairs/replacements.

**These items are exempted from (do not need to meet or exceed) the minimum total cost.

Eligible Replacement Items	Expected Useful Life (Years)
Appliances:	
Air Conditioners in Units (must be professionally installed) **	10 –15
Dishwashers (must have been installed originally)	10 –15
Exhaust Fans	8 –10
Laundry Washers and Dryers	10 –15
Ranges**	8 –15
Refrigerators**	10 –12
Water Heaters in Units**	7 –15
Interior Furnishings:	
Cabinets and Countertops (entire kitchen and bath)	15 –20
Carpet	5 – 10
Drapes, Shades, Blinds, Rods	5 – 20
Doors	15 – 20
Electrical Fixtures	20 – 25
Floor Tile and Vinyl	10 – 15
Exterior:	
Asphalt – Resurfacing	10 – 15
Asphalt – Sealcoating	5 – 10
Concrete Walks and Curbs	15 – 25
Doors	15 – 20
Downspouts, Gutters, Roofing, Shingles, Tile, etc.	15 – 25
Painting	5 – 10
Siding	15 – 20
Sprinkler System	20 – 25
Storm Windows and Patio Sliders	15 – 20
Windows	15 – 25
Plumbing	
Bathtubs	20 – 25
Bathroom Sinks	20 – 25
Fixtures	30 – 40
Kitchen Sinks	25 – 30
Plumbing Systems	40 – 50
Toilets, Valves, etc.	20 – 25

Eligible Replacement Items	Expected Useful Life (Years)
Air Conditioning Equipment	
Chillers	5 – 10
Compressors	5 – 10
Fans, Motors, etc. (central air systems only)	10 – 15
Heating System	
Baseboard Heaters (entire unit)	15 – 25
Boilers	20 – 30
Central Heating System	5 – 15
FWA Gas Furnaces	15 – 20
Pumps, Valves, etc.	15 – 20
Miscellaneous	
Computer System – Initial Set-Up (excludes upgrades)	5 – 10
Copiers, Fax Machines, etc.	5 – 20
Elevator	20 – 30
Energy Conservation Items	5 – 30
Safety/Security Systems	15 – 20
Smoke Detectors	15 – 25
Swimming Pools	15 – 25

Section A-2: Ineligible Reserve for Replacement Items

The following items are INELIGIBLE for reserve for replacement reimbursement, unless the Loan Documents specifically allow for reimbursement (i.e., “painting and decorating”):

Ineligible Reserve for Replacement Items
Equipment and fixtures
Golf Carts
Tools
Vacuum Cleaners
Weight Room Equipment
Plumbing
Plumbing Materials (including hoses, cesspool/septic system maintenance, etc.)
Toilet Seats (unless replacing entire toilet)
Interior Furnishings
Interior Painting (including supplies such as paint rollers, masks, putty knives, etc.)
Molding Replacement (unless result of flooring replacement)
Electrical
Replacement of Breakers, Switches, Outlets, etc.
Miscellaneous
Asphalt Patching
Landscaping Supplies and Shrubbery
Re-keying Locks
Roof Maintenance (i.e., moss removal, installation of zinc strips, etc.)