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Understanding the Replacement Reserve

What You Need to Know



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The Replacement Reserve is a fund used to replace or repair *capital items*.



What are Capital Items ?



- There are different kinds of capital items in a housing project, and most of them have long life spans. They consist of:
 - major building and property components, services and systems;
 - project facilities and equipment; and
 - items that require major repairs or renovations.
- The useful life of capital items end when repairs or maintenance will not significantly extend their useful life. For more information, please refer to the checklist *Replacement Guidelines and Average Useful Life of Building Components*.

How is the replacement reserve funded?



- The replacement reserve is funded through an annual or monthly transfer from a First Nation's operating budget.
- Money for the replacement reserve, along with accumulated interest, must be held in a separate bank account and/or invested only in accounts or instruments insured by the Canada Deposit Insurance Corporation or as mutually agreed upon by the First Nation and CMHC.

One replacement reserve for all projects (Post 96)



- Under the Post-96 Program, a First Nation can have only one replacement reserve for projects committed, regardless of the number of commitments.
- Replacement reserve funds can flow from one project to another at a portfolio level, and they may also be pooled for investment purposes.



How much money should be contributed to the replacement reserve?



- The amount to be transferred, which is an eligible operating expense, is the amount set out in the operating agreement, or another amount approved by CMHC.
- The replacement reserve allocation may be increased at the discretion of the First Nation, within subsidy limits, taking into account viability considerations.

Eligible items to fund from the replacement reserve



Major components (exterior)	Major building services	Basic facilities	Safety features	Other major facilities, equipment
Roofs	Heating systems, boilers, furnaces, fuel burning systems, chimneys	Kitchen facilities (stoves, refrigerators, sink and faucet installations, countertops and cabinets)	Fire alarm systems and smoke detectors	Garages, storage areas and driveway, walkway and parking surfaces
Painting / stucco			Required firefighting or fire prevention equipment	Interior floor coverings, including common areas
Doors and windows	water tanks, pumps	Bathroom facilities (toilets, sinks and fixtures, vanities, and tubs and fixtures)	Emergency lighting	Exterior fences
Caulking in restricted areas	septic tanks		Other safety items	Laundry equipment
Steps, landings, railings	HRV			Water softeners where required

Eligible Extensions to the Standard List



- repairing foundations or significant sections of foundations
- structural components such as wall, floor and roof framing
- brickwork
- retaining walls
- plumbing systems
- electrical installations, including project transformers and emergency generators
- balconies



When should a capital item be replaced?



- A capital item should be replaced when:
 - It is no longer performing or operating as it was meant to;
 - It is no longer cost-effective to maintain; or
 - It is no longer safe (represents a health or safety hazard)
- A capital item should also be replaced when a change introduced through a bylaw, building code, safety standard or other requirement introduced by the First Nation makes it so that the capital item no longer meets requirements.

Replacing Capital Items



- Capital items should be replaced with items of equivalent quality, standards of performance and expected useful life, unless:
 - A higher-quality replacement is more cost-effective because it is expected to last longer or have lower maintenance or operating costs. In this case, higher costs should be recoverable within five years.
 - The capital item being replaced was not appropriate due to climatic, geographic or other factors.

What costs cannot be paid using funds from the replacement reserve?



- Costs related to routine and preventive maintenance or repairs to keep housing in good operating condition and to preserve the expected useful life of capital items. These should be funded out of the maintenance component of the annual operating budget.
- Capital items that have been damaged or destroyed from abuse or vandalism.
- Costs related to replacing building components or mechanical services that are still functioning well, meet all regulatory requirements, but would not meet building regulations and codes for new construction.

What are the reporting requirements?



- Replacement reserve funds must be audited annually and reported in the annual financial statements.
- Once the loan has been paid in full, or upon expiry of the amortization period, the project operating agreement will end. Any replacement reserve funds will remain with the First Nation to be used for the continued benefit of the housing portfolio.
- Adjustments to the required replacement reserve fund balance are to be made and reported in the annual audited financial statements.

Thank You



*To be filled in by CMHC
staff – contact info, etc.*