

## The issues with sinking funds

difficult to forecast

lost opportunity cost

not a user pays approach

## THE ISSUES WITH SINKING FUNDS

Sinking funds have been proclaimed the saviour of strata buildings in recent times. Whilst we believe there is a place for sinking funds to cover unexpected expenses – **they are not a user pays system**.

### Who benefits?

What happens if you've contributed a significant amount over a number of years and then sell your property and the money has not been used for anything? Why contribute personal money to a sinking fund if you do not have the opportunity to benefit?

Your asset has not improved in value, which would have given you a higher sale price; you have not enjoyed the lifestyle benefits; or have not been able to achieve high rental or lease returns because of the improvements.

### It's not an investment fund

It's smart to try to gain as much interest on the balance of sinking funds. However some owners corporations use their sinking fund like an investment fund, building it up and trying to find attractive rates to invest in without risk.

While this is fine in the due course, in many cases the fund is often wasted, sitting around often unused or only achieving a poor return.

A sinking fund is not an investment fund. Individual owners valuable money is better served realized as improvements to their asset – the building, or invested elsewhere for higher returns.

The main issues with sinking funds are:

- The vast majority of schemes have insufficient funds to carry out obligatory repairs and maintenance
- Owners are reluctant to increase contributions to the needed level
- Sinking funds can only attract inadequate returns on funds invested
- There is an opportunity cost to owners as money contributed could be used elsewhere to generate higher returns.
- Sinking funds can be unfair, especially if contributions made by an owner are not converted into building improvements while they own the property. Often new owners have to contribute larger amounts to pay for the mistakes of the past.
- Despite the introduction of analysis plans it is extremely difficult to estimate and budget for an appropriate level. No one can plan for every building issue that may occur.

### Recommendations

Don't over contribute to your sinking fund.

Funding works today saves significant amounts on rising buildings costs (from 5 to 15% pa) and is more effective than saving.

Look at ways you can gain maximum return on your current sinking fund.

Educate owners about a user pays approach that is more equitable.

Carry out repairs and maintenance regularly to avoid significant expenses.

### Questions or help?

Contact us on 1300 301 068 or visit  
[www.stratafinance.com.au](http://www.stratafinance.com.au)

