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COMMON THREADS FROM CHURCH LOAN UNDERWRITERS

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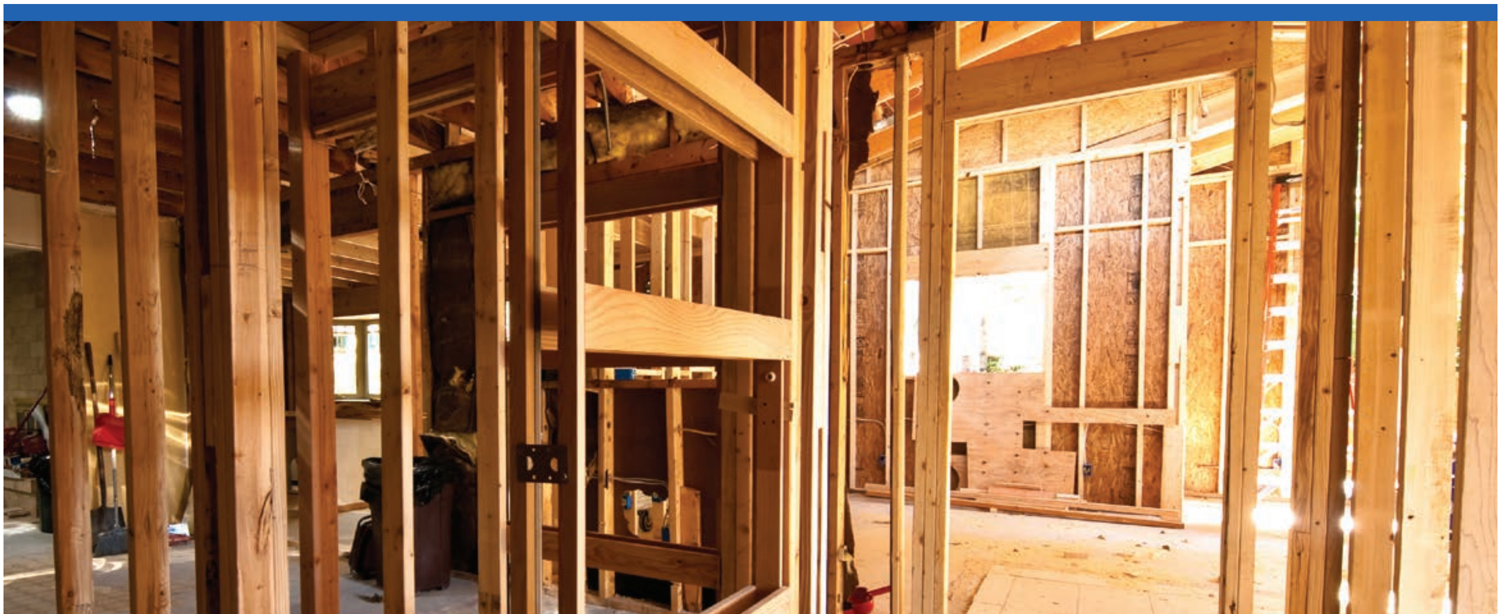

Second in a series

Our first post discussed making an apples-to-apples comparison of loan offers and mortgage options.

In this second post, let's dive into a discussion of construction costs, specifically those construction costs that don't add a dollar-for-dollar increase in value at the end of a project.

Common Thread No. 2: Understanding which construction costs don't add to property value

This can be a hard pill to swallow. Churches work so hard to be good stewards of their funds. Healthy, growing congregations and parishes often face the need to expand, update and maintain their facilities. Construction and renovation projects can be a financial stretch, as well as require a great deal of time and energy for both staff and volunteers.

The majority of these projects also require an element of financing. (Check out our article on financing projects.) It can be frustrating and puzzling when the cost of the project and the increase in property value are far from the same.

Let's look at some of the most likely culprits to cause this difference.

- **Soft costs –** These are primarily expenses related to expertise or services necessary to complete, or even begin, a project. Architectural fees, permits, legal fees and engineering costs can add up quickly. In complicated new site construction, they can be around one-third of the project. Unfortunately, when these expenses are incurred, they are rarely reflected in the market value of the property when completed.
- **Maintenance –** Maintenance items like carpet replacement, parking lot repair or painting do more to maintain the value of a church property than add to it. Wouldn't it be great if the expense to update your ceiling insulation added directly to the value of your home? Similarly, with churches, these expenses are not accretive in value. However, if left undone, they decrease the appraised value.
- **Furnishing, fixtures and equipment –** The good news is that this category does have an impact on appraised value. The bad news is that it is rarely a dollar-for-dollar increase. Items that may not stay with the building if ownership changes are generally not included in the value, but items that are built into the structure generally **do** add to the value. Items that become outdated quickly, such as built-in live-stream technology, will add value. However, because these items will require replacement or upgrades, the increased value is typically incremental. Upgrading fixtures and furnishings, such as adding high-efficiency lighting in common areas, may increase the value, but often the benefit is from the efficiency over time rather than from the increased value.
- **Environmental remediation** – If an environmental study or search uncovers issues requiring cleanup or restoration, the owner is required to remedy the problem. Not only can this cause delays to your project and add cost through delays, the work can be expensive. It may feel like an investment in the property, but most often this is an expense that protects the value rather than increases the value.

It's important to remember that these are generalizations and appraisals are subject to markets, which shift over time.

As you can see, this is not an exhaustive list of costs incurred for a construction or renovation project. If your project includes demolition, it's generally clear that the demolition expense doesn't impact the value of the replacement building. It's understandable that items like financing costs or consulting fees are outside the scope of an appraisal. Sometimes we need to remind our congregations, church boards or other vested parties that the total expense of a project does not equal the market value of the finished product.

Having examples and logic applicable to your situation can often help decision makers and donors get comfortable with the out-of-pocket expenses that don't equate to dollar-for-dollar increases in market value.

Next in our series

Common Thread No. 3: Understanding why different income sources are valued differently by an underwriter.

And, in case you missed it, the first post in this series was Common Thread No. 1: Understanding the differences in financing options.

Considering a church project?

You may also be interested in our post Financing Projects: Borrowing vs. Capital Campaigns.

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