



Buyer Beware...

What the Church needs to Know about Construction Accounting

Buying design and construction services has never been an easy task for the church. In today's economic climate, the challenge has become exponentially harder as struggling builders are becoming increasingly "creative" in how they account, or represent, the various expenses associated with building a place of worship. We will explore how contractor's present their fees and how those fees can actually result in a much different outcome once all things are considered.

Prior to exploring the accounting side of a construction project, let's define what the primary costs for the project are and how these costs can be represented, or even manipulated, to the financial gain of the builder, without the Church even knowing it. The primary cost items for a construction project are design and engineering, general condition costs, building construction costs which can include self-performed construction costs, reimbursable costs, fixture and furnishing costs, and builder overhead and profit.

Design and Engineering

Design and engineering expenses are related to the architect, building engineer, site engineer, acousticians, mechanical and electrical engineers, and more, who are responsible for the plans from which the builder will construct the building.

General Conditions

General conditions is a very important area for the church to focus on, as it is quickly becoming an area where "Creative Accounting" abounds. General conditions are costs that the builder incurs to build the building, but are not actually part of the building. Examples of general conditions include: the site trailer, temporary utilities, temporary restroom facilities, trash removal, site storage trailers, barricades, safety fencing, first aid kits and various safety equipment, quality control and material testing, traffic control, governmental compliance issues, site cleaning and building cleaning. The largest general conditions cost to any project is the site superintendent. The superintendent is typically the only person who is "charged" to the job. However, firms may often "lower" their stated overhead and profit by "moving up" various office staff costs to general conditions. When comparing several builder's bids, churches should add the general conditions costs to the builder's overhead and profit. This figure will offer a true picture of each builder's fees.

Construction

Construction costs are the basic bricks and sticks of your project along with the labor to put them in place. Construction costs cover everything from the bulldozer pushing dirt to the carpenter installing studs, to the painter putting the finishing touches on your new facility. Some builders may include self-performed work in their cost summary. Self-performed work is labor and materials that are supplied by the builder's own employees and is rarely competitively bid on the open market.



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Reimbursables/Allowances

Reimbursable costs are those costs that the designer or the builder are not able to get a firm estimate or bid, on. Many of these costs are owner preference or weather related. Churches should eliminate as many of these unknown variables, as possible. Every unknown, can, and usually will, lead to cost overruns for the church.

Fixtures and Furnishings

Fixtures and furnishings, also known as FFE, can become a large portion of a church project. Typical items considered FFE are: Seating, audio and visual systems, platform furnishings, office and classroom furnishings, café and kitchen equipment and athletic equipment. Prior to beginning any project, make sure that you have a point person that will work closely with the designer and builder to establish budgets and costing for your FFE accounts.

Builder Overhead and Profit

The builder overhead and profit, needless to say, is an important area for the church to evaluate. The overhead and profit allows the builder to pay their office support staff, maintain their home office, provide warranty on the finished project and supply a profit to the stakeholders for the risk taken and managed to build your building. Choosing a builder, solely on their “low” overhead and profit percentage, has sometimes become a rude awakening for churches around the country when they finally stumble upon the “hidden costs” of the project.

Faced with the daunting task of choosing the right builder for their project, building committees have resorted to shopping building firms based on their overhead and profit percentage, and ignoring the monthly general conditions costs. The thought is that overhead and profit is the only variable between builders. The remaining project costs (Design & Engineering, Construction Costs and Fixtures & Furnishings) are somewhat fixed. That assumption is far from accurate. As a picture says a thousand words, numbers, especially dollars, speak even more.

Example Project without Self-Performed Work

An example twelve-month project will be used to illustrate the accounting side of a typical construction project. The primary cost items, for the Design/Builders are:

- Design and Engineering \$ 150,000
- General Conditions Monthly Fee
- Construction Costs \$2,500,000
- Builder Overhead & Profit % of GC's & Construction Costs



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Design/Builder "A"

○ Design and Engineering	\$ 150,000
○ General Conditions	\$ 300,000
▪ \$25,000/Mo x 12 Months	
○ Construction Costs	\$2,500,000
○ Overhead & Profit @ 10%	<u>\$ 295,000</u>
○ Total Project Cost	\$3,245,000

Design/Builder "B"

○ Design and Engineering	\$ 150,000
○ General Conditions	\$ 480,000
▪ \$40,000/Mo x 12 Months	
○ Construction Costs	\$2,500,000
○ Overhead & Profit @ 7%	<u>\$ 219,100</u>
○ Total Project Cost	\$3,349,100

Design/Builder "C"

○ Design and Engineering	\$ 150,000
○ General Conditions	\$ 660,000
▪ \$55,000/Mo x 12 Months	
○ Construction Costs	\$2,500,000
○ Overhead & Profit @ 4%	<u>\$ 132,400</u>
○ Total Project Cost	\$3,442,400

At first glance, Design/Builder "A", whose overhead and profit is at 10%, appears to be the higher cost solution, Design/Builder "B", whose overhead and profit is at 7%, is in the middle of the pack while Design/Builder "C", whose overhead and profit is at 4%, appears to be the low cost solution. The fact that Design/Builders "B" & "C" are moving much of their office overhead into general conditions, actually makes them the high cost providers by almost \$100,000 and \$200,000, respectively!!!

Many times, attention is gained with a low overhead & profit figure from a builder, only to find later, that "costs" the builder has moved into general conditions have created a higher actual project cost to the church. When evaluating your design and build team, make sure that the general conditions costs and the overhead & profit are identified and carefully compared.



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Just when you thought the evaluation process could not get more complex, it can. Self-Performed work, for many builders, allows for a completely separate profit center. Church committees are challenged to insure that they are getting the best value on a segment of the work, often times upwards of 25% of the construction costs, that few builders will competitively bid. In essence, self-performed work comes at a premium that your builder controls and profits from. Let's look at how the previous example project changes with self-performed work as part of the formula.

Example Project with Self-Performed Work

We will now look at the project with Design/Builder "Z", who will self-perform \$500,000 of the \$2,500,000 of construction costs. Otherwise, the primary cost items for the Design/Builder "Z" are the same as the previous examples.

Design/Builder "Z"

○ Design and Engineering	\$ 150,000
○ General Conditions	\$ 660,000
▪ \$55,000/Mo x 12 Months	
○ Construction Costs	\$2,000,000
○ Self Performed Costs	\$ 500,000
○ Self Performed "Profit"	\$ 50,000
▪ 10% Premium on \$500,000	
○ Overhead & Profit @ 4%	<u>\$ 134,400</u>
○ Total Project Cost	\$3,494,400

Just like Design/Builder "C", Design/Builder "Z", whose Overhead and Profit is at 4%, appears to be the low cost solution. The difference is, after making an additional 10% of profit on the \$500,000 of self-performed work, that Design/Builder "Z" actually builds the facility for \$50,000 more than Design/Builder "C".

The gulf grows to a whopping \$250,000 when you compare Design/Builder "A", who has no self-performed work and an overhead and profit of 10%, against Design/Builder "Z", who does have self-performed work and an overhead and profit of 4%!!! That is \$250,000 that can best be used in ministry, not in the pocket of the builder.

Clearly, the "numbers" can be deceiving. The "low cost provider" can quickly become the "high cost provider" if you are not aware of their accounting methods and practices. Don't rely just on the builder's overhead and profit percentage when making such a large decision. All costs should be accounted for when comparing the various approaches that builders take to present their fees. An understanding of how your Design and Build Team accounts for the costs of your project goes a long way in making an accurate stewardship driven decision.



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