MINISTRY
PACIFIC

Can You Afford to Rebuild After a Catastrophic Loss?

Inside this guide:

- How to determine the real cost to rebuild
- Common errors and omissions
- Options to increase or change your coverage

CHURCH AND NONPROFIT FACILITY VALUATION GUIDE

If your facility is destroyed, will you have adequate insurance to rebuild?

Knowledge is power. Here are the facts to help you decide whether you're adequately covered in the event of a catastrophe.

Creating this guide is a peculiar task. Why? *Because we hope you never have to use this information!*

We don't want to see any church buildings damaged or destroyed. *Period.*

In Heaven, there'll be no need for insurance. But as long as we live in a fallen world, there will be risks to manage. Our goal is to help you do that.

Building valuation: The foundation of your property insurance

First, let's define terms. Your *building valuation*[1] is the key factor in determining your insurance payout if your facility is damaged or destroyed.

A building valuation is the amount for which your building and its contents are insured. This amount is determined by a number of factors, including your building's size, number of stories and unique architectural features. In addition, the valuation should incorporate property that's not part of the building itself (called *business equipment*). You could also refer to this as "non-structural items." These are usually mounted to the building and can't be easily removed. Examples include stained glass, pipe organs, pews, audio visual systems and solar panels. All of these are included as part of the building value.

A building valuation is not set in cement. If your church expands, then

[1]The insurance industry uses the term "Reconstruction Cost Estimate" when discussing building valuations.

your valuation needs to be updated (and filed with your insurer) to reflect this. In addition, market factors such as the cost of materials and labor will impact your building's replacement value.[2]

The problem of undervalue

Our experience, government data and private studies show the vast majority of church and commercial buildings are undervalued for insurance purposes.

Here's a hypothetical example. A property insurance contract has been written based on a building valuation of $700,000. However, the actual replacement cost could easily be more than $1 million (these numbers are for illustration purposes only). In this case, an inaccurate and incomplete building valuation did not prepare the church for all of the costs associated with rebuilding. Its construction budget fell short by $300,000. For most churches and nonprofits, that's a lot of money.

[2]For example, Fortune reports lumber prices increased as much as 323% between 2019-2021. Material prices impact rebuilding costs.

> The cost of rebuilding is much more than bricks and mortar.

Unfortunately, this is a common problem.

The cost of rebuilding includes much more than bricks and mortar. Elements beyond the physical structure include:

- Higher costs resulting from updated building codes.
- Expenses related to complying with expanded environmental regulations.
- Increased labor and materials costs.
- Renting a facility while your building is repaired or rebuilt.
- Removing debris.

An insurance contract that does not account for these and other factors will leave an organization scrambling to survive the loss of its building.

The good news? We can plan ahead to ensure we have the coverage to fully rebuild.

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Our experience, government data and private studies show the vast majority of church and commercial buildings are significantly undervalued for insurance purposes.

Why are church buildings often undervalued?

Multiple factors cause this deficiency. But the core problem is a lack of accurate information about the facility.

Let’s unpack this issue so you won’t be saddled with an inaccurate facility valuation.

1. Values are often determined by insurance sales people. They shouldn’t be.

Building values are often determined by insurance agents who – out of self-interest or ignorance – set the valuation too low. Why would they do this? Because it lowers the premium (price) of insurance and makes a sale more likely. Everyone likes a bargain, so who would object? Yet this “bargain” also sets the church up for a financial crisis in the event of a catastrophic facility loss.

In our experience, most church leaders do not know the replacement value of their facility. Yet facility replacement is the very purpose of insurance. *It’s not just a pesky detail.* If your facility is lost, the continuity of your ministry may be at risk.

Don’t outsource your facility valuation to a sales person. Your organization has a vested in making sure it is complete and correct.

Recently, a church insurer (not Ministry Pacific) provided a flier to its customers that contained this information:

“Our building value estimate is in no way intended as a formal building valuation or building appraisal. *No one should rely on our company’s building valuation estimate as a statement of actual cost that it will take to replace*

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a building in the event of a total loss. ... The company's internal process to estimate the value of buildings is not designed to capture all such factors. To accurately set the limit of insurance that you request on your buildings, it is recommended that you *consider conducting your own independent appraisal* of the buildings that you intend to insure, as the responsibility for selection of a sufficient limit of insurance on a building *rests principally with you.*"

This is stating that, if you rely on the sales rep's figures, your insurance limits will be based on a value *"no one should rely on."*

Churches can do better than this. If you have a facility valuation, make sure it's realistic. If you don't have one, it's time to create it. (See page 15 to learn how to get started.)

2. Building valuations are outdated.

Your organization may have developed an accurate facility valuation at the time it was built. However, commercial construction costs and related regulations are moving targets. If your valuation is more than two years old, your organization will benefit by reviewing it.

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Don't outsource your facility valuation to a sales person.

3. Replacement estimates vs. reconstruction costs

Many valuations are based on *replacement* estimates. This methodology uses the data in place at the time of a building's construction (among other flaws). In contrast, *reconstruction* cost analysis determines how much it will take to rebuild a duplicate facility, *taking current prices into account*. Obviously, the *reconstruction* model is the better option.

4. Business interruption is omitted.

If a building is damaged or destroyed, then business-as-usual stops. A temporary meeting place, office space and other expenses beyond reconstruction will be required. Many facility valuations lack this critical budget item.

5. Construction and facility details are omitted or inaccurate.

CG3 Builders is a national construction firm with decades of experience in church reconstruction. It notes these factors driving the undervaluation of buildings:

- **Building measurements** are often inaccurate. This usually happens when a building is expanded and not accounted for in the property valuation. In addition, a finished basement or unused floor may have been left out. These omissions add up and cause the church to come up short.
- **Demolition** of a facility is costly and often not included in rebuilding costs.
- **Debris removal** includes the cost of removing a burned or leveled building from its site. This cost is *in addition* to demolition and most be done in accordance with environmental laws.
- **Expanding environmental regulations** further drive the price of debris removal.
- **Hazardous materials** such as asbestos and lead paint can also impact values. Most churches do not have a current hazardous materials survey and are not aware of their presence. *Removal of these hazards can equal or surpass demolition costs*. Demolition cannot take place until hazardous materials are removed.
- **Unique finishes and surfaces** such as stained glass, custom masonry and woodwork, custom paint and paintings (i.e. gold leaf), interior arches, plaster, steeples, pulpits and pews all impact replacement costs.
- **Special equipment** such as pipe organs, lighting and sound systems must be documented.
- **Building code changes** often result in construction cost increases. These changes usually impact:

  • Electrical systems

  • HVAC

  • ADA (disability) access

  • Health and safety features

- Building setbacks
- Seismic response

In some cases, code compliance costs more than the actual construction project.

- **The location** of a project also impacts budgets. Construction costs are often higher in remote locations. In addition, cities and counties with high permit fees drive up costs.

- **Construction costs** ebb and flow. Prices of building materials including lumber, concrete and metal have recently experienced nearly 200% inflation. Although prices do fall, they tend to increase on average. In addition, labor prices have recently spiked.

The solution? Keep your building valuation current and accurate and modify your insurance policies accordingly.

When it comes to determining building valuation, who's in charge?

Here's a brief look at roles and responsibilities for each party.

When it comes to determining your facility's insurance valuation, who does what? That's a good question. We'll lay it out here.

Photo: Edward Stojakovic, Flickr, https://flic.kr/p/byZM5V; license: CC BY 2.0 – https://bit.ly/3wDfFZq; original modified by cropping and background layering.

Church leadership manages the overall business direction of the church, including managing risks to people and property. That means ultimate responsibility for creating an accurate building value rests with the church. You can get expert help, including free assistance from Ministry Pacific (see page 15), but the buck ultimately stops with church leaders.

Churches can best partner with insurers by providing complete and accurate information. This includes disclosing facility, health and safety risks. Other information important for insurers includes:

- Listing incidents where the church was declined property insurance coverage.
- Pending lawsuits.
- Building safety or structural problems.
- Other potential financial hazards.

The insurance agent should use care, diligence and sound judgment in obtaining the insurance requested by the church. Agents gather data from the church through the application process and submit it to the insurance company for review. This is why it's important the data provided by the church is accurate and thorough.

In the event of a catastrophic claim, the insurance company will determine the value of a facility based on the information collected and documented by the agent and church leaders.

Finally, the insurance company agrees to *indemnify* the church (indemnify means to compensate for loss). This compensation is made within the terms and conditions of the contract.

If my church building is destroyed, what role does the insurance carrier play?

This may seem obvious, but it's worth stating: Insurers don't rebuild damaged facilities. Instead, they provide insurance in the event of a loss so churches have the funds to rebuild.

Property insurance will pay out based on the *Total Insurable Value* (TIV) of an organization's building and assets. The TIV includes:

- The actual facility
- Facility contents
- Machinery
- Other components specified in the contract.

This highlights the importance of churches documenting their assets for insurance purposes. *If it's not documented, it probably won't be covered.*

What kind of funding does my insurer provide?

Insurance companies provide funds for five components. The sum of these equals the TIV of a building based on replacement cost. Here are the expenses that are covered.

1. The building

- The structure
- Completed additions
- Additions under construction
- Building alterations
- Fixtures, inside and out
- Permanent machinery and equipment
- Fire extinguishers
- Outdoor furniture
- Floor coverings
- Appliances
- Repairs not covered by other insurance
- Materials, equipment, supplies, and temporary structures within 100 feet of the premises used for maintenance, repair or construction

2. Business Contents Insurance

This coverage is for property that is "not nailed down." In other words, it safeguards non-structural components including:

- Office equipment
- Furniture

- Furnishings
- Computers
- Electronics
- Machinery
- Any movable items used by the organization

3. Debris Removal

If a building is damaged or destroyed, debris will have to be removed.

4. Building/ Environmental Code Updates

Building and environmental regulations are continuously changing. These changes usually drive costs higher – sometimes dramatically so.

5. Business Interruption

Even though churches are not businesses, the industry terminology here still applies. A catastrophic event that renders your building unusable will require you to spend money for a temporary meeting place and other stopgap measures. In addition, the interruption may result in a drop in giving. Business Interruption insurance accounts for these real-life scenarios.

Demolition and debris removal

When we think of rebuilding, all eyes go to bricks and mortar. But before we can go there, we have to remove the damaged facility.

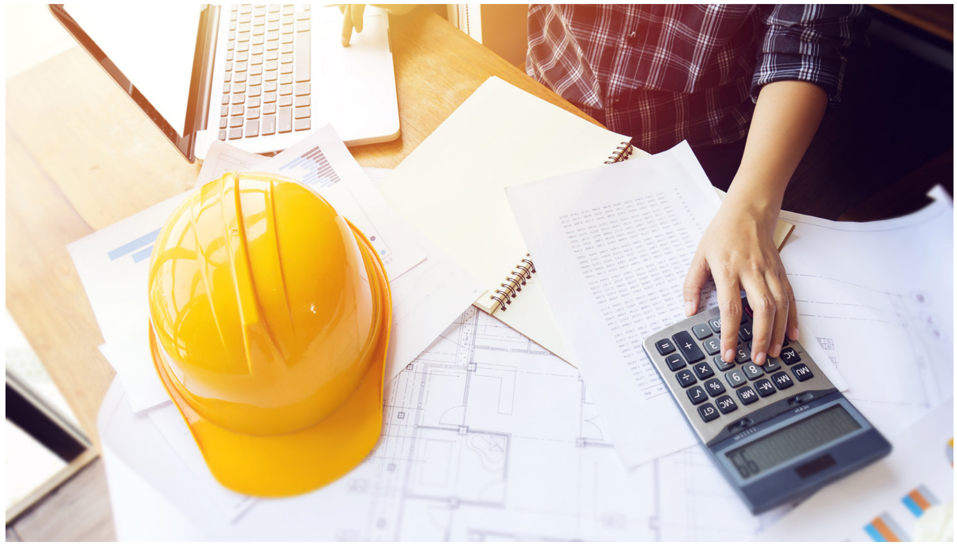
The first step is demolishing what remains of the building. This is obviously a dangerous job and must be done by professional contractors.

If the damaged facility contains hazardous materials, such as asbestos or lead paint, these must be removed before demolition. Removal costs can equal or surpass the actual demolition costs.

When that's done, the debris can be removed in accordance with state, federal and local environmental laws.

The good news? Property insurance includes funds for demolition and debris removal so you don't come up short. Make sure you're coverage is adequate.

What data to include in your building valuation



Make sure you have a handle on these facts about your facility.

The key to setting your building valuation properly is accurate and complete data. Here are some of the key points to include.

- **Square footage**
- **The year your facility was built** Older buildings' materials or construction techniques could affect the cost of rebuilding.
- **Occupancy usage**[3]
- **Architectural style**
- **Type of construction** (frame, joisted masonry, fire resistance, etc.).
- **Number of stories**
- **Foundation and basement** Churches should specify the type of foundation and any remodeling improvement work that has been done to the basement. In addition, an existing foundation may need to be brought up to code before framing can start. (Just because a foundation survives a fire, it does not mean the intense heat didn't compromise its integrity.)

[3]This describes the frequency and extent which your facility is typically used, ranging from the auditorium to a fellowship hall, Sunday School rooms and more.

Other factors

- *Stained-glass windows* Depending on the size, materials and complexity of design, window replacement could cost from $90 to $700 per square foot. When you multiply this cost per square foot times the number of stained-glass windows, the importance of including this data in a building's value is clear. Ministry Pacific recommends securing an up-to-date stained-glass valuation from a qualified artisan.
- *Pipe organs* can vary widely in value and size, ranging from $500,000 to millions of dollars. We recommend obtaining a value from an expert artisan so you can include a specified replacement cost in your valuation.

What insurance coverages are needed to successfully rebuild in today's market?

If you have property insurance, that's enough, right?

It may be enough. But it may not be. Why?

Think about any large construction project. Although the contractor provides an estimate, it's called an "estimate" for a reason. There are unpredictable cost factors that impact every build, rebuild or remodeling project.

If your church has done a thorough job researching its building value and documenting it for insurance purposes, then you have taken reasonable efforts to ensure you have the coverage you need. But if you want to be doubly sure insurance funds will be there for 100% of the costs, you may want to consider these types of coverage.

Building and Business Contents "Blanket" Policy
Once your church has created a detailed building valuation, you can request that your building and business contents are combined into a single dollar amount of coverage. Your church can draw from this total amount if building costs are higher than anticipated.

Replacement Cost Coverage
This endorsement (policy modification) provides for the cost to replace the damaged property with materials of like kind, quality, and utility. Although it costs more than property insurance alone, it also removes guesswork from the equation.

Extended Replacement Cost Coverage
This endorsement (policy

modification) increases your building coverage limits by as much as 25%, providing a safety net in the event your building valuation is lower than anticipated.

Special Form Endorsement Coverage
This is the most inclusive property coverage. Everything is assumed covered except for elements specifically listed as "not covered" in the policy.

Debris Removal Coverage
Additional funds are provided for the cost of removing debris from the damaged property and the cleanup of environmental contamination. The limits provided in most polices are too low to cover all cleanup costs. Studies have found cleanup expenses can range from 12-40% of rebuilding costs.

Business Interruption Coverage
Since your church can't continue operations in a building that's destroyed or damaged, you'll have to rent space. Your church will also incur other unanticipated expenses and may suffer a loss of charitable giving. For all these reasons, business interruption coverage is highly recommended (even though you are not a "business," the same principles apply).

Actual Loss Sustained Coverage
This is a form of business interruption coverage in which the organization is covered for the total amount of its loss.

Building Code and Ordinance Coverage
This provides for loss caused by building codes that regulate the construction and repair of damaged buildings. Code upgrades nearly always result in increased expenses, hitting older buildings hardest. In addition, many counties have building ordinances requiring any building that has sustained a specified amount of damage (typically 50 percent) to be demolished and rebuilt in accordance with current building codes.

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There are unpredictable cost factors that impact every build, rebuild or remodeling project.

There are also other types of policies we haven't listed here that could help you ensure you have adequate coverage to rebuild.

Contact us to learn more.

Frequent causes of building loss

It's easy to underestimate the risk of damage to our facility. After all, it's *our* facility. Nothing will happen to it, right?

We hope you are absolutely correct in that assumption.

Building catastrophes tend to take us by surprise. The list of potential threats here is not intended to be complete. And not all of these may be covered by your particular policy. They are listed here to help you consider the full range of possibilities that property insurance may cover.

Leading hazards for commercial properties

Fire and smoke
Wildfires, lightning, arson, electrical and other internal causes

Weather
High winds, snow and ice, hail, tornadoes, hurricanes, flash floods

Vandalism and theft

Geological
Volcanic and seismic activity; sinkhole collapse

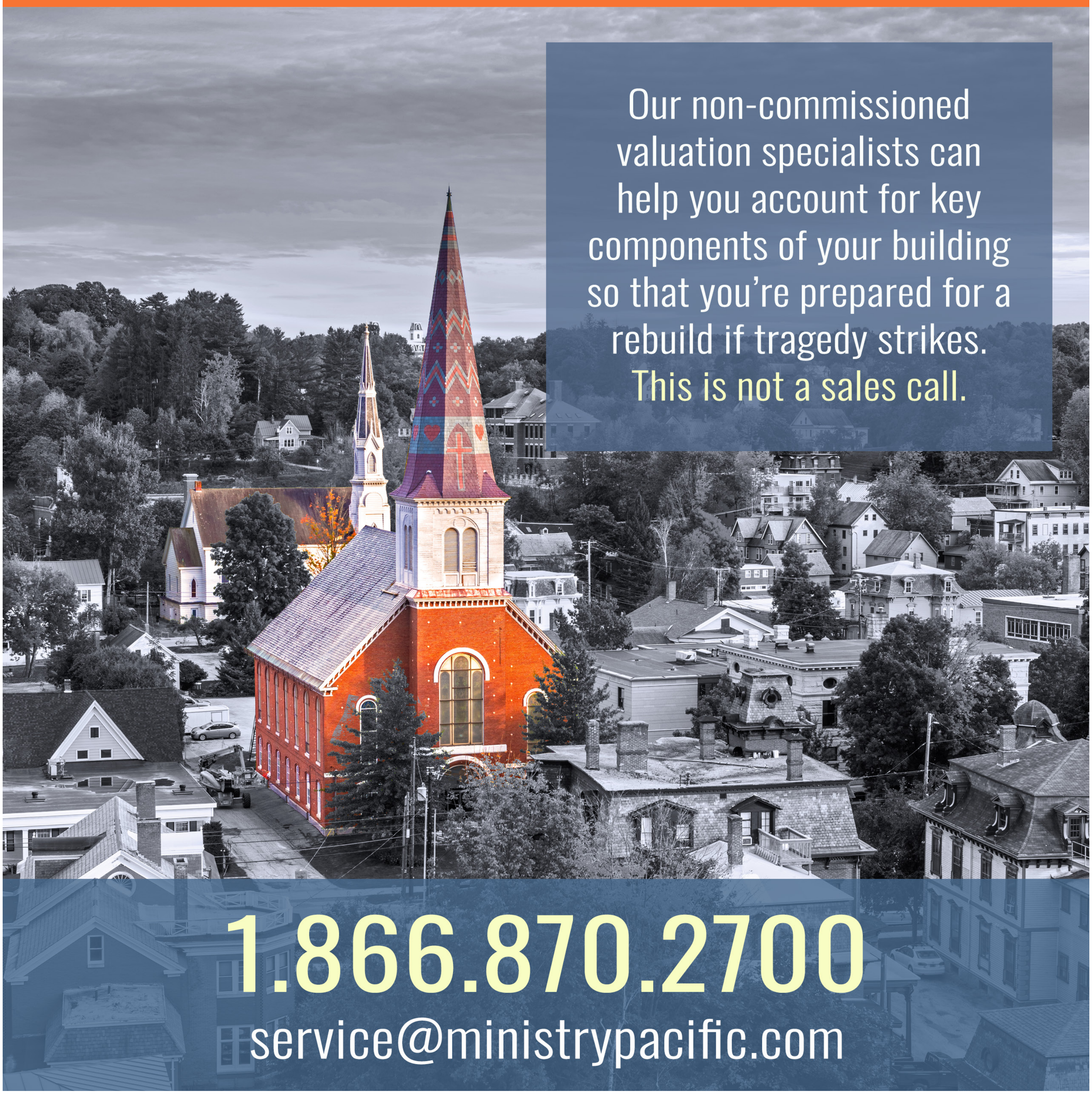
Structural failure/collapse

Water damage from internal sources
Sprinklers, plumbing failure, backups

Mold and fungus (often resulting from water damage)

Ministry Pacific Customers

Get free help in determing your facility's value so you can insure properly.

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