Issues, Ideas & Actions

Useful information from Ryun, Givens & Company

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Ryun, Givens & Company, P.L.C.

Facility Lifecycles

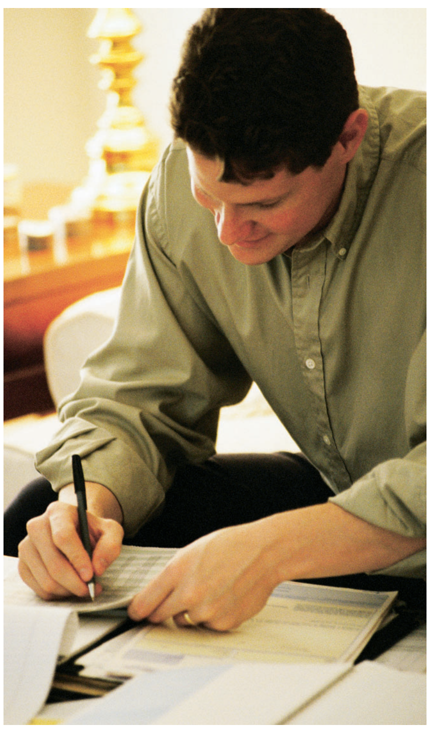
Senior Living Communities face the task of planning for constructing new facilities (or refurbishing old ones) every 30-45 years.

Given the length of this time span, and the personnel changes that take place over that time, most organizations are unfamiliar with, and poorly prepared for the processes involved.

This month's *Issues, Ideas and Actions* deals with understanding and preparing for the campus development process.

Over the years, Ryun, Givens and Company, P.L.C has had the opportunity to work with many organizations in the planning, forecasting, financing, and construction phases of campus development. What follows are some thoughts and ideas that we hope will be of benefit to those contemplating such an undertaking.

Do Your Market Research



We strongly recommend that Senior Living Communities operate from an up-to-date Market Research Report. A good report contains research and information that is critical to understand both the current and future needs of your market area.

Market Research Reports typically assess the following factors:

- Demographics, including age and income levels in your market
- Average residential home price
- Competition for services and pricing dynamics
- Demand for services as well as any opportunities for unmet needs
- Occupancy levels
- Mix of unit types and sizes
- Fee arrangements
- Types of services available and which are included in the fee structure or offered at an additional charge
- Any other issues that impact the viability of your facility

Also, be sure to consult industry sources to ensure your facility will meet the needs of baby boomers, (the oldest of whom are now 68). They will likely be much more active than previous generations of aging people.

Most underwriters and lenders require a copy of an up-to-date Market Research Report as a prerequisite to financing, because the report provides much of the information necessary to substantiate the feasibility of an organization's proposed plans.

Form a Development Team

Many organizations have paid dearly for attempting to "go it alone" or work with outside advisors who do not have the necessary background, local understanding, or experience that is essential to properly advise their clients.

Here are some examples of organizations that have suffered from taking such shortcuts.

- In one instance, an organization applied for government funding only to find out after waiting for twelve months that they didn't qualify for the funding.
- Another organization worked with a local architect who had no previous experience in constructing Senior Facilities. After spending approximately one million dollars in architect fees, the organization had to abandon those plans and hire a new firm with the necessary background, understanding and experience to get the work done properly.

- In yet another instance, an organization's board awarded the construction contract to a local contractor who incurred massive cost overruns, in excess of a million dollars. The organization eventually had to file for reorganization under bankruptcy.

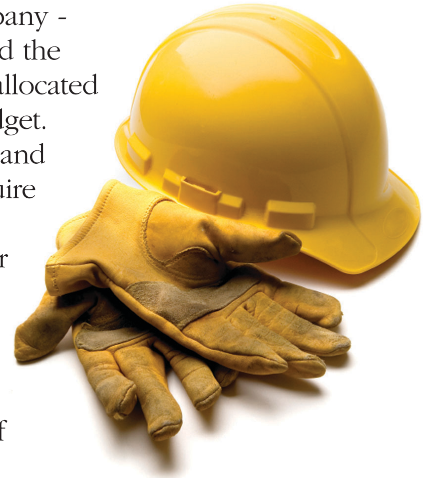
In these instances, (and many others) organizations that initially attempted to save a few dollars found that doing so was a very expensive choice.

The LeadingAge association has a series of templates that can be modified to your specific needs and serve as Requests for Proposals for the key members of the development team. Contact them at 515-440-4630 or, feel free to contact us at 515-225-3141 and we can help you obtain copies.

Here is a list of the parties that typically comprise a comprehensive development team:

- The CEO and a special committee from the Board of Directors
- Planning/Market Analysis Consultant - to compile the market research information.
- Architect - primarily responsible for the design of the project, and most often responsible for monitoring construction. An architect experienced with senior facilities is essential.

- Legal Counsel - necessary for review and approval of contracts covering services with other outside consultants, by-law or article changes, subsidiary formations, tax exempt financing, etc. Get a good one.
- Financial Feasibility Consultant - most often a CPA firm that has a strong understanding of senior communities, Medicaid and Medicare reimbursement, and has an extensive client list of those who have undertaken successful projects.
- Underwriter or Banker - prior experience and understanding proves invaluable. The underlying loan MUST fit the project well and take into consideration the projected cash flows of the organization. Most not-for-profits choose to work with an underwriter to issue tax exempt bonds and obtain permanent financing. A few will work with local lenders, primarily for local community PR considerations. They may, however, face interest rate resets approximately every 5-10 years doing this.
- Construction Company - their role is to build the facility within the allocated timeframe and budget. Most underwriters and some bankers require a "guaranteed maximum price" or GMP in order to assure that the organization does not assume the unnecessary risk of cost overruns.



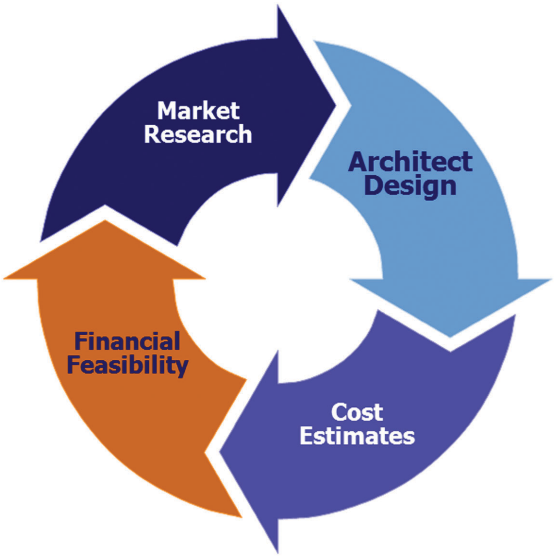
- Marketing Person/Firm - most sources of financing (underwriter or banker) will require that a portion of the units are "presold". They want to know that there is a commitment for occupancy by potential residents. This requires specialized skills in assisting potential residents to make a commitment prior to completion, and to establish programs and procedures to retain presales over a period of several months.

  The marketing function for a facility can come from three sources:
  - The organization can conduct its own marketing campaign with an on-staff marketing director.
  - The organization can conduct its own campaign with the assistance of an experienced marketing firm.
  - The organization can outsource the marketing of the project to an outside professional firm utilizing their own people.

Each has its benefits and drawbacks. Again, relevant experience in this position is a must.

The Process

The following graphic demonstrates the typical "process" of a campus development project. While it is rare that the initial plan results in a perfect, financially feasible project, the number of times around this circle can be dramatically decreased by working with a qualified development team that has a strong background, understanding of and experience in such projects. To do it right, expect 18-24 months of planning and preparation, and an additional 12-18 months of construction.



It is typical for a qualified CPA and underwriter to prepare an initial "cost not to exceed" contract for the architect to use as a guideline for the design of the project. The time involved in preparing this document is normally one hour and can save thousands of (if not a million) dollars.

A Recent Trend

Ryun, Givens and Company has found in recent years, that several organizations which have diligently saved and accumulated substantial cash reserves, have substantially OVERSPENT on their campuses. While "overspent" is a subjective term, there are industry norms available that can be used as a benchmark to identify cost and facility parameters. By overspending, an organization's management and board may have the best interests of their residents and the local community in mind. However, such thinking can be short-sighted and may potentially jeopardize the organization's future financial position.

For example, organizations contemplating a campus development project must consider the campus "half-life". The half-life is the point in which the "new" campus begins to need an additional and substantial infusion of cash to update, repair, refurbish or modify facilities. The industry norm is 7-12 years. While an organization may have the means to initially overspend, it may face a more difficult challenge obtaining the funds necessary for inevitable half-life expenditures.

Other Considerations

New construction often means that an organization needs to re-evaluate its current and future census mix. If the organization is currently serving 40% or more Title 19 residents, new construction, in order to be financially feasible, means that a higher percentage of private-pay residents will need to be included and the percentage of Title 19 residents reduced. Typically this is very feasible because private-pay residents are attracted to a senior community, at least in part, by its condition, age of construction and the "extra" features offered.

Contact Us - We Can Help

We have substantial experience in both large and small campus development projects. We can help you by getting you started in the right direction and/or putting you in contact with other experienced advisors with proven track records of success. We would also be happy to be a part of your Development Team in order to continually advocate for your best interests, and help you navigate through the many financial aspects of your project.

If you are considering such a project, send an email to sgivens@ryungivens.com or call Whitney Tucker at (515)225-3141.

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