

Establishing a Budget for a Renovation Project

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One of the most common ways of measuring the success or failure of a renovation project is to compare the final cost of the project to the original budget. Unfortunately, the process of developing a comprehensive budget is often neglected in the early stages of a project. Many times an association will receive a proposal from a contractor for a certain scope of work and the proposed amount becomes the “budget” for the project. This method of budgeting has many holes in it and does not account for many costs that are likely to be incurred.

Without a good budget, it can be hard to accurately gauge the success of a project. The goal of this article is to offer some thoughts to consider when establishing a budget for a renovation project. Not all of the items discussed will apply to all projects and not every issue that should be considered in a project budget is discussed. However, the advice below should put you in the right frame of mind for developing a comprehensive project budget.

Project Specifications or Detailed Proposal

Understand what scope of work is included in the contractor’s proposed price and what is not. The best way to be sure of what costs are included in the contractor’s bid price is to have a comprehensive and detailed set of specifications prepared and sent to all bidding contractors. Detailed specifications will tell the bidders what scopes of work to include in their pricing and will greatly reduce the likelihood of surprise charges after the project is started.

Unforeseen Conditions

Project budgets should always include a contingency for unforeseen conditions. An example of an unforeseen condition is a recent regrading project intended to direct water away from a building. During the project it was necessary to remove 4 feet of soil next to a building. In the process of removing the soil, the contractor found that the electric wires serving the parking lot lights were buried only 3 feet below the ground surface. Once the wires were exposed, they had to be reinstalled to a proper depth below the surface. The cost to reinstall the wiring was the result of an unforeseen condition.

Unforeseen conditions usually result in additional expenses that are not reflected in the original cost of the project. While, by definition, unforeseen conditions are difficult to predict, it is good practice to include a contingency amount in the project budget. Contingencies for unforeseen conditions typically range between 10 percent and 20 percent, depending on the size and complexity of the project.

Legal Fees

Any significant renovation project should involve the association’s attorney who will typically draft the contract between the association and the contractor. The attorney may also be involved if the project requires resolutions, votes of the membership or interpretations of ownership of various building or site components (homeowner owned vs. common elements).

The legal fees associated with a renovation project will depend on the size of the project, but the project budget should consider those costs.

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Loan Costs

Large renovation projects are often funded by loans taken by the association. Loans can be an effective means of funding project costs that exceed the association's available assets. However, there are additional costs associated with funding a project with a loan that will have a significant impact on the total project costs.

In obtaining a loan, there will be closing costs and interest charges paid to the bank. Along with these costs, the association is likely to require the assistance of its accountant, attorney and management company. All of these professional services typically incur costs for the association.

Typically, loan payments will be made by the association. The funds to make the payments will come from the membership, usually as monthly special assessment payments. Unfortunately, the association must anticipate that at some point during the loan repayment period, someone will miss payments. When this occurs, all of the other members must pay this bad debt and this must be accounted for in the budget.

Management Company Fees

Any significant renovation project at a community association is going to require extra work by the association's management team. In the planning stages, the manager typically serves as the quarterback for the project. The manager will coordinate meetings between the board and its engineers, contractors, banks, membership, etc. Once the project starts, the manager will typically disseminate information to residents, if needed, schedule access to homes and draw checks for payment of contractor's invoices.

Management companies often charge additional fees when a community performs a renovation project. These fees are necessary to cover the increased work required of management during the project.

Engineering Fees

The association may engage an engineer, or other design professional, to prepare plans and specifications for the renovation project. As discussed above, having a good set of specifications can help avoid surprise costs later in the project.

The association may also choose to have their engineer perform a construction inspection and administration services during the construction phase of the project. These services can range from occasional spot inspections to full time inspection and project administration.

CONTINUES ON PAGE 20.

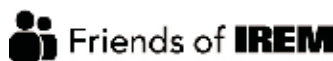


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BUDGET FOR A RENOVATION...
from page 19.

The engineering fees that the association will incur will depend on the scope of the project and the extent of services that they wish to have their engineer provide.

Building Permit Fees

Significant renovation projects at a community association require municipal building permits. The association's engineer or design professional should be consulted to determine if permits are required. If the association has not engaged a design professional, the manager should meet with the Municipal Building Code Official to discuss the need for permits.

The cost of building permits will vary with the size and scope of the project. Typically permit costs are in the range of 1 percent to 2 percent of the project cost.

Price Escalations

Material costs can have a major effect on the cost of a renovation project. The project specifications and/or contract should address material costs that occur during the course of the project. Some agreements will have a fixed cost of the work, regardless of material price increases. This type of agreement allows for a much more predictable budget.

One notable exception to the fixed pricing example is paving. Asphalt pavement material is a petroleum based product. The cost of asphalt pavement is very volatile and moves with the cost of oil. Pavement projects can base the material cost to be paid to the contractor on the New Jersey DOT Asphalt Index. This method adjusts the material costs based upon the cost of asphalt on the day that the pavement is installed.

The cost of construction materials continue to increase. If material cost increases can be passed along to the association, the project budget must account for those potential changes.

Conclusion

In preparing a project budget, the association should try to account for all potential costs that could be associated with the project. By working with its professionals, the board can develop a budget that reflects a comprehensive estimate of the cost of a project. By starting with a good budget, the association can launch its project toward a successful completion. ■



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