

THE COSTS OF A PCA SHOULD BE INCLUDED IN EVERY ACQUISITION, RESTRUCTURING OR MANAGEMENT OF AN ASSET. Deferring maintenance will often diminish the useful life of any building systems and components and subsequently further reduce the asset value. Unless funds are directed to assess the health of the asset and address any deferred maintenance, little preventative maintenance is possible because previously allocated funds will be eventually depleted in order to deal with unanticipated system failures. Without corrective action, deferred maintenance costs will continue to climb-up in direct proportion to the shortfall in annual maintenance requirements.

Planned maintenance and renewal should play a central strategic role in the acquisition and/or management of these assets. Good planning for maintenance requires that appropriate resources be allocated on a priority basis. In fact, routine maintenance is critical to preserve the asset so that it continues to provide acceptable services, achieves its expected life, generates the cash flow required to service the note and continue to exist as a stabilized asset. Failure to provide adequate maintenance results in deterioration of the property and eventually loss of use. A more important concern is the visible consequences of neglecting maintenance, which may not be apparent for many months. Once the signs of deterioration become visible, the repair cost likely will be far greater than the cost of preventative maintenance. A simple protocol called Property Condition Assessment (PCA) can help lenders, investors, brokers, receivers, attorneys and stakeholders gauge the physical characteristics of a commercial real estate asset and make an informed decision to acquire, maintain, stabilize or dispose of the asset.



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PCA

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The current industry standard for PCAs is ASTM E2018-08, *Standard Guide for Property Condition*

Assessments:

Baseline Property Condition Process.

Since its inception in 1999, the ASTM Guide was widely adopted as the standard of care by both the Commercial Mortgage Backed Security industry and by balance sheet lenders in the U.S. and Canada as well as savvy owners and equity investors to satisfy a de minimus level of due diligence.

Property Condition Assessment

A vital due diligence tool to help you make an informed decision.

In today's economy, more and more commercial real estate assets are expected to hit the marketplace and change hands. Troubled commercial real estate often presents big opportunities. However, as you begin your proactive evaluation process and try to analyze the full potential income of such an asset do not overlook the physical characteristics of the property.

Note: In the past two years, without sufficient funds to cover operating costs, borrowers and asset managers have chosen to defer routine maintenance of their commercial real estate assets in favor of more pressing financial requirements allowing the typical minor repair work to evolve into more serious conditions. The backlog of deferred maintenance has been growing and will certainly translate into significant asset deterioration if not addressed in a timely manner.... That is why you should schedule a Property Condition Assessment before you go any further on your next deal.



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A PCA is an asset management tool of a great importance...

that can be used as point of reference during acquisition and life of the asset to gauge the physical health of the different systems and components of the asset and priorities capital improvement requirements. A PCA provides reliable and detailed information on issues including the building's operating systems, overall design, and architectural features, energy efficiency, security systems, capital improvement requirements, and any signs of material physical deterioration or functional obsolescence that could detract from the building's potential to generate income. As part of the assessment, maintenance programs and latest annual inspection reports are assessed and the impact of local zoning regulations, building codes and any special hazards that may affect the income stability of a property is also examined.



What a PCR encompasses.

The level of due diligence often varies and depends on the risk tolerance of the end user and the purpose the PCA is to serve as well as the complexity of the asset (type of property, age of the improvements and time available for preparing the report and reviewing the opinions to be contained in the report.

A PCA typically includes four components: **Documentation Review and Interviews; Walk-Through Survey; Preparation of Opinions of Probable Costs to Remedy Physical Deficiencies; and Issuance of the Property Condition Report (PCR).** The report is generally formatted to cover the following site and building's systems and components:

- Site components including topography, flood zones and seismic zones; storm water drainage; access and egress; paving, curbing and parking; flatwork; landscaping and appurtenances and utilities
- Frame and Envelope including foundation; building Frame, building exterior and roofing
- Interior Elements
- Mechanical, Electrical, Plumbing and Vertical Transportation
- Fire/Life Safety
- ADA Compliance
- Asbestos/Environmental Concerns
- Building Code Violation Issues
- Document Review and Interviews

Based upon the walk-through survey and information obtained and reviewed, general-scope opinions of probable costs are prepared for the suggested remedy of the material physical deficiencies observed. The opinions of probable costs assist the end user in developing a general understanding of the physical condition of the asset. The written cost analysis of the report is typically broken down into short-term and long-term capital expenditures.



Benefits:

The benefits of having a PCA when planning to purchase or dispose of a real estate asset or maintaining any commercial property are always rewarding and far outweigh the cost of such an assessment. Properly conducted PCAs often end up saving the end user tens of thousands of dollars in the process. To list a few of the benefits, a PCA performed at appropriate level of due diligence and inquiry can often:

- Reduce the level of uncertainty associated with a purchase and prevent one from acquiring a money pit!
- Help properly price an asset
- Serve as an effective negotiating tool to reduce the purchase price of a property if major deficiencies are uncovered during the process or to direct the burden onto the seller to correct deficiency and pay for repairs
- Allow one to back out of the deal depending upon the property's physical condition
- Forecast future repairs and assist in preparing budgets and scheduling preventative maintenance
- Help to facilitate obtaining a loan and protecting lending institution and equity investors vested interest in the collateral property
- Produce vital tool in making a well informed acquisition decision

Qualifications and Cost

The quality of a Property Condition Report is highly dependent on the qualifications of your consultant and field observer(s). General guidance and limitations for the PCR are offered by The Baseline Property Condition Assessment Process outlined in the ASTM Standard Guide E2018-08. As a rule, experienced consultants with engineering background coupled with extensive experience in property assessments and inspections should be retained to perform the PCA.

Fees for PCA's will vary depending on the type of property to be assessed, its age, size, turnaround time and location. The PCA price is a function of the scope of services to be performed and its end use purpose. The cost of a PCA for a small retail building or an apartment complex and/or a large condominium building may vary from \$1,500.00 to over \$25,000.00. In the big picture, the cost to perform a PCA or update an existing PCA and Replacement Reserve Analysis is minimal considering the significant cost savings it will generate in the long run provided uncovered deficiencies are corrected and the asset is maintain in a normal operating condition.

CONTACT CLM AT 1.866.665.2870 WITH ANY QUESTIONS
OR TO SCHEDULE YOUR NEXT PCA.

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