

By Daniel M. Isard



## Rebuilding for the Future

Four key points to understand about your building and its relationship to your business.

**W**elcome back, worthy readers! By acknowledging another column (after last month's throw-down), I believe you are committed to working for a successful 2020 and beyond and willing to take a sledgehammer to your business model over the course of a year. In the end, we will all see the future more clearly.

This month, I will demolish your building.

One of the biggest issues with the funeral home building is that it is a single-purpose, specialty building and one that often predates community members. Even if you put in a reception center, it's still the reception center at a funeral home. If you rename the business with some un-funeralish name, it's still a reception center in a funeral home. That doesn't mean people won't use it. They will. And when they do attend a reception in the funeral home, the first thing they usually say is, "This is much nicer than I would have thought."

To sledgehammer your building for the sake of future planning, we must understand four key points about it and its relationship to your business.

### VALUATION

There are two ways to value a funeral home building. The first is to assume it is only commercial property and there is no funeral home limiting its use. This is the liquidation value. If your building is 10,000 square feet and commercial buildings in your community sell for \$200 per square foot, your building liquidation value is \$2 million. Therefore, if the business and the building value as a funeral home (to be discussed next) combined are not worth the liquidation value, then perhaps someday you wind up shutting down the funeral business and selling off the real estate for its commercial value.

The second method is the special-use valuation, a two-step process. First, determine fair market rents for this building, assuming its highest and best use is as a funeral home. Rent typically ranges from 6% of funeral service revenue (FSR) to a high of 8%. The higher rent is used if there are multiple buildings or if the building is a perfect design.

Funeral service revenue is defined as all revenue from

operations, excluding cash advances. Cash advances are not-for-profit revenue items, as they are merely exchange items to help a family, and thus are not included in FSR calculation.

If a business has \$1 million in funeral service revenue, its rent should be between \$60,000 and \$80,000. You might not be objective enough to determine the proper rent, but I am. This payment is assumed to be a triple net lease, meaning the lessee pays rent to the lessor, as well as paying all real estate taxes, insurance and maintenance expenses that arise from use of the property. The lessee does not pay for the replacement of capital assets. If a roof is leaking, the lessee pays the cost of repairs. If a roof needs to be replaced, the lessor/landlord pays for it.

If your real estate is in your business enterprise with the funeral home and you do not pay rent, the calculation is the same. We are trying to determine a cost for the use of the building. I can guarantee that if your real estate is in the enterprise, your pricing is probably off, as you are not allocating the proper cost of the building to your overhead.

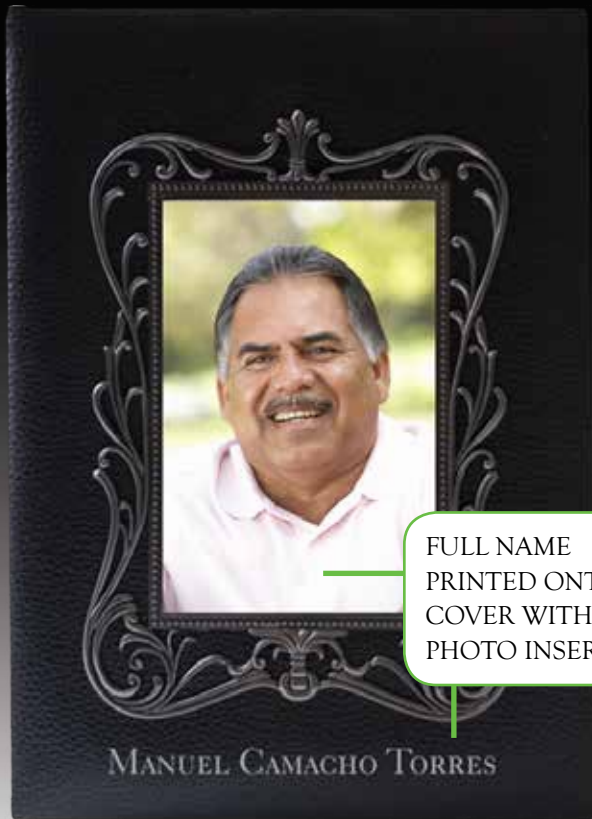
Once we know the rent, multiple by 10. Generally, it's that simple. If your business does \$1 million of FSR and it's a perfect building, the rent would be \$80,000. The value as a funeral home is therefore \$800,000.

A West Coast client was recently offered more than \$10 million for his real estate. We valued the business and real estate as a funeral home enterprise at about \$5 million. The client was ready to retire, and while there was a child running the business, the child could not buy the building at the commercial price. They asked what they should do. Unfortunately, it was a no-brainer. The building was sold and the business intangibles sold off to a local competitor.

### LOCATION

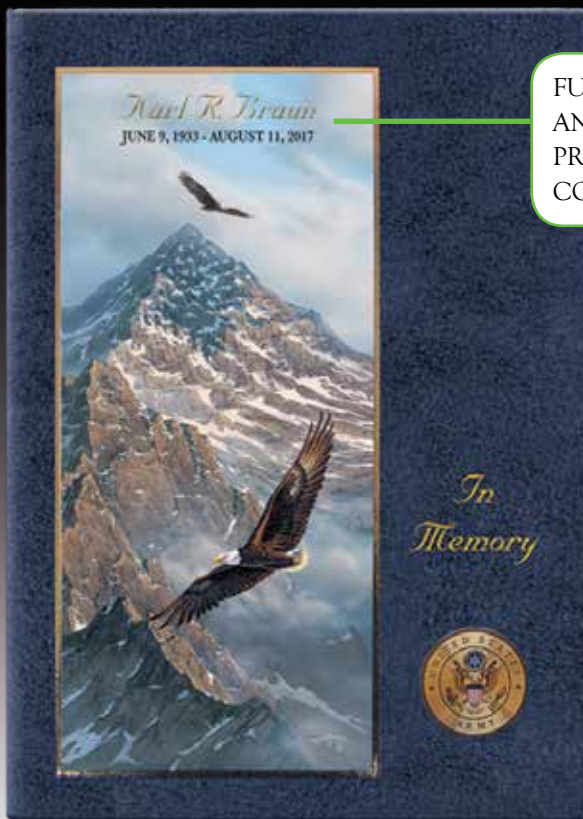
There are many reasons someone chooses a funeral home. According to annual NFDA survey data, convenience of location is the third most important reason on the list, which is why the building has so much importance in the business operation. By the same token, it is difficult to manage as the families you serve may move.

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Imagine you serve a Lithuanian community almost exclusively; you're even located next to the Lithuanian Catholic church. But over the past 50 years, families have moved 30 miles away. Suppose the church is shut down. Do you think this will impact case count?

Funeral homes are not easy to move. It is expensive and time consuming. In some cases, chasing your cases may allow someone else to move into your existing site and take some of your business away.

However, acknowledging the fear and expense, if you were to build new, would you relocate? If not, you're lucky! If you would relocate within your general service area, this is the time to start to thinking about doing that.

### BUILDING SIZE

The size of the building is another factor. Is it the right size for the number of families you serve? Is the chapel the right size for the number of people who attend a funeral service? Do you have enough area for viewing.

This is a difficult planning issue because funeral directors never want to deny a family. If you have two families in-house and a third calls, you don't want to ask the newest family to delay their plans. However, you probably should. There are only so many cars that can fit in your parking lot and so many families that can avail themselves of your services at the same time.

A client with a 60-call firm has two prices for its chap-

el or visitation; a standard price allows them to have multiple families served at the same time, and a higher price is charged for the exclusive use of the building. I asked, "How many times has a family chosen the exclusive use and you got another call at the same time?" The owner told me in the 10 years they had owned the business, that happened only twice!

Building out a funeral home is about \$200 to \$300 per square foot. Thus, a 10,000-square-foot funeral home could cost between \$2 million and \$3 million, plus the land and furniture, fixtures and equipment to construct. Let's be real! At these prices, can you afford to do low-cost cremations?

### SITE COMPONENTS

One key to a successful future building is building to meet the needs of the families you will be serving over the next 20 to 30 years. While computer screens are more important now than the felt push pin lettering boards, there are more needs to take into consideration.

Reception centers are one of the most talked-about items in the renovation or construction of a funeral home. People want a place to congregate and talk and share their common grief. If you have a graveside funeral and the mourners show up and then leave, that needed socialization is lost. And if your state law doesn't allow funeral homes to have reception centers, *change the law!* A reception center profit can offset the lost profit from partial services and lost merchandise sales.

A crematory should be as much a part of your building as a prep room. They both cost about the same to construct. The difference is that the prep room is being used less for embalming every year and the retort is being used more each year. I have found that for most crematory construction projects, if you are using a third-party crematory about 90 to 100 times a year, owning your own crematory will allow you to break even or make money.

Remember, the theme of this column for 2019 is it must be broken to make it better. A great book by Roger von Oech, *A Whack on the Side of the Head*, promotes business owner creativity. Continue to read this column each month for a new topic of consideration (next month, we'll focus on marketing), and please spend a few bucks on yourself and buy this book!

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