
CHAPTER 4. DEVELOPING FEASIBLE PROJECTS

- 4-1. GENERAL. This Chapter contains the basic instructions for use by field offices in processing Section 236 cases.
- 4-2. PRE-APPLICATION - INITIAL CONFERENCE. Prior to submitting an application for HUD-FHA feasibility review, a prospective sponsor should schedule a conference with the local HUD-FHA Field Office Director and his staff. Representatives appointed by the Directors of Economic Market Analysis Division, Housing Services, Property Management and Equal Opportunity may be included in the initial interview between the sponsor and the production staff. The production staff (MFC) has the primary responsibility for conducting the initial conference and should notify those other representatives immediately when a conference has been arranged with the sponsor. Among the subjects discussed at the initial conference will be market demand, a management program, project size, composition, design, cost, "market rent" and basic rent, Project Selection Criteria, and availability of contract authority. HUD-FHA will inform the proposed sponsor of market and other statistical data which are available.
- a. The Basic Objectives of the initial conference are:
- (1) To explore the sponsor's objectives and determine the best approach for the proposal;
 - (2) To inform the sponsor of its obligations and responsibilities under the Section 236 program;
 - (3) To inform the sponsor of HUD-FHA processing procedures and requirements;
 - (4) To acquaint the sponsor with the Project Selection Criteria; and
 - (5) To give the proposal a preliminary screening in order to inform the sponsor if the proposal is obviously ineligible or not feasible.
- b. The Sponsor should have a clear idea of the demand for the type of housing proposed, competition with which the project will be confronted, vacancy rates in similar apartments, and the market capacity for absorption of units at prevailing rent levels in the neighborhood. The sponsor should be aware

(4-2) of various amenities, services and equipment offered by housing which will compete for tenants with the proposed project. The sponsor must assess the acceptability to tenants of the proposed site and know whether zoning permits the intended use (or whether appropriate zoning can be obtained).

- c. It Must Be Emphasized to the sponsor that, at this initial conference, HUD-FHA requests only exhibits that are already prepared or easily obtainable and that the sponsor is not obligated to incur any additional costs at this time. However, the sponsor should provide HUD-FHA with any data or exhibits already prepared which will help to determine the project's feasibility.

For Some Sponsors, First Impressions of HUD-FHA Will Be Formed at This Initial Interview. Tact, diplomacy, genuine interest, and knowledge of the requirements of multifamily housing programs, must be displayed by all HUD-FHA personnel. The interview of the potential sponsor should be performed by the coordinator or an Assistant.

- e. To Assist the Sponsor in preparing the feasibility application, the conference should include discussion of proposed family sizes and income ranges to be served. The proposal must relate to demand as indicated by HUD market analysis. Relating the sponsor's proposal to current HUD rent and operating expense data should produce a tentative maximum supportable cost. The following points should, be emphasized:

- (1) The sponsor should keep the cost of the project as far below the maximum as is consistent with good design and the objectives of the program;
- (2) Any commercial space included in the project must be planned to generate sufficient income to carry its pro rata share of investment costs at the market mortgage debt service rate;
- (3) If cost data for comparable Section 236 projects indicate costs substantially below the costs which might be supported by the income levels, the sponsor is to relate project costs to the comparability costs, not to the income limits.

sponsor should be advised of the nature of the exhibits necessary to enable processing of the proposal and should be furnished with a kit containing all necessary written instructions and required forms.

- a. The Basic Kit is to contain the following items:
 - (1) The Sponsor's Guide (Reference (10) of the Foreword);
 - (2) Ground Rules for Sponsor's (Reference (11) of the Foreword);
 - (3) FHA Application Form (2013 or 2013R), with instructions for completion;
 - (4) FHA Form 2530 - Previous Participation Certificate;
 - (5) FHA Form 3433 - Request for Preliminary Determination of Eligibility as Nonprofit Sponsor or Mortgagor (if applicable);
 - (6) FHA Form 2417 - Personal Financial and Credit Statement;
 - (7) FHA Form 2010 - Equal Employment Opportunity Certification;
 - (8) Management Requirements in Processing Insured Multifamily Housing Projects (Reference (12) of the Foreword);
 - (9) Project Selection Criteria Questionnaire, FHA Form 3167; and
 - (10) Affirmative Fair Housing Marketing Plan, HUD Form 935.2.
- b. The Objectives of Assisting Sponsors to Submit Feasible Proposals under Section 236 may be achieved more easily when field office staff has assembled information and forms before the initial contact with a potential sponsor.
- c. The Rent Formula Rates in the Section 236 Tables are the composite rates which relate net basic income to support project cost. They provide for mortgage amortization on the hypothetical 1% Level Annuity Monthly Payment (LAMP) mortgage

and additional cash flow at a regulated rate. The additional cash flow for a limited distribution mortgagor is a 6% return on an assumed 10% equity investment. For a nonprofit

mortgage, the additional cash flow is a new income reserve amounting to 6% of the total net income.

d. For example, assuming a 40 year mortgage term (P & I @ 1% = 3.03427%).

(1) The rent formula rate for a limited distribution mortgagor would be:

Mortgage	90% x 3.034273%	=	2.731%
Equity	10% x 6.0%	=	.6 %
Rent Formula Rate		=	<u>3.331%</u>

(2) For a nonprofit mortgagor, the rent formula rate would be:

$$\frac{3.034273\%}{94\%} = 3.228\%$$

e. The Rent Formula Rates for Cooperative Mortgagors provide only for mortgage amortization on a hypothetical 1% LAMP mortgage without additional cash flow. Therefore, the rates for cooperative mortgagors are the same as the debt service rates on a hypothetical 1% LAMP mortgage.

4-4. APPLICATION FOR FEASIBILITY REVIEW. Subsequent to the initial (pre-feasibility) conference, the sponsor will submit a completed application for feasibility review on FHA Form 2013. This is the same form submitted as application for commitment of mortgage insurance. When the application requests feasibility review, the box marked "feasibility" in the right hand corner should be checked. All documents and information required for feasibility processing should be submitted simultaneously.

a. The Sponsor's Submissions must be reviewed in order to determine whether they are complete and acceptable for feasibility processing. The sponsor should submit all information requested except that marked with solid triangles on the application (FHA Form 2013).

(1) In the event the submission is incomplete, it is to be returned to the sponsor immediately with a clear statement concerning imperfections. Under no circumstances are incomplete submissions to be scheduled for processing.

- (2) Particular attention must be given to proper completion of the site information portion of Section (a) and all of Section (b) relating to land acquisition.
 - (3) All required project information must be entered on the FHA Form 2013 itself and not be referenced to other sources, documents or exhibits.
 - (4) When it is determined that the submission is sufficiently complete for processing, the Receiving Clerk should be notified so that a project number may be assigned. The Receiving Clerk must also be notified of any subsequent action that would require a change in the project number.
- b. The Sponsor Should Be Notified at the time of the initial conference if there is a lack of available contract authority. Should the sponsor still desire to submit an application, it may do so. In such circumstances, its submission should be reviewed for completeness and overall acceptability, and a Project Selection Criteria rating should be established. If the application is generally acceptable, the sponsor should be notified that the application will be held in abeyance pending receipt of further allocation of contract authority.
- 4-5. FEASIBILITY. Key decisions concerning project feasibility, including those concerning location, land value, project size and type, rent levels, expenses, project cost estimate, construction budget, tentative mortgage amount, expected cash requirements, and sponsor acceptability, are made at the feasibility stage of processing.
- a. During the Feasibility Processing Stage, the specific site and general area are to be examined to determine suitability for the type of project proposed and the market to be served. This determination is to be based on the overall merits of the general area and the specific site, giving appropriate consideration to the needs of the intended occupants. Included in the overall determination of site acceptability is the availability of alternate sites within the intended market area and available for the same use. Land planners and engineers may, at the discretion of the Program Manager (or MFC), be asked to participate in this stage of processing.

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- (4-5) b. The Financial Capability, Reputation, Experience and Ability of the Sponsor are to be analyzed to determine whether the sponsor will be able to develop a successful project and has the resources to complete it. An early determination of the acceptability of the sponsoring entity is fundamental to

multifamily processing. The initial determination as to acceptability requires an analysis of the sponsor's experience and ability to obtain credit as compared with the size and cost of the project which is proposed. Pertinent information about the sponsor and the project, including its financial requirements, are obtained from the sponsor's application and the accompanying exhibits (particularly from FHA Forms 2013 and 2417) and from data supplied by the Cost Analyst and the Valuation Section. If it appears that, on the basis of experience and credit, the sponsor is capable of undertaking the project, FHA Form 2530 (for previous participation clearance) will be processed in accordance with outstanding instructions. In the case of a nonprofit sponsor, FHA Form 3433 will also be reviewed in accordance with administrative instructions. FHA Forms 2013, 2417, 2530 and 3433 are included in the Appendix (see Appendices 7, 8, 9, and 10).

- c. The Feasibility Analysis includes determination, based on data from Economic Market Analysis Division (EMAD), of whether a market for the project exists (in terms of the number of units, their sizes, composition, and proposed rentals) at the proposed locations.
- d. The Design Concept and the Site Plan must be examined for suitability in terms of the number and placement of buildings on the site, and the location and amount of parking, availability of recreation facilities, landscaping, general aesthetic appeal, and related characteristics. Good design will make every feasible effort to offset any "low cost" stigma.
- e. The Sponsor must have an acceptable management program since efficient management plays an important role in the ultimate success of a project.
- f. In General, if the sponsor's estimated total project cost and required mortgage amount do not exceed by more than 2% the maximum cost and mortgage amount supported by debt service requirements as estimated by HUD-FHA, the project can be considered economically feasible; of course, the other essential elements of the proposal still must be acceptable to find the project feasible.

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- 4-6. PRE-FEASIBILITY PRESENTATION CONFERENCE. Following the investigation stage of processing, a Pre-Feasibility Presentation Conference may be held to permit the Field Office Director, the Chief Underwriter, or Director of Operations, to review the key decisions tentatively made as to the acceptability of a project.

This is an opportunity to confirm or to reject a proposal and to concur in decisions made by the MFC or production division prior to the Feasibility Conference with the sponsor.

- a. Presentation Package. FHA Form 2264, (reflecting processing conclusions, see Appendix 11), FHA Form 2013 (the sponsor's application), applicable exhibits, and the proposed Feasibility Letter, constitute a package to be presented at the Pre-Feasibility Presentation Conference (but see Chapter 9 for housing for the elderly and handicapped).
 - b. Further Investigation. If a review of the presentation package indicates a need for further investigation of the project, the sponsor will be notified as to which additional data and exhibits are required.
 - c. Acceptable Project. If the project is accepted at the time of this conference, the DO/CU and the Field Office Director indicate their concurrence by signing the FHA Form 2264, which serves as documentation of acceptability of conclusions in advance of the Feasibility Conference with the sponsor.
 - d. The Chief Architect selects the Design Representative with the concurrence of the DO/CU and the Program Manager (or MFC).
- 4-7. FEASIBILITY CONFERENCE. Projects for which feasibility review has been completed with a favorable result should be assigned funding in order of priority as established by the Field Office Director through use of the Project Selection Criteria. When the field office is ready to reserve contract authority for a project, a Feasibility Conference with the project sponsor should be scheduled. The purpose of the Feasibility Conference is to advise the sponsor that the project is acceptable. This is the key step in the processing procedure. Everything that transpired in the Initial Conference and in the investigative stage leading to the determination of project feasibility is culminated at the Feasibility Conference by the agreements reached between the Multifamily Coordinator and the sponsor.

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- (4-7) a. Issues to be Discussed with the sponsor at the Feasibility Conference include:
- (1) Acceptability of proposed sponsor.
 - (2) The anticipated market.
 - (3) Acceptability of proposed location.

- (4) Acceptability of the design concept in terms of the type of project appropriate for the site, the area, the program, and the market to be served.
 - (5) Acceptability of management. The sponsor is informed that HUD-FHA is concerned with all aspects of management after completion of construction. The MFC must be assured that the sponsor will provide competent, experienced, professional management.
 - (6) Project economic feasibility. The economic feasibility of the proposal will have been determined in advance of the Feasibility Conference. If the sponsor agrees that the project can be developed within the construction budget limit established by the economics of the proposal, while maintaining all of the necessary utilities, services, and facilities, the MFC issues the Feasibility Letter.
 - (7) Target dates.
- b. A Sample of a Feasibility Letter is included in Appendix 12. A Feasibility Letter for a Section 236 project should normally be written in accordance with this sample, including all elements of the format applicable to a particular proposal. A schedule of target dates should be attached to the Letter. Modifications should be kept to a minimum and be made only to cover unusual situations. When the land value is based on certain assumptions as to the unusual site conditions, a paragraph may be included to qualify the land value subject to confirmation of the assumed conditions.
 - c. The Maximum Mortgage will not necessarily be limited to the requested amount. This instruction is consistent with the concept of making available the maximum mortgage amount consistent with economic feasibility.

- d. During the Feasibility Conference, the MFC is to discuss the additional information and exhibits which will be required from the sponsor for subsequent processing. Only the material for the next stage (conditional or firm commitment) is required, although any additional exhibits, if available, should be provided to HUD-FHA. An important part of the Feasibility Conference is the discussion of future submissions and processing target dates, and agreement by the sponsor and its architect to meet these schedules. The decision of whether to move to either conditional or firm commitment depends on the extent of the sponsor's preparation. Assuming

that his preparation is the minimum required for determining economic feasibility, the sponsor will usually move to a conditional commitment rather than a firm commitment.

- e. The Feasibility Letter and the Preliminary Reservation of Contract Authority should be executed simultaneously. The Field Office Director will execute FHA Form 3126 (Preliminary Reservation of Contract Authority). The sponsor must be informed that there is a 60-day time limit, beginning on the date of issuance of the Feasibility Letter, for the submission of its application for commitment. The Field Office Director may extend this time period when, in his judgment, circumstances warrant it. Sponsors should not be encouraged to expect such extensions.
- 4-8. COMMITMENT PROCESSING. The sponsor, through his mortgagee, will submit an application for project mortgage insurance on FHA Form 2013 (with fees) marking the right hand corner of the form to indicate whether the application is for conditional or firm commitment. This application for mortgage insurance should be accompanied by a copy of the Feasibility Letter.
- 4-9. PROCESSING PROCEDURE FOR BUILDER'S AND SPONSOR'S PROFIT AND RISK ALLOWANCE (BSPRA) AND SPONSOR'S PROFIT AND RISK ALLOWANCE (SPRA). These instructions provide specific processing procedures for use when an (a) identity of interest exists, (b) does not exist, or (c) ceases to exist, between the mortgagor and general contractor in projects where the Builder's and Sponsor's Profit and Risk Allowance (BSPRA) or Sponsor's Profit and Risk Allowance (SPRA) is permitted by HUD-FHA regulations. An identity of interest will be construed to exist when the mortgagor has any financial interest in the general contractor; when one or more of the officers, directors or stockholders of the mortgagor is also

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- (4-9) an officer, director, or stockholder of the general contractor; when any officer, director or stockholder of the mortgagor has any financial interest whatsoever in the general contractor; when the general contractor advances any funds to the mortgagor; when the general contractor provides and pays, on behalf of the mortgagor, the cost of any architectural services or engineering services other than those of a surveyor, general superintendent, or engineer employed by a general contractor in connection with obligations under the construction contract; when the general contractor takes stock or any interest in the mortgagor corporation as part of the consideration paid; when there exist or come into being any side deals, agreements, contracts or undertakings entered into or contemplated, thereby altering, amending, or cancelling any of the required closing documents, except as

approved by the Assistant Secretary-FHA Commissioner.

- a. Required Processing or Re-Processing. Processing or reprocessing will be completed in accordance with the instructions set forth below for the given circumstances.
- (1) It is important that the field office ascertain from the sponsor, when an application is filed for feasibility, conditional commitment, and firm commitment, whether an identity of interest will exist between the mortgagor and the general contractor as of the date of the firm commitment for insurance upon completion cages or as of the date of initial endorsement for cases involving insurance of advances. (See Reference (7) of the Foreword.) If such an identity will exist, the case shall be processed with BSPRA included in the replacement cost of the project.
 - (2) If an identity of interest between the mortgagor and the general contractor will not exist, the case shall be processed excluding BSPRA but including a typical profit and a Sponsor's Profit and Risk Allowance (SPRA). The SPRA allowance shall be 10% of the sum of Architect's fees, Carrying Charges and Financing, and Legal and Organization expenses (see page 2, FHA Form 2264).
 - (3) If BSPRA was included in the replacement cost of a project and the identity of interest between the mortgagor and the general contractor ceases to exist prior to issuance of a firm commitment in insurance upon completion cages, or prior to initial endorsement in cases involving insurance of advances, re-processing is required as set forth in paragraph (2) above.

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- (4-9) (4) If BSPRA was included in the replacement cost of a project and the identity of interest between the mortgagor and general contractor ceases to exist after the issuance of a firm commitment for insurance upon completion cases but prior to initial-final endorsement, and prior to final endorsement for cases involving insurance of advances, revision of underwriting forms is not required. However, SPRA and a typical profit will be allowed in lieu of BSPRA in cost certification, and the final FHA Form 2580 must reflect the maximum insurable mortgage resulting from these adjustments.

b. Implementation.

(1) Administrative Consideration.

- (a) Where BSPRA has been included in FHA Form 2264, in cases involving insurance of advances, a clause shall be inserted in the firm commitment notifying the mortgagor and mortgagee that if, at initial endorsement of the mortgage, there is in fact no identity of interest between the mortgagor and the general contractor, the case will be re-processed to exclude BSPRA and to substitute a typical builder's profit and SPRA.
- (b) It is emphasized that, in all cases, the mortgagor entity cannot be changed without the prior written approval of the Assistant Secretary-FHA Commissioner and is subject to the FHA Form 2530 procedure. In granting such approval, the commitment must be adjusted in accordance with the new computation of replacement cost and the amount of insurable mortgage before issuance of a letter of approval of the new mortgagor entity. Any rebate of fees as a result of re-processing shall be made in accordance with outstanding fiscal instructions.
- (c) Changes in ownership during the construction period should be discouraged. However, when a change in the mortgagor entity is approved by the Assistant Secretary-FHA Commissioner after execution of the Agreement and Certification, FHA Forms 3306 and 3306-A, the new mortgagor is required to execute a new document on the appropriate form and assume, without exception, all obligations of the mortgagor set out in the form.

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- (4-9) (d) Where a change of mortgagors results in no identity of interest between the mortgagor and the general contractor, paragraph 12 of the Agreement and Certification negates the application of BSPRA in cost certification and entitles the mortgagor only to SPRA and the builder to a typical profit. The new owners, if acceptable to the Assistant Secretary-FHA Commissioner, should be informed of these facts at the time of execution of the Agreement and Certification. For more specific instructions involving changes in ownership beyond initial endorsement, see Reference (13) of the Foreword.

- (2) Underwriting Instructions. Any re-processing requires the completion of a revised FHA Form 2438 if one is already outstanding.
- (3) Cost Processing.
- (a) When re-processing is required, the Cost Analyst shall enter in FHA Form 2264 (Items G-44 and G-50), the same amount of builder's profit used in calculating architects' fees when the case was previously processed as a BSPRA project.
- (b) In cases where SPRA is substituted for BSPRA at the time of cost certification, the reviewing Cost Analyst shall allow a builder's profit as provided in subparagraph (a) above but no revision of FHA Form 2264 will be made. In addition, the net (plus or minus) effect of all approved changes shall be adjusted to reflect a builder's profit inasmuch as such profit was not included in the dollar amount of the changes during processing as a BSPRA project. The net dollar effect of all changes will be shown on the copy of the last approved FHA Form 2437 retained by the field office.
- (4) Valuation Processing. Please see Chapter 5 of this Handbook.

- (4-9) (5) Mortgage Credit Processing.
- (a) When reprocessing is required as indicated in subparagraph (3)(a) above, the mortgage credit processor shall complete a new FHA Form 2264-A based on the new FHA Form 2264 completed by the Project Appraiser. The amount of SPRA shall be entered in Section II, Part A, Item 5, inasmuch as it will not be available for payment during construction. In rehabilitation projects, the amount of SPRA should also be shown as part of the total entered in criterion 6a of that form.
- (b) If, in a case involving insurance of advances, the required re-processing occurs after completion of FHA Form 2283 and prior to initial closing, a new form must be completed to indicate the revised financial requirements for closing. The new form is to be completed as directed in outstanding instructions with the following exceptions: Delete

the words "Consultant Fee (nonprofit only)" from item 21, insert "SPRA" immediately thereafter and enter the amount thereof in the dollar column. Add the words and dollar space "MINUS SPRA \$ _____" to the wording in Item 26 and enter in the dollar column the amount of Item 25 reduced by the amount of SPRA. Delete the words "Consultant Fee (nonprofit only)" from Item 40, insert "SPRA" and enter the Amount thereof in the dollar column.

- (e) In cases where SPRA is substituted for BSPRA at the time of cost certification, the Mortgage Credit Reviewer will allow in Item 14b, FHA Form 2331-A, 10% of the sum of the allowed amounts for architects fees, carrying charges and financing, legal and organization expenses and off-site costs. The final FHA Form 2580 must reflect the maximum insurable mortgage resulting from the adjustments required by this paragraph. Therefore, if a change in ownership, as approved by the Assistant Secretary-FHA Commissioner, results in no identity of interest between the mortgagor and the general contractor,

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and such change occurs after issuance of FHA Form 2580 but before initial-final or final endorsement, cost certification determinations must be amended by substitution of SPRA for BSPRA, and a new FHA Form 2580 must be issued to supersede the outstanding FHA Form 2580.

- 4-10. PROTOTYPE UTILITY ANALYSIS. For each of the areas within their jurisdiction, field offices shall prepare prototype utility analyses of utility combinations and fuel types which provide maximum operating economy for buildings of various styles, sizes, and types of construction. Each analysis shall be prepared on HUD Form 51994 (Comparative Analysis of Utility Costs) in accordance with instructions and the procedures in Bulletin No. LR-11 (Selection of Utilities Low-Rent Housing).

All combinations of utilities, fuels and methods of purchase commonly used and available in each area should be considered and analyzed. Utility combinations considered acceptable shall be reviewed and updated at least annually, or any time that a new rate schedule becomes available or a significant change in utility rates or other cost factors occurs. As new analysis procedures or form are developed, changes will be included in revisions of Bulletin LR-11.

a. Preparation.

- (1) In an Area Office, the Architecture and Engineering Section is to prepare the prototype analysis, drawing on operating expense and other data held by the Real Estate and Valuation Section and Maintenance Engineer, Housing Programs Branch.
- (2) In an Insuring Office, the Architectural Section is to prepare the prototype analysis, with assistance from the Valuation Section and the Mortgage and Properties Division.

b. Review and Approval.

- (1) In an Area Office, each completed prototype utility analysis is to be routed through the Real Estate and Valuation Section and the Housing Management Division for review and recommendations and then routed to the

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- (4-10) Assistant Director, Technical Services Branch, for approval or rejection. The Assistant Director, Technical Services Branch, is responsible for determining that all feasible combinations of utilities and fuel types have been properly analyzed and that the most economical initial and long-term utility combinations and fuel types are selected for use in connection with subsidized housing programs.
- (2) In an Insuring Office, each completed prototype utility analysis is to be routed through the Valuation Section and Mortgages and Properties Division for recommendations and then routed to the Chief Underwriter for approval or rejection.
 - (3) A copy of each approved prototype utility analysis shall be sent to the Regional Office Utilities Specialist (or Maintenance Engineer if there is no Utilities Specialist) who is responsible for monitoring and advising Field Offices as to provision of utilities for all HUD assisted housing. The Utilities Specialist (or Maintenance Engineer) will recommend acceptable utility combinations when his analysis differs from that of the Area or Insuring Offices. He is to advise these offices of changes, such as in rate schedules, which may affect cost and provision of utilities.

- (4) The approved prototype utility analyses developed by Field Offices shall be made available to housing authorities, developers, sponsors, architects, and others who wish to submit proposals for housing construction.
- c. Local Authority or Sponsor's Submission of HUD Form 51994. When the utility combination desired by a sponsor would not produce the most economical use of utilities as shown by the list of HUD-FHA approved prototype utility analyses for the size and type of project, the applicant shall prepare HUD Form 51994 (Comparative Analysis of Utility Cost). This form shall be sent to the Architecture and Engineering Section (Area Office) or Architectural Section (Insuring Office) for review and recommendations and then routed as set forth in paragraph 4-9.b.(3)(b), above, for review and approval or rejection.