

**Cost Controls and Safe Harbor Standards  
for Homeownership Development  
Effective April 1, 2004**

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To expedite the homeownership review process, HUD is instituting safe harbor and maximum fee ranges for a number of costs relating to homeownership projects. *These cost controls only apply to homeownership plans that call for fee-simple sale of newly constructed or rehabilitated units receiving the benefit of public housing funds or public housing land.* The standards do not apply to programs where public funds are only used for direct financing to the purchaser, or programs where no public housing funds are involved. This guidance is specific to homeownership developments, and does not apply to rental phases or lease-purchase projects. Lease-purchase units must comply with the Rental Cost Controls and Safe Harbor Standards. Any terms previously approved by HUD through approval of the predevelopment agreement, development agreement, or program manager contract are not subject to further review.

HUD's Cost Controls and Safe Harbors are contained in the following chart. The chart provides a brief definition of each term, lists the safe harbor and maximum allowable fees, and briefly describes the risk factors or circumstances that may result in a fee above the safe harbor standards. Housing authorities, developers, and consultants should use these guidelines when negotiating terms and drafting homeownership documents for HUD review.

HUD will review the project terms when receiving predevelopment and development agreements, program manager contracts, homeownership proposals, and/or other documents that contain negotiated terms. If a project is at or below a safe harbor standard, no further justification to HUD will be necessary. If a project is above a safe harbor standard, additional review by HUD will be necessary. In order to approve terms above the safe harbor, the housing authority must demonstrate to HUD that the negotiated terms are appropriate for the level of risk involved in the project, the scope of work, any specific circumstance of the development, and the local or national market for the services provided.

## Cost Control and Safe Harbor Standards

Item	Defining Criteria	Safe Harbor	Maximum
<p>Net Developer Fee for Homeownership Developments (Developer Fee and Overhead)</p>	<p>The safe harbor and maximum standards apply to net developer fee, i.e., the portion of the developer fee received by the developer to cover overhead and profit.* Payments to developers such as “deferred developer fee” are considered part of the fee/overhead amount. The developer fee may not be paid from public housing funds.</p> <p>Net developer fee is expressed as a percentage of the project costs. Project costs are defined as all hard and soft costs of constructing a particular component with the <b>exclusion</b> of the following:</p> <ul style="list-style-type: none"> <li>• Third-party costs paid by the PHA under contracts entered into directly by PHA and third parties, which will not be reimbursed to PHA upon receipt of construction financing (e.g., where the PHA contracts separately for demolition services or program management services);</li> <li>• The developer fee itself;</li> <li>• All costs related to family self-sufficiency, homeownership counseling, and resident relocation activities.</li> </ul> <p>A homebuilder who is receiving a developer fee may receive up to a 6% fee for general conditions, but is not permitted to charge a fee for overhead or profit.</p> <p>Developers may receive up to a 1% addition to their fee (with a cap of 12% developer fee) in any of the following ways:</p> <ol style="list-style-type: none"> <li>1) Where the sales prices of some of the units exceed the construction/rehabilitation costs, the developer and housing authority may share the profit.</li> <li>2) Where actual sales prices of the units exceed the anticipated sale price, the developer and the housing authority may share the profit.</li> <li>3) Where there are cost savings from non-public housing sources, the developer and housing authority may share the savings.</li> </ol> <p>Profits or savings in excess of the 1% addition to the developer fee constitute PHA program income to be used for eligible program costs or other low-income housing purposes</p> <p>Developers should follow the construction lenders’ underwriting standard regarding required number of pre-sold homes.</p>	<p>9% or less of the project costs (profit and overhead).</p>	<p>12% of the project costs (profit and overhead) with justification to HUD.</p>

\* The safe harbor and maximum guidelines assume the net developer fee excludes any portion of the fee received by the developer or co-developer (including a PHA) that is returned to the project to cover project costs.

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Item	Defining Criteria	Safe Harbor	Maximum
<p>Net Developer Fee for Homeownership Mixed-Finance Developments (continued)</p>	<p>Developers with fees above the safe harbor standard should meet most or all of the following factors:</p> <ul style="list-style-type: none"> <li>• Developer obtains private debt financing to cover some portion of construction costs;</li> <li>• Developer and/or associated broker is responsible for sale of the homes and will not receive a separate broker's fee;</li> <li>• Developer obtains site control from an entity other than a PHA, PHA affiliate or City (fee increases with number of sites);</li> <li>• Developer acquires sites with own funds and is not reimbursed during pre-development.</li> <li>• Project is small (e.g., 20 units or less);</li> <li>• Developer carries the financing of model home(s);</li> <li>• Project is complex (e.g., financial, legal, site acquisition, non-contiguous lots, environmental, and/or political);</li> <li>• At least 50% of the homes are sold to existing public housing residents;</li> <li>• A minimum of 50% of the developer fee is deferred until 100% of the homes are sold;</li> <li>• The developer bears a minimum of 50% of the predevelopment costs (until developer's receipt of construction financing).</li> </ul> <p>All criteria apply to both for-profit and non-profit developers.</p> <p>PHAs or PHA affiliates that act as developer can only receive fees if they are first returned to the project and, to the extent that funds are remaining, subsequently classified as program income and used for low-income housing purposes.</p>		
<p>Pay-Out Schedule for Developer Fee/Overhead</p>	<p>Except as noted below, public housing funds may not be used for payment of developer fee/overhead. Where public housing funds pay 100% of the construction financing, only permanent, non-public housing fund sources may fund the developer fee. HUD limits the pay-out schedule, to the extent that non-public housing funds are available, by phase:</p> <ul style="list-style-type: none"> <li>• At mixed-finance closing, no more than 50% of the fee/overhead amount.</li> <li>• Upon sale of individual home; pro rata share of the remaining fee per home sold.</li> </ul> <p>A portion of the fee can be further deferred.</p> <p>On a case-by-case basis, HUD will consider advancing the developer fees where there is an extended predevelopment period caused by such external factors as environmental remediation, consent orders, etc. If HUD determines such an advance is warranted, the PHA can disburse up to 15% of the total developer fee/overhead amount (not to include legal fees) to the developer prior to receipt of construction financing.</p>	<p>Within recommended pay-out schedule.</p>	<p>Payments of greater than 50% upon receipt of construction financing and pro rata share per sale of individual home with justification to HUD.</p>

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Contractor Fee for Non-Bid Contracts	<ul style="list-style-type: none"> <li>Percentages are based on hard construction cost (not including contingency).</li> <li>General Conditions includes the bond premium.</li> <li>A homebuilder who is receiving a developer fee may receive up to a 6% fee for general conditions, but is not permitted to charge a fee for overhead or profit.</li> </ul>	Overhead: 2% Profit: 6%  General Conditions: 6%	14% is the maximum for these combined costs provided that the PHA justifies why the 2/6/6 percentages for the individual costs cannot be met.
Total Amount of Public Housing Funds for Construction Financing	The PHA may provide public housing funds for a construction loan, but the loan amount may not exceed the TDC limit.	N/A	The allowable Total Development Cost of the project.
Total Amount of Public Housing Funds for Permanent Financing	The PHA may provide public housing funds for permanent write-downs* and financing directly to purchasers. Collectively, these public housing funds must be within the TDC limit.	N/A	The allowable Total Development Cost of the units.
PHA Administrative/ Consultant Costs	<ul style="list-style-type: none"> <li>Costs should reflect only documented expenditure of time and overhead cost (supplies, equipment, telephone, etc.).</li> <li>Such costs include both in-house staff time and outside consultants (program manager, development advisors, relocation specialists, etc.), but exclude outside legal and community and supportive services costs. On the HUD budgets, these costs may be captured under multiple BLIs.</li> </ul>	3% of the total project budget (basis includes all hard and soft development costs <b>excluding</b> CSS expenses).	6% of the total project budget with justification to HUD.
Fee for Program Management Services	<ul style="list-style-type: none"> <li>Typically a fixed-price contract.</li> <li>Contracts must be performance-based with payments fixed to milestones (or monthly if tied to milestones).</li> <li>Size of fee should be related to the specific scope and role PM is expected to play.</li> <li>Costs for program management (either a full team or independently procured consultants) must be included in the PHA's Administrative Cost Cap.</li> <li>PHAs must comply with the provision of the procurement regulations that requires a PHA to prepare a cost estimate for procured services prior to receipt of bids.</li> </ul>	N/A; the fee must be contained within the PHA's overall Administrative Cost Cap. Use checklist of responsibilities and clearly defined scope to limit costs.	N/A

\* A permanent write-down is a grant that makes up the difference between the appraised value of the unit (i.e., sales price) and the actual construction cost.

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<p>Sharing of Third-party Predevelopment Costs</p>	<p>HUD recommends the following cost-sharing schedule:</p> <ul style="list-style-type: none"> <li>• PHA and Developer split third-party costs 75/25.</li> <li>• Developer's share of third-party costs (25%) will be reimbursed upon receipt of construction financing out of available sources.</li> </ul> <p>Costs to be shared are all third-party costs under the developer's scope of work (e.g., A/E, market study, etc.) incurred during the predevelopment period. Public housing funds may not be used to reimburse developer legal counsel prior to receipt of construction financing. Because site acquisition is not a third party cost, it is not subject to the 75/25 split of third-party costs.</p>	<p>Costs are shared up to 75% by the PHA and at least 25% by the Developer.</p>	<p>A PHA may pay up to 100% of third-party predevelopment costs to small, local, non-profit, and/or minority/disadvantaged firms with justification to HUD.</p>
<p>Identity of Interest Parties</p>	<ul style="list-style-type: none"> <li>• Identity of interest parties are those that share an ownership interest. Identity of interest relationships are most common between a developer and construction management, general contractor (GC), architect/engineer (A/E), broker, and/or equity provider.</li> <li>• PHAs are required to ensure cost competitiveness to the extent possible.</li> <li>• Where a developer and GC have an identity of interest, the PHA needs to conduct an independent cost estimate, and submit that estimate to HUD.</li> <li>• HUD recommends those developers who wish to select a homebuilder for construction of homeownership units do so through competitive selection.</li> </ul>	<p>N/A</p>	<p>N/A</p>
<p>Legal Fees</p>	<ul style="list-style-type: none"> <li>• Fees should be largely dependent upon the complexity of the project (e.g., number of sites, sales, and/or land transfers). HUD will review PHA legal costs when reviewing development budgets.</li> <li>• In order to reduce costs and provide an incentive to reach closing, public housing funds may not be used to pay developer legal costs prior to the developer's receipt of construction financing. The developer legal costs are in addition to the 25% of third-party costs the developer bears until receipt of construction financing.</li> </ul>	<p>N/A</p>	<p>N/A</p>

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Item	Defining Criteria	Safe Harbor	Maximum
Subordinate Mortgage Administrator	<p>Where the PHA provides subordinate mortgages to the purchasers in its homeownership program, the PHA may procure loan administration services instead of conducting this activity in-house. The loan administrator's responsibilities may include:</p> <ul style="list-style-type: none"> <li>• development of standardized loan documents with the PHA;</li> <li>• administration and servicing of the subordinate mortgage to purchasers; and</li> <li>• tracking of payment on the subordinate mortgage upon resale, bankruptcy, or foreclosure.</li> </ul>	Fees should reflect local market standards.	
Broker Fees	<p>The broker fees should reflect local market standards. If the broker has an identity of interest relationship with the developer, the PHA must require the developer to assure that the broker's fees are competitive. Likewise, a homebuilder's broker fees must be reflective of local market standards.</p>	Fees should reflect local market standards.	N/A
Homebuyer Training/ Counseling	<p>The PHA may choose to procure an entity or to perform these services in-house.</p> <ul style="list-style-type: none"> <li>• The homebuyer counseling contracts must be performance-based and are usually funded through the housing authority's Community and Supportive Services budget.</li> <li>• PHAs should refer to their locality's First Time Homebuyer program and existing providers of this service for guidance on appropriate homeownership counseling fees.</li> </ul>	Fees should reflect local market standards.	N/A