

Notes on the Development Budget

Note: This handout was created for cohousing financing workshops presented by Design Coalition in 1992

ACQUISITION COSTS

Lines 1-2

Land or property acquisition costs normally match the price paid to acquire the property. If the land or building(s) were acquired sometime ago, an estimate of current value will be necessary for the project.

CONSTRUCTION COSTS

Line 3

Site development refers to land improvements. "Usual" improvements are costs such as excavation for foundations or utilities, grading of the site, installing on-site utility lines, roads, walkways or parking areas. Landscaping, outdoor lighting and other permanent improvements to the site also qualify as usual improvements. Note that this category does not include the costs of soil borings or surveys.

"Unusual" improvements are costs which would not normally be incurred to prepare a site for construction or to put it in usable condition after construction. These costs include such things as demolition of existing buildings, removal of large amounts of earth to an off-site location or moving earth from off-site for fill or grading, off-site utility or road extensions, or other unusually large or exceptional costs.

Bear in mind that the cost of land improvements will typically be included in a construction contract even though the actual work may be done by a sub-contractor. Accordingly, these costs should be based on a contractor's estimate.

Line 4

Construction includes any rehabilitation of existing buildings as well as the cost of new buildings. The amount estimated under this heading should cover all costs included in the construction contract. Besides the "hard" costs of materials and labor, the contract price will typically include such items as an allowance for the contractor's project-related expenses such as building permits, site fencing, temporary utility connections and storage for materials. These expenses are referred to as "overhead" or "general requirements". This line item also includes the contractor's profit and the cost of a performance bond to ensure project completion.

The best way to estimate construction costs is to obtain a preliminary projection from a contractor. An alternative is to have your architect estimate the costs based on comparable projects. In some cases an architect or contractor may only wish to estimate the costs of material and labor. In such cases you can adjust that figure by adding: (A) 3-4% for overhead, (B) an estimate on bond costs from a bonding company or local lender, and (C) an allowance of 8-10% of all preceding costs for the contractor's profit.

PROFESSIONAL SERVICES

Line 5

Architectural fees should be based on an estimate from the architect. These fees may be based on a percentage of the construction contract, a fee per dwelling unit, a flat fee for services or some other basis. There is commonly one fee for design and another for inspection services.

The cost of a property survey, soil borings and mechanical and structural engineering tasks and other architect's consultants may be included under architectural fees because these costs are related to the design of the site plan and buildings, and are often sub-contracted by the architect on behalf of the sponsor. Be sure to ask what is covered in the estimate and, later, in the actual contract for services.

Line 6

Legal fees will be incurred throughout a project for tasks such as legal incorporation, contract negotiations, property acquisition, loan closings, management agreements and joint ventures. Unless your project is highly unusual and will require an inordinant amount of legal work, it is possible to get a ballpark estimate by comparing yourselves to other similar projects.

Line 7

In buying land or real property it is almost always necessary to get an appraisal of the property. It is important to make sure that the appraiser you plan to use is acceptable to your lender, since lenders rely on the quality of the appraisal when underwriting loans. Most lending institutions keep a list of approved appraisal firms from which you can choose. Those firms or individuals can provide you with an estimate for services.

Line 8

If the architect for your project does not include the price of the survey in the contract, you'll have to get one independently. Be sure to get estimates from a variety of firms and select one that meets your budget.

Line 9

Consulting fees may or may not be part of your budget. If you are not experienced with the housing development business you may choose to get some assistance from people with more experience.

The costs of engaging a developer or project manager can be significant, but the benefit of experience and assistance can save time and costly mistakes.

LOAN FEES & POINTS

Lines 10-12

Loan fees and points are part of the cost of the capital used to finance the project. These are one-time fees (a percentage of the total loan) which you pay to the lender at closing. Loan points, like interest rates, are changeable and sometimes negotiable. Shop around for financing at a variety of lending institutions, as rates and fees can vary considerably.

HOLDING COSTS

The period of time between the beginning of construction and the date when the project is fully occupied is called the holding period. Since any expenses the project incurs during this time are the responsibility of the developer/sponsor, it is important that you estimate them accurately.

Line 13

Predevelopment and construction loan interest is simply the interest accrued on financing before the final closing. It can be calculated by projecting the period of time you expect to be using those funds until the project is completed and this "interim" financing is replaced by permanent financing.

Line 14

Operating expenses incurred during the holding period should be included here, and will include things such as utility costs, maintenance and insurance.

Line 15

Real estate taxes usually have to be paid on a property during the construction period. The sponsor should consult with local taxing authorities to determine the basis on which the property will be assessed, based on preliminary development plans and on the anticipated starting and completion dates for construction. The annual estimated tax bill should be prorated for the construction and marketing period.

Line 16

The contractor will carry separate builder's risk and liability insurance, but the sponsor may want to

carry hazard insurance against damage to the building during construction. You may also wish to carry insurance against theft and liability for personal injury or property damage.

Line 17

These line items are to ensure that you have clear title to the property before construction begins. Title insurance protects the lender and recording the deed protects the title. The mortgage held by the lender must also be recorded. The sponsor's attorney or a title insurance company can estimate these costs for you, given a specific property and an estimate of development costs.

Line 18

Marketing and management start-up costs are incurred between completion of construction and full occupancy. The development budget should reflect your best guess at the lag between construction completion and the beginning flow of income to cover permanent debt payments. This figure should include any costs associated with the marketing or rental of units, including advertising and staff time for application reviews.

MISCELLANEOUS EXPENSES

These lines are included to cover costs that are particular to your project. This section can also be the place where you enter a contingency amount in the budget to cover unforeseen or expanded costs to the project.

PART II ~~ SOURCES OF FUNDS

Lines 22-28

This portion of the budget identifies all of the sources of project financing. As the model indicates, there are a variety of financing options available for housing development and the examples cited here are not meant to be exhaustive, but illustrative. Affordable housing projects will usually have more sources of funds and a more complicated "sources" budget. Permanent financing always "takes-out" (or replaces) the interim financing used during the predevelopment and construction periods.

Project sponsors should identify feasible sources of funding for the project. Initial meetings with potential lenders is a good place to begin, and will help you to identify the specific interest rate and terms of the loan(s) for your budgets.

Line 29

This line should reflect any differences between the project costs of development and the sources you believe will be available for financing. It is expressed as a "gap" that needs to be filled.

TOTAL PERMANENT FINANCING FOR THE PROJECT MUST EQUAL OR EXCEED THE TOTAL DEVELOPMENT COSTS TALLIED AT THE BOTTOM OF YOUR "USES" BUDGET.