

VIRGINIA HOUSING DEVELOPMENT AUTHORITY

COST CERTIFICATION GUIDE FOR MORTGAGORS,
CONTRACTORS AND CERTIFIED PUBLIC ACCOUNTANTS

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COST CERTIFICATION GUIDE

1. PURPOSE.

This guide sets forth the standards and criteria to be followed in the preparation of the Certificates of Actual Costs and in the conduct by independent public accountants of the audits (if required) for multi-family housing developments financed by the Virginia Housing Development Authority ("VHDA").

2. GENERAL.

(A) Purpose of Certification. The principal purpose of cost certification is to establish the total costs to acquire, construct and/or rehabilitate, as may be applicable, and finance the development so that VHDA may determine at final closing the total development cost of the development, the final principal amount of the mortgage loan and the mortgagor's equity in the development. As used herein, the term "construction" shall refer to new construction and/or rehabilitation, as applicable. The term "final closing" shall (i) in the case of a VHDA mortgage loan which provides the construction and permanent financing, refer to the final closing as described in the construction loan agreement, (ii) in the case of a VHDA mortgage loan which provides permanent financing only, refer to the closing of the VHDA permanent mortgage loan, or (iii) in the case of a construction and permanent mortgage loan financed by VHDA in participation with a private lender, the conversion of the construction loan to the permanent loan (referred to as the "Permanent Conversion" in the construction loan agreement).

This guide is not intended, and shall not be construed, to benefit or protect any person or entity other than the parties expressly made subject to the terms of this guide and their successors and assigns, or to provide any such other person or entity with any rights or remedies against the parties subject hereto, or to otherwise entitle any such other person or entity to rely on the implementation or enforcement of any term or provision of this guide. Nothing contained herein shall be construed to create any contractual or other legal relationship that does not otherwise exist under contract or by operation of law.

The term "contractor" as used in this guide shall refer to the general contractor under the construction contract. The term "subcontractor" as used in this guide shall include material and labor suppliers and equipment lessors.

(B) Identity of Interest Relationships. An identity of interest means any relationship that would give the mortgagor or contractor control or influence over the prices paid to subcontractors. The identity of interest relationship is usually created by a financial or ownership interest but could be created by other means such as a family relationship. The following are examples of relationships under which an identity of interest shall be construed to exist:

- (1) When the mortgagor or contractor or any officer, director, partner, member, or stockholder of the mortgagor or contractor is also an officer, director, partner, member or stockholder of any subcontractor or has any other direct or indirect financial or ownership interest in any subcontractor;
- (2) When any subcontractor or any officer, director, partner, member, or stockholder of such subcontractor has any direct or indirect financial or ownership interest in the mortgagor or contractor; or
- (3) When there exists any family relationship between the officers, directors, stockholders, partners or members of the mortgagor or contractor and officers, directors, stockholders, partners or members of any subcontractor.

The costs paid to identity of interest subcontractors shall be no higher than the best prices which could be obtained from other subcontractors with similar experience and capability providing comparable labor and/or materials in the area of the development. VHDA shall have the right to disapprove any costs paid or to be paid to an identity of interest subcontractor in excess of such best prices. In addition, VHDA shall have the right to disapprove any profit paid to an identity of interest subcontractor which failed to perform the subcontract as a "subcontractor" according to the customs of the particular trade (i.e., use and control of its own labor force, maintenance of payrolls, use of tools and equipment) or to perform the construction work by utilizing its own labor force to the extent customary in the particular trade or which served merely as a conduit subcontracting for the performance of work by others.

(C) Contracts for Performance of Contractor's Duties. In the event that the mortgagor or contractor shall enter into a contract with any other party (other than its own employees) for the performance of some or all of the duties and functions (such as subcontracting, coordinating or supervising the work) normally performed by the contractor under the construction contract, VHDA shall have the right to disapprove any fee, profit or overhead paid to such other party and any costs incurred by such other party for the performance of duties and functions also performed by the contractor.

(D) Time for Submission. The mortgagor's Certificate of Actual Costs and, if required, the contractor's Certificate of Actual Costs must be submitted to VHDA at least 30 days prior to final closing of the mortgage loan. VHDA will then review the Certificate or Certificates for compliance with the applicable contracts and this guide and upon completion of such review will establish a final closing date.

3. ELIGIBILITY OF MORTGAGOR'S COSTS AND COMPLIANCE REQUIREMENTS.

(A) General. The total development cost shall be the sum of the mortgagor's costs approved by VHDA as eligible hereunder. The eligibility of the mortgagor's costs shall be determined in accordance with generally accepted accounting principles except as modified by eligibility criteria described in this guide. The mortgagor's Certificate of Actual Costs must be on VHDA Form No. 100. A sample of this form is attached to this guide.

As a general rule, only the costs which have been or will be paid in cash no later than 45 days after the date of final closing or for which funds are escrowed with VHDA at final closing are eligible for inclusion on the mortgagor's Certificate of Actual Costs.

For the purpose of cost certification, the date of substantial completion is the date on which the certificate of occupancy is issued by the appropriate governmental entity for the last unit or units to be completed within the development (if the issuance of certificates of occupancy are not required to be so issued, such date of substantial completion shall be the date determined by VHDA). This date becomes the basis for the establishment of the cut-off date. The cost cut-off date is the date to which the mortgagor is permitted to include its costs for interest, taxes, and property insurance premiums, if any. This date may, at the option of the mortgagor, be either (a) the last day of the month in which substantial completion occurs, (b) the last day of the month following the month in which substantial completion occurs or (c) such other date as VHDA may approve.

The mortgagor's costs must exclude the amount of any kickbacks, rebates, allowances or trade or cash discounts or other similar sums received or to be received by the mortgagor in connection with the construction.

(B) Eligibility- VHDA Construction/Permanent Loans and Permanent Take-out Loans. In the case of developments for which VHDA provides the construction and permanent financing or the permanent financing within one year after substantial completion of construction, eligible costs of the mortgagor are as set forth below.

(1) Construction costs and contractor's profit.

- (a) The eligible amount of construction costs paid or to be paid to the contractor, including any contractor's profit, is the lesser of (i) the actual cash (including any contractor's profit) paid and to be paid by the mortgagor to the contractor no later than 45 days after the date of final closing or (ii) the total contract sum or other maximum contract price under the construction contract (as adjusted for the net effect of all properly approved change orders and including contractor's profit, if any). If the contractor is required by the construction contract to certify its costs in accordance with this guide, the construction costs and the contractor's profit must be shown separately on VHDA Form No. 100 (see paragraph 4(C)(8) below for the amount of contractor's profit which is eligible to be included), and the amount of actual cash paid or to be paid as described in (i) above shall be reduced by VHDA to the extent such amount includes any costs disallowed by VHDA in its review of the contractor's Certificate of Actual Costs. No amounts paid by the mortgagor to any general contractor other than the contractor or to any subcontractor shall be eligible unless the contract between the mortgagor and such other contractor or such subcontractor has been approved by VHDA, and the amount paid to such other general contractor or such subcontractor is correct and proper under such contract. No amounts paid to any employees of the mortgagor shall be eligible unless approved by VHDA.
- (b) If the mortgagor did not enter into a construction contract with a general contractor, the provisions of subparagraph (a) of this paragraph (1) shall not apply, and the eligible amount of construction costs shall be the actual cash paid or to be paid by the mortgagor directly to subcontractors, workers, material suppliers, and equipment lessors no later than 45 days after the date of final closing. Such eligible costs shall not exceed the contract prices in the contracts under which such costs were paid or incurred. Except as otherwise provided in the construction loan agreement, no approval by VHDA of such contracts is required. If any of the workers are employees of the mortgagor, eligible costs shall include the salaries, benefits and payroll taxes paid or to be paid to such workers based upon the time actually spent at the job site exclusively on the construction of the development as evidenced by a record keeping system.
- (c) The contract price for factory-produced modules paid by the mortgagor to the manufacturer will be accepted without cost certification by the manufacturer, unless the manufacturer has an identity of interest with the mortgagor or unless the construction loan agreement requires such cost certification.

(2) Architect's fees.

- (a) Architect's fees are limited to amounts paid or to be paid in cash for architectural design and supervision services, but not to exceed the fees for such services in the owner-architect agreement or agreements without the prior approval of VHDA. No portion of the architect's fee which is paid by means other than cash (e.g., stock subscriptions, notes, or other considerations) or accrues to the benefit of principals in the mortgagor (e.g., rebates or kickbacks) is eligible. Any part of the architect's fees refunded to the contractor is also ineligible.

- (b) Fees paid to an identity of interest architect for supervision services are not eligible, unless approved by VHDA. When it is determined at cost certification that an identity of interest architect performed both architectural design and supervision services, the eligible fee cannot, without the approval of VHDA, exceed the design services fee which is set forth in the owner-architect agreement. Identity of interest means any relationship which would give the mortgagor or contractor control or influence over the fees or performance of the architect. The following are examples of relationships under which an identity of interest shall be construed to exist:
1. When the architect has any ownership or financial interest in the development other than the fee for professional service.
 2. When the mortgagor or contractor or any officer, director, partner, member, or stockholder of the mortgagor or contractor is also an officer, director, partner, member or stockholder of the architect or has any other direct or indirect ownership or financial interest in the architect;
 3. When the architect or any officer, director, stockholder, partner or member of such architect has any direct or indirect ownership or financial interest in the mortgagor or contractor;
 4. When the mortgagor or contractor or any officer, director, stockholder, partner, member or employee of such mortgagor or contractor provides any of the required architectural services; or
 5. When there exists any family relationship between the officers, directors, stockholders, partners or members of the mortgagor or contractor and officers, directors, stockholders, partners or members of the architect.
- (c) Any payments received by the mortgagor or contractor from the architect must be disclosed to and approved by VHDA.

(3) Interest, taxes, and property insurance.

Eligible interest is the amount paid or accrued on the VHDA mortgage loan or other construction loan between the date of closing thereof and the cost cut-off date. Eligible taxes and property insurance premiums are the amounts paid or accrued during the same time period as is used for interest, provided that the amounts were paid in cash or will be deposited in escrow with VHDA at final closing.

(4) Title insurance, recording costs and title examination.

Amounts paid or to be paid for the title insurance policy or policies (including the costs of any title examination and bringdowns performed by the title insurance company) and recording taxes and fees paid at closing of the VHDA mortgage loan or other construction loan, during construction and at final closing are eligible. Legal fees for examination and bringdowns of title shall not be included in this category, but may be included in paragraph (6) of this subsection (B).

(5) VHDA processing and financing fees.

Processing and financing fees are eligible in the amounts paid to VHDA and (if VHDA did not provide the construction financing) to any construction lender. Fees paid to VHDA or such construction lender to renew an expired or terminated commitment or to extend an existing commitment are also eligible.

(6) Legal expenses.

Eligible legal expenses are limited to expenses incurred in organizing the mortgagor, acquiring the property on which the development is located, performing the title examination and bringdowns (if the costs of such examination and bringdowns are not included in paragraph (4) of this subsection (B)), review and preparation of documents for closing of the VHDA mortgage loan or other construction loan and for final closing, and other customary legal services at such closing and final closing and during the construction period. Legal expenses should not include costs incurred in connection with obtaining zoning, sale or syndication of interests in the mortgagor, groundbreaking ceremonies or entertainment. Any legal fees in excess of the amount shown in the mortgage loan commitment are not eligible, unless approved by VHDA.

(7) Off-site costs.

The costs paid under any supplemental contract between the mortgagor and any party other than the contractor in connection with off-site improvements are eligible, subject to approval by VHDA of such supplemental contract pursuant to subparagraph (a) of paragraph (1) of this subsection (B). However, such amount shall not include any off-site expenses which are not recognized in, or which are in excess of the amount allowed in, the mortgage loan commitment and shall not include any off-site expenses included within the construction costs in paragraph (1) of this subsection (B). These costs, however, are not eligible in the case of a leasehold estate in which the ground rent is based on a land value which reflects off-site improvements.

(8) Land, Improvements, and Structures.

The mortgagor is permitted to claim the least of (i) the fair market value (as determined by VHDA on the basis of an independent real estate appraisal) of the land and any improvements which were then located on the land and were retained and used as part of the development, (ii) the purchase price paid by the mortgagor (or, if the mortgagor did not acquire such land and improvements in an arm's-length transaction as determined by VHDA, then by the last party to acquire such land and improvements in an arm's-length transaction) and any carrying charges, such as taxes and interest on a purchase money deed of trust, incurred by the mortgagor or by such party and its successors in interest, or (iii) the amount for such land and improvements shown in the mortgage loan commitment. Notwithstanding the foregoing, if the above described last arm's-length transaction occurred at least two years prior to the filing of the mortgage loan application with VHDA and if the property was then acquired without intent to apply for and obtain a mortgage loan from VHDA, the eligible amount for such land and improvements shall be the lesser of the fair market value of the property as described above or the amount for land and improvements shown in the mortgage loan commitment.

(9) Tap fees, surveys, soil borings, building permits, and bond premium or letter of credit fees.

The mortgagor is permitted to claim costs for tap fees, surveys, soil borings, building permits, and completion assurance bond premium or letter of credit fees if such costs have not been included under either the construction contract or the owner-architect agreement and are not otherwise included as costs claimed on VHDA Form No. 100 or (if required) VHDA Form No. 100A.

(10) Appraisal fees.

Fees paid by the mortgagor for the appraisal(s) of the development required by VHDA or any construction lender are eligible costs in an amount not to exceed the amount shown therefor in the mortgage loan commitment.

(11) Fees of mortgage banker or broker.

Fees paid by the mortgagor to a mortgage banker or broker with respect to the submission to VHDA of the application for the mortgage loan are eligible costs in an amount not to exceed the amount shown therefor in the mortgage loan commitment.

(12) Audit fees.

If an audit is required pursuant to section 5 hereof, the fee paid to the independent public accountant to perform such audit is an eligible cost. Any other fees and costs for cost certification are not eligible.

(13) Relocation Assistance.

Costs attributable to the relocation of tenants as a result of the construction of the development are eligible in an amount not to exceed the amount shown therefor in the mortgage loan commitment.

(14) Incentive Payments and Liquidated Damages.

Incentive payments paid or to be paid to the contractor under the terms of the construction contract are eligible in the amount specified therein. Liquidated damages in the amount specified by the terms of the construction contract must be deducted from the mortgagor's eligible costs.

(15) Other costs.

All other costs must be reasonable, ordinary and necessary and directly related to the construction of the development and are subject to VHDA approval. The costs of any item in excess of the amount (if any) shown in the mortgage loan commitment therefor are not eligible.

(C) Eligibility- VHDA Refinancing or Acquisition Financing. In the case of developments not subject to subsection (B) of this section 3 (e.g., the VHDA mortgage loan is to refinance an existing development or the acquisition of an existing development), eligible costs of the mortgagor shall be as set forth below.

(1) Land, Improvements, and Structures.

The mortgagor is permitted to claim the least of (i) the fair market value (as determined by VHDA on the basis of an independent real estate appraisal) of the land and any improvements which were then located on the land and were retained and used as part of the development, (ii) the purchase price paid by the mortgagor (or, if the mortgagor did not acquire such land and improvements in an arm's-length transaction as determined by VHDA, then by the last party to acquire such land and improvements in an arm's-length transaction) and any carrying charges, such as taxes and interest on a purchase money deed of trust, incurred by the mortgagor or by such party and its successors in interest, or (iii) the amount for such land and improvements shown in the mortgage loan commitment. Notwithstanding the foregoing, if the above described last arm's-length transaction occurred at least two years prior to the filing of the mortgage loan application with VHDA and if the property was then acquired without intent to apply for and obtain a mortgage loan from VHDA, the eligible amount for such land and improvements shall be the lesser of the

fair market value of the property as described above or the amount for land and improvements shown in the mortgage loan commitment.

(2) Title insurance, title examination, and recording costs.

Amounts paid or to be paid for the title insurance policy (including the costs of any title examination and bringdowns performed by the title insurance company) and recording taxes and fees paid at final closing are eligible. Legal fees for examination and bringdowns of title shall not be included in this category, but may be included in paragraph (4) of this subsection (C).

(3) VHDA processing and financing fees.

Processing and financing fees are eligible in the amounts paid to VHDA. Fees paid to VHDA to renew an expired or terminated commitment or to extend an existing commitment are also eligible.

(4) Legal expenses.

Eligible legal expenses are limited to expenses incurred in: organizing the mortgagor and acquiring the property on which the development is located, if the VHDA mortgage loan is to finance the acquisition of the development by such mortgagor; performing the title examination and bringdowns, if the costs of such examination and bringdowns are not included in paragraph (2) of this subsection (C); review and preparation of documents for final closing; and other customary legal services at final closing. Legal expenses should not include costs incurred in connection with obtaining zoning, sale or syndication of interests in the mortgagor, groundbreaking ceremonies or entertainment. Any legal fees in excess of the amount shown in the mortgage loan commitment are not eligible, unless approved by VHDA.

(5) Appraisal fees.

Fees paid by the mortgagor for the appraisal of the development required by VHDA are eligible costs in an amount not to exceed the amount shown therefor in the mortgage loan commitment.

(6) Fees of mortgage banker or broker.

Fees paid by the mortgagor to a mortgage banker or broker with respect to the submission to VHDA of the application for the mortgage loan are eligible costs in an amount not to exceed the amount shown therefor in the mortgage loan commitment.

(7) Repair or rehabilitation costs.

The estimated costs of any repairs or rehabilitation required by VHDA to be performed within one year subsequent to the final closing are eligible costs in an amount not to exceed either the amount shown in the mortgage loan commitment or, if none, the amount estimated by VHDA.

(8) Other costs.

All other costs must be reasonable, ordinary and necessary and directly related to the VHDA mortgage loan or the acquisition (if any) of the development and are subject to VHDA approval. The costs of any item in excess of the amount (if any) shown in the mortgage loan commitment therefor are not eligible. Fees and costs for cost certification are not eligible.

(D) Maintenance of Records. Adequate records must be maintained by the mortgagor for the purpose of verifying costs, and all books, records, contracts, invoices, receiving reports, particulars of material, labor and equipment entering into the construction (if any) of the development, and other records appropriate to such accounts must be made available to VHDA and its representatives for inspection and copying upon request.

(E) Tax Exempt Bond Requirements. The mortgagor must ascertain from VHDA whether the mortgage loan is financed in whole or in part with the proceeds of bonds the interest on which is not included in gross income for federal income tax purposes under Section 142 of the Internal Revenue Code of 1986 ("Tax Exempt Bonds"). In the event that the mortgage loan is providing or will provide with proceeds of Tax Exempt Bonds financing of the acquisition and/or construction of the development or permanent financing upon completion of the construction of the development, certain restrictions and limitations apply with respect to the costs or the portions thereof which are eligible for inclusion in the total development cost. Such restrictions and limitations shall control in the event of any conflict or inconsistency with any other provisions of this guide. Such restrictions and limitations are summarized below:

(1) Unless the mortgagor is a governmental unit as defined in Section 150 of the Internal Revenue Code of 1986, as amended (the "1986 Code"), the mortgagor is required to expend an amount equal to not less than 95% of the proceeds of the mortgage loan (or such portion thereof as is financed with proceeds of Tax Exempt Bonds) for the acquisition, construction, and/or rehabilitation of a qualified residential rental project within the meaning of Section 142 of the 1986 Code, consisting of similarly constructed complete living facilities (including facilities functionally related and subordinate thereto) available for use by members of the general public on other than a transient basis (the amount so expended is referred to hereinbelow as "Qualified Costs"). For the purpose of the preceding sentence, qualified residential rental project shall include only land or property of a character subject to the allowance for depreciation provided in Section 167 of the 1986 Code, the costs of which are chargeable to capital account for federal income tax purposes or would be so chargeable either with a proper election by the

mortgagor or but for a proper election to deduct any such costs. The amount of Qualified Costs so expended by mortgagor must:

(a) be paid or incurred no earlier than 60 days prior to (i) the date on which VHDA approved its resolution authorizing the mortgage loan or (ii) if no such resolution was approved, the date on which VHDA approved a declaration of official intent to reimburse expenditures with proceeds of bonds expected to be issued to finance the development; or

(b) if paid or incurred prior to the 60 day period described in (a) above, be paid or incurred for preliminary expenditures by the mortgagor up to an amount not in excess of 20% of the VHDA's mortgage loan (or portion thereof financed by Tax Exempt Bonds). Preliminary expenditures include architectural, engineering, surveying, soil testing, and similar costs that are incurred prior to the commencement of acquisition, construction, or rehabilitation of the development, other than land acquisition, site preparation, and similar costs incident to commencement of construction.

No such amounts of Qualified Costs may finance (a) retail or commercial space (b) costs to provide swimming pools, recreation facilities, or other health club facilities (i) for which an independent charge is assessed or (ii) which are available to the general public or (c) costs to provide any facility primarily used for gambling or any store the principal business of which is the sale of alcoholic beverages for consumption off premises. No such amounts of Qualified Costs may represent costs to acquire used equipment unless such equipment was purchased as an integral component of an existing structure. No such amounts of Qualified Costs may represent the cost of property or land acquired from a party related to the mortgagor or a profit paid to a person (including the contractor) related to the mortgagor. (Related persons are defined in Section 144(a)(3) of the 1986 Code and include, but are not limited to, members of the same family, an individual and a corporation in which the individual owns, directly or indirectly, more than 50% of the outstanding stock, a subsidiary corporation and a parent corporation which owns more than 50% of the total voting stock of the subsidiary, and a partnership and a partner owning, directly or indirectly, more than 50% of the interest in the capital of the partnership.)

(2) The amount that may be claimed for land and improvements (other than structures) must be less than 25% of the proceeds of VHDA's mortgage loan or such portion thereof as is financed with proceeds of Tax Exempt Bonds.

(3) All amounts of Qualified Costs paid or incurred for rehabilitation costs, contractor's profit for rehabilitation, architectural and/or engineering design fee- rehabilitation, and architectural supervision fee- rehabilitation (collectively, the "Qualified Rehabilitation Amounts") must consist of costs which are chargeable to capital account and must be incurred by the mortgagor in connection with the rehabilitation of the building or buildings in the development before the date which is 2 years after the later of the date of the mortgagor's acquisition of such building or buildings or the date of issue of the VHDA's bonds. In the case of an integrated operation contained in a building before its acquisition, such Qualified Rehabilitation Amounts include the cost of rehabilitating existing equipment in the building or replacing it with equipment having substantially the same function. The Qualified Rehabilitation Amounts must equal or exceed 15% of the portion of the acquisition cost of the building or buildings financed with proceeds of the Tax Exempt Bonds. No portion of such Qualified Rehabilitation Amounts may represent (i) costs of acquiring the land, improvements and structures, (ii) any expenditure attributable to the enlargement of a building, (iii) any expenditure attributable to a certified historic structure or to a building located in a registered historic district unless either the rehabilitation has been certified by the Secretary of the Interior or, in the case of a building located in a registered historic district, the Secretary of the Interior has certified that the building is not of historic significance, or (iv) any expenditure of a lessee if, on the date the rehabilitation is completed, the remaining term of the lease (determined without regard to renewal periods) is less than 15 years.

(4) As a general rule, VHDA does not require the mortgagor to pay, or reimburse VHDA for, any of the costs of issuance of the Tax Exempt Bonds. However, if the mortgagor is required by VHDA to pay or reimburse VHDA for any such costs, the amount of such costs shall not be includable in Qualified Costs, and any such costs in excess of 2% of the principal amount of the mortgage loan (or portion thereof financed with proceeds of Tax Exempt Bonds) shall not be includable in the total development cost.

Compliance with the above restrictions and limitations under the 1986 Code shall be conclusively determined by VHDA acting with the advice of its bond counsel. Costs of the mortgagor shall be ineligible to the extent determined by VHDA on advice of its bond counsel to be necessary to cause the mortgagor to be in compliance with the above provisions.

The above restrictions and limitations shall apply to mortgage loans which finance with proceeds of Tax Exempt Bonds the acquisition and/or construction of the development or provide permanent financing upon completion of the construction of the development. In the case of the use of proceeds of Tax Exempt Bonds issued by VHDA to refinance a development then being financed with proceeds of tax exempt bonds of another issuer, compliance with the requirements of the Internal Revenue Code of 1954, as amended, or the 1986 Code, as applicable, shall be determined by VHDA on the advice of its bond counsel prior to the final closing, and the principal amount of the mortgage loan (or the portion thereof financed with proceeds of Tax Exempt Bonds) shall be reduced as necessary to cause the mortgage loan to be in compliance with such requirements.

If the development is owned by an organization exempt from taxation under Section 501(c)(3) of the 1986 Code and if the mortgage loan thereon is financed with proceeds of bonds the interest on which is not included in gross income for federal income tax purposes under Section 145 of the 1986 Code (such bonds are referred to therein as "qualified 501(c)(3) bonds") rather than Tax Exempt Bonds as described above, the applicable restrictions and limitations relating to

the use of the proceeds of such qualified 501(c)(3) bonds shall be set forth in the mortgage loan documents. Compliance with such restrictions and limitations shall be conclusively determined by VHDA acting with the advice of its bond counsel. Costs of the mortgagor shall be ineligible to the extent determined by VHDA on advice of its bond counsel to be necessary to cause the mortgagor to be in compliance with such restrictions and limitations.

4. ELIGIBLE CONTRACTOR COSTS.

(A) When Required. The contractor must certify its costs in accordance with this section 4 only if required to do so by the construction contract. The VHDA form of construction contract (VHDA Form No. CD 300- Conv) requires the contractor to so certify its costs.

(B) General. The contractor's Certificate of Actual Costs may include all reasonable, ordinary and necessary costs which are eligible under the construction contract and this guide and which are directly related to the construction of the development. The Actual Cost of Construction (as defined in the construction contract) shall be the sum of the contractor's costs approved by VHDA as eligible hereunder.

As a general rule, only the costs which have been or will be paid in cash no later than 45 days after the date of final closing or which are escrowed with VHDA at final closing are eligible for inclusion on the contractor's Certificate of Actual Costs. The contractor's Certificate of Actual Costs must be on VHDA Form No. 100A. A samples of this form is attached to this guide.

The contractor's costs must exclude any return on or cost of the contractor's working capital and must be net of any kickbacks, rebates, allowances, credits, trade or cash discounts or other similar payments which the contractor received or may be entitled to receive in connection with the construction contract.

Costs shall not be allowed for duplication of work if it is the result of improperly placed work, failure to take proper precautions to protect completed work, failure to comply with plans and specifications, failure to supervise the work properly, or any other reason within the control or responsibility of the contractor or if any other contractor performed the same work. In such instances, the excess costs resulting from such duplication of work, as determined by VHDA, shall not be eligible.

(C) Eligibility. Eligible costs of the contractor shall be as set forth below.

(1) Total structures cost and total land improvements cost.

- (a) These categories include the total of the subcontract costs paid or incurred by the contractor for all labor (including payroll taxes), material and equipment rentals provided to complete the land improvements and structures. Also included are the costs paid or incurred by the contractor for equipment, materials and supplies not furnished under any subcontract.
- (b) The contract price for factory-produced modules paid by the contractor to the manufacturer will be accepted without cost certification by the manufacturer, unless the manufacturer has an identity of interest with the contractor or unless the construction contract requires such cost certification.
- (c) In the event that the amount of the total structures cost shown on VHDA Form No. 100A exceeds by more than 20% the amount therefor shown on the trade payment breakdown attached to the construction contract (as adjusted by any change orders approved by VHDA), VHDA may require the contractor to explain the reason for such excess and to provide such supporting information as VHDA shall deem necessary. If VHDA shall not be satisfied that such excess is justified by an unforeseeable change in facts and circumstances subsequent to the date of the construction contract or by any other unforeseeable extenuating circumstances, VHDA shall have the right to approve such lesser cost as VHDA shall determine to be reasonable and necessary, but not less than an amount equal to 120% of the amount shown for total structures costs on such trade payment breakdown (as adjusted by any change orders approved by VHDA). Such approval shall not be construed as an approval of an increase in the contract price.
- (d) The contractor may claim self-owned equipment costs at a reasonable rate of depreciation for the time actually in use for the construction, and may include additional costs for fuel, lubricants, maintenance, and liability insurance where required by law. A reasonable rate of depreciation is normally the straight line method over the useful life of the equipment unless an accelerated method can be justified. Acceleration for tax purposes is not sufficient justification. VHDA may require the contractor to specify for the equipment (1) brand names, (2) model numbers, (3) sizes, (4) ages, (5) rates charged, and (6) time used. In lieu of specifying the above items and complying with the above requirement for eligibility of costs, the contractor may elect to include costs for self-owned equipment at 85% of the going rates established by the Associated Equipment Distribution Rental Rate Guide or a comparable acceptable publication, for equipment of like capacity and condition. Repair costs will not be eligible.
- (e) Off-site costs are eligible for inclusion in the contractor's Certificate of Actual Costs if incurred for work performed under the construction contract and if shown in the mortgage loan commitment. The eligible amount shall not exceed the amount shown in the mortgage loan commitment.

- (f) The contractor's costs with respect to identity of interest subcontractors shall be reduced to the extent any such costs are disapproved by VHDA pursuant to subsection (B) of section 2 hereof.
1. In the case of material suppliers which are identity of interest subcontractors, the contractor may be required by VHDA to specify quantities furnished and unit prices paid by the contractor, together with brand names, model numbers, sizes, lumber grades, etc., as applicable.
 2. In the case of equipment lessors which are identity of interest subcontractors, the contractor may be required by VHDA to specify for the leased equipment (1) brand names, (2) model numbers, (3) sizes, (4) rates charged, and (5) time used. In order to be eligible costs, (a) the rates charged must not be more than the lowest rate obtainable in the area based upon the least expensive applicable rental time period, which would include maintenance and repair, and (b) time charged must not be more than was absolutely essential for the job. In lieu of specifying the above items and complying with the above requirements for rates and time charges, the contractor may elect to include charges for equipment at 85% of the going rates established by the Associated Equipment Distribution Rental Rate Guide or a comparable acceptable publication, for equipment of like capacity and condition. Equipment maintenance and repair costs will be the responsibility of the lessor and will not be included as eligible costs.
- (g) When escrows are to be established for items of incomplete work which are the responsibility of a subcontractor, the full amount of the subcontract shall be reported ; provided, however, that if the subcontract is cost-plus fixed-fee with a guaranteed upset price, the contractor shall claim the lesser of (a) the cost of the completed work (including the fee), plus the VHDA estimated cost for the incomplete work, or (b) the upset price as adjusted by the VHDA cumulative estimate of cost of any approved construction changes relating to the trade item.
- (h) The contractor shall provide to VHDA such information on payables due subcontractors (including an up-date of the status of such payables) as VHDA may request. Such payables will be disallowed to the extent that VHDA is not satisfied that such payables will in fact be paid within 45 days of final closing and, when paid, will represent eligible costs under this guide.

(2) General Requirements.

- (a) Eligible costs in this category include costs for no more than one supervisor (hereby defined as the person who is responsible for and performs the direct on-the-job supervision and coordination of the construction work) and two assistant supervisors and/or foremen on the job site during any one time period, field office expense (including wages of no more than one full-time job clerical employee at any one time), temporary sheds, toilets, tool storage, temporary heat, water, light, telephone and power for construction, equipment rental (if not applicable to trade items), cleaning and rubbish disposal, watchmen's wages or other security, medical and first-aid facilities, signs, photographs, temporary walkways and fences, sidewalk and street rental, temporary roads, sidings and docking facilities. All of the foregoing items of cost must be incurred for labor or materials supplied at the job site. The items will vary due to project type, location and site conditions. Also eligible under this category are the costs of the contractor's public liability and workmen's compensation insurance to the extent such costs can be allocated solely to the development.
- (b) Salaries of officers or executive of the contracting firm are eligible only if and to the extent:
1. The executive performed the duties and responsibilities of a supervisor, and there is no supervisor on the job site during the time period that the executive performs such duties and responsibilities.
 2. The salary paid was in line with the going rates for the duties performed by supervisors in the area of the job site.
- (c) The time spent at the job site exclusively on the construction of the development by an executive eligible under (a) above or by a supervisor who is generally retained by the contractor and who is assigned to a specific job or jobs for the purpose of supervising and coordinating the work may be charged to the cost of construction based upon the portion of his total employment represented by such time so spent on the development. The time spent by such executive or supervisor must be supported by a record keeping system and cannot be based on an allocation of his time. Failure to so record such time or maintain such system shall result in the disallowance by VHDA of the cost of the time spent by such supervisor or executive.
- (d) Costs normally associated with the operation of a contractor's main office or any branch office or with carrying on a contractor's trade or business are not eligible even if such costs are incurred with respect to activities taking place at the job site. These ineligible costs include: salaries of a project manager (except for time spent on the job site supervising and coordinating the construction work and supported by a recording keeping system established in accordance with (c) above) or other administrative, secretarial and supervisory personnel not otherwise expressly eligible under this paragraph (2); salaries of any other employees where activities are principally

confined to work in the main office or any branch office; legal fees, except those incurred as a result of legal difficulties relating to construction for which the contractor is not responsible; accounting charges; consultant fees; computer expenses; bookkeeping; office supplies and equipment except those necessary for the supervisor to perform his duties and functions; entertainment expenses; and travel and subsistence expenses and allowances, except those of the supervisor (and officers and executives satisfying the requirements of subparagraph (a) of this paragraph (2)) and his assistants directly and exclusively related to the performance of their duties on the job site and except travel and subsistence expenses for the project manager of the contractor to and from the site and the contractor's home office, but in no event shall eligible travel and subsistence expenses and allowances exceed \$10,000. Such ineligible costs are covered by the Overhead in paragraph (3) of this subsection (C).

- (e) Contractor owned equipment costs which are not applicable to trade items but which are otherwise eligible under this paragraph (2) may only be claimed in accordance with the requirements of subparagraph (d) of paragraph (1) of this subsection (C).
- (f) Other costs may include site and topographic fees, soil borings, subsurface explorations, and soil and material tests provided that such fees were not included on VHDA Form No. 100 or part of the architect's contract or any subcontract.

(3) Overhead.

The eligible cost is the amount shown in the trade payment breakdown attached to the construction contract, plus any increase approved by VHDA in a change order.

(4) Bond premium or letter of credit fees.

The actual cost of a completion assurance bond or letter of credit is an eligible cost. In cases where the mortgagor paid the cost of the bond or letter of credit and such cost is claimed on VHDA Form No. 100, the cost shall not be certified on the contractor's cost certification.

(5) Tap Fees.

The actual costs of utility tap fees are eligible provided that such fees were not included on VHDA Form No. 100 or part of any subcontract.

(6) Building Permit.

The actual costs of the building and other permits are eligible provided that such costs were not included on VHDA Form No. 100 or part of any subcontract.

(7) Other Costs.

All other costs must be reasonable, ordinary and necessary and directly related to the construction of the development and are subject to VHDA approval. The costs of any item in excess of the amount (if any) shown in the mortgage loan commitment therefor are not eligible. Fees and costs for cost certification are not eligible.

(8) Contractor's profit.

The amount of contractor's profit as provided in the construction contract and as adjusted by any change orders approved by VHDA is eligible.

(D) Maintenance of Records. Adequate records must be maintained by the contractor for the purpose of verifying costs, and all books, records, contracts, invoices, receiving reports, particulars of material, labor and equipment entering into the construction of the development, and other records appropriate to such accounts must be made available to VHDA and its representatives for inspection and copying upon request.

5. AUDIT REQUIREMENTS.

An audit of the mortgagor's Certificate of Actual Costs must be performed by an independent public accountant ("IPA") if proceeds of Tax Exempt Bonds are to be used to fund a mortgage loan which finances the acquisition and/or construction of a development or which provides permanent financing upon completion of the construction of a development. Such an audit is not required if proceeds of Tax Exempt Bonds will be used to refinance a development then being financed with proceeds of tax exempt bonds of another issuer.

The IPA must be a certified public accountant or a public accountant licensed by a regulatory authority of a state or other political subdivision of the United States. The IPA must be independent within the meaning of the code of professional ethics of the American Institute of Certified Public Accountants ("AICPA").

The IPA is required to examine and express his opinion on whether the mortgagor's Certificate of Actual Costs presents fairly the costs paid or incurred by the mortgagor in connection with the acquisition and/or construction of the development through the cut-off date. The IPA is also required to make certain certifications as to compliance with the requirements under the 1986 Code relating to the use of proceeds of Tax Exempt Bonds to finance a qualified residential

rental project. The audit work must be sufficiently comprehensive in scope to permit the expression of such opinion and certifications and must be based on an examination performed in accordance with this guide and generally accepted auditing standards. The opinion and certifications by the IPA must be unqualified and addressed to VHDA and in the form set forth on VHDA Form No. 100. If either a qualified or adverse opinion or certification is expressed or if an opinion or certification or any part thereof is disclaimed, such opinion or certification shall not be acceptable to VHDA unless the reasons therefor are fully explained to the satisfaction of VHDA and unless VHDA is otherwise satisfied that the mortgagor's Certificate of Actual Costs complies with this guide.

The audit coverage and extent of tests must be shown in the audit working papers. The audit engagement letter or arrangement for audit between the IPA and the mortgagor must allow VHDA to examine the IPA's working papers supporting the mortgagor's Certificate of Actual Costs. For this purpose, the IPA should retain the working papers for at least three years following the final closing.