

728.1
:336.18
P81b

4-15-66

BUYING FROM DEVELOPERS

A NEW APPROACH TO PUBLIC HOUSING

How the "Turnkey" Method Works
Guide to Developers and Builders

U.S. Department of Housing and Urban Development
Public Housing Administration
Washington, D.C. 20413

4-15-66

Introduction. The Department of Housing and Urban Development has developed a new technique for the provision of public housing which permits a private developer or builder to deal with a local housing authority in essentially the same way as he is accustomed to deal with his private clients. Under this system, called the "turnkey" method, a developer who has a site or an option, or can obtain one, may approach the local housing authority with a proposal to build in accordance with plans and specifications prepared by his own architect and to a standard of good design, quality and workmanship. In the event that the developer's proposal is acceptable to the housing authority, the parties will enter into a contract under which the housing authority agrees to purchase the completed building. This contract will be backed up by the Public Housing Administration's financial assistance commitment to the housing authority, and it will enable the developer to secure commercial construction financing in his usual way. The details concerning this "turnkey" method are set forth below.

Local Housing Authority (LHA). Since the PHA can operate only through local housing authorities, such an authority which is authorized to operate in the place where the developer is interested in proceeding must be in existence or be established. There are now almost 1800 of these local housing authorities and they operate in more than 2400 localities. All the States except Utah and Wyoming have enabling legislation for their creation. The procedure for their establishment by a local governing body is simple, and the HUD Regional Office will provide all necessary

728.1
: 336.18
P818

paper work assistance. LHAs may also be created by Indian tribes and 64 have been created on Indian Reservations, including Reservations in Utah and Wyoming.

LHA Application. The LHA files an application with the Public Housing Administration--the arm of HUD that would finance such a development. This application must demonstrate the need for the number of dwelling units, and the type (regular, or specially designed for the elderly or the handicapped). If the LHA has a Program Reservation of a sufficient number of dwelling units, an application will not be necessary.

Information. HUD will inform all interested developers, builders, lenders, organizations, or anyone else interested in developing or building as to the LHAs that have filed applications. The LHAs will be requested to publicize information in their localities, including available information as to total number of units desired, type of units (regular, or specially designed for the elderly or the handicapped), and the unit size (bedroom distribution), and indicating their interest in receiving proposals from private builders or developers for their development of housing (including related facilities and amenities) to be acquired by the LHA upon completion. The developer may inquire at any LHA, or HUD or PHA office.

This will enable the LHA to entertain as many and as great a variety of proposals as possible at the earliest possible time before its ideas become fixed on any particular site or plan. It will also provide maximum time for discussion between the LHA and the interested parties of alternate proposals or solutions.

Developer-LHA Relationship. Type of Housing and Construction. It is anticipated that the developer will be working with architects,

contractors and subcontractors of his own choice and will bring to the LHA the benefits of his experience and know-how in producing the desired housing and related facilities and amenities. These should be suitable, well-designed, and well-constructed, able to stand hard wear for at least 40 years, be designed for economical administration and maintenance, be produced in the most efficient and economical manner, and be located in neighborhoods that will provide a healthful and decent environment and on sites acceptable to the LHA and PHA for low-rent housing. It will be necessary for the developer and the LHA to discuss in general terms the types and sizes (number of bedrooms) of the housing and facilities to be developed. The developer should consult with the LHA from time to time during the course of his planning to insure the acceptance of his plans when they are developed. The LHA will advise developers specifically as to any PHA or other requirements that are mandatory. The developer should assume that other PHA guides provided by the LHA are advisory only and that they should not hamper him or the contractors or the architect in proposing their own ideas and presenting the LHA with their own recommendations and solutions. Wage rates prevailing in the locality for the type of construction involved that the developer proposes to pay and that will have been submitted to and have been approved by the Secretary of Labor will be required (the LHA and PHA will provide an expeditious procedure for such approval). The developer will also be required to agree not to discriminate in employment.

Preliminary Proposal. It is assumed that at some point a particular proposal or proposals will be acceptable to the LHA based on a certain site or sites, schematic drawings and preliminary estimates of costs. When this

point is reached, the LHA will inform the developer that it desires to proceed further with the proposal, and the developer will be advised that if he submits preliminary plans and outline specifications sufficient in detail to fix and illustrate the developer's intent as to all essentials of the project, including the estimated price, the LHA will present the proposal in the form of a Development Program to the PHA for approval. The Development Program will also contain evidence of the approval of the site by the locality where such approval is required by law or agreement of the LHA. The PHA will, if it approves of the Development Program, enter into a financial assistance contract with the LHA to cover the purchase by the LHA of the finished product.

Letter of Intent. Upon execution of the financial assistance contract by the PHA, the LHA will issue a letter of intent to the developer to enter into the contract of sale described below. The LHA will obtain two independent appraisals of the land and proposed improvements. The proposed purchase price to be specified in the letter of intent will be negotiated and presented to the PHA for approval on the basis of these appraisals. The letter of intent will also provide that the final price in the contract of sale shall be the price stipulated in the letter of intent or the midpoint of two independent appraisals based upon PHA approval of final working drawings and specifications, whichever is the lesser, except that if the midpoint of the two appraisals is less than 95% of the price stipulated in the letter of intent, the LHA and the developer will not be obligated to proceed further with the project. The letter of intent will provide further that, in the latter event, and assuming that a satisfactory renegotiation acceptable to the PHA cannot be effected: (1) the LHA will pay the developer an agreed amount specified in the letter of intent for his costs of preparing the final working drawings and specifications; (2) the drawings,

specifications and other materials for which payment is made will become the property of the LHA; and (3) the LHA will, if the developer so desires, purchase the site at a price equal to the midpoint between the appraised values of the site as evidenced by the two appraisals or his cost, whichever is the lesser.

Working Drawings and Specifications. The letter of intent will provide that within a time specified therein the developer shall have caused to be prepared, under the supervision of a registered architect, complete working drawings and specifications which will comply with all applicable state and local laws, codes, ordinances and regulations as modified by any waivers which have been obtained from the appropriate jurisdictions, and which will meet the PHA requirements for approval of a contract of sale. The working drawings and specifications shall be equivalent to "bid documents" and shall set forth in detail and prescribe the work to be done; the materials, workmanship, finishes, and equipment required for the architectural, structural, mechanical, electrical, and site work. Upon approval of these documents by the LHA and PHA, the LHA will enter into the contract of sale with the developer.

Contract of Sale. Standards of Construction. Guarantees. The contract of sale between the developer-seller and the LHA will provide that the improvements will be built to the agreed-to working drawings and specifications, conditions, standards of workmanship and materials, finishes, etc., prepared in accordance with agreements reached pursuant to the preliminary proposal. These standards may be expressed or supplemented by reference to another building in the community selected by the LHA and the seller and specifically designated in the contract as the standard. The contract will also include the conventional one-year clause for remedying defects, backed up by a

guarantee in the amount of 2¹/₂% of the purchase price by way of a surety bond, an escrow of cash or negotiable securities, or an irrevocable letter of credit.

Inspections. The contract of sale will provide that the LHA inspections will be performed by an independent architect selected and hired by the LHA who has had experience in the design and inspection of similar private developments and who will be named in the contract of sale. The frequency and type of inspections are to be in accordance with prudent private practice. Inspections may also be made by employees of the PHA or LHA but only for purposes of informing the PHA or the LHA or its inspecting architect of conformance to the working drawings, specifications, and agreed-upon standards.

Completion Time - Delays. A time for completion will be specified, but automatic extension will be provided for delay due to strikes, labor disputes, fire, etc.,--causes beyond the seller's control or by delay authorized by the LHA.

Change Orders. The contract will provide that only change orders increasing or decreasing the contract price by a substantial amount, singly or in the aggregate, as specified in the contract of sale, shall be approved by the PHA.

Purchase and Settlement. The contract will provide that full settlement will be made within five days after completion as evidenced by the issuance of a certificate of occupancy and all other approvals by local officials necessary for occupancy and a certification by the LHA's inspecting architect that the property is in good and tenantable condition. The architect's

certificate will also describe any uncompleted parts of the property and an estimate of the amount necessary to complete such parts. Pending completion the LHA may withhold this estimated amount from the purchase price. This withheld amount shall be paid upon certification by the architect that there has been full completion.

Financing--PHA Assurance to Developer-Seller and Lender. The contract of sale between the developer-seller and the LHA will contain a reference to its approval by the PHA and that such approval signifies that the undertaking of the acquisition by the LHA constitutes it a "project" under the financial assistance (annual contributions) contract between the LHA and the PHA and that this project is eligible for the financial assistance of the PHA provided for in the annual contributions contract.

The annual contributions contract between the PHA and the LHA will contain a provision to the effect that if the LHA breaches its letter of intent or contract of sale with the developer-seller, such breach will be considered by the PHA to be a default of the LHA's annual contributions contract with the PHA, upon which the PHA will perform the letter of intent and sales contract with the developer-seller. This provision assures the developer-seller and the financing institution which agrees to provide the construction funds, that if the developer carries out his contract with the LHA he is assured of performance and payment by the Federal Government should the LHA default.

This is the same type of assurance, and is based on the same statutory authority, as has been utilized to assure bond holders who purchase LHA bonds (which provide the purchase money for public housing projects) that should the LHA default in its payment of the bonds, the PHA will take

possession or title to the project and continue the bond payments. It is on the basis of this security that LHA bonds have for many years enjoyed the highest triple-A rating of any municipal bonds on the market and sell at the lowest interest rates.

Opinion of PHA General Counsel. An opinion of the PHA General Counsel will be rendered to the developer and the lender as the developer may require. This opinion will set forth the pertinent provision of the annual contributions contract between the PHA and the LHA relating to the acquisition and financing of the project and will conclude that the LHA and the PHA have the power to enter into such contract and that the LHA is empowered to enter into the contract of sale with the developer.

Similarity to FHA-FNMA "Take-out" Financing. The financing arrangement, insofar as the private developer is concerned, sets up a method of development and construction financing by private lending institutions with a "take-out" upon completion analogous to the FNMA purchase of an FHA mortgage when a development is completed. Under this arrangement, the permanent financing "take-out" is accomplished with the proceeds from the housing authority's sale of its bonds secured by the pledge of PHA annual contributions, or, where necessary, with the proceeds from a PHA loan to the housing authority. Should the LHA default on its contract with the developer-seller, the "take-out" will be made through direct payment by the PHA. Thus, the developer-seller and his financing institution during construction are assured of an ultimate "take-out." Furthermore, if it is deemed desirable, an arrangement could be made whereby the "take-out" payment by the LHA, or by the PHA in the event of default, would be made directly to the lending institution. Such arrangement could be specifically provided for in the contract of sale and annual contributions contract.

Mixed Ownership Developments. HUD is desirous of promoting smaller publicly owned developments, especially to enable low-income families to live in the same environment with families or individuals of higher income and possibly under arrangements whereby the tenants and the property are not specifically identified as being public or private. For these reasons HUD will encourage and assist developers who propose sites considered to be too large for exclusively public housing to plan combined private-public developments which will benefit both the low-income tenants subsidized by the PHA through the LHA and the tenants of the developer who may be low, middle, or higher income, depending on financing and economic feasibility. Such a combination could also include cooperative or condominium housing.

Such an arrangement could be of substantial benefit to the privately owned portion of the undertaking since an LHA may be able to lease vacancies in the privately owned portion or purchase an additional portion if desirable. A developer should, therefore, not hesitate to approach an LHA with a site that may be too large for public housing alone if he is interested in such a joint arrangement or if he would be willing to entertain proposals by others to join with him in developing such a combined arrangement.

Public or Private Management. Housing developed under this method, whether exclusively publicly owned or under mixed ownership, could, if the parties agreed, be managed either by a private management organization or by the LHA unless, in the case of mixed-ownership, State law prohibited the LHA from doing so.

Commercial Facilities. Public housing may include unsubsidized commercial facilities which are considered necessary for the tenants, such as shops and stores. In the case of combined public-private ownership, the privately owned

portion may, of course, include non-detrimental commercial facilities which may or may not be necessary for the use of the tenants. Also, in the case where the residential portion is entirely publicly owned, the commercial facilities could be privately owned. In any case these commercial facilities may be in separate structures or part of the public or private residential structures.

HUD LIBRARY



T 10679