

February 18, 2016

TO: State Directors  
Rural Development

ATTN: Multi-Family Housing Program Directors, Coordinators,  
Specialists, State Architects, and Construction Analysts

FROM: Tony Hernandez /s/ *Tony Hernandez*  
Administrator  
Housing and Community Facilities Programs

SUBJECT: Guidance on the Capital Needs Assessment (CNA) Process

## **Introduction**

This Unnumbered Letter (UL) provides updated clarification and guidance on the Rural Development Capital Needs Assessment (CNA) process. This document is comprised of ten main sections: 1) References to CNA in [7 CFR Part 3560](#) and the RD MFH Handbooks; 2) [Contract Addendum](#); 3) [Requirements and Statement of Work for a CNA](#); 4) [The CNA Review Process](#); 5) Definitions; 6) [Guidance for the Multi-Family Housing \(MFH\) Property Owner Regarding Contracting for a CNA](#); 7) [Revising a CNA](#); 8) [Updating a CNA](#); 9) [Incorporating a Property's Rehabilitation into a CNA](#); 10) [Repair and Replacement Schedule](#); 11) [Transition to Underwriting Phase](#). There are also ten attachments to this UL identified as Attachments [A](#), [B](#), [C](#), [D](#), [E](#), [F](#), [G](#), [H](#), [I](#), [J](#) and [two Subattachments A-1 and B-1](#). This entire Unnumbered Letter should be made available to RD MFH property owners, applicants and CNA Providers who are or are planning to submit transactions using the MPR or any other RD RRH or FLH program loan making or servicing authorities.

EXPIRATION DATE:  
February 28, 2017

FILING INSTRUCTIONS:  
MFH Programs

## Purpose of the UL

The need for a CNA report arises from numerous property transactions and is intended to record the specific physical conditions of each MFH property in which RD has a financial interest. A properly documented report may become the basis for funding the reserve account or developing an alternative calculations intended to determine that an adequate reserve is established. The reserve account is established to address the physical replacement and repair concerns that are projected to occur for the full duration of the CNA cycle, while continuing to allow for the long term financial feasibility of the property. The CNA report shall include specific physical property items, systems and components that are not addressed in the annual budgeting of normal maintenance. Although, the listed CNA items can differ from property to property, the overall intent and goal is to assure that the property is covered financially, in its' entirety, for all maintenance, repairs and replacements necessary for suitable living/working conditions for all occupants and visitors of the property.

By following the guidance of this UL there is a higher probability of acceptance of the application and a higher probability of successful underwriting and performance of the property during the CNA cycle. Analyzing and establishing a property's reserve levels during the underwriting effort of each transaction may require logical adjustments to the repair and replacement schedule established in the CNA report. It is advisable that any adjustments be agreed upon by all parties with a financial interest in the property. Accuracy of the report and timeliness of the review process are critical to the CNA, reanalysis of the property's condition and underwriting process providing a benefit to the property.

### **1. References to CNA in 7 C.F.R. Part 3560 and the RD MFH Handbooks**

References to a Capital Needs Assessment (CNA) can be found in 7 C.F.R. Part 3560, HB-1-3560, HB-2-3560, and HB-3-3560; and 7 C.F.R. Part 3565 and HB-1-3565. (See [Attachment A, \*References to Capital Needs Assessment \(CNA\) in 7 CFR Part 3560 and Handbooks.\*](#)) These references include information describing when a CNA is required, suggested uses of a CNA, general requirements for a CNA, sources of funding for a CNA, and situations in which a CNA may be performed by Rural Development (RD) or other third party provider.

### **2. Contract Addendum**

Rural Development uses a Contract Addendum to supplement the basic CNA agreement or "contract" between the Owner and CNA Provider with additional details and conditions. It can be found in [Attachment B, \*Addendum to Capital Needs Assessment Contract\*](#) and must accompany all contracts executed between the Owner and CNA Provider for CNAs used on RD financed properties. If any conflicts arise between the "Contract" or "Contract Addendum", the "Contract Addendum" will supersede.

The Contract Addendum identifies the responsibilities and requirements for both the property owner and the CNA Provider. To assure proper completion of the contract documents the following key provisions must be completed:

a. The Contract Addendum will include the contract base amount for the CNA Provider's cost for services on page B-2, and provisions for additional services to establish the total price for the CNA.

b. Item I(e) requires an itemized listing for any additional anticipated services and their unit costs including future updates and revisions that may be required before the CNA is accepted by RD *Note: Any cost for updating a CNA must be included, in the "additional services" subpart, of the original CNA contract.*

c. The selection criteria boxes in II a, identify the type of CNA being provided.

d. In III (a), the preferred language for the blank on "report format" is: "[USDA RD CNA Template](#), current RD version, in Microsoft Excel format". This format will import directly into the underwriting template for loan underwriting purposes.

### 3. Requirements and Statement of Work for a CNA

The RD CNA template is the key document for compatibility of the data for underwriting the project. All other attachments represent minimums only and typically there will be more extensive requirements from laws and industry standards that will need to be addressed in the report. As such, the form, format and content of the final report may be based on alternative report sources. Minimum requirements for an adequate CNA can be found in [Attachment C, Capital Needs Assessment Statement of Work](#) (CNA SOW) This is supplemented by [Attachment D, Fannie Mae, Appendix D, Reference Effective Useful Life \(EUL\) Table, Instructions for the Property Evaluator, and Attachment J, Guidance on the Rehabilitation of MFH Properties](#). To resolve any inconsistency in the two documents, Attachment C, the CNA SOW will in all cases prevail over the [Attachment D, Fannie Mae, Appendix D, Reference Effective Useful Life \(EUL\) Table, Instructions for the Property Evaluator](#). Fannie Mae defines the "term" as "term of the mortgage and two years beyond". For USDA, the "term" will be 20 years, as defined in the CNA SOW. The CNA SOW is not a scope of work for the repairs or improvements that may ultimately be underwritten and approved for the project as addressed in the specific program underwriting guidance. See also #9 below.

Attachment C includes the required qualifications for the CNA Provider, the required scope of work for a CNA assignment, and general distribution and review instructions to the CNA Provider. CNA Providers must be able to report the current physical condition of the property and should **not** base their findings on the financial condition of either the property or the Owner.

Attachment D is a two-part document Rural Development uses as reference to the CNA process throughout the RD revitalization and demonstration program efforts. The two key components of this Attachment are: 1) guidance to the property evaluator; and 2) expected useful life tables. It includes general instructions used in completing CNA reports, specific instructions on how to use the expected useful life tables.

An acceptable CNA will appropriately address each of the following supplemental concerns within the report and narrative:

- a. [Attachment E, Accessibility Laws and Requirements](#), outlines the federal accessibility laws, regulations, and standards that apply to Section 515 and Section

514/516 Multi-Family Housing properties. The CNA Provider should use Attachment E as a guide in assessing how the property meets the requirements for accessibility to persons with disabilities. The CNA report should include any actions and estimated costs necessary to correct deficiencies in order for the property to comply with applicable federal, state, and local laws and requirements on accessibility. The report should also include an opinion based on the adequacy of a current, approved transition plan for the property or advisory that one was not presented for review.

b. [Attachment F, Existing Property Accessibility Checklist](#), contains general information in a checklist format that indicates a sample of the requirements for compliance that should be verified by the CNA Provider. For example, a transition plan that does not address all of the deficiencies listed in Attachment F, or is outdated, is not adequate. Attachment F should be used to indicate accessibility compliance corrections necessary to the property. It is the responsibility of the Provider to inspect and verify whether all accessibility features are compliant. The checklist is intended as a general guide and NOT intended to cover every aspect of accessibility (which may vary depending on site location). The Uniform Federal Accessibility Standards (UFAS) paragraph references are **bolded** and guideline language *italicized*. This Attachment provides relevant information extracted from the UFAS and paraphrased but is not necessarily quoted verbatim.

c. [Attachment G, Accessibility Requirements for Rural Development Financed Existing Multi-Family Housing \(Supplemental Questions & Answers\)](#), provides “Frequently Asked Questions” on accessibility for RD MFH Program involving the existing MFH properties, which may be helpful to the CNA Provider.

d. Attachment J, [Guidance on the Rehabilitation of MFH Properties](#) provides guidance on the rehabilitation of Rural Development Multi-Family Housing (MFH) properties using the Section 515 Rural Rental Housing and Section 514/516 Farm Labor Housing programs. It provides the primary guidance on the standards and requirements for projects using only Agency funding to complete the repairs or rehab. When financing sources include “third party” sources there may be other or additional construction requirements and conditions which will need to be discussed and mutually accepted by all parties involved. With projects using any third party (non-RD) financing the principles of Attachment J should be applied to the extent necessary to assure the Agency's security interest is adequately addressed.

#### **4. The CNA Review Process**

A CNA used by Rural Development will be reviewed by the designated RD CNA Reviewer serving the area. The CNA Reviewer will be an architect, construction analyst, appraiser, or other staff member with education, training, and experience in construction, rehabilitation, and repair of Multi-Family Housing (MFH) properties, especially as it relates to repair, replacement and maintenance costs throughout the term covered by the CNA.

A CNA obtained and used by a lender on a property that is only guaranteed by Rural Development, and has no other RD financing on the property, may be reviewed by the lender and borrower to establish adequate reserve levels. Adequate reserve levels are those reserve levels agreed to by the borrower and lender, using the CNA as guidance, that address the estimated physical needs of the property through the life cycle of the CNA (see HB 1-3565 Chapter 7).

A CNA report must be obtained by the property owner from a third party CNA Provider that has no identity of interest with the owner, management agent, buyer or any other principle or affiliate defined in 7 C.F.R. Part 3560, §3560.11, 7 C.F.R. Part 3565 §3565.3 and §3565.155. The property owner or the lender (strictly when only 538 financing is involved) will contract with the CNA Provider and is therefore the client of the provider. The lender should select a qualified CNA provider in consultation with the owner and does not need to consult with RD nor have the CNA reviewed by RD. However, for a Section 515/514 financed property the owner should consult with Rural Development before contracting with a CNA Provider to review Guidance for the MFH Property Owner Regarding Contracting for a CNA shown in this letter as Item 6, and the Addendum to Capital Needs Assessment Contract (Attachment B). The RD CNA Reviewer will evaluate a proposed agreement or engagement letter between the Owner and a CNA Provider using [Attachment H, Capital Needs Assessment Guidance to the Reviewer](#), prior to reviewing any CNA report. Unacceptable CNA proposals, contracts or reports will be returned to the applicant for appropriate corrections before they will be used for any underwriting determinations.

The CNA Reviewer will also review the cost of the CNA contract. The proposed fee for the CNA must be approved as an eligible housing project expense under 7 C.F.R. 3560.103 (c) for the agreement to be acceptable and paid using project funds. If the CNA is funded by the property's reserve account, selection of a Provider shall be in accordance with [HB-2-3560](#), Chapter 4, section 4.17-B. If the contract is funded by another source, or will be under \$3,500, a single bid is acceptable. (However, the Agency recommends multiple bids in all cases. There is no Agency requirement to select the "low bidder" and the owner may select a CNA Provider based on qualifications, as well as price after reviewing references and past work.)

If the proposed agreement is acceptable, the reviewer will advise the appropriate Rural Development servicing official, who will in turn, inform the owner. If the proposed agreement is unacceptable, the reviewer advises the owner and the CNA Provider in writing and identifies actions necessary to make the proposed CNA submission acceptable to Rural Development. Upon receipt of a satisfactory agreement, the RD CNA Reviewer should advise the appropriate Rural Development servicing or underwriting official to accept the proposal.

The CNA Reviewer will review a preliminary CNA report delivered to Rural Development by the CNA Provider using [Attachment H, Capital Needs Assessment Guidance to the Reviewer](#), (including the checklist provided) and [Attachment I, Sample Capital Needs Assessment Review Report](#), to write the preliminary CNA review report. The preliminary CNA report will be delivered to the Rural Development loan and servicing official(s) to jointly discuss the findings and reviewer's conclusions. If necessary, the loan official will then notify the owner in writing of any revisions that are necessary to make the CNA report acceptable to Rural Development. The CNA Reviewer will review the final corrected CNA report to verify that the report is

acceptable to Rural Development before delivering the final CNA review report to the loan official for a subsequent joint discussion to verify the report complies with the CNA requirements. Any difference of opinions exist regarding the findings at this time must be mutually addressed by RD staff before the final CNA review report is delivered to the owner. To confirm this discussion between the CNA Reviewer and loan official, **the final CNA review report must be signed by both the CNA Reviewer and the RD loan underwriting official.**

During the CNA review process, the CNA Reviewer and the underwriter must consult with the field office most familiar with the property for their input and knowledge of the property. Upon signature by the RD CNA Reviewer and Loan Underwriter this report becomes the “accepted” CNA indicating the actual condition of the property at the time of the CNA inspection – a “snapshot” in time – and will be marked “Current Property Condition” for indefinite retention in the borrower case file.

## 5. Definitions

The following definitions are provided to clarify terms used in conjunction with the CNA process:

**As-is CNA:** This type of CNA is prepared for an existing MFH property and reports the physical condition of the property based on that moment in time. This CNA can be useful for many program purposes other than the MPR, such as, an ownership transfer, pre-payment incentive and evaluating or resizing the reserve account. The As-is report will include all major repairs and likely some minor repairs that are typically associated with the major work; each major component, system, equipment item, etc. inside and outside; building(s); property; access and amenities in their present condition . A schedule of those items showing the anticipated repair or replacement time frame and the appropriate, associated hard costs for the ensuing 20-year term of the CNA serves as the basis or starting point in evaluating the underwriting that will be necessary to determine the feasibility and future viability of the property to continue serving the needs of eligible tenants. The As-is CNA is an important tool when a property rehabilitation is anticipated. A well document As-is report will provide an excellent assessment tool when the agency reviews the rehabilitation scope of work.

**“Post Rehab” CNA:** This type of CNA is done for an existing MFH property as well, but considers any planned rehab or major repairs proposed for the property transaction. It builds on the findings of the accepted As-is CNA and is typically prepared for a project that will be funded for a major rehabilitation. The Post Rehab CNA is adjusted to reflect the work intended to be performed during the rehabilitation. The assessment must be developed from the rehabilitation project plans and any construction contract documents to reflect the full extent of the planned rehab.

**Life Cycle Cost Analysis:** When a CNA is required prior to beginning the construction of a new project, then a more suitable process is known as a Life Cycle Cost Analysis (LCCA). An Architect or Engineer is the best qualified person(s) to prepare this report. A LCCA is an expanded version of a CNA and is defined at 7 C.F.R. Section 3560.11. The LCCA will

determine the initial purchase cost, the operation and maintenance cost, the “estimated useful life”, and the replacement cost of an item selected for the project. The LCCA provides the owner with the CNA information on repair or replacement costs and timeframes over a 20-year period. It also provides information that will assist with a more informed component selection and can provide the owner with a more complete financial plan based on the predictive maintenance needs associated with those components. If the newly constructed project has already been completed without any previous CNA requirement, either an “As-is” CNA or LCCA can be provided to assist in establish the required reserve needs analysis necessary for establishing program mandated reserve deposits.

**Consolidation:** In some circumstances, Rural Development may permit two or more adjoining properties to be consolidated as defined in 7 CFR 3560, §3560.410 when it is in the best interests of the government. The property owner should consult with the RD loan official before engaging the CNA Provider in any case where the CNA intends to encompass more than a single (one) existing RD property to determine if a consolidated CNA may be acceptable for RD underwriting. Rural Development requires that individual properties be identified by name or address so the condition reported is specific to a unit, building or property.

Any proposed consolidation of properties or merging of ownership interests in any form, must comply with the specific program authorities and requirements as specified in the respective program regulations and guidance before engaging the CNA provider CNAs, as well as 504 Self Evaluation/Transition Plans or other accessibility assessments, should be performed independently for each legal entity receiving federal funds

A CNA Provider should be fully aware of the intended use for the CNA because it can impact the calculations necessary to perform adequate accessibility assessments and can impact the acceptability of the report by RD. Unacceptable reports will not be used for any RD underwriting purposes even though they may otherwise be acceptable to the owner or another third party lender or participant in the transaction being proposed.

**Note:** *All CNA’s will be required to include all line items relevant to a property when a CNA is performed. Line items exceeding an EUL of greater than 20 years may or may not include a cost at the discretion of the CNA provider, Owner, or Agency Representative. When available, Lenders, owners and CNA providers are encouraged to use the eCNA developed between HUD and RD.*

## **6. Guidance for the MFH Property Owner Regarding Contracting for a CNA**

Rural Development State Offices maintain a directory of CNA Providers, and can forward that information to the MFH property owner or lender upon request at the time a CNA is being proposed. However, the property owner is not required to use a CNA Provider from the RD State directory. Note: Rural Development in no way guarantees the performance of the CNA Providers listed in their respective directories.

Property owners or lenders are advised to request an information package from several CNA

Providers and to evaluate the information before selecting a provider. At a minimum, the information package should include a list of qualifications, a list of references, a client list, and a sample CNA report but the Owner may request any additional information they feel necessary to evaluate potential candidates and select a suitable provider for this service. Consideration for the type of CNA required should be part of the owner's selection criteria and inserted into the contract language as well. The necessary skill set to perform the As-is versus the Post Rehab or New Construction CNA versions, need to be considered carefully. Knowledge of the accessibility laws and standards and the ability to read and understand plans and specifications could also be among the critical skill elements to consider.

[Attachment B, Contract Addendum](#) should be submitted to Rural Development with the contract, and signed by Owner and CNA Provider. The proposed agreement with the property owner and CNA Provider must meet Rural Development's qualification requirements for both the provider and the CNA scope of work, as specified in [Attachment C, Capital Needs Assessment Statement of Work](#). Rural Development should review the proposed agreement between the owner and the CNA provider, and concur only if all of the RD requirements and conditions are met. (See the previous section 4 of this UL, [The CNA Review Process](#).)

## **7. Revising a CNA (applies to RD actions)**

During transaction underwriting and analysis, presentation of the information contained in the "accepted" CNA may need to be revised by Rural Development to address financing and other programmatic issues. The Loan Underwriter and the CNA Reviewer (Lender or Agency) will work together to determine if revisions are necessary to meet the financial and physical needs of the property and established RD underwriting or servicing standards and principals. These may involve shifting individual repair line items reported in the CNA, moving work from year to year, or other adjustments that will improve cash flow. The revised CNA will be maintained by as supporting documentation of the loan underwriting, and used in the future as the anticipated schedule of replacements, establish reserve funding schedules, and operating budget preparation and analysis.

The initial CNA, prepared by the CNA Provider, will be maintained as an independent third party record of the current condition of the property at the beginning of the twenty-year cycle. Original CNAs will be maintained in the case file, clearly marked as either "Current Property Condition" ("As-is"), "Post Rehab Condition", "Revised Underwriting / Replacement Schedule", as applicable. Note: The CNA Provider is not the appropriate party to "revise" a CNA which has already been approved by the Owner and Provider, and concurred in by the Agency. The CNA Provider's independent opinion was the basis of the "As is" or "Post Rehab" CNA. The CNA developed for underwriting may **only** be revised by Rural Development staff or the third party lender during the underwriting process or as part of a post-closing servicing action.

## **8. Updating a CNA (applies to "As-is" and "Post-Rehab")**

A completed CNA (not yet underwritten by the agency) more than a year old at the time of Rural Development review and approval of the CNA should be "updated" prior to Rural Development approval. Likewise, if at the time of Underwriting the CNA is more than a year old (but less

than two years old), it should be updated before the transaction may be approved.

To update a CNA, the CNA Provider should review property changes (repairs, improvements, or failures) that have occurred since the date of the original with the owner, review costs and quantities, and submit a updated CNA for approval. However, if the site visit for the CNA occurred more than two years prior to the loan Underwriting, the CNA Provider should perform a new site visit to verify the current project condition.

Once the CNA has been updated, the CNA Provider will include a statement noting “This is an updated CNA of the earlier CNA dated \_\_\_\_\_” at the beginning of the CNA’s Narrative section. The CNA Provider should reprint the CNA with a new date for the updated CNA, and provide a new electronic copy to the owner and Rural Development.

***Please note:*** it is in the Owner’s best interest to furnish the CNA Provider with the most current and up-to-date property information for a more comprehensive and thorough CNA report. RD recommends that the Owner conduct a pre-inspection meeting with the Owner, Property Manager, maintenance persons familiar with the property, CNA Provider, and Agency Representatives at the site. This meeting will allow a forum to discuss specific details about the property that may not be readily apparent to all parties involved during the review process, as well as making some physical observations on-site. Certain issues that may not be evident to the CNA Provider due to certain weather conditions at the time of review should also be discussed and included in the report. Additionally, other issues that may need to be addressed include environmental hazards, structural defects, as well as complex accessibility issues.

This pre-inspection meeting also allows the CNA Provider to discuss with the Owner total number of units to be inspected, as well as identifying any specific units that will be inspected in detail. The minimum number of units required for inspection by the Agency for an acceptable CNA is 50%. However, inspecting a larger number of units generally provides more accurate information to identify the specific line items to be addressed over the “term” being covered by the CNA report. Owners are encouraged to negotiate with the CNA Provider to achieve inspection of all units whenever possible. The ultimate goal for the Owner and CNA Provider, as well as the Agency, is to produce the most accurate “baseline or snapshot” of current physical property conditions for use as a tool in projecting future reserve account needs.

## **9. Incorporating a Property’s Rehabilitation into a CNA**

A CNA provides a repair schedule for the property in its present condition, indicating repairs and replacements necessary for a property to function properly and efficiently over a span of 20 years. It is not an estimate of existing rehabilitation needs, or an estimate of rehabilitation costs. If any rehabilitation of a MFH development is planned as part of the proposed transaction, the rehabilitation repair list (also called a “Scope of Work”) should be developed outside of the CNA. This rehabilitation repair list may be developed by the owner, a project architect, or an outside party (such as the CNA Provider, when qualified) hired by the owner. A copy of the rehabilitation repair list or Scope of Work should then be provided to the CNA Provider.

With this information, the CNA Provider, if requested by the owner and approved by Rural

Development, shall prepare a “Post Rehab” CNA indicating what repairs are planned for the property in the coming 20 years based on conditions after the rehabilitation is completed. Items to be replaced during rehabilitation, such as appliances, that will need to be replaced again during the 20 years will be included in the “Post Rehab” CNA. Items, such as a new roof, that will not need replacement during the coming 20 years will also need to be included in the “Post Rehab” CNA- if the EUL is more than 20 years it is optional to include a cost for a particular line item. The line item should not be removed from the CNA, but no data input will be necessary until an updated CNA is required. Appropriate comments should be included in the CNA report to acknowledge the scope of work or rehabilitation repairs that were considered.

The Owner should not use repair line item costs taken from the CNA to develop the rehabilitation cost estimates for the rehabilitation loan as these costs will not be accurate. The repair costs in a CNA are based on “probable market costs” for the property to have selected items replaced. Typically, these market costs include the labor, materials, overhead and profit. For example, for CNA purposes, it’s the probable market cost to send a repairman out, remove an appliance, and put a new one in its place. No other “soft costs” are included. For rehabilitation cost estimates, the Owner typically intends to hire a general contractor to oversee and supervise the rehabilitation work, which is then considered a “soft cost”. The cost of rehabilitation includes the costs for that general contractor, his general requirements, the cost of a project architect (if one is used), tenant relocation (if needed), interim financing (if used), which are also considered soft costs attributed to the rehabilitation costs for the project. A CNA cannot be used to accurately establish cost data for a rehabilitation project as most CNA activities do not include “soft costs”.

## **10. Repair and Replacement Schedule**

A CNA is an estimate of the anticipated replacement needs for a property, over time, and its associated replacement costs. If all of the refrigerators are being replaced in a rehabilitation project, and have an Estimated Useful Life (EUL) of 15 years, all refrigerators should not be replaced in year 15. If good quality equipment is purchased initially, they might last longer. If a refrigerator needs replacement in year 13, the tenant will not be forced to wait two years for a replacement refrigerator. The goal of a CNA is not to set the replacement times, but to estimate having funds available to replace equipment as it is needed. Hopefully, materials will be well maintained and last longer than estimated in the CNA. However, the CNA cannot be used to mandate replacement times for the identified building components.

## **11. Transition to the Underwriting Phase**

The integrity of the CNA report is critical to the underwriting conclusions. Financial planning adjustments may only be done during the underwriting phase and collaboration among the technical and financial perspectives are key to a well maintained, viable property. The property reserve account should be established or resized during underwriting to show funds will be available to meet the physical (capital) needs of the property over the 20-year approved CNA cycle. The underwriter will size the annual deposit to require a positive ending balance in each year of the 20-year capital needs cycle. In all transactions, the reserve must be sized to show that 100 percent of the capital needs can be met from the reserve account in the year the need is

projected to occur. These should be met without additional funding from the Agency or without supplemental rent increases for specific items only occurring within a single operating year.

### **Training Tool**

Program Support Staff in the National Office developed a Power Point presentation that can be used to train staff, CNA Providers, or owners/managers on the CNA process. This presentation is posted to the Internet on <http://www.rurdev.usda.gov/rhs/mfh/MPR/MPRHome.htm>. Please contact William Downs (202-720-1499) [william.downs@wdc.usda.gov](mailto:william.downs@wdc.usda.gov), Meghan Walsh (202-205-9590) [meghan@walsh@wdc.usda.gov](mailto:meghan@walsh@wdc.usda.gov) or Michel Mitias (202-236-3203) [michel.mitias@wdc.usda.gov](mailto:michel.mitias@wdc.usda.gov) if you have questions on the presentation.

### **Handbook Updates**

A Procedure Notice incorporating this guidance into the appropriate RD Handbooks is planned. Handbook procedures regarding the CNA process will be revised over time as Rural Development continues to improve the process for using the CNA in underwriting and servicing. Any suggestions, comments, or questions on the current RD underwriting CNA guidelines should be directed to Carlton Jarratt, Finance and Loan Analyst at 804-287-1524 [carlton.jarratt@wdc.usda.gov](mailto:carlton.jarratt@wdc.usda.gov) or Tammy Daniels, Finance and Loan Analyst at 202 720-0021 [tammy.daniels@wdc.usda.gov](mailto:tammy.daniels@wdc.usda.gov)

## REFERENCES TO CAPITAL NEEDS ASSESSMENT (CNA) IN 7 C.F.R. PART 3560 AND HANDBOOKS

A comprehensive list of references to a Capital Needs Assessment, or CNA, found in 7 C.F.R. [Part 3560, HB-1-3560, HB-2-3560, and HB-3-3560](#) follows. These references include information on situations for which a CNA is required, suggested uses of a CNA, general requirements for a CNA, sources of funding for a CNA, and requirements for a CNA performed by Rural Development. Each reference may not include the entire content. Refer to the source document for complete guidance.

### [7 C.F.R. Part 3560](#)

- 3560.11 – A definition of “Capital Needs Assessment” is included in the definitions section.
- 3560.103(c)(2) - A CNA is required if a borrower requests an increase in the project’s reserve replacement account. The cost of the CNA will be approved as an eligible project expense.
- 3560.103(c)(4) - Borrowers may request an increase in the amount contributed to and held in the reserve account, based on a CNA, as part of the annual budget process.
- 3560.103(c)(5) - Borrowers may request amendments to loan or grant documents to increase the amount contributed to and held in the reserve account, based on a CNA.
- 3560.306(j) - Rural Development may approve a change in the reserve account funding level, based on a CNA.
- 3560.406(d)(5) - A CNA is required to identify a project’s repair and rehabilitation needs in a transfer or a sale with an assumption of the Rural Development loan.
- 3560.656(e) - In the preservation process, when an incentive is developed, Rural Development must consider the project’s capital needs, based on a CNA.

### [HB-1-3560, MFH Loan Origination Handbook](#)

- HB-1-3560, Ch. 3, ¶ 3.17(B) - A CNA prepared by the project architect and reviewed by the Agency State Architect or Engineer should be used to determine features and materials that may cost more initially, but reduce operations and maintenance costs over time.
- HB-1-3560, Ch. 4, Sec. 3, ¶ 4.18(C)(2) - A CNA should be included in a Stage I application as the basis for the annual contribution to the reserve account. The CNA will be reviewed to determine if the recommended reserves are sufficient to cover the projected capital needs.

### [HB-2-3560, MFH Asset Management Handbook](#)

- HB-2-3560, Ch. 4, Sec. 3, ¶ 4.14 - Rural Development may approve a change in the reserve account funding level based on a CNA.
- HB-2-3560, Ch. 4, Sec. 4, ¶ 4.20(B) - The Loan Servicer will review the CNA, if available,

- to assess the borrower's annual capital expenditure budget.
- HB-2-3560, Ch. 5, Sec. 2, ¶ 5.7, (A) *Capital Needs Assessment – Capital Needs Assessment Overview*
  - HB-2-3560, Ch. 5, Sec. 2, ¶ 5.7, (B) *CNA – General Criteria*:
    - A CNA should be prepared at a reasonable cost by a qualified provider.
    - A CNA should be prepared according to accepted industry standards.
    - A CNA should include the detailed items listed on Form RD 3560-11, *MFH Physical Inspection Report*.
    - A CNA assessment period should be between 10 and 20 years.
    - Estimated repair and replacement costs and expected useful life spans of components/systems in a CNA should be based on nationally recognized data sources (e.g., RS Means *Repair and Remodeling Cost Data*).
  - HB-2-3560, Ch. 5, Sec. 2, ¶ 5.7, *Capital Needs Assessment – C. CNA required*:
    - When ownership of the project is transferred;
    - When the loan is re-amortized;
    - When there is a write-down of the project loan; or
    - At the borrower's request.
  - HB-2-3560, Ch. 5, Sec. 2, ¶ 5.7, (D) CNAs and a proposed, updated annual operating budget, including a revised capital plan and any proposed increase in contributions to replacement reserves and project rents, are submitted to the Field Office for Agency review.

[HB-3-3560, MFH Project Servicing Handbook](#)

- HB-3-3560, Exhibit 7-1; Summary of Key Approval Requirements by Type of Transfer. This chart explains under what circumstances a CNA should be conducted.
- HB-3-3560, Ch. 7 Sec. 5 ¶ 7.22 Physical Inspections - All transfers require completion of a CNA. For properties of nine units or more, a third party CNA is required. For properties with eight units or less, this requirement may be satisfied in either of the following ways:
  - A third party CNA.
  - The purchaser accepts Rural Development's published average CNA needs. For approved FY 2007 MPR Demonstration transactions, annual capital needs averaged \$1,110 per unit per year in 2007 dollars. For example, for an 8 unit project, underwritten in 2008, capital needs would be entered into the analytical template at \$9,146 per year each year for 20 years (8 x \$1,110 x 1.03 to account for inflation from 2007 to 2008). The analytical template would add inflation for years 2-20. The National Office may publish from time to time a revised per unit per year amount reflecting the average needs from recent CNAs.

Based on this information, all transfers require re-sizing of the reserve balance (i.e., a one-time additional deposit to the reserve may be required at the closing of the transfer) and resizing of the ongoing deposits (i.e., a higher ongoing deposit may be required), so that

future major repairs and replacements can be funded solely from the reserve. The CNA includes an evaluation of any accessibility needs [7 C.F.R. 3560.406(d)(9)] and must identify all immediate and long term repair and rehabilitation needs, see [7 C.F.R. 3560.406(d)(5)].

- HB-3-3560, Attachment 7-B-1, Transfer Application Documents - The CNA will be reviewed by the Rural Development CNA Reviewer and may need to be revised or adjusted to conform with Rural Development program requirements. Final approval of the CNA must be provided by the Rural Development CNA Reviewer prior to final approval of the transfer. May be omitted for Deceased Borrower transfers (Paragraph 7.5 D).
- HB-3-3560, Attachment 7-E, Transfer Request Checklist – A CNA is a required document for a complete application submittal for Agency approval.

[HB-1-3565, MFH Project Servicing Handbook](#)

- HB-1-3565, 5.6 ARCHITECTURAL SERVICES AND CAPITAL NEEDS ASSESSMENTS - Capital Needs Assessments (CNAs) are required for every property to be rehabilitated regardless of the scope of work.
- HB-1-3565, 7.13 COMPLETING THE CAPITAL NEEDS ASSESSMENT AND RESERVE ANALYSIS - The purpose of the Capital Needs Assessment (CNA) and reserve analysis is to ensure that reserve levels will continue to meet the expected capital repair and replacement needs of the property. A CNA must be completed during the underwriting of all loans involving rehabilitation and reviewed by the lender at least once every five years. The Agency recommends that the lender use CNAs to determine adjustments to the reserve level requirements for all loans it underwrites (see Paragraph 7.7 D.) For projects that are being rehabilitated, required deposits to the replacement reserve account for the first seven years of occupancy will be determined by the lender through a CNA. The lender must update the CNA every five years and update the “per unit annual contribution” accordingly.

**ADDENDUM**  
**TO CAPITAL NEEDS ASSESSMENT CONTRACT**

**(Between Owner and CNA Provider)**

This ADDENDUM to the CAPITAL NEEDS ASSESSMENT (CNA) CONTRACT between \_\_\_\_\_ (“CNA Provider”) and \_\_\_\_\_ (“Owner”) is entered into this \_\_\_\_ day of \_\_\_\_\_, 20\_\_ (the “Effective Date”) for the property known as \_\_\_\_\_ (“Property”)

**DEFINITIONS**

“**Acceptance**” means the act of an authorized representative of the United States Department of Agriculture, Rural Development by which the representative approves the Agreement and this Addendum.

“**Agreement**” means the contract entered into between the Owner and the CNA Provider to provide a CNA of the property. It includes the original document entered into between the parties, this addendum, and any other document incorporated by the agreement.

“**CNA Report**” means a report in general conformance with the *Statement of Work* that is attached hereto and the *Fannie Mae, Appendix D, Reference Effective Useful Life (EUL)Table, Instructions for the Property Evaluator*.

“**CNA Reviewer**” means a person assigned to review the CNA report on behalf of the U.S. Department of Agriculture, Rural Development.

“**CNA Provider**” means the person or entity entering into the Agreement with the Owner to perform all work required to provide a CNA of the property.

“**Owner**” means the person or persons who have or will have legal title and/or ownership of a property participating under the U.S. Department of Agriculture, Rural Development programs.

“**Program**” means any Multi-family Housing program authorized by section 515 of the Housing Act of 1949, as amended and administered by the U.S. Department of Agriculture, Rural Development.

“**Property**” means any structure(s), dwelling(s) and/or land that is the subject of any Multi-family Housing program administered by the U.S. Department of Agriculture, Rural Development, and for which a CNA is required by U.S. Department of Agriculture, Rural Development.

“**USDA RD**” means the United States Department of Agriculture, Rural Development.

“**Work**” means the *CNA Statement of Work* as attached hereto.

**RECITALS**

**WHEREAS**, the property known as \_\_\_\_\_ (“**Property**”) is included Program being administered by the USDA RD.

**WHEREAS**, as a condition of participating in the Program, the Owner is required to obtain a CNA for the property, which has been prepared in accordance with the Statement of Work; Owner and CNA Provider must agree to a contract to prepare a CNA for the property.

**WHEREAS**, CNA Provider and Owner are parties to that certain CNA Contract, dated, \_\_\_\_\_, \_\_\_\_ (“**Agreement**”), pursuant to which Owner has retained the services of CNA Provider to provide a CNA for the Property for the base contract amount of \$ \_\_\_\_\_ and for itemized Additional Services as follows: (See listing inspection I.e below,) in the amount of \$ \_\_\_\_\_ per item or service. The total contract amount is \$ \_\_\_\_\_.

**WHEREAS**, the parties hereby wish to incorporate into the Agreement and its Exhibits certain additional provisions as set forth below.

**NOW, THEREFORE**, in consideration of the promises and mutual covenants contained herein and other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the parties agree to the following additional terms and conditions as follows:

**ADDITIONS TO THE AGREEMENT**

**(Between Owner and CNA Provider)**

**I. OWNERS OBLIGATIONS -**

**SUBMISSION OF CONTRACT FOR CONCURRENCE BY USDA RD**

Owner will promptly submit to USDA RD for review and concurrence a copy of the executed Agreement and this Addendum.

**NOTIFICATION OF CONCURRENCE OF AGREEMENT BY USDA RD**

Upon receiving notification from USDA RD of its concurrence of the Agreement, Owner will promptly furnish CNA Provider with evidence of this acceptance.

**ACCESS TO THE PROPERTY**

Owner shall allow CNA Provider and, if requested, the CNA Reviewer, complete, timely and unconditional access to the property and its premises for the purpose of conducting the inspections that are required for preparing the CNA.

## FURNISHING PROPERTY INFORMATION

At least \_\_\_\_\_ (number) days prior to the commencement of the CNA inspection, Owner shall furnish to the CNA Provider all information on any recent and/or immediate planned capital improvements to the property, any recent and/or scheduled repairs, finalized maintenance schedules, and information on the existence of any known environmental hazards at the property. In addition, Owner shall provide any available information on any current “Transition Plan” or “**Self Evaluation**” addressing proposals for complying with any federal accessibility requirements and other matters relevant to the CNA Statement of Work.

Specific items the Owner should provide the CNA Provider include:

1. Contact information for the Owner’s representative at USDA RD (Name, address, telephone number, email address, etc.)
2. Building-by-building breakdown of units by bedroom count and type (i.e. garden, townhouse, fully accessible) to aid in selection of units at time of inspection
3. Any available plans or blueprints of development (as-built drawings preferred)
4. Listing of capital expenditures for the property over the past three to five years and maintenance expenditures over the last 12 months.
5. Maintenance logs to help identify any significant or systemic areas of concern.
6. Copies of invoices for any recently completed capital improvements and/or copies of quotes for any pending/planned capital improvements.
7. A valid/current Section 504 Accessibility Self Evaluation/Transition Plan (No more than three years old).
8. Any available capital/physical needs assessments (CNA’s/PNA’s) that were previously completed.
9. Any available structural or engineering studies that were previously completed.
10. Any available reports related to lead-based paint testing or other environmental hazards (i.e. asbestos, mold, underground storage tanks, etc.) that were previously completed and/or related certifications if environmental remediation has been completed.
11. Reports including but not limited to: local Health Department inspections, soils analysis, USDA’s last compliance review, or USDA’s last security inspection.
12. If the Owner certifies below that (a) 3<sup>rd</sup> party funds have been committed for use in the transaction for which the CNA is required; and (b) USDA RD has communicated its acceptance or acknowledgement of the availability of these funds (whether by an award of points in a portfolio revitalization program or otherwise); and (c) these funds are to be used towards a rehabilitation program at the property, the Owner will provide the CNA Provider with a copy of the proposed rehabilitation scope and budget.

## ADDITIONAL SERVICES

**When a CNA exceeds the one-year duration beyond the original acceptance date of the document, the report is required to be updated. The contract should designate anticipated tasks and costs that would be necessary to update the CNA after the one year or two year time frames have been exceeded. The contract should include, at a minimum:**

1. Identify property where update is required.
2. Itemized list of possible tasks to be performed to accomplish the update
  - Time and materials
  - Interviews
  - Document reviews (photos, construction documents, contracts, etc.)
  - Additional site visit as required (travel)
3. Associated unit costs for each task required for the CNA Update.

## II. OWNER'S CERTIFICATIONS -

**Owner hereby certifies as follows:**

### **STATUS OF PROPOSED CNA (check correct box):**

- Owner **has** received a **commitment** for 3<sup>rd</sup> party funding for the revitalization transaction for which application was made. **The CNA Provider will create the CNA based on existing conditions (“as is”)**. Owner is responsible for the scope of work and budget for the proposed rehabilitation of the property (typically obtained from a project architect), incorporating any requirements of the 3<sup>rd</sup> party lender. The CNA Provider will then revise their CNA based on the anticipated conditions (“post rehab”) of the property after the rehabilitation. Both CNAs will be provided to Rural Development.
- Owner **has requested or will request** 3<sup>rd</sup> party funds but has no commitment. If Owner does not have a commitment of 3<sup>rd</sup> party funds, Owner agrees that it is within USDA RD’s sole discretion to determine whether the CNA Provider should consider any rehabilitation scope of work and budget for a “post rehabilitation” CNA after conducting a CNA based on the property’s “as is” condition. USDA RD will make such a determination on the likelihood of 3<sup>rd</sup> party funds being made available. CNA Provider should verify this decision with Rural Development prior to performing a “post rehabilitation” CNA.
- Owner does not anticipate 3<sup>rd</sup> party funds being utilized, or does not anticipate a rehabilitation at this time. In this case, the CNA Provider will conduct a normal review of the property, not including / anticipating any rehabilitation, and base the CNA on the existing conditions at the property.

***NOTE: The Owner will not instruct the CNA Provider to perform a “post rehabilitation” CNA without approval from Rural Development.***

## **COMPLIANCE WITH STATEMENT OF WORK**

Owner shall allow the CNA Provider to comply with the Statement of Work in creating and developing a CNA Report that will incorporate and meet all terms, conditions and requirements as set forth in the attached Statement of Work. Owner shall not impede or attempt to influence the CNA Provider's impartiality in applying the CNA requirements and guidelines established by RD in describing the physical condition and needs of the property.

## **AVAILABILITY**

Owner shall be available to promptly discuss any draft or preliminary CNA Report with the CNA Provider and shall address in writing to the CNA Reviewer any desired revisions, corrections, comments or concerns the Owner may have relating to such Report.

## **ADDRESSING DEFICIENCIES**

Owner shall promptly furnish to the CNA Provider the USDA RD's CNA Review Report. Owner will discuss any deficiencies observed by the CNA Reviewer and request that the deficiencies be addressed within five (5) days. Should deficiencies not be addressed within five (5) working days, Owner may order the CNA Provider in writing to suspend, delay, or interrupt all or any part of the work under the Agreement that remains to be performed for such period of time until deficiencies identified by the CNA Reviewer have been satisfied.

## **PAYMENT**

The Owner shall pay the CNA Provider 50% of the negotiated contract amount for the base CNA contract once the contract for CNA Services has been executed. If the owner chooses to include and pay for additional services from the CNA Provider exceeding the negotiated base CNA contract amount, then these services must be listed and the payment method addressed in the contract between the Owner and CNA Provider. If funds for additional services will be withdrawn from the reserve account, then 50% of the base contract amount along with the additional services will be paid once the contract for CNA Services has been executed.

Upon concurrence by the CNA Reviewer of the CNA Provider's final Report (signature of Reviewer and Underwriter required), the Owner will promptly satisfy and pay the remaining 50% balance of the base contract amount and additional services if they are paid for out of the reserve account. Any remaining fees and/or dues owed to the CNA Provider pursuant to the terms of the Agreement will also be due upon the CNA Reviewer's concurrence of the CNA Provider's final report. Other payments shall be subject to the schedule identified in the Agreement.

## **III. CNA PROVIDER'S OBLIGATIONS – (applies to “As-is” “updates” and “post rehab”)**

### **CNA PROVIDER'S RESPONSIBILITY FOR WORK**

The CNA Provider shall furnish all necessary labor, materials, tools, equipment, and transportation necessary for performance of the work as described in the Statement of Work,

which is attached hereto. The format utilized for this report shall be \_\_\_\_\_.  
(Write in “USDA RD CNA Template in Microsoft Excel format” or similar electronic format.)

**COMPLIANCE WITH STATEMENT OF WORK**

CNA Provider will comply with the Statement of Work by creating and developing a CNA Report that will incorporate and meet all terms, conditions and requirements as set forth in the attached Statement of Work.

**DELIVERY OF PRELIMINARY CNA REPORT**

CNA Provider shall promptly provide to the Owner and USDA RD a preliminary CNA Report.

**AVAILABILITY TO DISCUSS CNA REPORT FINDINGS**

CNA Provider shall take any reasonable measures to be readily available to discuss and respond to any findings, concerns, comments, or revisions the CNA Reviewer may have regarding the preliminary CNA Report.

**SUBMISSION OF FINAL CNA REPORT**

After receipt of the CNA Reviewer’s Report, the CNA Provider shall promptly provide the Owner and USDA RD with a finalized CNA Report. The finalized report will incorporate observations, comments and/or changes identified by the CNA Reviewer.

**IV. CNA PROVIDER’S CERTIFICATIONS**

**CNA Provider hereby certifies as follows:**

**LICENSING AND COMPLIANCE**

CNA Provider possesses valid and current licenses and certifications necessary to comply with the Statement of Work and as regulated by all applicable state, county, and/or local laws and/or ordinances.

**CONFLICTS OF INTEREST**

CNA Provider has no identity of interest as defined in 7 C.F.R. part 3560 with Owner or Owner’s property or the management agency / company for the property.

**PROPERLY TRAINED**

CNA Provider and any Provider personnel who will have actual responsibility for the property inspection and preparation of the CNA are properly trained and experienced in evaluating site and building systems, health and safety conditions, physical and structural conditions, environmental and accessibility conditions, and estimating costs for repairing, replacing and improving site and building components.

**PROFESSIONALLY EXPERIENCED**

CNA Provider and any Provider personnel who will have actual responsibility for the property inspection and preparation of the CNA are professionally experienced in preparing and providing CNA's for multifamily housing properties that are similar in scope and operation to those typically financed in USDA RD's Multi-Family Housing Program.

**KNOWLEDGEABLE OF CODES**

CNA Provider and any Provider personnel who will have actual responsibility for the property inspection and preparation of the CNA are knowledgeable about applicable site and building standards and codes, including federal, state and local requirements on environmental and accessibility issues.

**f. DEBARMENT AND SUSPENSION**

CNA Provider is not debarred or suspended from participating in Federally assisted programs and will comply with the requirements of 7 C.F.R. part 3017 and 2 C.F.R. part 417 or any successor regulation, pertaining to debarment or suspension of a person from participating in a Federal program or activity.

**g. SIGNED CERTIFICATION**

Include a written and signed certification by the CNA Provider that it meets all of the above qualifications for the proposed agreement with the property owner for CNA services. [The CNA Provider's execution of this Addendum will constitute its "written and signed certification" that it meets these qualifications.]

**V. MISCELLANEOUS**

**USDA RD PROVISIONS**

Upon request of the CNA Provider or Owner, USDA RD will make available pertinent project data such as the reserve replacements for the last 2-3 years, budget summary of the last two years, and copies of Physical Inspections and Supervisory visits for the property, if available.

**ASSIGNMENT OF CONTRACT**

CNA Provider shall not assign or transfer any interest in or performance of this Contract, without written authorization from the Owner and the USDA RD representative.

**ENTIRE AGREEMENT**

If there are inconsistencies between any provision in this Addendum and any provision in the Agreement, the provision in this Addendum shall govern. No oral statements or representations or prior written matter contradicting this instrument shall have any force and effect.

**GOVERNING LAW**

All matters pertaining to this Addendum (including its interpretation, application, validity, performance and breach) in whatever jurisdiction action may be brought, shall be governed by, construed and enforced in accordance with the laws of the state of \_\_\_\_\_.  
(Location of the "Property")

**HEADINGS**

This Addendum shall be governed by and interpreted as part of the Agreement and its general terms and conditions.

**TERMS AND CONDITIONS**

Except as expressly stated herein, all other terms and conditions of the Agreement shall remain in full force and effect.

**IN WITNESS WHEREOF**, the undersigned who are duly authorized to execute and enter into this Addendum, intending to be legally bound hereby, have executed this Addendum as of the date first written above.

Project: \_\_\_\_\_

Project Location: \_\_\_\_\_

\_\_\_\_\_  
Owner

\_\_\_\_\_  
CNA Provider

By its: \_\_\_\_\_  
(title / position)

By its: \_\_\_\_\_  
(title / position)

Concurred by:

The United States Department of Agriculture, Rural Development

\_\_\_\_\_  
Rural Development Representative

\_\_\_\_\_  
(title / position)

# CAPITAL NEEDS ASSESSMENT STATEMENT OF WORK

## **Nature of the Work -**

A Capital Needs Assessment (CNA) is a systematic assessment to determine a property's physical capital needs over the next 20 years based upon the observed current physical conditions of a property. The CNA report provides a year-by-year estimate of capital replacement costs over this 20-year period for use by the property owner and USDA Rural Development (RD) personnel in planning the reserve account for replacements and other funding to cover these costs.

*Note: RD will use the CNA report as a key source of information about expected capital needs at the property and the timing of these needs. However, the CNA report is only an estimate of these needs and their timing. It should not be viewed as the formal schedule for actual replacement of capital items. Replacement of capital items should occur when components reach the end of their actual useful life, which may occur earlier or later than estimated in the CNA report.*

## **Payment -**

The Owner shall pay the CNA Provider 50% of the negotiated contract amount for the base CNA contract amount once the contract for CNA Services has been executed. If the owner chooses to include and pay for additional services from the CNA Provider exceeding the negotiated base CNA contract amount, then these services must be listed and the payment method addressed in the contract between the Owner and CNA Provider. If funds for additional services will be withdrawn from the reserve account, then 50% of the base contract amount along with the additional services will be paid once the contract for CNA Services has been executed. Upon concurrence by the CNA Reviewer of the CNA Provider's final Report (signature of Reviewer and Underwriter required), the Owner will promptly satisfy and pay the remaining 50% balance of the base contract amount and additional services if they are paid for out of the reserve account. Any remaining fees and/or dues owed to the CNA Provider pursuant to the terms of the Agreement will also be due upon the CNA Reviewer's concurrence of the CNA Provider's final report. Other payments shall be subject to the schedule identified in the Agreement

## **Qualifications -**

### **The CNA Provider must:**

Possess valid and current licenses and certifications necessary to comply with the Statement of Work and as regulated by all applicable state, county and / or local laws and / or ordinances.

Have no identity of interest as defined in [7 C.F.R. part 3560](#), with Owner or Owner's property. An architectural firm performing a CNA which is also involved in the rehabilitation of the

property would be considered an Identity of Interest. For example: the architect that performs the CNA assessment could overstate the conditions of the property in order to inflate the rehabilitation scope, resulting in an increase to the architect's compensation which is typically a percentage of the construction costs.

Be properly trained and experienced in evaluating site and building systems, health and safety conditions, physical and structural conditions, environmental and accessibility conditions, and estimating costs for repairing, replacing, and improving site and building components. (This applies to the CNA Provider or any Provider personnel who will have actual responsibility for the property inspection and preparation of the CNA)

Be professionally experienced in preparing and providing CNAs for multi-family housing properties that are similar in scope and operation to those typically financed in USDA RD's Section 515 Program. (This applies to the CNA Provider or any Provider personnel who will have actual responsibility for the property inspection and preparation of the CNA)

Be knowledgeable about applicable site and building standards and codes including federal, state and local requirements on environmental and accessibility issues. (This applies to the CNA Provider or any Provider personnel who will have actual responsibility for the property inspection and preparation of the CNA)

Not be debarred or suspended from participating in Federally assisted programs and will comply with the requirements of 2 C.F.R. parts 417 and 180 or any successor regulation, pertaining to debarment or suspension of a person from participating in a Federal program or activity.

### **Statement of Work -**

#### **The CNA Provider shall:**

Perform a Capital Needs Assessment (CNA) in general conformance with the document: "Fannie Mae, Appendix D, Reference Effective Useful Life (EUL)Table, Instructions for the Property Evaluator," except as modified herein.

Inspect the property. A minimum of **50%** (45% if property includes 50 – 99 units, 40% if the property contains 100 or more units) of all dwelling units shall be inspected in a non-intrusive manner. Consideration shall be given to inspecting at least one unit per floor, per building, and per unit type (one-bedroom, two-bedroom, etc.) up to the threshold percentage. CNA Providers shall ultimately be responsible for appropriate unit sampling but are encouraged to consult with site representatives to gather adequate information. This will help ensure that unit samples represent a cross-section of unit types and current physical conditions at the property and are reflective of substantive immediate physical condition concerns. All site improvements, common facilities (every central mechanical room, every laundry etc.), and building exteriors shall be inspected. (ASTM guidelines, allowing for "representative observations" of major elements are not adequate in this regard. Although inspections are "non-intrusive", CNA Providers shall include an inspection of crawlspaces and attics (when these spaces can be reasonably and safely accessed) in a number sufficient to formulate an opinion of the condition of those spaces and any work necessary.) All units designated as fully accessible for the handicapped shall be inspected. The inspection shall include interviews with the property owner, management staff, and tenants

as needed. It should also include consideration of all relevant property information provided by the owner, including –

Contact information for the client’s representative at Rural Development (Name, address, telephone number, email address, etc.)

Building-by-building breakdown of units by bedroom count and type (i.e. garden, townhouse, handicap accessible) to aid in selection of units at time of inspection

Any available plans or blueprints of development (as-built drawings preferred)

Listing of capital expenditures for the property over the past three to five years and maintenance expenditures over the last 12 months

Maintenance logs to help identify any significant or systemic areas of concern

Copies of invoices for any recently completed capital improvements and/or copies of quotes for any pending/planned capital improvements

A valid/current Section 504 Accessibility Self-Evaluation/Transition Plan (No more than three years old).

Any available capital/physical needs assessments (CNAs/PNAs) that were previously completed

Any available structural or engineering studies that were previously completed

Any available reports related to lead-based paint testing or other environmental hazards (i.e. asbestos, mold, underground storage tanks, etc.) that were previously completed and/or related certifications if environmental remediation has been completed

Reports including but not limited to: local Health Department inspections, soils analysis, USDA’s last Civil Rights compliance review, USDA’s last security inspection.

If the Owner certifies that: (a) 3<sup>rd</sup> party funds have been committed for use in the transaction for which the CNA is required; and (b) USDA RD has communicated its acceptance or acknowledgement of the availability of these funds (whether by an award of points in a portfolio revitalization program or otherwise); and (c) these funds are to be used towards a rehabilitation program at the property, the Owner will provide the CNA Provider with a copy of the proposed rehabilitation scope and budget. Attachment J provides more rehabilitation requirements.

Prepare a report using forms developed by Rural Development or other similar documents. The report shall be on an electronic worksheet commonly used in the industry, or as prescribed elsewhere herein. The report shall contain the following components, as a minimum:

Project Summary. Identification of the CNA Provider and property owner, and a brief description of the project, including the name, location, occupancy type (family/elderly) and unit mix.

Narrative. A detailed narrative description of the property, including year the property was constructed or rehabilitated (of each phase if work completed in multiple phases), interior and

exterior characteristics, conditions, materials and equipment, architectural and structural components, mechanical systems, etc. It shall also include:

Number, types, and identification of dwelling units inspected and used as a basis for the findings and conclusions in the report;

An assessment of how the property meets the requirements for accessibility to persons with disabilities;

a) The report shall include any actions and estimated costs necessary to correct deficiencies in order for the property to comply with applicable federal, state, and local laws and requirements on accessibility. The report shall also include an opinion on the adequacy of any existing and approved transition plans for the property in accordance with USDA/Rural Development requirements. CNA Providers shall not assume that a property built in accordance with accessibility standards prevailing at the time of original construction is “grandfathered” on accessibility requirements.

b) Attached is a checklist (Attachment F) setting out those items that should be included in any accessibility evaluation. It is meant to provide guidance to CNA Providers, but is not represented to be all-inclusive (i.e., CNA Providers are expected to be familiar with applicable federal accessibility requirements and standards (Architectural Barriers Act of 1968 and Section 504 of the Rehabilitation Act of 1973) and are required to ensure that the accessibility evaluation is based on such requirements and standards). Also attached are some frequently asked questions and answers regarding Rural Development policies and expectations with respect to certain accessibility issues. Finally, CNA Providers are strongly encouraged to review Appendix 5 to USDA Rural Development [Handbook HB-2-3560](#).

An assessment of observed or potential on-site environmental hazards (e.g., above or below ground fuel storage tanks, leaking electrical transformers);

*Note: The narrative portion of the report must address and include any existing testing results for the presence of radon, lead in water, lead based paint, and other environmental concerns. CNA Providers are not expected to conduct or commission any testing themselves. However, where test results provided by the owner affirmatively point to hazards, the CNA Provider should inquire about subsequent remediation steps and include cost allowances for any identified hazards not yet remediated.*

Recommendations for any additional professional reports as deemed necessary by the CNA Provider, such as additional investigations on potential structural defects or environmental hazards;

*Note: The narrative portion of the report must address each study or report necessary, why, and what expertise is needed so that the owner can alleviate that issue, including estimates for repairs, prior to underwriting. It is not the CNA Provider’s responsibility to estimate the cost of the study or repairs / remediation necessary.*

Needs of the property funded or to be funded from a third party (if any), such as tax credits, including a brief description of the work, the source of funding, the year(s) the work is planned to be completed, and the total estimated costs in current dollars; and:

*Note: For projects where the property owner advises the CNA Provider that third party funding for rehabilitation is committed and the work will begin within 12 months, the CNA should address the existing conditions at the property, **and** the post-rehabilitation needs at the property. An example would be a property owner who has submitted a pre-application to Rural Development for the Multi-family Portfolio Revitalization (MPR) Demonstration where Rural Development has awarded points to the application for third party funding, and it has committed third party funding. Under the MPR, an owner who has applied for third party funding for rehabilitation but does not have a commitment for this funding should have the CNA prepared based on conditions at the property “as is,” not post rehabilitation. In these cases, consult with Rural Development as to whether a “post rehab” CNA should be done. When a property owner receives the funding commitment, and rehabilitation is planned within the next 12 months, the CNA contract must be renegotiated to indicate that rehabilitation is planned and specify that a post-rehabilitation CNA should be prepared.*

*In preparing CNAs for these properties, the CNA Provider should undertake the CNA on the basis that the third party funded rehabilitation will occur as described in the scope of work for the rehabilitation project provided by the property owner and determine the property’s post-rehabilitation capital needs over the next 20 years. In these cases, the CNA Provider is expected to review and understand the scope of work for planned rehabilitation funded from third party sources, but aside from apparent substantive omissions is not required to comment on the planned rehabilitation.*

*If there is no evidence that third party funding for rehabilitation has been committed (e.g., if rehabilitation is not indicated in the Rural Development MPR pre-application and/or Rural Development has not awarded points for it), then the CNA Provider should verify with the Rural Development contact prior to performing a post rehab CNA. If no funds are committed, and Rural Development does not agree to a “post-rehab” CNA, the CNA Provider may note the owner’s rehabilitation proposal in the CNA but the report should be undertaken as though there will be no immediate rehabilitation. In these cases, the CNA should be based on the CNA Provider’s independent professional opinion of current and future needs at the property. (For example, if the owner wishes for a rehabilitation, but has no funds allocated to perform one.)*

Acknowledgments (names and addresses of persons who: performed the inspection, prepared the report, and were interviewed during or as part of the inspection).

Materials and Conditions. This component shall be reported on a Microsoft Office Excel © worksheet. The following major system groups shall be assessed in the report: Site; Architectural; Mechanical and Electrical; and Dwelling Units. ALL materials and systems in the major groups shall be assessed (not every specific material used in the construction of the property), including the following items:

Item Description;

Expected Useful Life (EUL). Data entries must be based on the Expected Useful Life Table included in the “Fannie Mae, Appendix D, Reference Effective Useful Life (EUL)Table, Instructions for the Property Evaluator”, unless otherwise explained in the report based upon the installation or most recent replacement date, quality, warranty, degree of maintenance or any

other reasonable and documentable basis. Any EUL entry that varies from the table must include explanation in a “Comments” column. Any EUL that varies from the table by 25% or more must be adequately supported separately from spreadsheet (for example, provide the documentation or explanation in the Narrative section);

Age. The actual age of the material or system;

Remaining Useful Life (RUL). Any RUL entry that varies from the difference between the EUL and Age must be explained in the “Comments” column. Any RUL entry that varies 2 years or more must be adequately supported separately from the spreadsheet (for example, provide the documentation or explanation in the Narrative section). Variances of more than 25% will not be accepted;

Condition. The current physical condition (excellent – good – fair – poor) of the material or system;

Description of action needed (repair – replace – maintain construct – none); and,

Comments or field notes that are relevant to the report.

Capital Needs. This component shall be reported on a Microsoft Office Excel © worksheet. This component identifies all materials and systems for each of the four major system groups to be repaired, replaced, or specially maintained. It shall include the following items for such materials or systems:

Year or years when action is needed;

Number of years to complete the needed action (duration of the repair work);

Quantity and Unit of Measure. Any data entry that is not from a physical property measurement or observation during the inspection shall be explained in the report (contrary to ASTM guidance, lump sum allowances shall be used only for capital projects, such as landscaping, that cannot readily be quantified); and,

Estimated repair, replacement, or special maintenance unit cost and total cost in current local market based (un-inflated) dollars for each line item. The report shall identify the source(s) used for the cost data. Entries shall include estimated costs for materials, labor (union or non-union wages, as appropriate), overhead & profit. Consultant fees, and other associated costs may be incurred by the property owner when repair or replacement work involves extensive capital activities (e.g., a major landscaping or site drainage project). These activities are likely to include design costs, or the involvement of general contractors, with associated overhead and profit considerations. If the CNA Provider anticipates work will be affected by these cost factors, notes should be added to the CNA spread sheet/report to explain the cost logic. Discussions with the owner and the Agency will be necessary to confirm the proposed cost of these capital activities. CNA Providers using such standard cost sources shall use cost allocations that include overhead and profit. **All costs should appropriately reflect the market conditions of the project.**

***Note:*** An estimated unit cost that is significantly different from an industry standard cost, such as R.S. Means or equivalent, must be adequately supported.

Generally, replacement actions shall involve “in-kind” materials, unless a different material is more appropriate, approved by the State Historic Preservation Office, if applicable, and explained in the report. Exceptions shall be made for components that are seen as inadequate (e.g. twenty gallon water heaters, prompting resident complaints) or below contemporary design/construction standards (e.g. single-glazed windows in temperate climates). Rural Development also encourages the consideration of alternative technology and materials that offer the promise of reduced future capital and/or operating costs (more durable and or less expensive to maintain over time, reduce utility expenses, etc.). CNA Providers are not expected to conduct quantitative cost-benefit analyses but shall use sound professional judgment in this regard.

In addition to the exceptions described in the paragraph above, Rural Development may consider the inclusion of market-comparable amenities/upgrades (e.g. air conditioning in warm climates) proposed by the owner when such features are essential to the successful operational and financial performance of the property. Such items should be identified specifically in the CNA report as “owner-recommended upgrades” and include an explanation of why these upgrades are necessary in supporting the financial and operational performance of the property. Where included, CNA Provider comments on the feasibility and appropriateness of the upgrade are required.

The capital needs shall be presented in two time frames:

a) Immediate Capital Needs. All critical health and safety deficiencies (e.g. inoperative elevator or central fire alarm system, missing/unsecured railings, blocked/inadequate fire egress, property-wide pest infestation) requiring corrective action in the immediate calendar year. Separately, the owner shall provide any repairs, replacements, and improvements currently being accomplished in a rehabilitation project, regardless of funding source, and anticipated to be completed within 12 months. The owner will include the budget for any planned rehabilitation (e.g., rehabilitation proposed in the property owner’s pre-application to the MPR). CNA Provider can, but is not required, to offer comments about the rehabilitation budget. The CNA shall not include minor, inexpensive repairs or replacements that are part of a prudent property owner’s operating budget. (If the aggregate cost for a material line item is less than \$1000, then the line item shall not be included in the CNA. An aggregate cost for a line item is an item which needs to be replaced in any given year, the cost exceeds the \$1000, and the item should be replaced in the one year duration. **Applying a duration that exceeds one year may decrease the aggregate amount below the \$1000 threshold, thus circumventing the intent of the threshold to include a particular item in the CNA.**

Where immediate rehabilitation is proposed by the owner using 3<sup>rd</sup> party funds, the CNA Provider shall note the current condition and remaining effective useful lives of affected systems and components in an “as is” CNA.

b) Capital Needs Over the Term. Such capital needs include significant maintenance, repairs, and replacement items required during subsequent twenty calendar years to maintain the property’s physical integrity and long term marketability. It shall include repairs, replacements, and significant deferred maintenance items currently being planned and anticipated to be completed after the immediate calendar year and corrections for violations of applicable standards on environmental and accessibility issues. It shall also include the needs described in paragraph 3.b.v. above in the appropriate year(s), if any, if these will not be completed within 12

months from the closing of the program revitalization transaction. The CNA shall not include minor, inexpensive repairs or replacements that are part of a prudent property owner's operating budget. (If the aggregate cost for a material line item is less than \$1000, then the line item shall not be included in the CNA. An aggregate cost for a line item is an item which needs to be replaced in any given year, the cost exceeds the \$1000, and the item should be replaced in the one year duration. Applying a duration that exceeds one year may decrease the aggregate amount below the \$1000 threshold, thus circumventing the intent of the threshold to include a particular item in the CNA.

**Exceptions to these exclusions may be appropriate for very small properties, and/or for low cost items that may affect resident health and safety (e.g., a damaged or misaligned boiler flue). For example, in small projects (total of 12 units or less), items exempted would be for material line items less than \$250, not \$1,000. The report shall be realistic and based on due diligence and consideration of the property's condition, welfare of the tenants, and logical construction methods and techniques. The estimated unit costs and total costs to remedy the detailed needs shall be provided in current (un-inflated) dollars.**

Capital Needs Over the Term shall be based on the actual remaining useful lives of the components and systems at hand. Aside from formal work that is accounted for in the Immediate Capital Needs section, capital activities shall not be "front-loaded."

*Note: New components or upgrades addressed in a property's rehabilitation may have long-term capital needs implications as well. Those items with expected useful lives of less than twenty years (e.g. air conditioners) also will need to be accounted for in Capital Needs Over the Term.*

Executive Summary. This component shall be reported on a Microsoft Office Excel © worksheet. It shall include:

Summary of Immediate Capital Needs – the grand total cost of all major system groups (in current dollars);

Summary of Capital Needs Over the Term – the annual costs and grand total cost of all major system groups (in current and inflated dollars). The inflation rate shall be 3 percent; and,

Summary of All Capital Needs – the grand total costs for the immediate and over the term capital needs (in current and inflated dollars). The grand total costs (in current and inflated dollars) per dwelling unit shall also be included.

Appendices. This component shall include a minimum 25 color digital photographs that describe: the property's buildings (interior and exterior) and other facilities, specific material or system deficiencies, and the bathrooms and kitchens in the units accessible for the handicapped. Include a property location map and other documents as appropriate to describe the property and support the findings and summaries in the report. The CNA Provider should provide some sort of visual documentation for each line item that cannot be clearly identified by a written description alone. For instance, if an entrance needs to become handicap accessible, a picture of the entrance will help the owner understand where the construction should take place. The Owner needs to be able to associate reserve account funds with the correct line items during the life of the CNA during the underwriting process.

Deliver the following:

A minimum of one electronic copy of the report shall be delivered on a compact disk, or other acceptable electronic media, e.g. e-mail, to both property owner and USDA Rural Development for their review and written acceptance. To the greatest extent possible, delivery should be made within 15 business days of execution of the agreement with the property owner.

If the report is not acceptable, the CNA Provider shall make the appropriate changes in accordance with the review comments. A minimum of one electronic copy of the revised report shall be delivered on a compact disk or via e-mail to both property owner and USDA Rural Development for their review and written acceptance. The delivery should be made within 5 business days of receiving the review comments.

If the revised report is still not acceptable, additional revisions will be made and electronic copies delivered on compact disks or via e-mail to the property owner and USDA Rural Development until the report is acceptable to both property owner and USDA Rural Development.

Be available for consultation, with the property owner or USDA Rural Development prior to written acceptance of the report, on any of its contents.

The CNA Provider shall **NOT** analyze the adequacy of the property's existing or proposed replacement reserve account nor its deposits as a result of the capital needs described in the report.

# FANNIE MAE PHYSICAL NEEDS ASSESSMENT GUIDANCE TO THE PROPERTY EVALUATOR

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- 1) Transfer of Project Ownership;
- 2) Loan Reamortization;
- 3) Loan Write-down; or
- 4) Development of an Equity Loan Incentive or Equity Loan for a Sale to a Non-profit Sponsor.

## Introduction

While many factors affect the soundness of a mortgage loan over time, one of the most significant is the physical condition of the property - past, present and future. A prudent lender must be concerned with the past maintenance and improvements because they may indicate owner and management practices as well as expenses to be incurred in the future. The lender must be concerned with the condition of the property at the time the loan is made, and over the term of the loan, because property condition may directly impact marketability to prospective tenants and the need for major expenditures may impact the economic soundness and value of the property. The lender must also be concerned with the condition of the property at the end of the loan term. If the property has deteriorated, the owner may not be able to secure sufficient financing to pay off the loan at maturity.

Most lenders have always given some attention to physical conditions and needs of properties in their underwriting. However, the amount of attention, the data secured, the quality and analysis of that data, and the impact of this information on underwriting has varied widely. Indeed, many properties and the loans that they secure are now in trouble because of inadequate consideration of physical needs in the underwriting coupled with inadequate attention to property maintenance which has diminished the marketability and overall value of the property.

## Specific Guidance to the Property Evaluator

### *Purpose*

The purpose of the Physical Needs Assessment is to identify and provide cost estimates for the following key items:

- Immediate Physical Needs - repairs, replacements and significant maintenance items which should be done immediately
- Physical Needs Over the Term - repairs, replacements and significant maintenance items which will be needed over the term of the mortgage and two years beyond.

As part of the process, instances of deferred maintenance are also identified.

The assessment is based on the evaluator's judgment of the actual condition of the improvements and the expected useful life of those improvements. It is understood that the conclusions presented are based upon the evaluator's professional judgment and that the actual performance of individual components may vary from a reasonably expected standard and will be affected by circumstances which occur after the date of the evaluation.

### **Items (EUL)**

Each of the four forms has a number of frequently-occurring systems and components listed. This list represents only the most frequently observed and is not meant to be all inclusive. *Every system present at the property must be observed and recorded.* Any system not listed on the form may be included in the spaces labeled Other. Note that the assessment includes the systems and components in both residential and non-residential structures. Thus, garages, community buildings, management and maintenance offices, cabanas, pools, commercial space, and other non-residential buildings and areas are included.

The Expected Useful Life (EUL) figure which appears in parentheses after the Item is taken from the Expected Useful Life Table provided. This table provides standard useful lives of many components typically found in apartment complexes. Where the parentheses do not contain a number, it is because there are various types of similar components with differing economic lives. The evaluator should turn to the Expected Useful Life Table and select, and insert, the appropriate Expected Useful Life (EUL) number. If the Expected Useful Life (EUL) will, without question, far exceed the term of the mortgage plus two years, the Expected Useful Life (EUL) number need not be inserted.

Note: It is recognized that the Expected Useful Life Tables represents only one possible judgment of the expected life of the various components. If we receive substantial material to the effect that one or more of the estimates are inappropriate, we will make adjustments. Until such changes are made, the Tables provide a useful and consistent standard for all evaluators to use. They avoid debate on what the appropriate expected life is and permit focus on the evaluator's judgment of the effective remaining life of the actual component in place, as discussed below.

### **Age**

The evaluator should insert the actual Age of the component or may insert "OR" for original. If the actual age is unknown, an estimate is acceptable. If there is a range in Age (for example, components replaced over time), the evaluator may note the range (i.e., 5-7 years) or may use

several lines for the same system, putting a different Age of that system on each line.

### **Condition**

This space is provided to indicate the Condition of the component, generally excellent, good, fair, or poor, or a similar and *consistent* qualitative evaluation.

### **Effective Remaining Life**

This space is provided for the evaluator to indicate the remaining life of the component as is. For standard components with standard maintenance, the Expected Useful Life Table provided by the Lender could be used to determine Effective Remaining Life by deducting the Age from Expected Useful Life (EUL). However, this should not be done automatically. A component with unusually good original quality or exceptional maintenance could have a longer life. On the other hand, if the component has been poorly maintained or was of below standard original quality, the useful life could be shorter than expected. *The evaluator applies his or her professional judgment in making a determination of the Effective Remaining Life.*

*If the Effective Remaining Life is longer than the term of the loan plus two years, no deferred maintenance exists, and no action needs to be taken during the life of the loan, no other columns need to be filled out.* The only exception may be Diff? (Difference), as discussed below. This should be noted when the evaluator's estimate of the Effective Remaining Life varies by more than two years from the standard estimate.

### **Diff? (Difference)**

The Age of the component should be deducted from the Expected Useful Life (EUL) in parentheses and the answer compared to the Effective Remaining Life estimated by the evaluator. Where there is a difference of over two years, the evaluator should insert a footnote number in the DIFF? (Difference) column and supply, in an attached list of footnotes, a brief statement of why, in his or her judgment, the Effective Remaining Life of the component varies from the standard estimate. This approach provides consistency among evaluators while making best of the evaluators' professional judgment.

### **Action**

If any Action is required - immediately, over the life of the loan, or within two years thereafter - the Action should be recorded as *repair, replace, or maintain*. Repair is used when only a part of an item requires action, such as the hydraulics and/or controls of a compactor. Replace is used

when the entire item is replaced. Maintain is used where special, non-routine maintenance is required, such as the sandblasting of a swimming pool. In cases where a repair or maintenance may be needed now, and replacement or further maintenance may be needed later, separate lines may be used to identify the separate actions and timing.

## Now?

If the item involves a threat to the immediate health and safety of the residents, clearly affects curb appeal, will result in more serious problems if not corrected, or should otherwise be accomplished as part of an immediate repair, maintenance or replacement program, this space should be checked. Replacements which may be needed in year one, but do not require immediate attention, need not be checked.

## DM (Deferred Maintenance)

The DM (Deferred Maintenance) space is marked in any instances where current management practice is clearly inadequate and the owner's attention should be called to the item, even if no major expenditure or significant labor may be required.

## Quantity

For items requiring action, the evaluator should note the Quantity of the system, with the applicable unit of measure entered (each, unit, square feet, square yards, linear feet, lump sum, etc.).

## Field Notes

This space, as well as attachments may be used to record the type of component (16cf, frost. free, Hotpoint), the problem (valves leaking) or other information (consider replacement for marketing purposes, replace 30% per year, work in progress, etc.) that the evaluator will need to complete the Evaluator's Summary.

*Countertop/sinks* are 9 years old. (The entry could also be "OR"). Condition is excellent, with an Effective Remaining Life of 10 years. This is significantly different from the anticipated Effective Remaining Life of 1 (an EUL of 10 years minus an Age of 9 years). Therefore, there is a footnote entry "1" in the Diff? (Difference) column. The footnote will indicate that this item is made of an exceptionally durable material (Corian), along with a top quality stainless steel sink. The evaluator's estimate of an Effective Remaining Life of 10 years + is beyond the term of +2. No capital need would be reported.

*Refrigerators* are also original, reported as 16 cf frost free Hotpoint. Replacement is expected around the Effective Remaining Life, noted as 20% annually and beginning in the 5<sup>th</sup> year of the loan when the refrigerators are 14 years old.

*Disposals* range from new to original (Age = 0-9). 20% per year replacements will be needed starting in year 1. The evaluator notes that disposals appear to be replaced as part of the project's normal operations.

*Bath fixtures* are original, and in good condition. No replacement is expected to be required during the term +2 years. The note indicates that they are "dated looking," which may prompt a market consideration for replacement.

*Ceiling* is a special entry. The “04” stack of units has experienced water damage to ceiling from major plumbing leak. This is noted for repair NOW. As this apparently occurs in all 10 units in this stack and therefore is likely to have more than a modest cost, this action would be reported on the Immediate Physical Needs summary form.

### **Evaluator’s Summary: Immediate Physical Needs**

*Unit Cost* - This is the cost per unit (sf, ea, lf, etc.) in current dollars to implement the required action. The source of the cost estimate should be listed in a separate attachment. The sources may include a third-party estimation service (e.g., R.S. Means: *Repair and Remodeling Cost Data*), actual bid or contract prices for the property, estimates from contractors or vendors, the evaluator’s own cost files, or published supplier sources.

*Total Cost* - This is the result of multiplying the quantity times the unit cost. It is expressed in current year dollars.

*DM (Deferred Maintenance)* - If the item evidences deferred maintenance, this column is checked.

*Comments* - the comments column, or an attachment, should clearly provide information on the location and the nature of problem being addressed for each item. The information should be adequate for the owner to begin to implement the action.

### **Evaluator’s Summary: Physical Needs Over the Term**

*Cost by Year* - the result of multiplying the quantity times the unit cost, in current dollars, is inserted in the column for the year in which the action is expected to take place. Generally, the Effective Remaining Life estimate provided by the evaluator on the Systems and Conditions will indicate the action year. For example, if the evaluator has indicated that the Effective Remaining Life of the parking lot paving is 4 years, the cost, in current dollars, is inserted in Year 4. If the items are likely to be done over a number of years, the costs, in current dollars should be spread over the appropriate period. For example, if the Effective Remaining Life of the Refrigerators is estimated to be 4 years, or 3-5 years, one third of the cost of replacing the refrigerators may appear in each of Years 3, 4, and 5.

*Total Uninflated* - After inserting all of the appropriate action items, the evaluator should total the items for each year.

*Total Inflated* - The evaluator should multiply the Total Uninflated times the factor provided to produce the Total Inflated.

*Total Inflated All Pages* - On the last sheet, the evaluator should include the Total Inflated Dollars for that page and all prior pages.

*Cumulative Total All Pages* - On the last sheet, the evaluator should insert the Total Inflated

Dollars of that year and all prior years.

### **Special Repair and Replacement Requirements**

While performing a property inspection, the evaluator must be aware that certain building materials and construction practices may cause properties to experience (or to develop in a short time period) problems that can be corrected only with major repairs or replacements. The following identifies some specific construction related problems; however, the evaluator must be aware that other construction related problems may be found in any property and should be identified. If any of the following requirements are not met or if the evaluator determines that the following conditions (or others) are present, *the evaluator must contact the lender immediately to discuss the timing as well as the cost of the repairs or replacements.* The evaluator should ensure that any of these conditions are thoroughly addressed in the Physical Needs Assessment.

*Minimum Electrical Capacity* - Each apartment unit must have sufficient electrical capacity (amperage) to handle the number of electrical circuits and their use within an apartment. Therefore, the evaluator must determine, based on referencing the National Electric Code as well as local building codes, what is the minimum electrical service needed. In any event, that service must not be less than 60 amperes.

*Electrical Circuit Overload Protection* - All apartment unit circuits, as well as electrical circuits elsewhere in an apartment complex, must have circuit breakers as opposed to fuses as circuit overload protection.

*Aluminum Wiring* - In all cases, where aluminum wiring runs from the panel to the outlets of a unit, the evaluator's inspection should ascertain that the aluminum wiring connections (outlets, switches, appliances, etc.) are made to receptacles rated to accept aluminum wiring or that corrective repairs can be done immediately by the owner.

*Fire Retardant Treated Plywood* - While performing the roof inspection, the evaluator should investigate whether there is any indication that fire-retardant treated plywood was used in the construction of the roof (primarily roof sheathing). This inspection should focus on sections of the roof that are subjected to the greatest amount of heat (e.g., areas that are not shaded or that are poorly ventilated) and, if possible, to inspect the attic for signs of deteriorating fire-retardant treated plywood or plywood that is stamped with a fire rating.

Our concern is that certain types of fire-retardant treated plywood rapidly deteriorate when exposed to excessive heat and humidity or may cause nails or other metal fasteners to corrode. Common signs of this condition include a darkening of the wood and the presence of a powder-like substance, warping of the roof and the curling of the shingles. Fire-retardant treated plywood is most likely to be in townhouse properties or other properties with pitched, shingled roofs that were constructed after 1981 and that are located in states east of the Mississippi River and some southwestern states.

### **Narrative Conclusion and Attachments**

A complete narrative summary of the property and its components is not required. However, the evaluator should supply a concise summary of the conclusions reached concerning the overall condition of the property, its future prospects, and the quality of the current maintenance programs. *Any items affecting the health and safety of residents should be clearly flagged.*

The summary should include a discussion of the sampling approach used, discussed above, and any market issues which the evaluator believes it may be appropriate to address or which were noted by the lender.

The narrative, the forms use and the attachments (footnotes explaining Differences, information regarding sources of costs, and, if necessary, information needed to identify the location and type of problem addressed in the Evaluator's Summary: Physical Needs Over the Term) should be supplied.

# CNA e-Tool Estimated Useful Life Table

CNA e-Tool Estimated Useful Life Table		The following table lists the recommended average useful life of the categories of assets that should be considered in a Capital Needs calculation. If a specific item is not listed, it should be assigned to the most closely related category. The Standard EUL for a component type is fixed. The user may estimate the Remaining Useful Life of any existing component independent of the Standard EUL by entering the estimated RUL in the appropriate space on the Components tab of the Excel Assessor/Lender Tool. When identifying an alternative to the existing component the user may specify an EUL for the alternative which differs from the Standard EUL for that component type but must enter an explanation in the comment space on the Alternatives tab of the Tool.			EUL		
Index	System Description	Overall General Description	Sub-Component	Component Description	Family	Elderly	
3				System Description and Observations			
	3.1			Overall General Description			
	3.2			Site Systems			
		3.2.1		Topography			
		3.2.2		Storm Water Drainage			
		3.2.2.1		Catch basins, inlets, culverts	50	50	
		3.2.2.2		Marine or stormwater bulkhead	35	35	
		3.2.2.3		Earthwork, swales, drainways, erosion controls	50	50	
		3.2.2.4		Storm drain lines	50	50	
		3.2.2.5		Stormwater mgmt ponds	50	50	
		3.2.2.6		Fountains, pond aerators	15	15	
		3.2.3		Access and Egress			
		3.2.3.1		Security gate - lift arm	10	10	
		3.2.3.2		Security gate - rolling gate	15	15	
		3.2.4		Paving, Curbing and Parking			
		3.2.4.1		Asphalt Pavement	25	25	
		3.2.4.2		Asphalt Seal Coat	5	5	
		3.2.4.3		Concrete Pavement	50	50	
		3.2.4.4		Curbing, Asphalt	25	25	
		3.2.4.5		Curbing, Concrete	50	50	
		3.2.4.6		Parking, Gravel Surfaced	15	15	

3 tiers of categorization:  
Need Category, Need Item,  
Component Type

Need Category

Need Item

All items not color coded are "Component"

Need Item

Need Item





















## Accessibility Laws and Standards

Law and Regulation References	Act/Section Application	Accessibility Standard	Accessibility Requirements
<p>Public Law 90-480 (42 USC 4151-4157)</p> <p>(not referenced in regulations)</p>	<p>The Architectural Barriers Act of 1968 requires certain facilities financed with Federal funds be designed and constructed as to be accessible to the physically handicapped. These include rental properties with on-site offices.</p> <p>Rural Development projects financed with Federal funds include:</p> <ul style="list-style-type: none"> <li>• Section 515 Rural Rental Housing</li> <li>• Section 514/516 Farm Labor Housing grants and loans.</li> </ul>	<p>Uniform Federal Accessibility Standard (UFAS)</p>	<p>All areas open to the public must be fully accessible to persons with disabilities. (For a MFH development, this would apply to the rental office. Other spaces - such as laundries, community rooms, etc. – are generally “common areas” for the use of tenants and their guests, and are not considered public spaces.)</p> <p>(Requirements of the Architectural Barriers Act are met when meeting Section 504 of the Rehabilitation Act.)</p>
<p>Public Law 93-112 (29 USC sections 790-794)</p> <p>7 C.F.R. part 15b also 7 C.F.R. 3560.60(d))</p>	<p>Section 504 of the Rehabilitation Act of 1973 requires programs and facilities receiving Federal financial assistance be designed and constructed as to be accessible to the physically handicapped.</p> <p>Rural Development projects receiving Federal financial assistance</p>	<p>Uniform Federal Accessibility Standard (UFAS)</p>	<p><b>Substantial Alteration (7 C.F.R. 3560.60(d)(2)):</b></p> <ul style="list-style-type: none"> <li>• Substantial alteration defined as 50% or more of the full and fair cash value of the building. (See UFAS.)</li> <li>• Buildings undergoing substantial alteration are treated as “new construction” in UFAS due to the level of rehab.</li> </ul> <p><b>Properties ready for occupancy</b></p>

	<p>include:</p> <ul style="list-style-type: none"><li>• Section 515 Rural Rental Housing</li><li>• Section 514 / 516 Farm Labor Housing grants and loans</li></ul>	<p><b>after 6/10/82:</b></p> <ul style="list-style-type: none"><li>• At least 5% of all dwelling units, or a minimum of one dwelling unit (DU) must meet <u>mobility impairment requirements</u>. (Always round up. 5% of 21 units = TWO fully accessible units.)</li><li>• The mix of accessible units is to be comparable to the variety of other project units (ie. 1, 2, and 3 bedrooms).</li><li>• Public and common use areas must be accessible per UFAS.</li></ul> <p><b>Properties ready for occupancy on or before 6/10/82:</b></p> <ul style="list-style-type: none"><li>• Borrowers are encouraged to make 5% of units fully accessible. If a unit undergoes extensive repair, it will be made accessible to the extent possible, up to the 5% requirement. (7 C.F.R. 3560.60(d)(2))</li><li>• Borrowers must conduct self-evaluations, and if needed develop transition plans</li><li>• Borrowers must make common areas accessible when financially and structurally</li></ul>
	<p>Section 504 of the Rehabilitation Act (con't)</p>	<p>feasible (Common areas include mailboxes, office, community room, trash areas, playgrounds, laundry facilities, etc.)</p> <ul style="list-style-type: none"><li>• When a qualified individual with a disability applies for admission, borrowers must make the unit accessible and usable to the individual.</li></ul> <p><b>Other Considerations:</b></p> <ul style="list-style-type: none"><li>• For existing facilities, accessibility must be provided to the maximum extent feasible. If structurally impractical, a referral agreement may be used in lieu of making the facility accessible.</li></ul>

			<ul style="list-style-type: none"> <li>• An applicant / tenant may request “reasonable accommodation” at owner/ project expense at any time.</li> </ul>
<p>Public Law 101-336 (42 USC sections 12111 et seq.)</p> <p>28 C.F.R. Parts 35 and 36</p> <p>7 C.F.R. part 3560.60(d)</p> <p>Public Law 90-284 (42 USC sections 3601 et seq)</p> <p>24 C.F.R. Part 100 and 54 C.F.R. Part 3232 (HUD’s regs implementing FHAA)</p> <p>7 C.F.R. section 3560.60(d)</p>	<p>The Americans with Disabilities Act of 1990 requires all places of public accommodation and commercial facilities be accessible to persons with disabilities. Applies to all new construction and any repair / rehab. This law applies to all public spaces, regardless of financing (public or private).</p> <p>Rural Development projects include:</p> <ul style="list-style-type: none"> <li>• Section 515 Rural Rental Housing</li> <li>• Section 514 / 516 Farm Labor Housing grants and loans</li> </ul> <p>The Fair Housing Amendments Act to the 1964 Civil Rights Act requires all “covered dwellings” to be adaptable. “Covered dwellings” are all ground floor units (or all units in an elevator building) in buildings with four or more units constructed after 3/13/91. This law applies to all Multi-family Housing, regardless of financing (public or private).</p> <p>Rural Development projects include:</p> <ul style="list-style-type: none"> <li>• Section 515 Rural Rental Housing</li> <li>• Section 514 / 516 Farm</li> </ul>	<p>Americans with Disabilities Act Accessibility Guidelines for Buildings and Facilities (ADAAG)</p>	<p>All areas open to the public must be fully accessible to persons with disabilities. (For a MFH development, this would apply to the rental office. Other spaces - such as laundries, community rooms, etc. – are generally “common areas” for the use of tenants and their guests, and are not considered public spaces. Exceptions would be a community room used for polling, training, etc. or a dining room serving outsiders.)</p> <p><b>Properties ready for occupancy after 1/26/93:</b></p> <ul style="list-style-type: none"> <li>• Public areas must be accessible per ADAAG standards.</li> <li>• Once UFAS requirements are met, typically the additional ADAAG requirement is for a “van accessible” parking space at the office.</li> </ul> <p><b>Properties ready for occupancy on or before 1/26/93:</b></p> <ul style="list-style-type: none"> <li>• When public areas are altered, they must be altered to ADAAG standards. (Public areas are those areas used by individuals other than tenants and their guests. This includes offices used to pay bills or to inquire about rentals, public restrooms, and spaces used for voting, public meetings, or meals for outsiders.)</li> </ul> <p><b>Properties ready for occupancy after 3/13/91:</b></p> <ul style="list-style-type: none"> <li>• At least one building entrance must be on an accessible route</li> </ul>

	<p>Labor Housing grants and loans</p>	<p>unless impractical due to terrain. (24 C.F.R. 100.205(a)) (Unless terrain does not permit and “site impracticality” test performed, all ground level units or all units in an elevator building on an accessible route.)</p> <ul style="list-style-type: none"><li>• Townhouses and buildings less than 4 units exempted from requirements.</li><li>• All public and common use areas must be accessible. (24 C.F.R. 100.205(c)(1))</li><li>• All external and internal doors must be wide enough to accommodate wheel chair access. (24 C.F.R. 100.205 (c)(2))</li><li>• All “covered dwellings” must contain the following features of adaptable design:<ul style="list-style-type: none"><li>◇ Accessible route into and through the DU (24 C.F.R. 100.205 (c)(3)(i))</li><li>◇ Light switches in accessible locations (24 C.F.R. 100.205 (c)(3)(ii))</li><li>◇ Reinforcements in bathroom walls for grab bars and , (24 C.F.R. 100.205 (c)(3)(iii))</li><li>◇ Usable kitchens and bathrooms for persons in wheelchairs (24 C.F.R. 100.205 (c)(3)(iv))</li></ul></li><li>• Applicant / tenant may request “reasonable accommodations” to the unit, at the tenant’s expense.</li></ul> <p><b>Properties ready for occupancy on or before 3/13/91:</b></p> <ul style="list-style-type: none"><li>• Fair Housing has no accessibility requirements for projects constructed prior to this date.</li></ul>
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# Existing Property Accessibility Checklist

<b>DISCLAIMER</b>	This information was developed to assist CNA Providers in developing repair lists for existing MFH properties financed through USDA Rural Development's Section 515 program, as part of a Capital Needs Assessment (CNA). This analysis was not intended to address all accessibility requirements of any Federal, State, or local laws or regulations nor should this information be relied on for that purpose. To ensure full compliance, borrowers, architects, loan officials, CNA Providers, contractors, and other interested persons should refer to the Uniform Federal Accessibility Standards, the HUD Fair Housing Accessibility Guidelines, the Americans with Disabilities Act Accessibility Guidelines, and all other applicable Federal, State, and local standards. Please be aware that the owner(s) of this building are responsible for compliance of all applicable accessibility regulations.	
<b>SITE -</b>	(For each item, enter "Y" for "Yes", "N" for "No", or "NA" for "Not Applicable" in the first column. For each "N", transfer into the CNA a cost estimate for correction. Include details, notes, or photographs as appropriate to explain the situation.)	
<b>Parking:</b>	1.	Proper number of accessible spaces? (min. 1 / accessible unit + 1 visitor / office space – <i>UFAS 4.1.1(5)(d)</i> ) (min. 2% of parking - DM 2.23) (must meet both)
	2.	Proper width (8' wide min.) and access aisle adjacent? (5' wide min.) ( <i>UFAS 4.6.3</i> ) (DM 2.21)
	3.	Correct slope of accessible parking / access aisle (2%). (No ramp projecting into access aisle or parking space.) ( <i>UFAS 4.6.3</i> )
	4.	Visible designation sign? (not obscured by vehicle due to height of sign post) ( <i>UFAS 4.6.4</i> ) (DM 2.21)
	5.	Shortest distance (closest space to accessible apartment, office, laundry, or site amenity) ( <i>UFAS 4.6.2</i> ) (DM 2.20)
<b>Accessible Route:</b>		
	1.	Curb cuts with flared sides (1:10 max) from parking to sidewalk, and where accessible route crosses pavement ( <i>UFAS 4.7.1 and 4.7.5</i> ) (DM 2.22)
	2.	Sidewalk adjacent to parking provides minimum 36" width accessible route beyond car's overhang ( <i>UFAS 4.3.3</i> )
	3.	Accessible route links all elements on site (min. 36" wide, 8% slope max.): accessible units ( <i>UFAS</i> ), adaptable units ( <i>DM</i> ), common areas, mailboxes, trash areas, common laundry, amenities, etc. (DM 1.6, 2.8, 2.9, 2.16) ( <i>UFAS 4.1.1, 4.3.2, 4.3.3, 4.34.7.1</i> )
	4.	Accessible route includes no changes in level greater than ½" unless beveled or ramped ( <i>UFAS 4.3.8</i> )
	5.	If accessible route slope exceeds 5%, constructed as a ramp ( <i>UFAS 4.8</i> ) (DM 1.7-1.8)
	6.	Ramps provided have max.1:12 (8.3%) slope, min 36" width, and cross slope

		max. 1:50? ( <i>UFAS 4.8.2, 4.8.6</i> ) (DM 1.7, 1.8)
	7.	Ramps with greater than a 6" rise or 72" length, handrails on both sides ( <i>UFAS 4.8.6</i> ) (DM 1.8)
	8.	Ramps with drop-offs have curbs or edge protection min. 2" high ( <i>UFAS 4.8.7</i> )
	9.	Handrails extend 12" beyond both ends of ramp ( <i>UFAS 4.8.5</i> ) (DM 1.8) (May be omitted only if extension would obstruct a path of travel, no matter how designed.)
	10	If stair in circulation path and open underneath, protect stair bottom below 80" headroom with stair protection up to 27" high maximum ( <i>UFAS 4.4.2</i> ) (DM 2.18)
	11	Exterior stairs or interior common use stairs do not have open risers (at least partially closed) ( <i>UFAS 4.9</i> ) (DM 2.17)
<b>COMMON AREAS</b> - (halls, community rooms, laundries, lobby, etc.)		
	1.	Entrance threshold max, 1/2" at entry ( <i>UFAS 4.13.8</i> ) (DM 1.11)
	2.	Doorways 32" min. clear width ( <i>UFAS 4.13.5</i> ) (DM 1.11)
	3.	Lever hardware required ( <i>UFAS 4.13.9</i> ) (DM 1.11)
	4.	Floor covering is stable, firm, slip resistant. Carpeting, if provided, is low pile ( <i>UFAS 4.5.3</i> )
	5.	Switches / outlets / thermostats / controls within reach range? (typically 15" - 48") ( <i>UFAS 4.27</i> ) (DM 5.3-5.9)
	6.	If provided, restrooms fully accessible: 18" clearance on pull side of door; maneuvering room (5' circle or T-shape); correct grab bars; bottom of mirror 40" max. above floor; lavatory 34" max. high, open beneath, lever faucets, & pipes covered. ( <i>UFAS 4.19 &amp; 4.22, fig 28,29 &amp; 30</i> ) (DM 2.28-2.30) (NOTE: maneuvering room not required if restroom is one lavatory and one water closet and provides a 30" x 60" clear space outside swing of door) *(See note)
	7.	If common kitchen provided, accessible route into, sink accessible: 34" or less high, open beneath, lever faucets, & pipes covered ( <i>UFAS 4.1.1, 4.24</i> ) (DM 2.14)
	8.	Laundry - at least one front loading washer and dryer, located in laundry nearest each accessible unit(s) ( <i>UFAS 4.34.7.2</i> )
	9.	Washer / dryer controls within reach and 30' x 48" clear space at door / washer / dryer / sink ( <i>UFAS 4.2, 4.13, 4.24</i> ) (DM 2.26 - 2.27)
	10.	Playground - if provided, must be on an accessible route (accessible play equipment not required) ( <i>UFAS 4.1.1</i> ) (DM 2.9)
	11.	Mailboxes - 30" X 48" clear space, some boxes within 9" - 54" reach range ( <i>UFAS 4.1.1, 4.2</i> ) (DM 1.6 and 2.10)
	12.	Dumpster / trash areas – on accessible route, opening within reach range (typically 9" - 54") ( <i>UFAS 4.1.1</i> )
<b>PUBLIC AREAS</b> - (onsite office, community room / etc. if open to more than tenants and guests)		
	1.	Meet all <b>COMMON AREAS</b> requirements (see above)

	2.	Van accessible parking space with proper width (8' wide min. or 11' wide universal space) (ADAAG 4.6.3) (DM 2.6 and 2.8)
	3.	Access aisle adjacent to van space (8' wide for 8' space, 5' wide for 11' universal space) (ADAAG 4.6.6) ( <b>UFAS 4.6.3</b> ) (DM 2.8)
	4.	Visible designation sign and "Van-accessible" sign (not obscured by vehicle) ( <b>UFAS 4.6.4</b> ) (ADAAG 4.6.4) (DM 2.21)
	5.	Correct slope of accessible parking / access aisle (2%). (No ramp projecting into access aisle or parking space.) (ADAAG 4.6.3)
	6.	Van accessible parking located on shortest accessible route (closest space to office or public space) (ADAAG 4.6.2)
<b>ACCESSIBLE UNITS</b> - (5% of total units required if constructed after 6/10/82 per USDA Departmental Regulations at 7 C.F.R. 15b)		
<b>General:</b>	1.	Minimum 5% of total units fully accessible (NOTE: Always round up. A 20 unit project requires 1 fully accessible unit. A 21 unit development requires 2 fully accessible units.) (7 C.F.R. 15b) ( <b>UFAS 4.1.4</b> ) (UFAS 4.1.4(11)).
	2.	Unit mix of accessible units reflects unit mix of all apartments (NOTE: If only one accessible unit provided, it would be the prevalent bedroom mix in the complex, usually a 2-bedroom unit. If a second accessible unit is provided, it would be the next prevalent bedroom size, usually a 1 bedroom unit.) (7 C.F.R. 15b) *(See note)
	3.	Entrance threshold max. 1/2" at entry ( <b>UFAS 4.13.8</b> ) If sliding glass doors provided, threshold beveled to max. 3/4" (UFAS 4.13.8)
	4.	All rooms on a 36" wide accessible route (min. 32" clear at door openings) ( <b>UFAS 4.3.3 and 4.34.2(3)</b> )
	5.	Lever type hardware on entrance door (UFAS 4.13.9)
	6.	Switches / outlets / thermostats / controls in reach range? (typically 15" - 48") ( <b>UFAS 4.27.3</b> )
	7.	Clothes closets - rod within reach (max. 54" height) ( <b>UFAS 4.2.5, 4.25.3</b> )
	8.	Storage (linen, etc.) - some shelving within reach (between 9" and 54" above the floor; for side approach, between 9" and 48" for front approach) ( <b>UFAS 4.2.5, 4.25.3</b> )
	9.	<b>Floor covering is stable, firm, and slip resistant. If carpet provided, low pile</b> ( <b>UFAS 4.5.3</b> )
<b>Kitchen:</b>	1.	Minimum 40" clearance between opposing sides (60" in U-shaped kitchens) ( <b>UFAS 4.34.6.1</b> )
	2.	30" X 48" clear space at appliances ( <b>UFAS 4.34.6.2</b> )
	3.	Work surface - counter 30" wide min., no more than 34" above floor (with clear knee space or removable cabinet) ( <b>UFAS 4.34.6.4</b> )
	4.	Wall cabinet storage above work surface 48" max height for at least one shelf ( <b>UFAS 4.34.6.10</b> )
	5.	Sink space 34" max. above floor (with clear knee space or removable cabinet), 30" wide min. ( <b>UFAS 4.34.6.5</b> )
	6.	Accessible sink controls (lever or push type controls) ( <b>UFAS 4.34.6.5(4)</b> )
	7.	Sink pipes insulated / covered ( <b>UFAS 4.34.6.5(8)</b> )
	8.	Cabinet hardware accessible ( <b>UFAS 4.34.6.10</b> )

	9.	Front mounted range controls (UFAS 4.34.6.6) Oven self cleaning or adjacent to 30" clear open work space. (UFAS 4.34.6.7)
	10.	Separate switch for range hood / light within reach range (UFAS 4.34.6.3, 4.27, 4.1.2(12))
	11.	Refrigerator meets requirements (50% of freezer space in reach range) (UFAS 4.34.6.8)

<b>Bathroom:</b>	1.	30" x 48" clear floor space at door (UFAS 4.34.5.1) *(See note)
	2.	Knee / toe clearance under 34" maximum height lavatory (or removable cabinet) (UFAS 4.34.5. and 4.19.2)
	3.	Lavatory pipes insulated / covered (UFAS 4.34.5.3, 4.19.4)
	4.	Mirror 40" max. off floor (UFAS 4.22.6)
	5.	30" x 48" clear floor space at toilet (UFAS 4.34.5.2(1)) *(See note)
	6.	Grab bars in place and anchored securely (at toilet and tub / shower) (UFAS 4.34.5)
	7.	30" x 48" clear floor space at tub / shower (UFAS 4.34.5.4, 4.34.5.5) *(See note)
	8.	Tub controls located properly (UFAS 4.34.5.4(4))
	9.	Secure tub seat provided? (if not built in as part of unit) (UFAS 4.34.5.4(2))
	10.	Hand held shower nozzle, 60" min. long (UFAS 4.34.5.4(5))

**ADAPTABLE UNITS** - (Remaining ground level in buildings with 4+ units first occupied after 3/13/91)

<b>General:</b>	1.	All ground level units on accessible route, or site / building impractical to achieve that accessibility (DM 1.40-1.55)
	2.	Low (max ¾") threshold at primary entry door, max. 4" step other exterior doors (DM 3.10)
	3.	36' accessible route to all rooms (entry door min. 32" clear opening, passage doors min. 31 5/8" clear opening) (DM 3.3, 3.5, 4.3)
	4.	Switches / outlets / thermostats / controls in reach range? (typically 15" - 48") (DM 5.1-5.9)
<b>Kitchen:</b>	1.	30" X 48" clear floor space at each fixture and appliance (DM 7.2)
	2.	31 5/8" min. clear opening into kitchen (DM 3.3, 3.5, 4.3)
	3.	Min. 40" between facing counters (in "U" kitchen, min. 60" if any fixture at bottom of "U" OR 40" min. if sink has removable front) (DM 7.2, 7.7-7.16)
<b>Bathroom:</b>	1.	Blocking for grab bars in place (DM 6.1-6.16, 7.33)
	2.	31 5/8" min. clear opening door to bath (DM 7.33)
	3.	30" x 48" clear space for wheelchair to enter, close door, and exit, outside of the door swing (DM 7.33)
	4.	30" x 48" clear space for wheelchair at each fixture (DM 7.33)
<b>COMMENTS -</b>		Note if project has water fountains, public telephones, or other site amenities that require accessibility, and if they comply or not. (Per UFAS, or UFAS and DM if built after 3/13/91.)
		Include details, notes, or photographs as appropriate to explain the situation for accessibility shortcomings.

<b>NOTE -</b>	The CNA process indicates work with an existing building. RD recognizes that it may not be possible to make an existing structure as accessible as new construction. Items marked "(See note)" particularly may be difficult or impossible to achieve without great expense. For those items, provide as much accessibility as possible without moving walls or relocating units. Relocating walls in bathrooms may be necessary if it is impossible to provide space for a wheelchair outside the swing of the door, and / or a useable bathroom will not result. Always when working with an existing building, seek accessibility "to the extent possible".
	With multiple accessibility requirements, the more restrictive code or regulation applies.
<b>KEY -</b>	UFAS - <b>Uniform Federal Accessibility Standard</b> (implements Section 504 of the Rehabilitation Act of 1973) (Implementation date for Rural Development was 6/10/82. Projects funded after that date must have accessible common areas and 5% fully accessible units.) See <a href="http://www.wbdg.org/ccb/ASTAND/handi.pdf">http://www.wbdg.org/ccb/ASTAND/handi.pdf</a>
	<b>ADAAG = Americans with Disabilities Act Accessibility Guidelines.</b> (Implementation date 1/26/93. Projects funded after that date, or performing repairs after that date must comply.) See <a href="http://www.access-board.gov/adaag/html/adaag.htm">http://www.access-board.gov/adaag/html/adaag.htm</a>
	<b>DM = HUD's Fair Housing Act Design Manual</b> (implements the Fair Housing Act Accessibility Guidelines) (Implementation date was 3/13/91. Projects funded after that date must provide adaptable ground level units, or all units in elevator buildings, in buildings of four or more units. Common areas must be accessible.) See <a href="http://www.huduser.org/portal/publications/PDF/FAIRHOUSING/fairfull.pdf">http://www.huduser.org/portal/publications/PDF/FAIRHOUSING/fairfull.pdf</a>

# Accessibility Requirements for Rural Development Financed Existing Multi-Family Housing

## Supplemental Questions & Answers for Multi-Family Housing Portfolio Revitalization Demonstration Program (MPR)

As part of its Multi-Family Family Portfolio Revitalization (MPR) demonstration program, Rural Development (RD) is providing additional guidance specifically to assist CNA Providers understand the level of accessibility requirements for properties with RD funding.

The primary source for guidance on accessibility requirements is available from Rural Development's MFH Asset Management handbook, [HB-2-3560](#), Appendix 5 on Civil Rights requirements. See <http://www.rurdev.usda.gov/regs/handbook/hb-2-3560/AM%20Appendix%205.pdf> Pages 9-20 include Frequently Asked Questions and Answers to a range of accessibility issues found in existing MFH properties.

Some additional situations / interpretations that are specifically relevant to the MPR have developed over time, which have not yet been incorporated into Appendix 5. Information about these topics are covered in the questions and answers below along with the FAQs from Appendix 5 which deal with the physical environment.

### 1. How do borrowers meet 7 C.F.R. 15b numerical requirements for fully accessible units?

In MFH projects ready for occupancy after **June 10, 1982**, [7 C.F.R. part 15b](#) standards require:

- At least **5 percent or one unit**, whichever is greater, must be fully accessible. To meet the 5 percent minimum, borrowers must round up to the next whole unit. For example, a 24-unit MFH project must have at least two fully accessible units (8.3 percent) rather than one (4.2 percent).
- Fully accessible units must be comparable in variety to other project units. For example, in a 24-unit project with 12 one-bedroom units and 12 two-bedroom units, one of the fully accessible units should be a one-bedroom unit and the other should be a two-bedroom unit.
- Rents for fully accessible units must be comparable to other same sized project units.
- If a project has more than one site, fully accessible units may not be clustered at one site, unless only one fully accessible unit is required.
- When a project has a wide variety of units (one, two, three or four bedrooms), borrowers are not required to exceed the 5 percent requirement simply to have a fully accessible unit of each type.

### 2. What are the requirements for van accessible parking?

The requirements vary based on when a project became ready for occupancy. The parking lot of all projects with public areas such as an on-site office, ready for occupancy after **January 26, 1993**, must be properly striped for van accessible parking and access aisles. All projects

with public areas ready for occupancy before January 26, 1993, must be striped for van accessible parking and access aisles whenever the parking lot is re-striped. This includes either an 11' wide space and 5' access aisle (preferred), or an 8' wide space and 8' wide access aisle.

3. **If accessible parking is located across the drive from the building it serves, must a crosswalk be painted on the drive?**

No, it's not required. However, having a crosswalk is a good idea since it would indicate a crossing exists, and hopefully would signal a driver to slow down. There is no requirement for a painted crosswalk in the accessibility standards. Further, there is no requirement for the color of paint to be used. White is most commonly used, and sometimes blue or yellow. Curb ramps from the drive to the site are required.

4. **What is the concept of "visitability," what is required, and when does it apply?**

The concept of "visitability" is that **a disabled person should be able to visit every apartment on site**. If that is not possible (due to a lack of elevators), the disabled person would like to visit every ground floor unit. The [Fair Housing Amendments Act \(FHAA\)](#) greatly furthered the concept of visitability by **requiring an accessible entrance to all ground floor units in buildings of 4 or more units, constructed for first occupancy after 3/13/91**. FHAA further requires those units to be "adaptable" to persons with disabilities. This is greatly improving accessibility in MFH throughout the nation, since the FHAA requirements apply to all multi-family housing, whether financed by the federal government or not.

**Buildings constructed prior to 3/13/91 do not have to comply with the requirement for an accessible route to each ground floor unit.** Section 515 and Section 514/516 properties built prior to 3/13/91 must comply with the Section 504 requirement for 5% fully accessible units, but there is no requirement for all ground floor units to be on an accessible route. Borrowers may incorporate the concept of "visitability" if they so choose, but Rural Development cannot require such modifications in properties built before this date.

5. **What does it mean that MFH playgrounds must be accessible?**

As a site amenity, playgrounds or "tot lots" must be accessible. **"Accessible" for a playground means that the playground must be on an accessible route.** A disabled parent or child must be able to get "to" the playground. A concrete or asphalt sidewalk to the playground meeting the requirements of an accessible route is sufficient. It is recommended that there be a turnaround at the end of that route, so a disabled individual does not have to "back out". If the playground has a defined edge (railroad ties, change in surface material, etc.), that is where the accessible route would end. If the playground is merely "in the grass", the accessible route does not have to go to any, or every, piece of equipment. It should end "reasonably close" to the equipment.

**Accessible play equipment is only required for a "public" playground. The playground**

on a MFH site is for “tenants and their guests”. It is a “common” area, not a “public” area.

6. **At existing properties with very hilly sites, does Rural Development expect an accessible route between every building and common facility?**

For properties built after 3/13/91, under the FHAA requirements, an accessible route to common areas and all ground level units in buildings with four or more units was required. (Even under those requirements, a “site impracticality” test was allowed to reduce accessibility throughout the site for hilly sites.) For properties built prior to that date, there is no requirement for an accessible route throughout the site. The requirement is that the office, 5% fully accessible units, and one common area of each type (laundry, trash enclosure, mailbox area, playground, etc.) be on an accessible route. In sites where a pedestrian accessible route cannot be provided, an accessible route using a vehicle is permitted.

For example, if an accessible route cannot be provided from the fully accessible unit(s) to the playground using sidewalks and ramps, an accessible parking space can be provided near the playground with an accessible route from the parking space to the playground. The tenant would then wheel out to their parking space, drive to the playground, and wheel to the playground. Obviously, this is not ideal, but is acceptable in situations where site constraints warrant it.

Bear in mind that there may be situations where “more than one” of a common site amenity must be on an accessible route. For example, if the site has two accessible units at opposite ends of the site, the laundry nearest each accessible unit should be on an accessible route and available for their use. In this situation, more than one accessible laundry room would be required.

7. **Are “open risers” on common area stairs permitted?**

Open risers are not allowed on common area stairs. Stairs are not part of an accessible route. That said, UFAS provides requirements for “accessible stairs” at UFAS 4.9. What/where are “accessible stairs”? **Stairs required to be accessible are any stair that serves more than one unit, or any exterior stair serving a single unit.** The only stairs on a Rural Development financed MFH site that would not be “accessible stairs” would be an interior stair that serves only one unit – where you open the door, do directly up the stairs, and typically end up in the unit’s living room. All exterior stairs and all interior stairs serving more than one unit are common use stairs.

Because of their common use, UFAS has greater accessibility requirements for those stairs. The stairs will be used by tenants and their guests. The tenant, or their guests, could be mobility or visually impaired. If they are, the possibility of a foot going through the open riser of a stair exists.

**Due to that possibility, UFAS requires some form of “blocking” for the open riser. Note that UFAS does not say “closed risers are required”. UFAS 4.9.2 reads “Open risers are not permitted.”** Vertical or horizontal strips (wood or metal), decorative wire mesh, or

other materials may be used. Many owners choose not to fully enclose the risers due to water, rain, light, ventilation, and security issues.

**8. What is Rural Development's expectation regarding existing developments that feature split foyer design, with all units below or above entry grade?**

Where an architect or engineer has determined that it is structurally impractical to make physical changes, a referral agreement to another nearby property with a fully accessible unit is an acceptable solution. However, cost alone should not be viewed as a basis to ignore physical modifications that achieve accessibility at the subject property, particularly if it is undergoing major rehab. For example, a split foyer design with all units below or above entry grade, it may or may not be structurally impractical to provide accessibility, depending on site and building conditions.

**9. What are the requirements for accessibility for a community room kitchen / kitchenette?**

In many situations, the requirements for an accessible dwelling unit kitchen have been applied to a common use kitchen or kitchenette. The Fair Housing Act Accessibility Guidelines and UFAS have similar requirements.

- The community room must be accessible, including an accessible route into the space, accessible doors, switches and outlets at proper height, etc.
- The kitchen area must have an accessible sink per UFAS 4.24. This includes a mounting height no higher than 34", knee clearance underneath, clear floor space at the sink, insulated piping, and an accessible faucet.
- UFAS 4.25 and 4.1.2(11) further requires that a portion of the storage provided (shelves, drawers, and cabinets) have clear floor space and be within the reach range. This requirement is normally met with standard kitchen base cabinets.
- The kitchen must have a 60" turning circle or "T" turn around for maneuverability. Space in the community room or a hallway immediately outside the kitchen may be used to meet this requirement.
- There is no requirement in a common use kitchen for an accessible work surface, range or cooktop with accessible controls, self cleaning wall oven, or an accessible refrigerator (with 50% of freezer space within reach ranges). These requirements appear in UFAS 4.34, and only apply to an accessible dwelling unit.

These requirements for a common use kitchen or kitchenette are minimums. Provision of additional accessibility in a common use kitchen or kitchenette is encouraged, but not required.

**10. For an existing Section 515 property built after 6/10/82 with only townhouse units, what can be done to provide an accessible unit?**

For existing Section 515 units meeting the above criteria, there are three possible actions:

- a) Construct a new fully accessible single story unit (often not financially possible);

- b) Convert an existing townhouse to be accessible “to the extent possible” (the next best solution); or
- c) Develop a “referral agreement” (the choice when neither Action “a” nor Action “b” are feasible).

Consultation with the State Office Program, Technical, and Civil Rights staff will be necessary to determine the best solution, on a case-by-case basis. The financial status of the property will be a major determining factor on what choice is made. If conversion is selected, the best possible solution is usually to add a bedroom and bath on the first floor. In that way, a disabled parent or child could utilize the bedroom and bath, and access the first floor. No access to the second floor would be added. This is not an ideal solution, but for a property that cannot afford to add a new fully accessible unit, it may be an acceptable solution. A “referral agreement” is the last possible choice in all cases of accessibility. It requires finding a similar property (similar bedroom mix, amenities, subsidy, assistance, etc.) within the area with accessible units that will accept applicants from this property. Since the subject property would be without accessible units, a “referral agreement” provides access to the “program” (providing housing) without providing an accessible unit on site.

**11. What are the requirements about the height of wall cabinets in “fully accessible” units?**

In cases of repair / rehabilitation / creation of a fully accessible unit in a Rural Development financed property, confusion exists over the height of wall cabinets. Unfortunately, UFAS is not clear on the requirements for the height of the wall cabinet. In one place, UFAS 4.34.2(8) requires cabinets to be accessible, but requirements are unclear. In UFAS 4.34.6.4 it refers to Figure 50. Figure 50 shows a maximum height to the bottom shelf of the wall cabinet over the work space of 48”.

**In consultation with the Access Board (the writers of UFAS), Rural Development received guidance that the requirement for a lowered wall cabinet was intended only over the work space, not throughout the kitchen.** All wall cabinets may be lowered, to provide an even plane. If no wall cabinets have been lowered in a unit, or if no workspace has been provided, then the wall cabinet over the work space as a minimum must be lowered to comply with Figure 50. Figure 50 shows the UFAS preferable (not required) method of lowering all wall cabinets. Remaining wall cabinets at standard height allows use of a microwave or coffeemaker under the wall cabinet, on the countertop.

**12. Does installation of a wall shelf at 48” in lieu of re-positioning wall cabinets satisfy Rural Development requirements?**

The Access Board has indicated that a shelf between base cabinets provides “equivalent” accessibility when it is not possible to lower wall cabinets. The shelf should not become the standard solution, but can be considered on a case-by-case basis. For example, if funds for rehabilitation are limited, the shelf may be a less expensive solution to removing and relocating the wall cabinet over the work space. If funds are available, the wall cabinets should be relocated. Although deemed “equivalent,” the shelf does not have doors to cover the storage space and should not be used if relocating wall cabinets is possible.

**13. Is a 30" x 34" high workspace required in an accessible dwelling unit kitchen? While UFAS 4.34.6.4 requires this, it is not included in the list in Attachment B or added to the MFH Physical Inspection Form.**

Yes, it's required. The list in Attachment B was not intended to be all inclusive of UFAS standards, but to hit the big issues.

**14. Where are grab bars required?**

Grab bars are required in the 5 percent of units that are “fully accessible.” UFAS 4.34.5 uses the language “If provided, grab bars will ....” Rural Development has taken the position that grab bars will be installed in order to make the “fully accessible” unit ready for a person with disabilities. Grab bars are also provided in those units in which a tenant has requested them as a “reasonable accommodation.” In those ground floor units constructed since 1991, FHA/AG required blocking for “adaptability.” In those units, grab bars may be installed later as a form of “reasonable accommodation” when requested.

**15. An item on the MFH Physical Inspection form refers to a “functional emergency call system.” Are emergency call systems required in all fully accessible units?**

If the fully accessible unit presently has an emergency call system, it should be functional. If no emergency call system is in place, the borrower does not have to provide one at this time.

It may be necessary to add one as a “reasonable accommodation” per a tenant request in future. In such a case, a portable unit may suffice. There has been considerable confusion on this issue, and we realize that this may be a different answer than you have received in the past. HUD’s old Minimum Property Standard (MPS) required an emergency call system in elderly housing. This standard was dropped in the 1980’s, but has led to the confusion.

**16. Is a 5’ turning circle in a dwelling unit bathroom required?**

Some Transition Plans are indicating a need to enlarge the bathroom in an accessible unit to provide a 5' turning circle, which UFAS requires in a common use bathroom. Writers of Transition Plans are incorrectly applying this requirement to a dwelling unit. Rural Development staff should understand that an accessible dwelling unit bathroom must have clear floor space at the tub/shower and commode, but a 5’ turning circle is not required within a dwelling unit bath. Also, UFAS provides an exception in 4.22.3 for public toilets with only one lavatory and commode. In those common use toilets, a 5’ turning circle is not required.

**17. We have an existing MFH property with multiple laundry rooms. Must each laundry room be made accessible?**

Not necessarily.

- For a property constructed for first occupancy after March 13, 1991 and subject to the Fair Housing Amendments Act design requirements, laundries for the covered units must

be on an accessible route, and the space must be accessible. This would apply to all ground floor laundries (or all laundries in a building with an elevator).

- In addition, for properties constructed, or with substantial alterations, after June 10, 1982, UFAS also applies. UFAS 4.1.3(3) states "Common Areas: At least one of each type of common area and amenity in each project shall be accessible and shall be located on an accessible route to any accessible dwelling unit." This sets a minimum of one accessible laundry. If accessible units are located near one another, the nearest laundry must be made accessible. If accessible units are located on opposite ends of the property, it may be necessary to make more than one laundry room accessible, depending on location and site topography. In such a situation, the nearest laundry room to each accessible unit must be made accessible.
- Regardless of when a property was constructed, it is the policy of RHS that, to the extent possible, barriers to common use areas that prevent any mobility impaired person from having full access will be removed. This does not, however, require borrowers to exceed the above standards unless it is necessary to do so in response to a request for a reasonable accommodation from a person with disabilities.

In addition, UFAS 4.34.7.2 states that washing machines and clothes dryers in common use laundry rooms shall be front loading." RHS has taken the position that this requirement is met if at least one washer and one dryer is front loading in every laundry room that is required to be accessible by UFAS. This position is taken, in part, in recognition that there may be some increase in cost to provide front loading washers and dryers.

#### 18. How quickly must owners correct deficiencies in meeting accessibility requirements?

USDA regulations at 7 C.F.R. 15b describe the use of a Self Evaluation and Transition Plan. The information in [HB-2-3560](#), Appendix 5 further defines the process. In essence, a Self Evaluation is conducted to determine what accessibility shortcomings exist on a property. If physical issues arise (beyond their "policies and procedures"), a Transition Plan is required to remedy those issues. Each item must be identified, a corrective action proposed, with a cost associated with it, and a schedule for implementing the correction. Rural Development recognizes that typically a property cannot afford to fix everything at once.

A Transition Plan allows the property up to three years to schedule corrections. That gives the property time to raise money through it's normal operating budget, find an outside source (loan, grant, owner's contribution, transfer, assumption, rehabilitation, MPR process, etc.). If the items can be corrected during the three year timeframe, the process is complete. If the list is extensive, or finances are such that the repairs cannot be completed in three years, the Transition Plan may be amended to continue for an additional three years. The concept is that a Transition Plan will be used to continue the property on schedule providing additional accessibility, until all items are completed. A Transition Plan should never be used to "postpone" or "avoid" accessibility. **As part of the MPR anticipates that accessibility issues should be corrected. Ideally, accessibility issues would be included in the property's rehabilitation.** Remedy the accessibility issues that can be funded during rehabilitation / through the MPR process, and capture the remaining items either in year 1 or

in a Transition Plan, to be continually repaired until complete.

Owners should understand that a Transition Plan is not a one-time process. If one is done and completed, there is no guarantee that a future Transition Plan will not occur. For example, if sidewalks settle over time and provide a greater than ½” level change on an accessible walk, field staff may point that out, and request a new Self Evaluation / Transition Plan to correct the problem. (If sufficient funds in maintenance cannot correct it “now”.) Likewise, trash enclosures may change over time. With a new trash service company, larger dumpsters without side openings may be used. Without a side opening, the dumpster may no longer be within the reach ranges. A change in the trash enclosure area would be required to adapt to the new equipment. So, changes in the site or buildings over time may affect accessibility, and require changes. What is accessible today is not guaranteed to be accessible tomorrow.

**19. In common areas, such as corridors, lounge or dining areas, are “visual” and “audio” alarm systems required in an existing property?**

The correct answer: it depends. If the property does not presently have a smoke or fire alarm system in place, or if the property is not receiving a rehabilitation as part of the servicing tools being used, there is no requirement from RD to add an alarm or revise any existing alarm system. However, if the locality or state law requires that an alarm system be added, the new alarm system must meet the requirements for both “visual” and “audio” signals. (See UFAS 4.28.) If the property is being rehabbed and an alarm system added, the Access Board has advised us that an alarm system that is both “visual” and “audio” must be added to the common areas.

Please note that these comments are directed to alarm systems in common areas. The only dwelling units that would be required to have a “visual” alarm are the fully accessible units.

# Capital Needs Assessment Guidance to the Reviewer

## AGREEMENT TO PROVIDE CAPITAL NEEDS ASSESSMENT

	<b>GENERAL NOTES:</b>
A	Reviews of proposed agreements for Capital Needs Assessments (CNA) should be based on Rural Development and other Rural Development -recognized guidelines.
B	If all review items are answered “NO”, the reviewer should advise the appropriate Rural Development official that the Agreement should be accepted.
C	Any review items answered with a “YES” should be explained in writing to the proposed Provider in sufficient detail for clarity and appropriate actions to be taken.
D	If all review items answered with a “YES” are satisfactorily addressed or corrected by the proposed Provider, the reviewer should advise the appropriate Rural Development official that the Agreement should be accepted.
E	If any review items answered with a “YES” cannot be satisfactorily addressed or corrected by the proposed CNA Provider, the reviewer should advise the appropriate Rural Development official that the Agreement should NOT be accepted.

	<b>REVIEW ITEMS:</b>	<b>YES</b>	<b>NO</b>
1	Does the proposed Agreement omit Rural Development’s Addendum to CNA Contract?		
2	Does the proposed Agreement omit Rural Development’s CNA Statement of Work?		
3	Is there any evidence or indication that the proposed CNA Provider has an identity of interest, as defined in 7 C.F.R. part 3560?		
4	Is there any evidence or indication that the proposed CNA Provider is NOT trained in evaluating site and building systems, and health, safety, physical, structural, environmental and accessibility conditions?		
5	Is there any evidence or indication that the proposed CNA Provider is NOT trained in estimating costs for repairing, replacing, and improving site and building components?		
6	Is there any evidence or indication that the proposed CNA Provider is NOT experienced in providing CNAs for MFH properties that are similar to those in the Section 515 Program?		
7	Is there any evidence or indication that the proposed CNA Provider is NOT knowledgeable of site, building and accessibility codes and standards?		
8	Is there any evidence or indication that the proposed CNA Provider is debarred or suspended from participating in Federally-assisted programs?		
9	Does the proposed fee appear to be unreasonable?		

**CAPITAL NEEDS ASSESSMENT REPORT**

	<b>GENERAL NOTES:</b>
A	Reviews of preliminary Capital Needs Assessment (CNA) reports should be based on: <ol style="list-style-type: none"> <li>1. The Statement of Work referenced in the written agreement with the provider</li> <li>2. Rural Development case file, such as property records and inspection reports</li> <li>3. Latest available cost data published by RS Means</li> <li>4. Rural Development guidelines</li> <li>5. Fannie Mae guidelines</li> </ol>
B	The reviewer should give special attention to the line items with the highest total costs.
C	The reviewer should be careful to note whether all systems or components that should be included have indeed been included in the report.
D	If all review items are answered “YES”, the Provider should be advised to finalize the CNA with no or only a few minor changes.
E	Any review items answered with a “NO” should be explained in writing to the Provider in sufficient detail for clarity and appropriate actions taken.
F	The final report should be reviewed to verify that any minor changes and items answered with a “NO” in the first review have been satisfactorily addressed or corrected.
G	When item “D” is completed, the CNA Reviewer should advise the appropriate Rural Development official that the CNA should be accepted as the final report.

	<b>REVIEW ITEMS:</b>	<b>PRIMARY BASIS *</b>	<b>YES</b>	<b>NO</b>
1	Is the report in the required format?	1		
2	Does the report fully describe the property?	1		
3	Are photographs provided to generally describe the property’s buildings and other facilities?	1		
4	Does the report identify who performed the on-site inspection?	1		
5	Does the report identify who prepared the report?	1		
6	Was an adequate number of dwelling units inspected?	1		
7	Is the length of the study period adequate?	1		
8	Is the list of property components complete?	5		
9	Is the list divided into the appropriate major system groups?	1		
10	Are the existing property components accurately described?	2		
11	Are the expected useful lifetimes of the components reasonably accurate?	5		
12	Are the reported ages of the components reasonably accurate?	2		
13	Is the current condition of each component accurately noted?	2		
14	Are the effective remaining lifetimes of components correctly calculated?	5		
15	Are proposed corrective actions appropriately identified?	1		
16	Are critical immediate repairs appropriately identified?	1		
17	Are items being replaced with “in-kind” materials when appropriate?	1		

18	Are the component quantities reasonably accurate?	2		
19	Are photographs provided to describe deficiencies?	1		
	<b>REVIEW ITEMS:</b>	<b>PRIMARY BASIS *</b>	<b>YES</b>	<b>NO</b>
20	Does the report adequately address environmental hazards and other relevant environmental issues?	1		
21	Does the report adequately address accessibility issues?	1		
22	Does the report address any existing accessibility transition plans and their adequacy?	1		
23	Are photographs provided to describe existing kitchens and bathrooms in the fully accessible units?	1		
24	Are the proposed years for repair or replacement reasonable?	5		
25	Are the repair/replacement durations appropriate and reasonable?	5		
26	Are the detailed estimated repair and replacement costs calculated in current dollars?	1		
27	Are the estimated repair and replacement costs reasonable?	3		
28	Are the sources for cost data explained in the report?	1		
29	Is the projected inflation rate appropriate?	1		
30	Have the costs in current and inflated dollars been totaled for each year?	1		
31	Have the costs for each year and grand totals been correctly calculated?	5		
32	Does the data in the report narrative and summary charts match?	5		
33	Does the report exclude routine maintenance, operation, and low cost expenses?	4		
34	Does the report include all deficiencies known to Rural Development?	2		
35	Does the report include all other relevant data or information known to Rural Development?	2		

\* see General Note "A"

COMMENTS:

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# Sample Capital Needs Assessment Review Report

## SAMPLE CAPITAL NEEDS ASSESSMENT REVIEW REPORT

### [REVIEW OF PRELIMINARY / FINAL CNA REPORT]

**Property Name and Location:**

**CNA Provider:**

**CNA Reviewer:**

**Date of Preliminary / Final CNA Report:**

**Date of Review:**

**Reviewer's Comments:**

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**Purpose / Intended Use / Intended User of Review:**

- The purpose of this CNA review assignment is to render an opinion as to the completeness, adequacy, relevance, appropriateness, and reasonableness of the work under review relative to the requirements of Rural Development.
- The intended use of the review report is to help meet Rural Development loan underwriting requirements for permanent financing under the Section 515 Revitalization demonstration program. The review is not intended for any other use.
- The intended user of the review is only Rural Development.

**Scope of Review:**

**The scope of the CNA review process involved the following procedures:**

- The review included a reading/analysis of the following components from the CNA report and the additional due diligence noted. The contents from the CNA work file were not reviewed. The components that were reviewed are:
  - Date of the Report
  - Narrative
  - Description of Improvements
  - Photographs of the Subject Property
  - Capital Needs Summary
  - Systems and Conditions Forms
  - Critical Needs Forms
  - Capital Needs Over the Term Forms
- This is a desk review, and the reviewer has not inspected the subject property.

- The reviewer has/has not confirmed data contained within the CNA report.

**Review Conclusion:**

**In the reviewer's opinion, given the scope of the work under review:**

- The subject CNA *meets / does not meet* the reporting requirements of Rural Development.
- The data *appears / does not appear* to be adequate and relevant.
- The CNA methods and techniques used *are / are not* appropriate.
- The analyses, opinions, and conclusions *are / are not* appropriate and reasonable.
- This is a review report on a *preliminary / final* CNA report. The *preliminary / final* CNA report is subject to review discussions between Rural Development and the owner of the subject property and between the owner and the CNA provider. The owner is the CNA provider's client, and only the client can instruct the CNA provider to revise the *preliminary / final* report. To be acceptable to Rural Development, the final CNA report should address any errors or deficiencies identified in the *Reviewer's Comments* section of this review report.

Signed by:

\_\_\_\_\_  
(CNA Reviewer)

\_\_\_\_\_  
(Underwriter / Loan Official)

*(Please note: For the CNA Review Report of the preliminary CNA, only the CNA Reviewer needs to sign the report on behalf of Rural Development. For the CNA Review Report of the final CNA, the CNA Reviewer and the Underwriter / Loan Official shall sign the report. This is to encourage discussion between the Agencies parties, so that both the CNA Reviewer and the Underwriter are involved in the process of accepting the final CNA for the property.)*

## Guidance on the Rehabilitation of MFH Properties

- 1) References to Rehabilitation in 7 CFR Part 3560 and the Handbooks
- 2) Background Considerations
- 3) Repair or Rehabilitation
- 4) Architectural Services
- 5) Financial Considerations
- 6) Construction Funding
- 7) Protecting the Government's Interest
- 8) Construction Administration.

Use of referenced RD Forms are required when new or subsequent direct RD funding is involved. When no new RD financing is applied and depending on the magnitude of the project, the use of American Institute of Architects forms or other industry accepted forms are appropriate. Two attachments are included.

### 1) **References to Rehabilitation in 7 CFR 3560 and the MFH Handbooks**

Subattachment A-1, *References to Rehabilitation in 7 CFR 3560 and MFH Handbooks*, consists of a comprehensive list of references to the term rehabilitation in 7 CFR 3560, HB-1-3560, HB-2-3560 and HB-3-3560. These references include information on rehabilitation in order to revitalize a property.

Please note that many of the requirements of new construction from RD Instruction 1924-A and 7 CFR 1924 apply to rehabilitation. Further guidance on what portions of RD Instruction 1924-A and 7 CFR 1924 apply is given in this Unnumbered Letter and Subattachment B-1 "*Repair vs. Rehabilitation Reference Guide*".

### 2) **Background Considerations**

Consider the financial and physical condition of the property in determining whether a project needs repairs and maintenance or requires rehabilitation. Also consider how best to manage the funds for the rehabilitation or repair. A property that has been well maintained may only need to capitalize or put money into the reserve account now for repair or

replacements that will be completed over the 20 year repair and replacement schedule. This schedule is an estimated plan for the way in which repairs and replacement work may occur and the amount of funds that should be set aside, each year, over the term, to address those physical facility needs. On the other hand, a property where there has been a lack of funds necessary to address physical issues may need to be rehabilitated and may also include the transfer to a new owner.

Rehabilitation typically occurs in one of two ways: 1) the owner (or purchaser) proposes rehabilitation or, 2) the Agency's Capital Needs Assessment (CNA) Reviewer and Underwriter) jointly agree that rehabilitation is appropriate for the property. In both situations, the owner contracts for an "As-is" CNA based on existing conditions at the property and should follow the guidance concerning CNAs from the above attachments (primarily B and C).

**A. Property Owner/ Purchaser Proposes Rehabilitation.** When the property owner (or purchaser / transfer owner) proposes rehabilitation and has funds committed by RD or a third party source, the owner contracts for an "As-is" CNA and follows the guidance the appropriate CNA attachments above. Then the owner and Rural Development jointly develop a rehabilitation repair list (also called Scope of Work) for the planned rehabilitation. The Scope of Work is a separate document and developed outside the CNA. The owner should get estimates for the cost of rehabilitation from other sources including an architect, cost estimator, or actual bids. The owner should provide a copy of the Scope of Work approved by RD to the CNA Provider who will then prepare a "post rehabilitation" or "Post-Rehab" CNA as if the rehabilitation had been completed. This "post rehabilitation" or "Post-Rehab" CNA will be used to evaluate the project's Reserve Account to assure the physical needs of the property can be met over the term of the CNA.

If the project has requested funds for rehabilitation, but they have not been committed, an "As-is" CNA is still performed. If funds are not available for rehabilitation, the CNA performed would be an "As-is" CNA, reflecting the anticipated repair and replacement schedule for the property over the next 20 years. A "Post-Rehab" CNA would not be performed until funds are available and committed since this is an additional cost to the owner and the Agency.

**B. Rehabilitation Recommended by CNA Reviewer/ Underwriter.** The CNA Reviewer and Underwriter jointly may recommend rehabilitation. This decision could be made during review of the CNA itself, or more likely, during underwriting of the financial assistance after the CNA has been reviewed and accepted by Rural Development.

The CNA Reviewer may know the property or be concerned over the quantity of repairs shown as necessary in the first few years. In discussions between the Underwriter and CNA Reviewer there may be agreement that the better financial solution for the property would be to pull the items in those first few years (years 1-3, or whatever time period makes the most sense) into a rehabilitation to be performed "now" (in the first year). If the Agency and owner both concur, the CNA Reviewer makes those comments in the

draft or final review of the “As-is” CNA Report to the CNA Provider. The CNA Provider then prepares both the “As-is” CNA and the “Post-Rehab” CNA. The items included in the rehabilitation are pulled from the years they were planned in the CNA and a “Post-Rehab” CNA is created. In such a situation, the “Post-Rehab” CNA may show “zeros” for repairs for the property in those first few years. However, the individual line items should still be shown in the CNA and not removed if they will require repair or replacement during the 20 years of the CNA. A subsequent CNA will be required to address those elements that fall outside of the 20 year schedule. The “Post-Rehab” CNA must be as accurate as possible by reflecting the anticipated as-built conditions of the rehab project.

The CNA Provider may be due an additional fee to revise his contract to create both an “As-is” and a “Post-Rehab” CNA.

If the decision to rehabilitate is determined later in the process by the Agency and the Agency has approved the CNA, **Agency staff** will need to revise the CNA, as described later under “Financial Considerations”. After the either CNA has been approved, the Agency should not and cannot go back and require the CNA Provider to revise the report. It is the responsibility of the Agency to revise the CNA to reflect the Agency’s decision to require a rehabilitation of the property.

The Agency decision on whether to pull items forward and require rehabilitation for a property should be a joint decision between the CNA Reviewer (who has the expertise on the CNA process), the Loan Underwriter and the Owner. In doing so, consultation with the applicable field office, the MFH Coordinator / Program Director and the Team Leader is appropriate. The CNA Provider may be consulted as well.

### 3) **Repair or Rehabilitation**

**For a Multi-Family Preservation and Revitalization (MPR) or Credit Sales transaction, if the combined repair and replacement costs for year 1 and 2 of the property totals, or per unit costs are relatively high, you may consider a “rehabilitation” project; For example, an eight unit property with repairs totaling over \$100,000 “rehabilitation” may be considered. For a property with more units, a higher figure would be the threshold to perform a rehabilitation. The determination would be among the interested parties.**

The Underwriter should first look at the amount of repairs needed in the first year of the CNA. The immediate needs under “Health & Safety” may be added to year one of the CNA if those issues have not yet been resolved. If, for example, a 24 unit property lists \$360,000 in repairs in year one, a rehabilitation should definitely be considered. If the 24 unit property lists \$260,000 in repairs in year one and \$90,000 in repairs in year 2, the interested parties need to evaluate whether it is in the best interests of the tenants, the property and the Agency to combine years one and two for a rehabilitation of the property. As noted in the previous section, this should be a joint decision made by Agency staff, including field, State, and the National Office Team Leader.

If high repair and replacement costs are encountered, it does not necessarily mean that rehabilitation must be done. For example, roof replacement could be a large cost in a large property, but could be done as repair / replacement. **It is important to first determine if the cost is a factor in the consideration. Then, determine if the repair item(s) warrants rehabilitation.**

The rehabilitation consideration on each project can be affected by the funding source (i.e., LIHTC or GRRH thresholds) and the jurisdiction of the project. Staff should consider all factors and conditions as to whether rehabilitation is appropriate.

In a repair and replacement scenario, the Agency will typically have only one CNA: the “As-is” CNA for the property. With committed rehabilitation funds, or the Agency determines that a rehabilitation is necessary, **the Agency will have two CNA’s: the “As-is” CNA, which is the CNA Provider’s report of existing, “point in time”, conditions at the property and the “Post-Rehab”, which is a Provider’s report based on the document scope, plans and specs of the rehab, that accounts for the property conditions after the rehabilitation is complete.** (Also see Definitions page V)

#### 4) Architectural Services

Questions will arise as to when it is appropriate to seek a project architect’s services to design and oversee the rehabilitation. Generally speaking, if the definition or monetary threshold of “rehabilitation” described above is met; architectural services should be obtained.

There are a number of factors that enter into the decision to use architectural services and it will need to be made on a case-by-case basis, with guidance from the State Office and the Team Leader. Factors to consider in making the decision to use architectural services include:

- Cost / quantity of the work: Evaluate the scope of the rehabilitation. If the cost of the work exceeds \$500,000 and administration of the construction will require numerous visits to perform inspections, review pay estimates, check and approve change orders and to provide contract administration, it is appropriate to have a professional architect to perform these duties.
- Type/ complexity of repairs needed: Consider whether the repair(s) require multiple building trades. Repairs may be costly, but if the scope is to replace roofing for every building in a 100 unit development, while costly, may not be complex and therefore an architect may not be needed. On the other hand, solving a site drainage and moisture problem property may not be as costly, but would demand professional expertise. Both an architect and an engineer might be involved in that case.
- Structural changes: Whenever structural changes are needed as part of the rehabilitation, an architect should be consulted for the structural issues as a minimum. Typically, this would indicate a need for architectural services throughout.

- Additional structures or facilities: In some cases, there may be a need to add an accessible unit, an office, or site amenities such as a laundry or community room to a property. If new construction is required, architectural services should be sought.
- Accessibility issues: If a property requires a number of accessibility corrections, a project architect may prove invaluable in determining the best, most cost effective way to achieve the needed results.
- State law: In some states, an architect may be required by state law for rehabilitation work of a certain dollar amount or scope.
- Local or state building departments: Some local building departments perform a plan review and perform building code inspections at set times during the workday, using trained, qualified personnel. Others merely take a check and issue a building permit. Other areas may have no “building department” at all. The level of involvement and competency of local building department staff overseeing the project can be a factor in deciding to use architectural services. In some states, the state government may have a state fire marshal plan review and inspections while others do not. State Fire Marshal oversight may also be a factor in deciding to use architectural services. For many states, rehabilitation work has no required permitting or inspection process. It is important to determine what resources are locally available and to what extent they will need to be involved in the project rehabilitation.
- State Office staffing: In states without a State Architect, a project architect may provide additional assurance and risk reduction, confirming that all of the items requiring rehabilitation have been addressed. This could be a determining factor. However, having a State Architect on staff does not mean that the need for a project architect is eliminated.
- Field expertise & staffing: If the field staff overseeing a rehabilitation project have years of experience in MFH and in construction, the need for outside architectural oversight may be reduced. In other cases, a project architect provides good assurance that building codes will be met.

The determination of whether to require architectural services for rehabilitation needs to be made by the MFH Program Staff in the State Office along with the Team Leader, considering the factors described above.

The cost for architectural services in new construction typically runs approximately 5-7% of the total construction costs in our program. Architectural services typically run approximately 50% higher for rehabilitation work. An architect’s fee range of 7-12% of the construction costs for rehabilitation may be appropriate. Architectural services are described in 7 CFR section 1924.13(a)(5).

**The Agency will provide oversight during the rehabilitation for the benefit of the Agency regardless of the source of any other required inspections, supervision or oversight. Additional project monitoring shall be provided as necessary through an accepted independent third party entity. The monitoring responsibilities may include construction inspections, cost and schedule monitoring and pay application reviews. These services can be performed by the project architect or other professional with appropriate qualifications similar to the experiences of a construction manager. The**

**Agency and owner should agree on the need and role regarding the administration of the construction phase.**

**5) Financial Considerations**

For simple repairs, (transactions that fall short of the above-mentioned rehabilitation threshold) the Underwriter will establish funding so that all financial tools available under the MFH program are disbursed through the Reserve Account. States are to follow the established procedures set out in Handbook HB-2-3560, Chapter 4, Paragraph 4.17 for withdrawing funds from the Reserve Account. Either obligation of loan funds using the multiple advance method or disbursement of funds in a single advance are typical options. For guidance on properly setting up multiple advance loans in AMAS (or current system) refer to the AMAS Manual, Chapter 2.

**A) Separate Construction Accounts for Rehabilitation Work.** For rehabilitation work, (transactions that exceed the thresholds described earlier) the rehabilitation funds will be deposited into a separate construction account. This is to avoid co-mingling rehabilitation funds with reserve account funds. Disbursement of these funds shall be closely monitored and require Agency concurrence in order to assure the funds are used appropriately, especially when Agency funds are involved, Rehabilitation funds may be disbursed either as multiple advances or through a construction lender (using interim financing). If using multiple advances, the Underwriter will disburse all loan funds through a supervised bank account set up following 7 CFR 1902. The Agency and property owner will follow the requirements in RD Instruction 1924-A and 7 CFR 1924 for obtaining bids, providing plans & specifications, contract documents, surety, payments, change orders and inspections. *In short, handle these transactions the same way a Section 515 repair loan would be handled.*

**B) Hard Costs v. Soft Costs.** The Underwriter should review the costs and finances to make sure that all applicable “soft costs” typically associated with construction and rehabilitation have been adequately addressed in the financial analysis. (“Hard costs” are the bricks and mortar - tangible elements of construction. “Soft costs” is the common nomenclature used for those items that are not “hard costs” – not easily seen on site.) The term “soft costs” normally include such items as:

Architect’s fees	Engineer’s fees
Environmental fees	Legal fees
Closing costs	General Requirements (incl surety)
Overhead	Profit
Interest during Construction	Contingency
Tenant Relocation expenses	Cost Certification
Other Fees	

**C) CNA Falls Short of Bid.** CNA repair and replacement (r & r) estimates sometimes fall short of a bid from a contractor to rehabilitate the property. One reason is that

CNA Providers include a “probable cost” for r & r, which differs from a cost estimate or proposal for rehabilitation. CNA Providers use industry standard cost data bases for the repair item costs. Those data bases normally include costs for labor, materials, overhead and profit. These are the normal costs a vendor would have in replacing **an item** at the property. With rehabilitation, on the other hand, there are typically more soft costs than just the overhead and profit. A rehabilitation project usually involves multiple construction activities performed by several contractors or subcontractors resulting in a cost proposal that includes acceptable management, coordination/scheduling and other related “soft costs” necessary to complete the project successfully. The line item costs in a CNA do not include soft costs. Other examples of soft costs would include surety, interest during construction (if any), a construction trailer, etc. Additionally, costs to relocate tenants can be considerable and are part of the development costs but should not be included in the CNA line items.

Other reasons for a CNA estimate to fall short of an actual bid could be the age of the CNA (needs adjusting for inflation), or a decision to replace items with a higher quality item rather than an “in-kind” material (wood flooring rather than carpet, for example). Generally the items will be replaced with “in-kind” materials. There may be situations where replacement of an item with a higher quality material makes sense, i.e. if it has a longer Estimated Useful Life (EUL), less maintenance, less energy usage, etc. If using higher quality materials, the costs for the higher quality should be correctly reflected in the rehabilitation costs as specified in the Statement of Work.

CNA Providers may use RS Means, or similar data, to enter their line items. RS Means is a database tool that provides cost information to the construction industry so contractors can provide accurate estimates and projections for their project costs. If used, the RS Means cost database includes materials, labor, overhead and profit. RS Means costs typically don’t include those other “soft costs” listed earlier. When adjusting the financials for the underwriting and to ensure that all the “soft costs” are accounted for, the Agency should not “double count” by adding in for overhead and profit a second time. If the CNA Provider used some other cost database than RS Means, contact them to determine if the cost numbers they provided included material, labor, overhead and profit, or just materials and labor. The CNA Provider should note the source of their cost information in the “Narrative” section of the CNA.

**Profit.** Profit or contractor charges (fees) are normally calculated on the totals of the “hard” costs only of a construction project. For new construction, 10% profit is an industry average. For rehabilitation, 10-15% is also an industry average for profit, depending on the size and scope of the rehabilitation. These averages are established from decades of contract performances and may fluctuate based on economic factors or other market conditions. Larger rehabilitations will be closer to 10% profit. Smaller rehabilitations, with budgets closer to the \$350,000 definition of rehabilitation, will be closer to 15% profit. To get a rough estimate for the costs of rehabilitation, input a profit percentage, based on the size and scope of the project to the line

items in the CNA. However, Owners sometimes provide written cost estimates for the rehabilitation. In this case, the profit would be listed separately in the cost estimate and those numbers can be transferred directly to the CNA. (*Reference Sources & Uses on the Underwriting Template*). When the rehabilitation, construction work is performed by the property owner, RD should consider and evaluate the level of profit requested by the owner and determine if the request is appropriate for the project. In the owner/builder scenario there is added risk to the Agency.

**D) Overhead & General Requirements.** Per the Forms Manual Insert (FMI) for Form RD 1924-13, “Estimate and Certificate of Actual Cost” under “Overhead” includes items that are part of “doing business. Overhead is defined at 7 CFR 3560.11 and includes costs such as tools, equipment, workman’s compensation, unemployment tax, social security, medicare, management and secretarial salaries, profit sharing, pensions, office insurance / rentals / utilities / equipment, liability insurance, legal costs, automobile / truck expenses and depreciation.

“General Requirements” are those items that are required for a specific project, not just “doing business” and is also defined at 7 CFR 3560.11. These costs would include field supervision / superintendent, field office / phones, shed / storage / toilets, performance and payment bonds (surety), building permits, site security, temporary utilities, property insurance on the project, and trash removal.

Without historical data, establishing a cost figure for “Overhead” and “General Requirements” for rehabilitation work is difficult. “Overhead” for a rehabilitation business is similar to a company performing new construction. When determining overhead for rehabilitation, it is prudent to use the same estimate of 4% overhead as in new construction (this should have already been included in the cost base for the CNA line items). “General Requirements” will be a range of 7-9%, based on the size of the rehabilitation. Again, a large rehabilitation job would be closer to 7%, whereas a smaller job, nearer the \$350,000, would be closer to 9%. An adequate cost estimate from the owner should include amounts for overhead and general requirements. In order to be acceptable to the Agency for underwriting purposes, the Scope of Work cost estimate for the rehabilitation provided by the owner must be complete and thorough. If Agency financing is involved, Form RD 1924-13 is the preferred format. The owner may obtain those estimates through an architect, cost estimator, or through bidding to contractors.

**E) Contingencies and Cost Over-runs.** Estimating contingency funds, (“Contingencies”) set aside for unanticipated required changes in rehabilitation work is also challenging. For new construction, contingencies of 5-10% of the construction cost are common in commercial work. For rehabilitation, there are more unknown conditions that can contribute to necessary changes in the work. In estimating “Contingencies” for rehabilitation, use a range of 10-15% of the construction cost. The lower number would be used for cases where the work is fairly well defined and less complex in nature. For a project with less well defined work (for example, addressing a myriad of accessibility issues on a site, or a property with moisture

problems), a higher contingency is appropriate. **If contingency funds remain at the end of the rehabilitation, additional work that would be an eligible loan expense in the program may be added as a change order, or the remaining funds may be deposited into the reserve account.**

Rehabilitation funds will be separated out from the loan funds that will be used to capitalize the Reserve Account, which is specifically for use in maintaining the property over the remaining years of the CNA. Part of the loan application process requires a signed statement from all applicants agreeing to pay for cost overruns from non-project sources. **It is not the intent to have cost overruns funded from reserve funds as this could cause shortages in the Reserve Account resulting in unmet needs during the 20 year CNA period.**

#### **F) Repair v. Rehabilitation cost estimating**

**Soft Costs for Rehabilitation.** For rehabilitation, the CNA should be used to estimate the cost of repairs needed for the property over the coming 20 years. If a Scope of Work and a “Post-Rehab” CNA are provided, the Underwriter needs to review the Scope of Work and estimates, with the CNA Reviewer, for the rehabilitation to verify that all the appropriate “direct and soft costs” for that project have been reflected in the estimated cost of the rehabilitation work. The repair costs for the CNA should have been taken from a valid data source and should not need review at Underwriting since they were reviewed earlier by the CNA Reviewer. If all “soft costs” are not accounted for, the Underwriter needs to work with the Owner to estimate those costs and include them. Once the estimated cost for the rehabilitation has been determined, the Underwriter can then determine the financial needs for the Reserve Account, based on the 20 year repair costs from the “post-rehab” CNA.

**Agency determined rehabilitation/ Agency revising CNA.** If the CNA completed for the property was an “As-is” CNA and the CNA has already been accepted by the Agency and the Underwriter, in consultation with the CNA Reviewer and Owner, and it is determined that rehabilitation is in order, the Agency will be responsible for revising the CNA. The Underwriter or CNA Reviewer will take the existing “As-is” CNA and remove repair items and costs that will be part of the rehabilitation from the CNA template. The items may be located in different years of the CNA projections. These items will be used to create a Scope of Work and estimates for the rehabilitation. A portion of this Scope of Work would be the list of repair items taken out of the CNA. The owner will be responsible to obtain estimates that cover the costs of implementing and resolving the CNA concerns within a rehabilitation effort. As noted earlier, the owner may utilize an architect, a cost estimator, or constructor bids to obtain costs for the rehabilitation. Depending on the complexity of the project, the estimate of costs would be from a professionally developed scope of work that includes and considers the work, the process and the associated direct and indirect requirements of a construction project

**Cost Estimates.** As described earlier, the cost estimate for rehabilitation work from a contractor normally includes materials, labor, general requirements, overhead and profit. Costs such as architectural services, engineering services, tenant relocation, legal fees, closing costs, interest during construction, cost certification, or contingencies would not normally be included. These are the kinds of “soft costs” that the Underwriter needs to ensure are included in the total rehabilitation funding. The CNA Reviewer or State Architect may be able to assist in estimating some of these costs.

Cost certification may be required. If the contractor has an identity of interest with any of the suppliers, the owner, or the management company, a cost certification conforming to the requirements of RD Instruction 1924-A and 7 CFR part 3560.72(b) will be required and must be included in the estimate of “soft costs”.

The Underwriter will show the “rehabilitation” on the Underwriting Template on the Transaction Variables Page under Sources and Uses along with the appropriate additional “soft costs” for the rehabilitation of that property. With Agency proposed rehabilitation, the Underwriter or CNA Reviewer should verify that 1) the rehabilitation items were “zeroed out” on the Rural Development Post Rehab CNA Template to be used for future repairs and reserve account funding and 2) repaired items completed earlier than originally scheduled in the rehabilitation are listed again in the Post Rehab CNA schedule for future replacement as appropriate based on their EUL. Base the new annual required Reserve Deposit funding on the revised, “Post Rehab/Underwriter Revised CNA” schedule.

**As-is vs. Post-Rehab and Underwriter Revised CNAs.** It is important to remember that the CNA Provider’s original “As-is” or “Post Rehab” CNA is not wrong if it needs to be revised. CNAs can only be revised by the RD Underwriter. Updates or corrections to a CNA should be performed by the CNA Provider. However, in reviewing the financial status of the property, the Underwriter may make a recommendation that it is in the best interest of the tenants, the property and the government to rehabilitate the property at this time. The Agency (Underwriter, CNA Reviewer, Program Director, Team Leader and possibly National Office staff) consider the recommendation and will make the decision whether to rehabilitate now or in the future depending on funding. If the rehabilitation occurs now, the CNA needs to be revised as the CNA Reviewer “accepted” the original CNA. It was correct, as it provided a true reflection of the property’s condition. The CNA Provider is not obligated to “correct” or “change” the CNA once it has been accepted by the Agency. The Agency will have two CNA’s on this property:

- the *accepted As-is CNA* that the Agency (and Owner) agreed to and
- the “Post-Rehab / Underwriter Revised(UR)”, **UR-CNA** used for underwriting purposes.

The original CNA shows the determination of an independent provider as to what repairs will be needed. The second CNA gives the replacement schedule anticipated for the future 20 years of the project. Therefore, the Agency needs to maintain a copy of both CNAs in the case file to adequately document the transaction. *Again, the CNA Reviewer and/or Underwriter need to verify that the repair items completed earlier than originally*

scheduled *are listed in the CNA for replacement, as appropriate.* **The CNA Reviewer and Underwriter should work together in developing this “revised” UR-CNA.**

There are cases where:

1. Rehabilitation has been determined to be the preferred course of action (rather than a repair) prior to the CNA contract or completion of the CNA. In this case the CNA Provider gives the Agency both an “As-is” and an “Post-Rehab” CNA; or
2. Rehabilitation has been determined necessary during underwriting by the Agency, in which case the Agency develops an Post Rehab-CNA and retains the original “as-is” CNA from the CNA provider.
3. The CNA has been finalized and approved by the CNA Reviewer, Underwriter, Provider and Owner, but the funding in the Reserve Account will not support line items necessary for replacement over the 20 year term, The Underwriter should discuss the situation with the Team Leader. There are two choices:
  - a. Develop a Post Rehab-CNA, derived from the existing CNA. This is necessary in order to preserve the data contained in the original CNA, allowing the Agency to maintain a “baseline” for the condition of the property. Upload the data from the original CNA into the Underwriting Template and use it to redistribute replacement of line items throughout the 20 year period. This will allow the CNA Reviewer and Underwriter, working together, to insure that sufficient funds are in the reserve account for replacement line items at any given time during the replacement period. Once the CNA Reviewer and Underwriter are able to come to an agreement as to what is the best replacement schedule for the long term viability of the project, the UR-CNA will then be generated from the data in the Underwriting Template. This UR-CNA should be acceptable to the Agency and owner to be used as the working CNA throughout the repair and replacement schedule and Agency’s use in servicing the property. In this way, the Agency has developed a replacement period schedule that will work based on the funds available.
  - b. Discuss what other options are available with the Team Leader. It may be that the poor condition of the property and the available financial assistance cannot overcome the present problems.

**Retain all “As-is” and “Post Rehab” CNAs.** Whenever a UR-CNA is provided, the original CNA and UR-CNA must both be retained in the Agency file for the property and distributed to the Owner. The final repair and replacement CNA must be on file with the property management on-site as well. A developed UR-CNA is an Agency solution for a CNA submitted by a CNA Provider which did not reflect the availability of funds in Reserve. If the reserve funds necessary to repair line items at any given time throughout the estimated replacement schedule

are insufficient, a UR-CNA is developed. The UR-CNA is not developed by the CNA Provider, but by the Agency designated CNA Reviewer, Underwriter and Owner or other Agency representatives who may provide assistance in the development process.

## 6) Construction Financing

There are three methods for handling construction financing for rehabilitation:

- A) The Agency prefers interim construction financing. The Owner finds a lender willing to finance the cost of the rehabilitation. Once rehabilitation is completed, the Agency will expend funds from the financing tools or other Agency servicing action to pay off the construction loan. During the rehabilitation, payments to the contractor are made from the lender's construction loan. The money paid out accrues interest during the period of the work. At the end of the job, the permanent financing (3<sup>rd</sup> party, MPR tools, Section 538 guaranteed loans, or Agency financing) is dispersed to pay off the loan, interest that accrued during the construction and any closing costs. This is the preferred method because the Agency makes one final payment and the interim lender assumes all risk associated with the rehabilitation work. The Agency still needs to perform progress inspections of the work per 7 CFR 1924.6 and should receive copies of the pay requests upon verification that the work is progressing normally and that the payments to the contractor are limited to the percentage of work completed to protect the government's security interest. (In this instance, the Underwriter must remember to include the construction interest as a "soft cost" for the rehabilitation work.)
- B) The second method of financing the rehabilitation would be through multiple advances by the Agency. If the Agency is providing the funds for the rehabilitation, rather than draw all the money out at the beginning of work and place it in a Supervised Bank Account, funds are drawn out on a monthly basis or as needed. "Multiple" advances of funds are made throughout the job, rather than all money at the beginning (into a supervised bank account) or the end (from interim financing). An estimate of costs or schedule should be developed prior to beginning work indicating when funds would be required. Generally, the contractor would provide such a schedule. Funds are requested on a monthly basis to pay for work completed and / or materials suitably stored on-site. This payment schedule may need to be revised as work progresses. The Agency must inspect the work to verify the work is progressing adequately, and must verify that the amounts for the draw requests are appropriate. The Agency must obtain appropriate documentation showing previous payments were properly applied (subcontractors and vendors paid) and that there are no liens of record. In addition, the Agency must track the funds, to verify that the work is on target, on budget, that funds are requested in time to make necessary payments and that adequate funds remain. This would include all expenses for "hard costs" as well as "soft costs".
- C) If third party funds are being used for the rehabilitation (including Section 538 guaranteed loans) and interim financing is not being used, set up a separate construction account, force account, or Supervised Bank Account (each State Office may have a

different name for this type of account) for the funds. If the third party financier requires, funds can be requested over time, although depositing all in the account at the beginning of work is preferred as it eliminates the need to track funds for deposits. The Agency should complete progress inspections to verify work is proceeding normally and concur in pay requests. The payments must reflect the percentage of work completed in order to protect the government's security interest. Because the third party funds are being expended to rehabilitate a property in which the Agency has a financial interest, the Agency should track all draws / pay requests. This would include draw payments to the contractor (normally monthly), architect's fees, engineering fees, relocation expenses and all other soft costs associated with the property.

**Funds Disbursement.** Funds for the rehabilitation would be disbursed through either a construction lender or a construction account (supervised bank account set up according to RD Instruction 1902-A) and the initial required deposit to the reserve account, if any, as part of the financing tools would be deposited into the reserve account at closing.

**7) Using a Section 538 Guarantee in the Rehabilitation of a Section 515 or 514/516 Property**

This section will clarify which standards apply when using Section 538 funds to rehabilitate an existing Section 515 or Section 514/516 property. There are some differences between the requirements of the Section 538 Guaranteed Rural Rental Housing program and the Section 515 or 514/516 programs. Generally, the Section 515 or 514/516 program requirements are stricter, and generally the stricter requirements will apply to the property. MFH staff should be consulted for specific questions regarding rehabilitation funded by Section 538 guaranteed funds. Section 538 reserve account requirements would be used. For contingencies during rehabilitation, use the Section 538 requirement for 2% of construction cost, funded from the owner, bank letter of credit and unused funds going to the Operations and Maintenance fund first, then to owner, as cited in 7 CFR part 3565. For occupancy and rent restrictions, use the more stringent standards, which are currently found in 7 CFR part 3560.

If the Section 538 guarantee is for permanent financing only, follow the construction monitoring requirements of RD Instruction 1924-A and 7 CFR 1924, subpart A, as explained in this document. Surety for 100% of the contract amount should be obtained, in the form of performance and payment bonds, a bank letter of credit, or cash deposit. See 7 CFR 1924.13(e)(iii) and HB-1-3650, Chapter 5, paragraph 5.15. Performance and payment bonds are the preferred and most common form of surety for construction. A certified and audited cost certification is required pursuant to 7 CFR 3565.303(d)(8). If the Section 538 guarantee covers construction as well, follow the requirements of HB-1-3565, chapter 5, paragraph 5.21 as if it were new construction. In this case State Office staff would review, but not sign pay requests. Surety in the form of a performance and payment bond is preferred, but a bank letter of credit for 100% of the contract or acceptable collateral may be acceptable to the lender. Cost certification requirements outlined in Handbook 3565 will be followed. An identity of interest with the contractor

will require audited and certified costs on Form RD 1924-13.

#### **A) Protecting the Government's Interests**

To protect the Government's security interest in a property that is receiving government funding support, it is important to ensure a smooth, thorough and professional rehabilitation process. Construction durability, accessibility to the disabled population, compliance with building code and municipal regulations as well as improved marketability of the property are critical to the security interests of the Government as the lender. In the construction industry, there are cases where a contractor builds poorly, does not pay subcontractors, or abandons a job in the middle of construction. In these instances, the property may be in worse shape than it was before construction began. Since partially completed units cannot be rented, the income stream for the property could be interrupted, for an unknown and potentially lengthy period of time. Unpaid subcontractors might place liens on the property if they have not been paid by the contractor. Bringing in a new contractor to complete the work could be expensive as well as time consuming. To prevent these situations from arising, it is important that a representative of the Agency visit the site during construction to verify that work is progressing on time and on budget. If the work is not progressing satisfactorily, it is important to make sure that the project gets back on track with the schedule, budget and quality of work as soon as possible. You should meet with the Owner, the Architect and the contractor to address the problems and develop solutions.

Prior to the commencement of construction, verify that security for the Agency's investment is in place, generally in the form of surety for 100% of the cost of the construction work as required by 7 CFR section 1924.13(e)(1)(iii). Primarily, the surety is provided in the form of performance and payment bonds provided by the Contractor. Further explanation of the allowable security options is noted below in paragraph 8)B).

#### **8) Construction Administration**

Many of the same issues dealing with Contracts and Construction Administration apply to rehabilitation work, just as they apply to new construction. Examples of issues addressed in RD Instruction 1924-A that apply for the rehabilitation of a MFH property include:

##### **A) Procurement –7 CFR 1924.13(e)(1)**

If new funding is provided by the Agency, the preferable method of development for rehabilitation work is by competitive bid as defined in 7 CFR 1924.13(e)(1)(i). A negotiated bid may be accepted if an exception is granted by the State Director as described in 7 CFR 1924.13(e)(1)(vii). If an identity of interest as defined in RD Instruction 1924-A exists between the applicant and a contractor or any persons providing goods or services to the property (including the management company), and 7 CFR 1924.13(e)(1)(v) requires a cost certification for the rehabilitation. The State Director may also require a cost certification for cases where he/she determines it appropriate. The requirements in RD Instruction 1924-A that address surety

requirements, progress inspections, retainage, pay requests and change orders will be followed. Typical contract documents with Agency Guides will be used.

If no new funding is provided by the Agency, the requirements of RD Instruction 1924-A should be implemented to the greatest extent possible as it pertains to the bidding process or the contract documents with Agency supplements. The requirements in RD Instruction 1924-A addressing surety, progress inspections, retainage, pay requests and change orders provide the criteria for implementation and should be done so in a practicable manner. These recommendations will assist in protecting the Government and our security interest in the property if problems arise. As noted below, surety will be required due to the original funding / lien on the property.

**B) Surety – RD Instructions 1924.6(a)(3) and 7 CFR 924.13(e)(1)(iii)**

Surety will be required in certain circumstances as listed in 7 CFR 1924.6(a)(3) and 1924.13(e)(1)(ii). Surety may be provided in the form of Performance and Payment Bonds, a cash deposit (Minimum 100% construction contract. See 7 CFR 1924.6, or a bank letter of credit. 1924.6(a)(3)(iii)(C) allows less than 100% coverage with additional conditions (ie: 40% retainage on all portions of the work not covered by surety). All of these options are the responsibility of the contractor/constructor and the designated surety and would not become project funds unless a major failure of the contractor's performance occurred. Surety is provided to protect the owner and the lien holder in the event the contractor is unable to complete the work, or does not pay suppliers and subcontractors. Surety protects the Agency should a contractor fail to perform, abandon a project or not pay subcontractors. The Agency's investment would be at great risk. When Performance and Payment Bonds are provided for the project, the amount must be enough to complete the construction. If the contractor is unable to provide bonds, a procedure exists in RD Instructions 1924.6(a)(3) and 7 CFR 1924.6(a)(3)(iii) and (iv) to request an exception or alternative.

Surety may be required even if a construction lender / interim financing is used for the rehabilitation; however, the Agency is less concerned about surety with new construction that is using interim financing because the Agency does not have anything invested in the property until the project is completed. On the other hand, in rehabilitation projects, Agency security interest is affected at the commencement of construction due to existing mortgages on the property. It is important to require surety or some alternative financial security product allowed by 7 CFR 1924.6, if the construction lender / interim financing does not require it. For rehabilitation projects, a latent defects bond is appropriate for security during the warranty period when other forms of surety are provided other than performance payment bonds,

When a lender's (interim financing) surety requirements are in effect and RD funds are not involved with the project, then RD staff should evaluate the extent and adequacy of those requirements and request supplemental measures as necessary. Surety requirements

are slightly different when a Section 538 guarantee covering the construction is provided as explained earlier.

**C) Cost Estimates – RD Instruction §1924.13(e)(1) and 7 CFR 1924.13(e)(1)**

Form RD 1924-13 or comparable detailed estimate form, is required whenever Rural Development has a financial interest in the property. When the loan is obligated through AMAS, key in the data from this form as required by AMAS. In projects where architectural services are being provided, there will be sufficient work involved to warrant use of the form. The form will assist in tracking project funds to determine if the project is over / under budget and will assist in determining when change orders are necessary to move funds from one line item to another. Since estimates in rehabilitation work tend to vary more than in new construction, it's anticipated that variations in funds from the estimate to the final cost data will occur.

**For those cases with Agency funding where the rehabilitation is small and no architectural services are required, the Agency will determine on a case-by-case basis if Form RD 1924-13 will be required or a similar detailed cost estimate form is adequate.**

For those transactions where Rural Development is not providing any new funds, the form is not required. However, the Agency still needs the detailed cost estimate information for underwriting the loan, even if not provided on Form RD 1924-13.

**D) Contracts – RD Instruction §1924-A, §1924.13(e)(1)**

If new Rural Development loan funds are part of the rehabilitation transaction, all requirements of RD Instruction 1924-A and 7 CFR 1924, subpart A for contract documents must be followed. Construction Contract A101 and General Conditions A201, both part of American Institute of Architects (AIA) family of contracts with appropriate Agency guides (See RD Instruction 1924-A, Guide 1, Attachments 6 and 10) as appropriate, must be completed, reviewed and accepted by the Agency. While the standard AIA contract was not created specifically for rehabilitation work, it is sufficient to be used in rehabilitation projects. The Agency will consider the use of other contracts, but will require the necessary Federal funding language from the RD Instruction 1924-A Guide documents to be included as part of the contract. If no specific Agency contract guide document is available for use with the chosen contract, existing appropriate guides can be tailored for adaptation to the contract to ensure the applicable language is applied to the project. In these cases an regional OGC pass-thru is required.

If there are no new Rural Development funds as part of the transaction, the owner may choose to use the AIA Construction Contract A101 or a different contract for the rehabilitation. The Agency Guide is not required when the Agency is not providing new funding. However an Agency review of the contract may determine that some

implementation of the Guide language (i.e.; Surety, retainage, EEO and Agency role language) should occur prior to Agency concurrence.

All contracts for rehabilitation must indicate that work will be completed in a reasonable, realistic time frame. It is expected that rehabilitation should be completed within a maximum of 12-18 months.

**E) Pre-Construction Conference – RD Instruction 1924-A §1924.6(a)(11)(i) and 7 CFR 1924.6(a)(11)(i)**

A Pre-Construction Conference (PCC) is required for any new Agency property rehabilitation regardless of funding source.

A PCC is a good time to discuss construction administration issues prior to beginning the work. It is an opportunity for all parties (owner, management company, architect, Agency contacts and rehabilitation contractor) to meet face to face and exchange contact information, discuss roles and responsibilities, and discuss anticipated questions or issues on the project. At the PCC, parties should discuss the process and schedule of rehabilitation, the impact on tenants who may need to be relocated, the timing and frequency of inspections, processing of pay requests and change orders, retainage as written in the contract, as well as expectations and requirements for close out items to be provided at final inspection. The Agency should be a participant, not the leader of the meeting, so as not to create confusion about the responsibility for the work. The project architect should chair this meeting, if there is a project architect on the project. If there is no project architect, the Contractor or the Owner should lead the meeting, depending on who is best suited. Form RD 1924-16, “Record of Pre-Construction Conference”, may be used to document the issues discussed. A well run PCC can prevent serious problems later and is worth the time.

**F) Inspections – RD Instruction 1924-A, §1924.9 and §1924.13(a)(5)(v) and 7 CFR 1924.9 and 1924.13(a)(5)(v)**

Agency inspections are required in all cases, whether new Agency funds are used or not. See 7 CFR sections 1924.9 and 1924.13(a)(5)(v).

In new construction, inspections are required for “footing”, “framing” and “final”. See 7 CFR section 1924.9. In rehabilitation, an inspection is needed only at the “final” stage. In situations when adding a new unit, new community room, new laundry room or other feature, inspections are required at all stages.

For typical rehabilitation work, there may be cases where walls are relocated or opened and RD Instruction 1924-A and 7 CFR section 1924.9 would require a framing inspection before the wall is closed, to assure that electrical, plumbing, mechanical, insulation, etc. are in place and done correctly before the wall is closed. The majority of the inspections in rehabilitation work are based on a request for payment. The contractor wants to get paid at regular intervals during the work and an inspection is required to dispense funds.

It is recommended that Agency staff inspect the rehabilitation work as often as possible during the construction period. If Agency staff are not able to visit the property before each pay request, the pay request may be approved based on the percentage of work completed from the inspection report from the inspecting architect or the local authority having jurisdiction (a local building department). Typically, the time frame for payments is monthly. Review the contract to determine what the frequency of contractor payments is and determine how notice of a pay request and / or inspection will be handled by the parties involved. Agency inspections are to verify the work has been completed in proportion to the funds requested, that work is progressing adequately, that the work is of acceptable quality and that the government's security interest is being protected.

After the project architect has inspected the project, the Agency should ask for his/her inspection reports (or field reports or site visits). If the local jurisdiction / building department is making inspections, the Agency should ask for copies of those reports.

**G) Change Orders - RD Instruction 1924-A, §1924.10 and 7 CFR 1924.10**

Agency approval of change orders should follow the process set forth in 7 CFR 1924.10 regardless of the funding source, as they impact our security interest in the property.

During an inspection, if there are items that are different from what was described in the scope of work, plans and/or specifications, it is important to call attention to these items. A change order will be required as set forth in 7 CFR 1924.10. Anticipate change orders in rehabilitation projects. Much of the Scope of Work will have been based on assumptions. Once work begins, many unforeseen circumstances or conditions may arise that need to be addressed. The contractor or project architect should document these variances as change orders. Change orders should be approved prior to the work being done. However; the work is sometimes performed before the change order is approved. This typically occurs when the item is essential to the project and further work could not have proceeded without the change. In such cases, include copies of the change order in the project file to document the work.

Although change orders may either reduce or increase the contract amount and the work, most change orders in rehabilitation will be for those unforeseen items that add to costs. A balance must be struck between the funds available (including any "contingencies" that were built into the funding), the work needed, and the work planned. While part of the application process is to obtain a signed statement from the owner/applicant agreeing to pay for cost overruns from personal resources, there may be situations where it is important to develop a "no cost" change order, that acknowledges the additional unforeseen work needed and funds it by reducing work elsewhere in the job to balance the costs out.

The "no cost" change order in rehabilitation work would be anticipated only after all contingency monies have been used and more unexpected work has arisen. Typically, in new construction, landscaping is reduced to help offset cost overruns. The Agency could

determine that reducing landscaping in a rehabilitation job was acceptable to help offset additional work needed.

However, the owner has agreed to cover cost overruns. Decisions to adjust the scope of work because of cost overruns, even it only involves landscaping, should be made in conjunction with the Agency's Team Leader, the owner and the architect. The determination of where funds come from for cost overruns after contingencies have been depleted needs to take into consideration the best solution for the property, tenants, Agency and owner.

If the financing was set up to include "Contingencies", they should be treated as a separate line item cost shown on one of the blank lines of Form RD 1924-13 (lines 56 or 57). Each expenditure of funds from "Contingencies" will be documented by a change order. Track contingencies funds, provided through the Agency program financing, in the same way as a soft cost item – architect's fees, engineering fees, etc. If, at the end of the job, contingency funds remain, they may be used for additional work (as long as it would be an eligible loan expense for a new loan), or will be placed into the reserve account and used for future replacements. There is only one "contingency" to be used to cover overages in either "hard" or "soft" costs. As discussed previously, Section 538 guaranteed loan funds have a different contingency percentage and requirements.

**H) Pay Requests / Payments – RD Instruction 1924-A, §1924.6(a)(12) and §1924.13(e)(1) and (2) 7 CFR 1924.6(a)(12); 1924.13(e)(1) and (2)**

When new Rural Development funds are being provided, payments will be made by one of the following contract methods: "One Lump Sum" or "Partial Payments". See 7 CFR section 1924.6(a)(12)

A lump sum payment may be appropriate rather than partial payments, when there is one area of work that does not affect other systems or spaces of the building. An example would be the replacement of a roof. While it is usually an isolated and straightforward element of work, the cost may exceed \$350,000, and could be considered "rehabilitation", rather than "repair". This is a judgment call on the part of the underwriter in collaboration with the State Architect. Whether it is "rehabilitation" or "repair", there would need to be a schedule for the work and a corresponding payment schedule. Because the time period for completion of such work may be very short (one or two months), payment may be issued in one lump sum upon 100% completion of the work. It is important to ensure that the contract is written stating that payment will be made upon completion of all work and inspection and approval by Rural Development staff. For this situation, it might be appropriate to use the Form RD 1924-6, "Construction Contract", rather than a full AIA standard contract.

Typically, contractors will ask for monthly payments for work completed and/or materials suitably stored on site. Whatever the payment schedule will be, it should be described in the contract and agreed to beforehand in a Pre-Construction Conference (PCC). Before approving a pay request, either the project architect or Agency

representative (and preferably both) will inspect to verify that the work has been performed and that the pay request appropriately reflects the completed work. Retainage as set forth in the contract is held back on the total amount requested, until the project is completed. To protect the government's security position, require the contractor to provide the Agency with an executed Forms RD 1924-9 "Certificate of Contractor's Release" or RD 1924-10, "Release by Claimants", following each payment executed by all persons who furnished materials or labor on the property. These forms should likewise be discussed at the PCC.

The Agency may track the payments and funds to determine that adequate money exists in the account for remaining work. Form RD 402-2, "Statement of Deposits and Withdrawals", or a similar system will be used to track construction funds. An Excel spreadsheet could be used as well. Form RD 402-2 or similar document would be completed in accordance with the FMI for Form RD 402-2. If no new RD funding is involved then RD should assure that an acceptable "third party" financing entity tracking system is being implemented.

If no new Rural Development funds are being provided, the same conditions set out above for pay requests/inspections may be followed, but are not required. As a minimum, the Agency will review and approve all pay requests and change orders. Inspections and tracking of all contract funds for rehabilitation of an individual property with no new Rural Development funds is not required, but may be performed by the Agency on a "time available" basis.

**D) Final Inspection / Payment – RD Instruction 1924-A, §1924.6(a)(12), §§1924.9(d) and (e) and §1924.13(e)(1) and (2) and 7 CFR 1924.6(a)(12); 1924.9(d) and (e); 1924.13(e)(1) & (2).**

Final inspection and payment procedures are the same whether Agency funds or third party funds are used in financing the rehabilitation.

In making final payment to the contractor for the work, the Agency representative needs to verify that the work has been completed. Typically, the project architect performs a "substantial completion" inspection and creates a punch list, or list of what minor items need to be completed. The Agency representative will attend the final inspection, when the contractor has completed all items on the punch list.

All costs outside the contract (soft costs) must be dealt with at the final inspection. Prior to approving the final payment on a contract, the contractor must provide a signed copy of Forms RD 1924-9, and 1924-10, (or other industry standard form) from all persons who furnished materials or labor in connection with the contract.

Often times, a final change order is provided to reconcile the final costs for the project along with the request for final payment. Prior to making final payment, verify that the owner received the warranties for any equipment replaced as a part of the rehabilitation and all contractor lien release certifications were provided.

**J) Cost Certification – RD Instruction 1924-A, §§1924.13(e)(1)(iv) and (v)**

Per 7 CFR section 3560.72(d), a cost certification is required in all cases where there is an identity of interest as defined in 7 CFR 1924.4(i) between the contractor and applicant or any persons providing goods or services to the property (including the management company). The State Director may also require a cost certification for cases where he/she determines it appropriate. If the rehabilitation is funded by a Section 538 guaranteed loan, use the Section 538 Program cost certification requirements. However if there is an IOI contractor the certified and audited costs will be presented in the format contained on Form RD 1924-13, “Estimate and Certificate of Actual Costs”.

For rehabilitation work without Agency funding and if cost certification is not required by the other funding entities, cost certification would still be required by the Agency, but as noted for rehabilitation funded with Section 538 permanent financing only, the cost certification does not need to follow the Form RD 1924-13 format as long as the costs are audited and certified. (For example, the cost certification created for a tax credit property would suffice.)

**K) Warranty – RD Instruction 1924-A, §1924.4(p), 1924.12, and §1924.13(a)**

Warranty requirements are the same under 7 CFR 1924, Subpart A whether Rural Development funds or third party funds are used in financing the rehabilitation.

As with new construction, the contract for the rehabilitation shall require a full one year warranty on the work. Copies of all warranties for equipment that was replaced (heating and air-conditioning equipment, kitchen appliances, etc.) shall be provided to the owner prior to final payment. Also with new construction, if problems occur that are the result of poor workmanship or poor quality materials (as opposed to normal “wear and tear”), the contractor should be contacted to respond to warranty issues. If he does not respond in a timely manner, the project architect (if one is involved in the project) should contact the contractor to work toward a resolution. If no project architect was involved in the rehabilitation, the owner or management company should attempt a resolution. If no resolution results, in extreme cases, the contractor could be suspended or debarred from performing future work with the Federal government based on a refusal to honor warranty work. Reasonable and appropriately valued payment and performance bonds should be in place, during the warranty period to protect the project if the contractor fails to perform as required.

For monitoring purposes, enter the 11 month warranty inspection in MFIS under Supervisory Activity.

**Reference Guide**

Attachment B, *Repair vs. Rehabilitation Reference Guide*, is provided as a reference for field staff and program participants to summarize the requirements of this Unnumbered Letter. This may be helpful in understanding the different requirements for repair work

(which is funded on an annual basis by the reserve Account) and rehabilitation work (which is funded as part of the underwriting and handled through a separate account). Also, differences between rehabilitation funded by the Agency or funded by third party lenders are identified.

### **Conclusion**

A Procedure Notice that will incorporate this guidance into one of the 3560 handbooks will follow this UL. Handbook procedures regarding rehabilitation of units will be revised over time. At this time, all rehabilitation work performed that is deemed necessary in accordance with 7 CFR 3560 will need to follow these guidelines.

Any suggestions, comments, or questions on the current guidelines should be directed to William Downs or Michel Mitias, Architects with the Program Support Staff at 202-720-1499 or 202-236-3203, or directed to Carlton Jarratt, Senior Loan Specialist with the Multi-Family Housing Preservation and Direct Loan Program (MPDL) at [carlton.jarratt@wdc.usda.gov](mailto:carlton.jarratt@wdc.usda.gov), or 804-287-1524.

## REFERENCES TO REHABILITATION IN 7 CFR 3560 AND HANDBOOKS

Listed below is a comprehensive list of references to rehabilitation found in 7 CFR 3560, HB-1-3560, HB-2-3560 and HB-3-3560. These references include information on rehabilitation, sometimes as part of a transfer and sometimes in order to revitalize a property.

### *7 CFR 3560*

- 3560.11 – A definition of “Rehabilitation” for use in 3560 is included in the definitions section.  
3560.11 and 3560.252(d)(2) Under Rental Assistance new construction units are defined to include units provided in conjunction with substantial rehabilitation.
- 3560.52 - The Agency uses appropriated funds to finance the construction, rehabilitation of program properties, or purchase and rehabilitation of MFH and related facilities to serve eligible persons in rural areas.  
3560.53(b)- Eligible use of funds includes rehabilitation of buildings.  
3560.58(b)- The Agency will consider the purchase and rehabilitation for an existing structure located in the central business area of a rural community.  
3560.63(d)(2)- The Agency may recognize developer’s fee paid from “soft dollars” (not loan funds) available through other sources on rehabilitation up to 15% of the total development costs.
- 3560.63(f) – Sets maximum debt limit for new construction or rehabilitation loans.
- 3560.70(b)(2) – Rehabilitation of existing RRH manufactured housing units is included as an eligible property.
- 3560.105(f)(1)(ii) – Requires builder's risk insurance for new construction or rehabilitation.
- 3560.159(c) – Uniform Relocation Act applies for tenants displaced by rehabilitation.  
3560.202(e)- Fund from rehabilitation loans will not be counted towards reducing rents.
- 3560.303(b)(1) – Professional service contract expenses as part of a rehabilitation (for design and inspection) are an eligible expense.
- 3560.406(d)(5) – For transfers, immediate, long term and rehabilitation needs will be identified by a Capital Needs Assessment.  
3560.406(d)(14)- A limited profit Rural Rental Housing transferee’s initial investment and return on investment will remain the same provided to transferor less the transferee contributes additional funds for rehabilitation and the Agency agrees to the higher initial investment.
- 3560.455(b)(3)(iv) – Loan re-amortization may be used for rehabilitation in conjunction with a subsequent loan.
- 3560.752(b)(2)(ii) – Describes “Prospective Value” for appraisal after rehabilitation is completed.

*HB-1-3560, MFH Loan Origination Handbook*

- Ch. 1, paragraph 1.5 - Section 515 loans can be used to build, acquire and rehabilitate, or improve dwellings in rural areas.
- Ch. 1, paragraph 1.10B - Sites and dwellings developed or rehabilitated with Section 515 or Section 514/516 funds must meet the construction standards described or referenced in RD Instructions 1924-A and 1924-C.
- Ch. 2, paragraph 2.4A - The Agency does make initial loans for the purchase and rehabilitation of existing properties when it is in the Agency's best interest.  
Ch. 3, paragraph 3.13A- The Agency must conduct due diligence for hazardous substances for applications to rehabilitate existing structures.  
Ch. 3, Exhibit 3-2- Applicable federal accessibility regulations for rehabilitations.  
Ch. 3, paragraph 3.19- A subsequent loan for rehabilitation may not include expenses incurred for the temporary relocation of tenants.
- Ch. 4, Exhibit 4-3 – Rehabilitation listed as an eligible loan purpose.
- Ch. 4, paragraph 4.16.D.4 – For a borrower to be considered eligible to receive rehabilitation or equity funds, the project to be funded must either be in compliance, or be brought into compliance with applicable civil rights laws or physical accessibility standards with the receipt of loan funds.  
Ch. 4, paragraph 19.A.1- Developer's fee for rehabilitation can be up to 15 percent of the total development cost.  
Ch. 4, Attachment 4-B rehabilitation of existing buildings not previously financed by the Agency is an eligible loan purpose.
- Ch. 5, paragraph 5.11.C – Subsequent loans for repair and rehabilitation may be amortized over 50 years or the remaining economic life of the project, whichever is less.  
Ch. 6, Exhibit 6-3- The developer's profit for rehabilitation should be in contents of a Memorandum of Understanding (MOU) with state financing agencies.  
Ch. 6, Attachment 6-B- Developer's fee limit for rehabilitation listed in sample MOU.
- Ch. 7, paragraph 7.9.B and Attachment 7-A – Multi-layered financing, involving multiple financing sources, has become the norm in the building and rehabilitation of affordable housing.
  
- Ch. 10, paragraph 10.2.A – A subsequent loan might be appropriate to complete needed repairs and rehabilitation work.
- Ch. 10, paragraph 10.2.A – Subsequent loans for repair and rehabilitation do not compete for funding and borrowers can apply for a subsequent loan at any time. The processing of subsequent loans for repair or rehabilitation typically begins when the Agency and borrower identify the need for improvements.
- Ch. 10, paragraph 10.3.C – Lists eligibility for Repair and Rehabilitation subsequent loan funds.  
Ch. 10, paragraph 10.3.B- The annual funding notice to the states specifies the funds available for rehabilitation.
- Ch. 10, paragraph 10.4 – All improvements, repairs and modifications made as part of a subsequent loan must be in accordance with RD Instructions 1924-A and 1924-C.  
Ch. 10, paragraphs 10.9- Loans for rehabilitation are funded from a separate allocation and do not compete for funding with new construction. Lists what borrower must do to apply for a rehabilitation loan.

- Ch. 10, paragraph 10.10.A – While subsequent loans to repair or rehabilitate existing units are processed in accordance with loan priorities established by the National Office, Loan Originators should set submission deadlines based upon the timing of the subsequent loan request. However, any deadlines must allow the applicant reasonable time to gather and prepare the necessary documentation, which is generally at least 30 days.
- Ch. 10, paragraph 10.11.D.1- For repairs or rehabilitation a unit by unit inspection should be schedules as part of the loan underwriting process.
- Ch. 10, paragraph 10.12.B- The required restrictive use language for rehabilitation projects must be appended to the mortgage.
- Ch. 10, paragraph 10.13- subsequent loans made for major rehabilitation may require temporary relocation of tenants.

*HB-2-3560, MFH Asset Management Handbook*

- Ch. 1, paragraph 1.5 - Section 515 loans can be used to build, acquire and rehabilitate, or improve dwellings in rural areas.
- Ch. 1, paragraph 1.10B - Sites and dwellings developed or rehabilitated with Section 515 or Section 514/516 funds must meet the construction standards described or referenced in RD Instructions 1924-A and 1924-C.
- Ch. 2, paragraph 2.4A - The Agency does make initial loans for the purchase and rehabilitation of existing properties when it is in the Agency's best interest.
- Ch. 3, paragraph 3.5 – Accessibility review of property required for a rehabilitation loan.
- Ch. 3, Attachment 3-E - Professional service contract expenses as part of a rehabilitation (for design and inspection) are an eligible project expense.
- Ch. 4, paragraph 4.31- Quarterly reports are required at the completion of rehabilitation.
- Ch. 4, Attachment 4-A, paragraph 5- Professional service contract expenses are part of rehabilitation and are an eligible project expense.
- Ch. 5, paragraph 5.3.C - A project constructed after 3/13/91 must meet Fair Housing Act Accessibility Guideline requirements after rehabilitation.
- Ch. 6, paragraph 6.32.B - Lease may be terminated due to a required rehabilitation.
- Ch. 8, paragraph 8.8.B.- Rental Assistance may be suspended during rehabilitation.
- Ch. 9, paragraph 9.17.B.- The Agency should review the situation 180 days after disaster to assess rehabilitation.

*HB-3-3560, MFH Project Servicing Handbook*

- Ch. 1, paragraph 1.5 - Section 515 loans can be used to build, acquire and rehabilitate, or improve dwellings in rural areas.
- Ch. 1, paragraph 1.10B - Sites and dwellings developed or rehabilitated with Section 515 or Section 514/516 funds must meet the construction standards described or referenced in RD Instructions 1924-A and 1924-C.
- Ch. 2, paragraph 2.4.A. - The Agency does make initial loans for the purchase and rehabilitation of existing properties when it is in the Agency's best interest.
- Ch. 6, paragraph 6.6.A. – Requires unit-by-unit inspection to determine whether rehabilitation may resolve problem.
- Ch. 6, Exhibit 6-3 – Project obsolescence would include cost of rehabilitation as a factor. Rehabilitation must comply with building codes. Consider expected useful life after

- rehabilitation.
- Ch. 6, paragraph 6.6.C – Size of rehabilitation loan may have an impact on Project Obsolescence.
  - Ch. 7, Exhibit 7-1 – Identify additional physical condition requirements when a rehabilitation is involved with a Transfer with Rural Development funds or Third Party funds.  
Ch. 7, paragraph 7.1- Transfers offer opportunity to improve the quality of housing through rehabilitation.
  - Ch. 7, paragraph 7.7.A. – The Loan Servicer should be particularly diligent in analyzing the budget and proposed rents when the transferee will also receive a subsequent loan or other third party financing or there are significant repairs or rehabilitation plans.  
All project rehabilitation costs must be reflected in project basic rents which may not exceed comparable market rents.
  - Ch. 7, paragraph 7.7.C.- If rehabilitation will be performed basic rents should not increase until after completion of construction and inspection by the Agency.
  - Ch. 7, paragraph 7.9A– The transferee contributes equity for payment of hard costs of construction (repair or rehabilitation) and Rural Development agrees to recognize a higher initial investment as described in Paragraph 7.9 B.
  - Ch. 7, exhibit 7.3- Example of how to calculate the return to owner based on rehabilitation.
  - Ch. 7, paragraph 7.13- Revitalization effective processing strategy includes establishing the scope of rehabilitation.
  - Ch. 7, paragraph 7.20.C.- Borrower should consult with state preservation office for the transfer historical property which includes rehabilitation facade.
  - Ch. 7, paragraph 7.20.D- MFH should do a design review when rehabilitation affects the design of the property.
  - Ch. 7, paragraph 7.22 - The CNA includes an evaluation of any accessibility needs [7 CFR 3560.406(d)(9)] and must identify all immediate and long term repair and rehabilitation needs, see [7 CFR 3560.406(d)(5)].
  - Ch. 7, paragraph 7.22.A - For transactions that include third-party funded rehabilitation (for example, transactions involving the acquisition of tax credits), the scope of work requires the CNA provider to use the proposed (and Rural Development -approved) third-party funded rehabilitation scope and develop a 20-year Replacement Reserve schedule that assumes that the third-party funded rehabilitation will occur as planned. Because the rehabilitation will not be funded from the reserve, Rural Development does not require the CNA to include the rehabilitation and does not require the CNA provider to review the rehabilitation costs or scope.
  - Ch. 7, paragraph 7.22.B - After receipt of the draft CNA, the Loan Servicer will make an on-site inspection of each vacant unit and 10 percent of the remaining units in the project being transferred. When substantial rehabilitation issues are involved, additional units may be inspected.
  - Ch. 7 paragraph 7.22.C - For Rural Development funded repairs, the detailed repair and rehabilitation plans and costs will be based on the CNA.  
Ch. 7, paragraph 7.23.C- The agency will consider rehabilitation in evaluating the feasibility of a proposed transfer.
  - Ch.7, paragraph 7.25 - The subsequent loan and its impact are accurately reflected in the transferee's budget and repair and rehabilitation plans.

- Ch. 7, exhibit 7-5, Monitoring rehabilitation work is part of basic steps for implementing transfers.
- Ch. 7, paragraph 7.33C - Rural Development will monitor all repairs and approve payments using the procedures outlined in Chapter 9 of HB-1-3560. Completing this step allows Rural Development to verify that the property will be restored to a decent, safe and sanitary condition.  
Ch. 7, Attachment 7-A- Providing rehabilitation loans is listed as a servicing authority. Transfer repair agreement should include costs of relocating tenants if displaced by rehabilitation.
- Ch. 7, Attachment 7-B-2- Rehabilitation costs should be calculated in sources and uses of funds.
- Ch. 7, Attachment 7-D- Specific prospective value should be considered in appraisal if rehabilitation work is conducted.
- Ch. 12, paragraph 12.9- If rehabilitation costs are excessive, abandonment of security interest may occur if chattel property has no market value.

## REPAIR vs. REHABILITATION REFERENCE GUIDE

The following chart maybe useful for the repair or rehabilitation of MFH properties.

ITEM	REPAIRS <sup>1</sup>		REHABILITATION <sup>1</sup>	
	Only RD Funds <sup>2</sup>		Only RD Funds <sup>2</sup>	3 <sup>rd</sup> Party Funds <sup>3</sup>
Architectural Services (7 CFR 1924.13(a))	Recommended but typically not necessary.		Required, but can be waived by National Office on case-by-case basis	Required, but can be waived by National Office on case-by-case basis
Procurement (7 CFR 1924.13(e)(1))	Minimum 2 bids recommended if work done under one contract > \$3500.		Competitive bids required (Competitive bids negotiated with S.D. exception.) Cost cert if IOI.	Recommend competitive bids and cost cert if IOI.
Surety (7 CFR 1924.6(a)(3) & 1924.13(e)(1)(iii))	Required unless an exception is granted.		Surety required. (Impacts Agency loan security.)	Surety required. (Impacts Agency loan security.)
Cost Estimates (7 CFR 1924.13(e)(1))	Minimum 2 bids recommended if work > \$3500. If architectural services required, use Form RD 1924-13 Cost Estimate form..		Use Form RD1924-13 Cost Estimate or similar format containing adequate detail.	Cost estimates for underwriting are needed. Use Form RD 1924-13 Cost estimate form or similar acceptable document.
Contracts (7 CFR 1924.13(e)(1))	Contracts required. (Even if just acceptance of bid.)		Contract docs per 1924-A. (AIA with Agency guides are preferred and are the standard.)	Must be a “contract” with similar AIA standards. Agency guides required if applicable.
Pre-Construction Conference (7 CFR 1924.6(a)(11)(i))	. N/A		Required. Use RD Form 1924-16.	Recommended. Form RD 1924-16 may be used or similar content.
Inspections (7 CFRs 1924.9 & 1924.13(a)(5)(v))	Agency and third-party contractor, if approved, will inspect work.		Agency will inspect work. Use Form RD 1924-12.	Agency and third-party contractor, if approved, can inspect work. Use Form RD 1924-12.
Change Orders (7 CFR 1924.10)	N/A		Agency approval required. Use Form RD 1924-7.	Agency approval required. Use Form RD 1924-7.
Pay Requests / Payments (1924.12)	Agency review not required.		Agency approval required. Use Form RD	Agency review payments. Third Party to

(Subattachment B-1)

& 7 CFR 1924.13(e)(1) & (2)) Section 538 UL Dated 8/16/11		1924-18. Get Form RD 1924-9 and Form RD 1924-10. Track funds on Form RD 402-2 or similar.	track payments by acceptable system.
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Final Inspection / Payment (7 CFRs 1924.6(a) (12), 1924.9(d) & (e), & 1924.13(e)(1) & (2))	N/A	Agency inspects. Use Forms RD 1924-12, 1924-9 and 1924-10. Use 1924-7 if necessary.	Agency inspects. Use Forms RD 1924-12, 1924-9 and 1924-10. Use 1924-7 if necessary.
Cost Certification (7 CFR 1924.13(e)(1)(iv) & (v))	Required if IOI.	Required if IOI or State Director requests. Use Form RD 1924-13.	Required if IOI. Does not have to follow Form RD 1924-13.
Warranty (7 CFRs 1924.4(p), 1924.12, & 1924.13(a))	Warranty required.	Warranty required. Use Form RD 1924-19.	Warranty required. Form RD 1924-19 may be used.

**NOTES:**

1. See Unnumbered Letter for definitions of “Repairs” and “Rehabilitation”.
2. “Only Rural Development funds” would include debt deferral, subsequent loan, MPR grant, or other MPR servicing tools from Rural Development. (Not Section 538 guaranteed funds.)
3. “3<sup>rd</sup> Party Funds” would include Section 538 GRRH funds, Low Income Housing Tax Credit Funds, Home Funds, a local bank, or any source of funds other than Rural Development.