



## OWNER'S & CONTRACTOR'S COST CERTIFICATION GUIDELINES

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## **1. Owner's & Contractor's Cost Certification Guidelines**

### **I. GENERAL**

These guidelines are designed to assist owners, contractors, and independent certified public accountants in the preparation and submission of the Contractor's Cost Certification Forms for the Kentucky Housing Corporation's development programs including the Low Income Housing Tax Credit Program (LIHTC). KHC, under the guidance of its Board, desires to cause the development of as much quality affordable housing as possible with the resources it has at its discretion. Implementing the cost certification process for general contractors will create greater transparency and accountability of the resources available to the affordable housing development community and will assist in developing a database of comparable construction data to aide in the development of future safe, decent and affordable housing for all Kentuckians.

The purpose of the cost certification is to establish the total costs incurred by the contractor and the owner in the development of a project. This will enable KHC to determine certain development costs and the amount of subsidy to be allocated to the project. All costs are included in the calculation of the total development costs; however, not all such costs are necessarily recognizable in determining the eligible basis and the amount of LIHTC to be allocated.

The cost certification is required of all owners and all general contractors. The owner of the project is obligated to submit or cause to be submitted the cost certifications applicable to itself and the general contractor prior to issuance of IRS Form 8609 or funding award closeout for LIHTC only projects. Where there is an identity of interest relationship between the general contractor and/or the owner and a subcontractor (defined in Section 1-II), KHC will require a cost certification of that sub-contractor. Any overhead, profit and general requirement fees paid to that sub-contractor will be added to the general contractor's overhead, profit and general requirements and limited to the percentages discussed in Section 1-III.

The general contractor is entitled to include in costs, all ordinary and necessary expenses directly related to the construction contract, including amounts paid to subcontractors, all labor and material required for the purpose of performing the contract, insurance premiums, and all types of ordinary and necessary costs related to the construction (light, power, telephone, water and other utilities furnished to the construction job, and all other ordinary expenditures of the contractor incidental to the performances of the contract). All expenditures must be reduced by the amounts of any kickbacks, rebates, allowances, trade discounts or other sums that the owner has received or is to receive.

KHC reserves the right to exclude any line item of cost when the amount is determined to be so high as to be out-of-line with reasonable and necessary costs as compared with comparable projects in similar areas.

### **II. IDENTITY OF INTEREST**

An identity of interest (IOI) exists when one of the following conditions exists between any owner or related party general contractor as party of the first part, and any general contractor, subcontractor, material supplier, or equipment lessor as party of the second part:

1. The party of the first part has a financial interest in the party of the second part;

2. One or more of the officers, directors, stockholders, members or partners of the party of the first part is also an officer, director, stockholder, or partner of the party of the second part;
3. An officer, director, stockholder, member, or partner of the party of the first part has a financial interest in the party of the second part;
4. The party of the second part takes an ownership or a financial interest in the party of the first part as part of the consideration to be paid them; or
5. There exists or come into being any side deals, agreements, contracts or understandings entered into thereby altering, amending, or canceling any of the legal documents entered into by the party of the first part and the party of the second part pertaining to the property and resulting in compensation or other benefit to the party of the first part.

If an identity of interest exists between the owner and the general contractor, incentive performance fees may only be paid to the extent that they are included in the fee limitations described in Section 1-III.

### **Subcontractors Acting as General Contractors**

In the case where a sub-contractor is acting as a General Contractor, by entering into sub-contract arrangements for portions or all of the original sub-contract agreement, KHC reserves the right to require the sub-contractor acting as a General Contractor to the same audit requirements of all General Contractors. If it is determined that these arrangements involve identity of interest relationships, the General Contractor and/or sub-contractor will be limited to the defined fee amounts for general requirements, contractor overhead and contractor profit identified in Section 1-III. These sub-contractor relationships should be identified as early as possible in the application process.

The owner's and contractor's identity of interest certifications must be submitted with the KHC Forms for the Contractor's Cost Certification.

### **III. COSTS ALLOWABLE IN CONTRACTOR'S COST CERTIFICATION**

Costs to be reported by general contractors are as follows:

#### **1. Trade Items: Construction Cost - Detail**

Allowable costs under this heading include amounts paid or owing to all subcontractors, laborers, or material supplier(s) for the construction of on-site (except off-site costs under a supplemental contract) physical improvements included under the general construction contract. Labor can be aggregated in one total for each line item. A trade item listing is stated in [\*Masterformat® Numbers & Titles\*](#), which clarifies the desired trade item captions and a general description of what should be included in those trade items. Costs for incomplete items should be handled by including the amount of the work in the appropriate line item and inserting next to the contractor's name and amount, the word "incomplete."

2. General Requirements

General requirements may not exceed 6% of the total construction cost, exclusive of contractor profit, contractor overhead, and general requirements, from the Contractor's Cost Certification Forms. See [Masterformat@ Numbers & Titles](#) for items to be included in general requirements.

3. Contractor's Overhead

Contractor's overhead, also called builder's overhead, may not exceed 2% of the total construction cost, exclusive of contractor profit, contractor overhead, and general requirements, from the Contractor's Cost Certification Forms.

4. Contractor's Profit

Contractor's profit, also called builder's profit, may not exceed 6% of the total construction cost, exclusive of contractor profit, contractor overhead, and general requirements, from the Contractor's Cost Certification Forms.

**IV. CONTRACTOR'S COSTS ALLOWABLE IN OWNER'S COST CERTIFICATION**

The owner's certified costs generally should include all costs to finance and construct the development, whether or not they are includable in LIHTC eligible basis. The costs to syndicate or otherwise sell interest in the development must be included with the Owner's Cost Certification Forms. If any estimates are included in the Owner's Cost Certification Forms, they must be identified as such.

The construction costs from the Contractor's Cost Certification Forms should be segregated into the following construction categories on the Project Costs section of the Owner's Cost Certification Forms as follows:

Construction – Residential New Construction: Comprised of all trade items not identified as being Furnishings/Appliances, Site Improvements, Offsite Improvements, or Other Fees Paid by the General Contractor contained within the Contractor's cost breakdown.

Construction – Residential Rehab: Comprised of all trade items not identified as being Furnishings/Appliances, Site Improvements, Offsite Improvements, or Other Fees Paid by the General Contractor contained within the Contractor's cost breakdown, for projects that have been identified as an acquisition/rehabilitation project.

Construction - Commercial: Should represent the costs incurred to construct or renovate any commercial space as part of the overall development of the project. Costs for the commercial portion of the project should be specifically identified to allow for proper segregation on the contractor's cost certification. If costs for the commercial space are not specifically identified, then the auditor will need to allocate the costs for the commercial space based upon a reasonable allocation method. NOTE: A third party (architect and/or engineer) computation of allocable costs for the commercial space would be acceptable supporting documentation.

Furnishings/Appliances: Comprised of the following trade items from the contractor's cost certification: Appliances, Blinds and Shades, Artwork, and Carpeting.

General Requirements: Enter the amount from the sub-schedule for general requirements, contractor overhead and contractor profit. This category would include fees paid by the General Contractor such as building permit fees, tap fees, impact fees, construction insurance, bond premium costs, and site security as examples.

Contractor Overhead: Enter the amount from the sub-schedule for general requirements, contractor overhead and contractor profit.

Contractor Profit: Enter the amount from the sub-schedule for general requirements, contractor overhead and contractor profit.

Construction management and construction guarantee fees will be included, along with consulting fees, in the owners cost certification forms and will be aggregated with the developer fees and limited to the maximum allowable amount of developer fees.

## V. GUIDANCE TO CERTIFIED PUBLIC ACCOUNTANT

### **Minimum Audit Procedures**

Audits shall be prepared and conducted in accordance with Generally Accepted Auditing Standards. The following are required minimum audit procedures provided for the use and consideration of the Accountant. The technical standards referred to above and these required procedures are not intended to replace the Accountant's use of professional judgment or knowledge of the client, programs, and the affordable housing industry in determining the appropriate level of testing required to issue his/her opinion on the Owner's/Contractor's Cost Certification.

The Accountant must obtain and review a sub-contractor listing to search for any identity of interest relationships between the owner, general contractor, sub-contractor, material supplier, or equipment lessor based upon information provided by the client. The Accountant should also inquire of KHC about their knowledge of identity of interest relationships and compare that information to the information obtained from the client.

If identities of interest sub-contractors are being utilized by the general contractor, then those sub-contractors will also be subjected to an audit of their sub-contract to determine the actual cost and the contractor's overhead, contractor's profit and general requirements.

Owner and General contractor shall provide to their respective Accountant:

- a. Completed KHC Owner's/Contractor's Cost Certification Forms, including any required descriptions of costs – see [Masterformat@ Numbers & Titles](#).
- b. Copy of construction contract and any change orders.
- c. Listing of all sub-contractors utilized on the job, with amounts paid and to be paid.
- d. Listing of all "other costs/fees" paid and/or incurred for the project by the contractor.

The Accountant must send third party confirmations to at least three (3) vendors who comprise a majority of the sub-contractor costs.

- a. Confirm contract amount.
- b. Confirm any change orders.
- c. Confirm what additional costs were incurred outside of the contract, if any.
- d. Confirm type of services provided (trade breakdown).
- e. Confirm amounts paid to date and balance to be paid.

The Accountant shall select at least five (5) other sub-contractors haphazardly or by a sampling method, and verify the amounts paid to each sub-contractor by reviewing check copies, contract documents, change orders, and other supporting information to verify amounts included within the cost certification for each sub-contractor selected.

Coverage should be at least 40% of total cost incurred on the construction contract. If not, the Accountant shall select additional sub-contractors and perform procedures above until the 40% requirement is exceeded.

The Accountant shall inquire about the rental equipment used in the development activities. If an identity of interest exists with the equipment lessor, the Accountant shall disclose this in the notes to the Owner's/Contractor's Cost Certification and perform a reasonableness test by comparing the rental rates charged to the project to those charged by independent equipment lessors.

The Accountant shall inquire about the use identity of interest material suppliers used in the development activities. If an identity of interest exists with a material supplier, the Accountant shall disclose this in the notes to the Owner's/Contractor's Cost Certification.

The Accountant shall perform a comparison of actual costs to the amount budgeted at time of application and obtain explanations for significant variances.

The Owner's/Contractor's Cost Certification Forms must be accompanied by the unqualified opinion of the Accountant. Inclusion in the opinion of any qualifying language will make the opinion and the form unacceptable to KHC. When there is an identity of interest between two or more of the parties required to certify costs, certification of the parties having such identity of interest must be by the same Accountant.

KHC reserves the right to determine whether the Owner's/Contractor's Cost Certification received is satisfactory and meets the standards set forth by KHC.

## **2. Contractor's Cost Certification Forms**

KHC's required contractor's cost certification forms referenced in this document are available on KHC's [Multifamily webpage](#) under [Post-Award Resources](#).