



**Report on MassHousing's Review  
of the Cost Certification for**

**Carriage Lane, LLC**

**dated January 5, 2006**

**a M.G.L. Chapter 40B Development**

**No. 2008-PE-005**

**March 28, 2008**

## Executive Summary

The purpose of MassHousing's analysis of this Cost Certification Report (the "Cost Certification") is to determine compliance of the Cost Certification with applicable accounting and reporting standards, and legal requirements and published guidelines for the preparation of these reports as further described in the Procedures section. MassHousing has developed procedures to help assure that the scope of the review is sufficient to fulfill that objective and to ensure consistency in the review process.

MassHousing has reviewed the Developer's Cost Certification Report and limited dividend calculation as of September 30, 2005, of Carriage Lane, LLC (the "Developer"). As a result of applying our procedures we determined that all required information was included in the Cost Certification. However, we did determine, as a result of our procedures that the limited dividend calculation as reported in the Cost Certification requires the proposed adjustments identified below. The proposed adjustments identified do not put the limited dividend percentage in excess of 20%, the maximum allowable. As a result, MassHousing has concluded that the project is in compliance with this limitation on dividends.

The following schedule reflects the final limited dividend calculation as adjusted for project sales and cost findings noted in this report:

Description	Per Report	Proposed Adjustment	Final	Ref.
Total Project Sales	\$ 6,989,300	\$ -	\$ 6,989,300	-
Total Project Costs	5,962,373	10,000	5,899,744	A
		4,461		B
		(74,100)		C
		(2,990)		D
Computed Profit from Sales	<u>\$ 1,026,927</u>	<u>\$ 62,629</u>	<u>\$ 1,089,556</u>	
Profit Percentage	<u>17.22%</u>		<u>18.47%</u>	
Excess	<u>-</u>		<u>-</u>	

- A. The locus in question originally consisted of two parcels of land. The land value policy in effect at the time of site approval provided that Land Value was determined by the lesser of an appraisal or an arm's-length transaction occurring within the past three years. Because one of the parcels involved a related-party sale, an appraisal was utilized for this parcel, and MassHousing has utilized the appraised value in its analysis. The adjustment to land value reflects the value stated in that appraisal, which was \$10,000 higher than what the Developer reported.

- B. MassHousing was the construction lender for this development, and its records reflect that the Developer understated the total amount of construction loan interest that was paid by \$4,461.
- C. MassHousing has disallowed this amount of Developer overhead as it was not “commercially reasonable.” See the discussion on pages 7-8.
- D. Based upon subsequent discussions between CHAPA and the Developer’s CPA, it was determined that the Developer’s brokerage commission costs were slightly overstated in the Cost Certification.

In addition, with the exception of the proposed adjustments noted above, we conclude that the Cost Certification, which includes the following schedules

- Schedule of Chapter 40B Maximum Allowable Profit from Sales
- Schedule of Total Chapter 40B Project Costs,

is free of material mathematical errors; reflects sales revenue from all units; reflects the number of units in the project as agreed to in the Regulatory Agreement; reflects project costs that appear to be reasonable based on a review of the project budget; reflects site acquisition costs in a manner consistent with then existing policy; and includes Notes to Schedules that appear to cover the full scope and time frame of the project.

#### **A Note About This Report**

The public accounting firm, Sharkansky & Company LLP, performed a review of Carriage Lane’s Schedules in accordance with Statements on Standards for Accounting and Review Services issued by the American Institute of Certified Public Accountants. CHAPA, MassHousing’s monitoring agent, subsequently retained an independent CPA (Daniel Dennis & Co.) to analyze the work of the Developer’s CPA (the “CHAPA Report”).

There are significant differences between the objectives of an audit and a review based on professional standards. The objective of an audit is to provide a reasonable basis for expressing an opinion regarding the schedules taken as a whole. A review does not provide a basis for the expression of such an opinion because a review does not include obtaining an understanding of an entity’s internal controls or assessing control risk, performing tests of accounting records and responses to inquiries by obtaining corroborating evidential matter through inspection, observation or confirmation, and certain other procedures ordinarily performed during an audit. A review does not provide assurance that the CPA will become aware of all significant matters that would be disclosed in an audit.

The Developer’s CPA performed a review rather than an audit at the direction of MassHousing’s monitoring agent (CHAPA). This direction was issued in light of the relatively small (16 units) size of this development. MassHousing, as lender, accepts responsibility for any confusion relating to the appropriate level of accountant review in the preparation of this report. Accordingly, as a compensating measure in verifying the contents hereof, MassHousing subsequently obtained a “Developer’s Certificate,” attached hereto as Appendix B. This certificate, executed under seal and

under the pains and penalties of perjury, serves an additional safeguard in verifying the data set forth in this report. Subsequent to the issuance of the borrower's review of this report, MassHousing issued cost certification guidelines clarifying the requirements relating to an independent accountant's examination and making the "Developer's Certificate" a mandatory element of cost certification.

## Overview

On October 3, 2001, MassHousing issued a project eligibility letter evidencing fundability of the Carriage Lane project under the "Housing Starts" construction loan program. MassHousing notes that at this time, neither the "Local 40B Review and Decision Guidelines" (the "MHP Guidelines") dated November 2005 nor MassHousing's own Cost Certification Guidance (August 2007) had been developed. In May 2002, the Town issued a Comprehensive Permit for Carriage Lane.

In November 2002, MassHousing's Board approved a \$3 million revolving construction loan for the project. In the course of reviewing this application for MassHousing financing, MassHousing also reviewed the Developer's pro forma and signed an agreed upon "Sources and Uses of Funds" at the time of closing. The loan closed on February 3, 2003. Simultaneously with the loan closing MassHousing, the Developer and the Town executed: (i) a Regulatory Agreement, and (ii) a Monitoring Services Agreement appointing the Citizen's Housing and Planning Association (CHAPA) as monitoring agent.

The last unit in the development was sold in April 2005. Pursuant to the Regulatory Agreement and Monitoring Services Agreement, MassHousing has the responsibility to review the Limited Dividend Requirement which involves determining the Developer's compliance with the Allowable Profit limitation through approval of Total Development Costs and reviewing the Monitoring Agent's evaluation of the Developer's Cost Certification.

## Procedures

In connection with its responsibilities under the Regulatory Agreement and Monitoring Services Agreement, MassHousing reviewed the following:

- Review dated January 5, 2006, by Sharkansky & Company LLP (the Developer's Cost Certification Report), including Independent Accountants' Review Report, Schedule of Chapter 40B Maximum Allowable Profit from Sales, Schedule of Total Chapter 40B Project Costs, and Notes to Schedules.<sup>1</sup>
- HUD-1 Settlement Statements for sales of units submitted in connection with requests for partial releases of MassHousing mortgage.
- Land appraisal prepared by Fidelity Appraisal Group, Inc.
- Loan requisitions and supporting materials.
- MassHousing Sources and Uses of Funds Statement and accompanying Cash Flow Statement executed in connection with construction loan closing on February 3, 2003.

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<sup>1</sup> The Developer's Cost Certification Report indicates that it covers sales and project costs incurred from December 2002, the date of the inception of Carriage Lane, LLC, to September 30, 2005. Our review however, indicates that costs incurred prior to December 2002 were accounted for in the Developer's Cost Certification Report. Provided those costs are in relation to project, the date of incorporation of LLC should not cause those costs to be excluded.

- Real estate records in Banker & Tradesman for sales of units.
- “Housing Starts Process and Guidelines”
- “Guidelines for Housing Programs in Which Funding is Provided Through a Non-Governmental Entity” (the “NEF Guidelines”).
- The MHP Guidelines.

While neither the NEF Guidelines nor the MHP Guidelines were in effect during the development of this project, to the extent they are reflective of preexisting industry standards, they are referenced in this memorandum as guidance; to the extent they constitute new guidance for Chapter 40B stakeholders, they are distinguished from the state of affairs existing when Carriage Lane was in active development.

**Project Revenue Sales**

MassHousing reviewed appropriate documentation for all unit (16) sales.

<i>Sales Revenue from all 16 units</i>	Amount
Affordable Unit Sales Per Cost Certification – 4 units	\$ 660,000
Market Unit Sales Per Cost Certification – 12 units	<u>6,329,300</u>
Total Sales Revenue Per Cost Certification	<u>\$ 6,989,300</u>

The Developer submitted a signed and notarized certificate stating that no units were sold to a related party. The average unit sales price for an affordable unit was \$165,000 while the average unit sales price for a market rate unit was approximately \$527,500.

Our procedures included reviewing on-line records at the Registry of Deeds (Middlesex South County) for all unit sales at Carriage Lane and HUD-1 Settlement Statements. In addition, records were reviewed for subsequent unit sales occurring within 12 months of the original sale date. No subsequent sales were noted.

There are certain restrictions imposed on the resale of any affordable unit under Chapter 40B. It is the responsibility of the Monitoring Agent to review and approve the subsequent sale of all affordable units.

**Project Costs**

**Land**

This site consists of 2 land parcels, 717 Boston Post Road (1.75 acres) and 729 Boston Post Road (.68 acres).

The land at 717 Boston Post Road was valued at \$600,000, based on a Purchase and Sale Agreement and Quitclaim Deed. This transaction was considered to be arm’s-length between

Richard & Deborah Babineau (seller) and Carriage Lane, LLC (buyer); accordingly, under the MassHousing policy for establishing land value in effect at the time, this third-party sale was utilized in establishing land value. As additional support for the \$600,000, MassHousing staff obtained sales data from Banker & Tradesman that showed that 167 single-family homes were sold in Sudbury between January 1 and August 3, 2001. The average sales price of these sales was \$640,439 and the median sales price was \$561,500. Carriage Lane, LLC listed the acquisition cost of this property as \$639,000. This figure includes \$39,000 in carrying costs which have been documented. These carrying costs were reported as option payments less collected rents. Since these carrying costs are reasonable based on the facts and circumstances involved, the \$639,000 acquisition cost for this property is allowed.

An appraisal dated August 30, 2001, was completed by Fidelity Appraisal Group, Inc. for the property at 729 Boston Post Road (the "Appraisal"). MassHousing required this appraisal at the time of project eligibility because the applicant owned and occupied a 3-bedroom home at this address and, therefore, land value could not be established by an arm's-length, third-party transaction. The accepted appraised value for 729 Boston Post Road at that time was \$435,000. The Cost Certification, however, listed the value at \$425,000; since the appraisal was the operative document for establishing land value, MassHousing utilized the \$435,000 appraised value.

<i>Land Value</i>	Amount
729 Boston Post Road Land Value – cost certification	\$ 425,000
729 Boston Post Road Land Value Per Appraisal 8/30/01	435,000
Difference	<u>\$ 10,000</u>

#### **Related Party – Interest Costs**

Commercially reasonable interest is an allowable Project Cost. In this case, however, the development entity in its Cost Certification elected to exclude interest in the amount of \$43,491, paid to the Roth Family LLC, Investor Member. Robert Roth personally guaranteed MassHousing's \$3,000,000 construction loan and contributed \$300,000 in equity towards the cost of the project. Since the determination of commercial reasonableness of a rate of interest unlike, for example, the determination of the actual numerical figure stated in an appraisal, necessitates an exercise of discretion and judgment, MassHousing will not disturb the Developer's conclusion that the interest paid to Roth should not be included as an expense of Carriage Lane.

#### **Construction Loan Interest on the MassHousing Loan**

The Cost Certification showed total construction loan interest of \$116,448, yet as the lender for the project, MassHousing has confirmed that a total of \$120,909 was received from the Developer. See calculations below.

<u>Construction Loan Interest</u>	<u>Amount</u>
Construction Loan Interest – Cost Certification	\$ 116,448
Actual Construction Loan Interest paid to MassHousing	<u>120,909</u>
Difference	<u>\$ 4,461</u>

Since the amount of interest paid to MassHousing exceeds the amount in the Cost Certification, and this number, like the numerical figure stated in the appraisal is readily and objectively discernable, MassHousing has increased this expense by \$4,461, increasing total development costs as well.

### **Related Party: Sales of Units**

According to the Developer’s Certificate, no such related party sales took place.

### **Commissions – Market Units**

The Developer’s Cost Certification Report lists \$317,195 as the total amount of brokerage commissions, yet the Notes to schedules state that total brokerage commissions were approximately \$314,000 (including \$41,964 paid to Alan Marrone) representing 4.96% of the total revenues from the 12 market units. CHAPA brought this discrepancy to the attention of the Developer’s CPA who explained that the \$3,195 difference might have been costs that were categorized incorrectly. Because there was no explanation for these additional costs MassHousing utilized \$314,205, which is the lesser of the two numbers. All of the units in the Development were sold before the MHP Guidelines were published. At that time, the determining test for cost certification purposes was whether a cost was “commercially reasonable.” A 4.96% commission rate, even where a disclosed related party was involved meets this standard. Since part of the function of the MHP Guidelines was to increase public awareness of some of the quantifiable aspects of “commercial reasonableness,” it is useful to note that for related-party broker commissions the MHP Guidelines limit the commission on the sale of market units to between 5% and 6%. The relevant calculations appear below:

<u>Commissions – Market Units</u>	<u>Amount</u>
Market Unit Sales	\$ 6,329,300
Commissions Reported	317,195
Total Allowable Commissions	<u>314,205</u>
Difference	<u>\$ (2,990)</u>

### **Marketing/Lottery Costs – Affordable Units**

Again, in this area, while not in effect during the relevant period, the MHP Guidelines which limit Marketing and Lottery costs to the greater of \$20,000 or 3% of the sum of affordable unit sales provide a means of assessing “commercial reasonableness.” However, according to the Cost Certification there were no commissions paid on the 4 affordable units.



## Hard Costs – For Informational Purposes Only

One issue in cost certification of Chapter 40B developments is whether construction costs are inflated in an effort to increase developer return. For this reason, MassHousing’s August 2007 Cost Certification Guidance (not applicable to this development) introduces, for purposes of establishing a “safe harbor” of hard construction costs, RS Means data.

RS Means is recognized as an independent cost authority in the home construction business. The RS Means “Cost Data” guides provide reasonably accurate cost information to help developers, contractors and others project costs for new construction when only a general description of size and amenities is available. For purposes of our review, we used, for comparison purposes only, new home construction cost data from the RS Means Residential Cost Data Guide 2005, 24th Annual Edition (“RS Means”).

The cost certification results were compared to the RS Means 2005 Base Residential Cost Per Square Foot, and Carriage Lane’s total square footage of 30,880 was based upon information reported by the Developer in the construction loan application submitted to MassHousing. MassHousing estimates that the reported cost per square foot was approximately \$5 lower than the RS Means residential construction cost and approximately \$15 lower than the safe harbor cost per square foot. See calculations below.

<i>Hard Costs</i>	Amount
Total Residential Construction – Cost Certification	\$ 3,163,382
Total Square Footage	30,880
Cost Per Square Foot – Cost Certification	\$ 102.44
<i>Calculations</i>	
RS Means Residential Construction Cost	\$ 107.08
Safe Harbor Percentage Factor	110%
Safe Harbor Cost Per Square Foot	\$ 117.79
Cost Per Square Foot – Cost Certification	\$ 102.44
Difference	<u>\$ 15.35</u>

## Soft Costs

### **(Developer’s) Overhead**

The total developer’s overhead charged to the project according to the Cost Certification is \$138,100. Of these costs, \$134,100 were paid to Linda Marrone, the wife of developer Alan Marrone, and this was a related party expense. Again, since this transaction predated the MHP Guidelines, the applicable standard here is one of “commercial reasonableness.”

Staff requested additional documentation from the Developer to support the commercial reasonableness of this expense. The response from the Developer indicated that Linda Marrone had

the role of clerk of the works, responsible for all administrative and bookkeeping duties of the project.

Overhead expenses were a significant focus of the work that resulted in the MHP Guidelines. The MHP Guidelines, in this instance, represent not a determination to change policy (as was done by adopting the "Uniform Land Value Policy"), but rather an effort to further define or explain the then existing "commercially reasonable" test. As a result, Daniel Dennis (CHAPA's accountant) determined in its August 10, 2007 report that it would disallow overhead in excess of the MHP Guideline standard. MassHousing has done likewise.

<u><i>Developer's Overhead</i></u>	<u>Amount</u>
Total Developer's Overhead – Cost Certification	\$ 138,100
MHP - Allowable Developer's Overhead Per Unit	\$ 4,000
Total Units	16
MHP - Total Allowable Developer's Overhead	<u>\$ 64,000</u>
Difference	<u>\$ (74,100)</u>

Since the overhead charged to the project exceeded what was commercially reasonable, we have disallowed \$74,100, decreasing total development costs.

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**Appendix A**

Summary of MassHousing's Review of Cost Certification  
Carriage Lane LLC

	Developer's Cost Certification	Adjustment	Draft Final
Sales			
Market	6,329,300	-	6,329,300
Affordable	660,000	-	660,000
Total Project Sales	6,989,300	-	6,989,300
Project Costs			
Land	1,064,000	10,000	1,074,000
Building	-	-	-
Total acquisition costs	1,064,000	10,000	1,074,000
Residential Construction	3,163,382	-	3,163,382
Site Preparation	361,693	-	361,693
Landscaping	253,517	-	253,517
Furniture & Fixtures	-	-	-
Hard Cost Contingency	-	-	-
Total hard costs	3,778,592	-	3,778,592
Architectural	117,722	-	117,722
Survey and permits	31,635	-	31,635
Engineering	37,524	-	37,524
Legal - real estate	140,620	-	140,620
Legal - organization	1,615	-	1,615
Title and recording	36,946	-	36,946
Accounting	31,383	-	31,383
Marketing	13,977	-	13,977
Real estate taxes	11,864	-	11,864
Insurance	85,329	-	85,329
Appraisal and market study	10,000	-	10,000
Construction loan interest	116,448	4,461	120,909
Financing/application fees	500	-	500
Utilities	28,923	-	28,923
Overhead	138,100	(74,100)	64,000
Brokerage commissions and marketing	317,195	(2,990)	314,205
Soft cost contingency	-	-	-
Total (soft) other project costs	1,119,781	(72,629)	1,047,152
Total development costs	5,962,373	(62,629)	5,899,744
Profit from Sales	1,026,927	62,629	1,089,556
Profit Percentage	17.22%		18.47%
(Excess) Profit contributed to Municipality	-		-
Max allowable (20% of total costs)	1,192,475		1,179,949

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**Appendix B**

I/Ch40B/MonInst/DevCert  
10.6.06

### DEVELOPER'S CERTIFICATE

This Certificate is provided in connection with the cost certification of Carriage Lane, LLC (the "Developer") for a Chapter 40B development known as Carriage Lane (the "Development"), located in Sudbury, Massachusetts (the "Municipality"), for purposes of assisting the Massachusetts Housing Finance Agency, as Project Administrator (the "Project Administrator") authorized by the Department of Housing and Community Development ("DHCD") under *Guidelines for Housing Programs in Which Funding is Provided Through a Non-Governmental Entity* (the "Guidelines"), in determining the Developer's compliance with the limitations on profit from the Development allowable under the Guidelines and Chapter 40B.

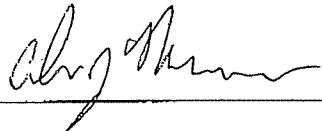
The undersigned hereby certifies to the Project Administrator, DHCD, CHAPA and the Municipality, under penalties of perjury, as follows:

1. The information contained in the Schedules of Chapter 40B Maximum Allowable Profit from Sales and Total Chapter 40B Costs (the "Schedules") in the report of Sharkansky & Company LLP dated January 5, 2006 (the "Sharkansky Report") is accurate and complete. The Schedules are fairly presented in conformity with the instructions provided by the Project Administrator.
2. All amounts shown on the Schedule of Total Chapter 40B Costs in the Sharkansky Report have been paid other than items listed as accruals.
3. The Schedule of Total 40B Maximum Allowable Profit in the Sharkansky Report reflects revenue from all of the units in the Development.
4. Except as noted on Exhibit A attached hereto, none of the amounts listed on Schedule of Total Chapter 40B Costs were paid to a Related Party. A "Related Party" is (i) any person that, directly or indirectly, through one or more intermediaries, controls or is controlled by or is under common control with the developer; (ii) any person that is an officer of, member in, or trustee of, or serves in a similar capacity with respect to the developer or of which the developer is an officer, member, or trustee, or with respect to which the developer serves in a similar capacity; (iii) any person that, directly or indirectly, is the beneficial owner of, or controls, 10% or more of any class of equity securities of, or otherwise has a substantial beneficial interest (10% or more) in, the developer, or of which the developer is directly or indirectly the owner of 10% or more of any class of equity securities, or in which the developer has a substantial beneficial interest (10% or more); and (iv) any relative or spouse of the developer. The Project Administrator reserves the right to determine whether the related party test should apply in any other case where it appears reasonable under the circumstances.

5. Except as set forth on Exhibit A attached hereto, there are no:
  - a. Sales of units to a Related Party
  - b. Purchases of materials/supplies from a Related Party
  - c. Purchases of services from a Related Party
  - d. Financing made with a Related Party
6. We have reviewed the information presented in the RS Means Schedule attached hereto (prepared by MassHousing as lender for the construction loan for the Development), and the schedule is an appropriate representation of the Development.
7. There are no developer overhead costs included in other line items on the Schedules.
8. There are no costs in the Schedules that are included more than once.
9. There are no costs listed in the Schedules that do not relate directly to the Development (except for permitted overhead expenses not duplicated in any other line item).
10. The costs shown on the Schedules are net of all rebates, adjustments, discounts, promotional or advertising recoupment or similar reimbursement made or to be made to the Developer or any Related Party.
11. We will retain all records underlying the information provided in the Schedules for a period of at least four years from the date the Project Administrator has accepted the final report of its reviewing auditor, and will allow the Project Administrator and the Municipality the right to inspect such records at reasonable times during the retention period.

EXECUTED under seal this 2 day of <sup>May</sup> April, 2007.

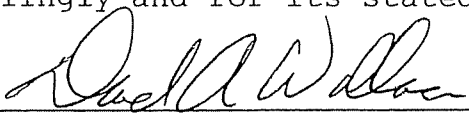
Developer:

Signature: 

Title: Manager

Commonwealth of Massachusetts  
Middlesex, ss May 2, 2007

On this date, Alan Marrone, personally known to me, appeared before me and acknowledged that he signed the preceding document willingly and for its stated purpose.

  
David A. Wallace, Notary Public  
My Commission Expires 8/16/07

## EXHIBIT A

### Disclosure of Related Party Transactions

#### Payments made to Related Parties:

Name of Payee	Nature of Relationship	Amount Paid
<u>Alan Marrone</u>	<u>Managing Member</u>	<u>\$ 41,964</u>
<u>Linda Marrone</u>	<u>Managing Member's Spouse</u>	<u>\$134,100</u>
<u>Roth Family, LLC</u>	<u>Investor Member</u>	<u>\$ 43,491</u>
<u>Alan &amp; Linda Marrone</u>	<u>Managing Members</u>	<u>\$425,000</u>

#### Sales of units to Related Parties:

Name of Payee	Nature of Relationship	Amount Paid
<u>None</u>	<u>None</u>	<u>\$-0-</u>

#### Purchases of materials/supplies from a Related Party

Name of Payee	Nature of Relationship	Amount Paid
<u>None</u>	<u>None</u>	<u>\$-0-</u>

#### Purchases of services from a Related Party

Name of Payee	Nature of Relationship	Amount Paid
<u>Alan Marrone</u>	<u>Managing Member</u>	<u>\$ 41,964</u> <u>Commission fees</u>
<u>Linda Marrone</u>	<u>Managing Member's Spouse</u>	<u>\$134,100</u> <u>Consulting fees</u>

#### Financing made with a Related Party

Name of Payee	Nature of Relationship	Amount Paid
<u>Roth Family, LLC</u>	<u>Investor Member</u>	<u>\$ 43,941</u> <u>Interest expense</u>

#### Other transactions with a Related Party

Name of Payee	Nature of Relationship	Amount Paid
<u>Alan &amp; Linda Marrone</u>	<u>Managing Member/Spouse</u>	<u>\$425,000</u> <u>Acquisition of land</u>