# How to Prepare a Supportive Housing Operating Budget

*Disclaimer: Corporation for Supportive Housing (CSH) is providing this information to assist interested organizations to develop a general understanding of the supportive housing development process. CSH is not rendering legal, accounting or other project-specific advice. For expert assistance, please contact a qualified professional.*

The Operating Budget is the tool used to analyze the expenses of a project during operations. It provides a listing of ongoing project expenses. The Operating Budget is critical to establishing the feasibility of the project. If accurately projected revenues (revenue projections are not covered in this document) are not sufficient to cover operating costs, real estate taxes, and debt service *over time*, the project cannot be deemed feasible.

The generic components of the Operating Budget are fairly constant from place to place around the county, but the terminology used to describe them sometimes varies. Even within the same locality, different lenders, investors and government funders may use different terms to describe what they are talking about.

Following are issues that need to be considered in preparing an Operating Budget:

- Costs can vary significantly from place to place and at different times;
- Cost projections that use actuals or good comparables are always best;
- Funders may require that certain underwriting standards be used;
- Operating and replacement reserves may be capitalized in the Development Budget or funded through the Operating Budget;
- Project specifics will determine costs (e.g. a project with elevators will use more electricity than one that does not);
- Vacancy factors should closely track the target population **and** local market conditions; low income housing projects **can,** and do, suffer market failure; and
- Debt service levels may have an impact on the ability of the project to support operating costs.

The three most critical aspects of evaluating the Operating Budget are:

1. **Is it complete?** Does the budget include all of the costs that the Owner/Property Manager will incur to properly maintain and manage a successful project? Recognizing that labels and categories vary from place to place, you will need to understand the project well and ask questions about the construction and management to clarify the extent to which the budget is complete.

2. **Is it accurate?** Evaluating the Operating Budget early in the development process can be difficult. As you get closer to construction, you gain more detailed knowledge about the project and can refine operating cost projections and budgets. The basic question is: what are the underlying assumptions in establishing operating costs, and are they reasonable?

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Note: This document is included within the D*evelopment and Finance* section of CSH's *Toolkit for Developing and Operating Supportive Housing*, which is available at [www.csh.org/toolkit2](http://www.csh.org/toolkit2).

3. The best assumptions to use are the actual costs for comparable projects. In addition, try to use local accepting underwriting standards for operating expenses. Other questions to consider in evaluating the accuracy of an Operating Budget are: what is the target population? What are the local market conditions? What is the local environment in terms of climate and utility costs? How will the type of construction affect operating costs? What role will the Owner play in operations? Is there a property management plan? And has the proposed Property Manager been involved in developing the operating projections?

**Is it realistic *over time*?** Unlike the Development Budget, which deals with the one-time costs of building the project, the Operating Budget deals with the continuing costs of operating the project over time. Therefore, multi-year projections should be carefully scrutinized to ensure that escalation factors are prudent given the nature of the project and expected economic conditions. For example, the impact of real estate abatements or exemptions that may decrease or expire over time should also be considered. The multi-year analysis should also make realistic assumptions about rental assistance, especially regarding the impact of renewals (or lack thereof) and tenant mobility. Also, have you trended the expense assumptions to cover the expected increases over the years of operation? Most projections assume that operating expenses will increase at between 2% and 5% per year.

The table that follows describes the typical items found in a supportive housing operating budget and provides guidance to determine the underlying assumptions and results. (Unless otherwise noted, all costs are quoted on an annual basis.) The order and grouping of these costs is typical of what is found in an actual maintenance and operating budget for supportive housing.

| Operating Expense | Cost Evaluation Approach |
| --- | --- |
| ***GENERAL & ADMINISTRATIVE*** | *Note that the costs described below are solely for the real estate operating costs, and do not include services and program costs that are typically found in supportive housing.* |
| ***Management Fee*** | This fee is intended to cover the cost of property management services, whether provided in-house or by a private firm. The allowable fee is usually set by the lenders' underwriting standards, and typically ranges from 6% to 8% of net rental income. In some locales, the fee is established based on a flat per unit per month rate, typically between \$35 and \$40. For small-scale projects, the higher percentage fee should be used, because of the inefficiencies of operating these projects. Note that the fee will not necessarily cover the real cost of in-house management, especially if your organization has a small portfolio and/or particularly complex management responsibilities (e.g., administering Section 8 or Low Income Housing Tax Credit compliance).<br><br>If this is the case, check to see if your management fee matches what it will cost you. If it's tight, make sure that you have adequate agency operating support to cover the full cost of property management. If the property |

management is being contracted out to a private firm, however, make certain that they have relevant experience with low-income and supportive housing projects. It is also important to confirm that the Property Manager has been involved in the design of the project and is committed to working closely with service providers to develop integrated management and service delivery protocols.

*Tax Credits*

When using an outside management firm, send a copy of the equity investor's Property Management Agreement and Addendum (if one exists) to the agent before their fee proposal is submitted to your organization. This is because equity investors will sometimes mandate specific fee agreement and contractual requirements. Ideally the firm should have experience in managing tax credit projects, since the reporting requirements are more complex than most traditional affordable housing projects.

***Office Supplies & Expense***

The cost of "other-than-personnel-services" ("OTPS"), office supplies, for example, related to on-site activities are usually part of the supportive services operating budget, and thus not included in the M&O budget. In limited cases, this cost cannot be supported by other sources, and if the lender allows, it can be included here. The cost is entirely driven by the staffing plan, and should be prepared as a budget detailing each cost.

***Legal & Accounting***

Legal expenses largely refer to the cost of carrying-out evictions ("dispossesses"). They can be estimated on a per unit basis, about $80 per unit, or on a per-project cost, usually about $2,000. This cost is difficult to project since it is not known how many tenants will be evicted each year until operating experience is gained. This could easily become a higher-than-projected cost if eviction rates are higher than anticipated, especially in the first year of operation. In this event, the additional cost would come from savings on other line items or from the operating reserve.

For accounting services, which include end of year tax filings and audit, projects generally allow about $2,000 to $5,000 annually.

*Tax Credits*

In the case of tax credits, there should be an increased allowance for accounting, since the reporting requirements to the Investors and tax filings are more extensive than projects that are not syndicated. Generally allow $10,000 to $12,000 for accounting in these cases.

***Annual Partnership Management Fee***

This fee only applies to projects syndicated under the Low-Income Housing Tax Credit Program. The fee is intended to compensate the General Partner (subsidiary of the sponsor) for the additional required reporting to the limited partners (largely financial in nature). The fee is set by equity investor's underwriting and is usually between $5,000 and $15,000, as determined by the complexity and scale of the project. This fee may be included as an operating cost, or may be paid to the extent of cash flow, after all other operating expenses are covered. Whether this is a "must pay" expense or funded from excess cash flow is negotiable with the Investors and is sometimes dictated by other funders' requirements.

***PAYROLL & RELATED***

Since supportive housing projects have limited rental revenue, they usually cannot support much in the way of program or services staffing costs without additional outside funding (e.g., HUD Supportive Housing Program).

***Administrative Payroll***

Some supportive housing projects will include limited administrative payroll costs in the operating budget, while others will fund it out of the supportive services budget. This cost may include such staff as: the Resident Manager, Administrative Assistant, Receptionist and Bookkeeper. The payroll cost is a function of the staffing plan, and should be detailed in as budget back up. If this cost is included, check with lenders to make sure it is allowable, and also compare with services budget to make sure that there are no redundant costs. The amount of the payroll cost is highly variable.

***Maintenance Payroll***

Maintenance staff costs typically include Superintendents, Janitors, Handypersons and occasionally, Housekeepers, and are generally charged directly to the operating budget. The number of maintenance staff is a function of the project's scale and maintenance demands (e.g., housing for persons with AIDS requires a higher maintenance standard to protect tenants with weakened immune systems). One standard for supportive housing calls for a full-time Superintendent, and in addition, one Janitor for every 40 units after the initial 40 units, up to 120 units; then one Janitor for every additional 80 units. This standard also adds one Handyperson for the first 100 units and an additional Handyperson for every 70 units thereafter. The overall goal of this maintenance standard is to maintain a ratio of 1:35 of Janitor/Handyperson to units.

The Superintendent's salary should be based on local standards, but make sure it is not set too low as it will be difficult to hire a qualified person. Typical salaries are $15,000 to $20,000, including fringe and an on-site 2-bedroom apartment. If an apartment is not provided, the Section 8 Fair Market Rent for a 2-bedroom unit should be added to the base salary. Janitors' salaries typically range from $12,000 to $15,000, and Handypersons salaries can range from $15,000 to $18,000. Review the maintenance payroll budget with the Property Manager to make certain that the salaries are properly set and consistent with local practices and the market. In high cost areas, the salaries noted above could easily be double.

***Security Payroll***

Security costs are sometimes included in supportive housing project operating budgets, though full coverage is difficult to accommodate. The security configuration and related costs are quite variable among projects, and are affected by such factors as: building scale, level of vulnerability of tenants, tenant involvement in building security, sponsor's philosophy, daytime staffing pattern, and the rate and nature of crime in the neighborhood. Most projects have at least evening and weekend coverage, and a front desk clerk typically handles security. Full security coverage -- 24-hour, 7 day -- requires approximately 5 full-time shifts (including allowances for vacation and sick time). Evening and weekend coverage -- about 4 full-time shifts -- may be sufficient for smaller projects or those with a strong staff presence during business hours.

Security costs are usually calculated on an hourly rate basis, which will vary significantly by location. These rates can range between $8 and $12 per hour, and may be lower if tenants are working under a stipend program. Full security coverage at $8 per hour translates into a total of $83,200 per year, plus fringe benefits. Check with other non-profit housing operators to verify local costs.

In some localities, security costs may be funded by a supportive services contract or tenant employment program. As noted earlier, it is generally difficult to support a significant share of the security costs in the M&O budget, so other sources should be identified to supplement them.

***Benefits, Payroll Taxes & Insurance***

In most cases, you will want to factor in the cost to provide health and retirement benefits as well as payroll taxes and worker's compensation insurance for your property management staff.

## ***UTILITIES***

***General***

Utility costs can vary widely among projects based on such factors as: efficiency of heating systems, energy ratings of insulation and windows, type of construction (new vs. rehabilitation), local climate, local utility rates, conservation practices of tenants and Property Managers, and air conditioning and ventilation systems. **Important:** Costs given in this section should be used with particular caution; utility rates vary a great deal from region to region. The best information will be from the actual, recent operating expenses of comparable projects in your area.

***Heating***

Heating costs for systems that are master metered and paid out of the project operating budget are generally projected on a per room or per square foot basis, and are typically part of the local lenders underwriting standards. If your project will be individually metered, see below. Annual heating costs for typical substantial rehabilitation projects in the Northeast are estimated at $175 per room (for #2 oil or gas) or $.90 per square foot (gross square footage). These costs can be estimated by an engineer (ask the project architect to request a projection from their engineer). While local utility companies can provide rough estimates, it is better to go through the engineer who is familiar with the building's systems and design. You can also consult with other property managers or non-profit developers to see what the actual costs are for comparable projects.

***Master Metering***

Some supportive housing projects have master-metered gas and electric (versus individual metering for each unit). Because usage is not metered individually for each tenant, these costs are estimated and then included in the rent. The Property Manager then pays the actual cost based on usage for the entire project. It is especially important that the costs are estimated accurately; if the cost is underestimated, the Owner, not the tenant, will end up paying the difference. These costs are then included in the rent and paid by the Owner. Gas and electric costs are usually calculated on a per unit basis, and are typically about $230 per unit for a studio apartment, and include common area costs. Check with other non-profit supportive housing providers operating comparable projects (similar population, design and appliances) to determine typical usage and costs. Note that if the project has unusual systems (e.g., central air conditioning) the estimate should account for the atypical usage.

***Individually Metered***

In some cases electricity as well as gas for heating may be individually metered (each tenant pays for actual usage) while cooking gas is still master-metered (and included in rent). Again, check with comparable projects to verify this cost. Typical costs for master metered cooking gas are $10 to $12 per unit per month, or about $140 per unit annually. It is important to note that if the tenants will be paying for their own heating costs, this will impact their contribution towards their rent payment as it would be a part of their

***Common Area Utilities***

Common area gas & electric is budgeted separately when tenants are responsible for their own utilities. This utility cost covers such areas as: public area lighting, on-site offices, elevators, activity rooms, commercial kitchens, congregate dining and laundry rooms. Typical charges are $37 per room for a "walk-up" building and $42 per room for an elevator building. Check with comparable projects to verify this cost.

Energy costs vary considerably across the country, and in areas experiencing energy shortages, rates are likely to climb considerably. The uncertainty surrounding gas and electric rates is a compelling reason to budget operating reserves conservatively. These rates, along with insurance costs, are probably the most unpredictable operating costs in the current environment.

***Water & Sewer***

Charges for municipal water and sewer services are based on either a lump sum "frontage charge" or on actual usage (as measured with individual water meters per building). Frontage charges are based on the width of the building, and are usually a poor indicator of actual usage, but easier to project reliably. If this system is used in your locality, verify the charge with the appropriate agency (often the department of finance or taxation). Be sure that the current rate is being used and that any anticipated increases are included in the projection. If the building will be individually metered, check with other comparable projects for usage and factor by the expected rate. Note that some localities are changing over from frontage systems to individual metering and that historical costs are not reliable. Frontage charges often understate the actual usage and individual metering can be a significantly higher cost. Family projects generally use significantly more water than projects housing individuals.

***Telephone***

Telephone costs for general administration and supportive services are generally included as an OTPS cost in the project's operating contract. However, if the cost is to be included in the M&O budget, check comparable projects. Comparable projects should have similar staffing plans, since staff levels largely drive this cost. Tenants are generally responsible for their own telephone costs.

## ***MAINTENANCE & REPAIR***

***Exterminating and Supplies***

This cost is for supplies used in routine cleaning and maintenance and the cost of regular extermination services. It is partly a function of apartment turnover, ease of maintenance (e.g., the presence of resilient floor covering vs. carpet), the use of outside vs. in-house extermination services, and the amount of common area space. Costs can range from $70 to $200 per unit, depending on these factors. Best to check with comparable projects of similar construction and that are managed similarly, or get actual vendor quotes, to verify these costs. In some localities, the underwriting will list "Exterminating" separately from "Supplies."

***Repairs***

This includes the non-personnel costs of repairs done by maintenance staff and the cost of repairs performed by outside vendors or under services contracts (other than elevator). These costs are affected by the intensity of use by tenants, the durability of the buildings systems and surfaces and the level of ongoing maintenance. Typical costs range from $200 to $250 per unit, and should be verified with comparable projects. Note that if the project does not involve substantial rehabilitation or new construction, this allowance should be adjusted upward (perhaps up to $300 or so per unit).

***Trash Removal***

This cost should only be included in budgets where municipal service is not available, and trash removal is performed privately or by the municipality for a charge. Consult the locality's department of public works to determine the policy. Note that some projects in commercial areas (e.g., downtown SRO's) may not have municipal service available. Verify private rates with garbage collection firms and/or other non-profit providers.

***Snow Removal/ Grounds Upkeep (Landscaping)***

This cost is usually included in the maintenance staff and supplies budget lines. However, if the project requires snowplowing service or special grounds upkeep beyond the scope of on-site maintenance staff, the cost should be included here. These costs are more likely to be incurred in suburban or rural settings where there are more extensive grounds to maintain. Verify the cost with contractors and/or other non-profit providers.

***Painting & Decorating***

This should cover the cost of painting the apartments and common areas on regular intervals, usually about every 3 years. Projects that anticipate a higher than average rate of turnover among tenants (in particular, transitional housing) should budget a higher amount, since the apartment units are generally re-painted upon turnover. Typical costs for painting are $35 to $40 per unit plus an allowance for common area of $100 to $150 per year per floor. On a 3-year cycle, this translates into $105 to $120 per unit for re-painting. Consult other non-profit providers for recent costs for re-painting.

***Elevator Maintenance***

If the project will have an elevator(s), the budget should include an elevator maintenance contract separate from the other maintenance costs. This is a very specialized service and is usually retained through an elevator maintenance firm on a contract basis. Typical costs here are $4,200 per elevator cab, though this can vary considerably among localities. Make sure that the projected cost is based on a real quote from a qualified firm or on a comparable project. Note that if a rehabilitation project does not involve major overhaul or replacement of existing elevator equipment, the cost can be significantly higher than the $4,200 per cab.

***Replacement Reserve***

This reserve is used to fund the cost of replacing furniture, appliances, carpeting and other building fixtures that have a limited useful life. Projects that expect an unusually high rate of tenant turnover should budget an additional allowance. Typical reserves are based on 2% to 3% of gross rental income, a percentage of the cost of construction, or approximately $150 to $250 per unit per year. For new construction or substantial rehabilitation, the reserve should build-up in the early years of operation (7 to 10 years), and be available to fund costs that begin occurring in the 10 to 15 year range. All projects must include a budgeted replacement reserve. These costs cannot realistically be funded from cash flow. Lenders will likely have their own underwriting standards for calculating the reserve, and tax credit investors may have standards for these reserves as well that must be adhered to.

## ***MARKETING & LEASING***

***Advertising/ Credit Investigations/ Leasing Fees***

The cost of marketing and leasing is usually not applicable to supportive housing since referrals are typically made through social services agencies or through outreach/intake staff (funded through operating contracts).

Advertising costs are generally not incurred. The cost of leasing the unit should be included in the scope-of-services of the Property Manager. These costs are more often found in rental or homeownership housing for families.

## ***TAXES & INSURANCE***

***Real Estate Taxes***

Many supportive housing projects will be able to receive real estate tax abatements or exemptions, depending on your locality's policies. Do not assume that the project will be exempt on the basis of non-profit ownership, as the operation of housing in and of itself is not considered to be a non-profit tax-exempt activity. Similarly, projects developed using tax credits are owned by for-profit entities and may not be eligible for tax programs targeted to nonprofit-owned affordable housing. If there is no abatement or exemption program available, the taxes should be projected on the basis of the assessed value of the completed project, at the tax rate likely to be in effect at the beginning of operation. Check with the local department of finance or taxation to determine the assessment policy (e.g., some localities do not assess at full value, but rather at a percent of value). Recently completed comparable projects are the best source of determining projected taxes. Make sure that you check whether there are other charges on the tax bill that your project would be responsible for. This can be done by reviewing the prior year's tax bill.

***Other Taxes or Fees***

Water and sewer charges (see "Utilities") are sometimes included under the category of "taxes." You may also have to pay for a local business license.

***Insurance***

The cost of premium payments for a comprehensive fire and liability insurance policy must be included and should be based on a quote from an experienced insurance broker. Since quotes are usually only held for up to 6 months, they are not a totally reliable source for projections. Better still is an estimate from an experienced broker for the insurance costs likely to be in effect at the time of operation. Property insurance is one of the most volatile costs, particularly in the current "post 9/11" environment, and a good broker will have a sense of where the industry is going. Short of a quote or estimate, assume about $2.50 per $1,000 of replacement cost (though the local standard may be quite different from this).

*Tax Credits*

Check with all financing sources, including the equity syndicator, on any specific insurance requirements. Be certain to forward any property insurance requirements to the broker before the quote or estimate is prepared.

Note: CSH's *Toolkit for Developing and Operating Supportive Housing* contains many other documents that may be useful for understanding supportive housing financing issues. Please see the tools under *Assembling the Financing* in the *Development and Finance* section of the *Toolkit*, at [www.csh.org/toolkit2development](http://www.csh.org/toolkit2development).