



## AUDIT REQUIREMENTS FOR MOHCD-FUNDED PROJECTS (updated March 14, 2016)

*This announcement was created to inform MOHCD-funded projects that MOHCD has established requirements for audits submitted as part of annual reporting. These requirements are applicable for reports that have due dates of 5/31/2016 or later. MOHCD will also include a reminder about these audit requirements in the annual email we send to owners listing the projects that are due to submit reports for the year.*

In 2013, the California Department of Housing and Community Development (“HCD”) & the California Housing Finance Agency (“CalHFA”) launched a joint [Audited Financial Statements Handbook](#). HCD and CalHFA are coordinating selected administrative functions such as the joint Audited Financial Statements Handbook to improve the State's ability to serve and coordinate housing needs and to achieve administrative efficiencies.

Both the Staff from HCD and owners of projects in the MOHCD portfolio that are subject to HCD reporting requirements have found the revised procedures to have been effective because:

- the requirement has fostered timely collaboration between project staff and project auditors **prior to** the HCD reporting deadline
- improved accuracy and completeness in initial reporting reduced the time needed to make corrections to reports and audits

MOHCD is aiming to make similar improvements to its reporting process through the creation of requirements for audits that are submitted as a part of MOHCD annual reporting. MOHCD informally surveyed several owners and auditors and found all parties to be in agreement with a proposal to change audit requirements. Based on that input, MOHCD has created the following audit requirements for all projects subject to MOHCD annual reporting, regardless of whether HCD is a funder of a given project. Please be advised of the following changes and requirements:

1. The deadline for completing audits and submitting the MOHCD Annual Monitoring Report (“AMR”) will be extended one month later than the prior deadline. For projects whose business year ends on 12/31, the AMR must be submitted by 5/31; for projects with whose business year ends on 6/30, the AMR must be submitted by 11/30.
2. For projects not owned by a single-asset entity and whose financial activity is accounted for and audited as part of the sponsoring, parent corporation’s finances, owners may request up to a one-month extension of the deadline to allow for additional time to complete consolidated audited financial statements for the parent corporation in accordance with the audit requirements.
3. The Supplemental Section of the project’s Audited Financial Statement must include an additional report which shall be titled “*Supplementary Information Required by MOHCD.*” The *Supplementary Information Required by MOHCD* must include:
  - a. Schedule of Operating Revenues
  - b. Schedule of Operating Expenses
  - c. Computation of Operating Cash Flow/Surplus Cash

d. Summary of Replacement Reserve and Operating Reserve Activity

4. To eliminate the need for additional data entry, the *Supplementary Information Required by MOHCD* template will be included as an additional worksheet in the MOHCD Annual Monitoring Report (“AMR”) workbook. Most of the fields in this worksheet are auto-filled with data that is entered on Worksheet 2. Project Owners/auditors may print this worksheet to create the required Supplemental Schedules in the Audited Financial Statement. Alternatively, the audit requirement may be satisfied by using a form generated by the Owner's accounting system or the Project's auditors, as long as the form includes all the elements contained within MOHCD's template.
5. The Independent Certified Public Accountant (auditor) must adhere to the American Institute of Certified Public Accountants (“AICPA”) and Yellow Book Independence Standards and must be aware of and file appropriate audit submissions as may be required by other governmental agencies, investors, etc. in their formats. The auditor must use professional judgment to add supplemental information and to determine the extent of testing necessary to support the opinion in the financial statements. The auditor must not be responsible for the preparation or the maintenance of the project's basic accounting, financial records or for creation of a trial balance. Although the auditor expresses an opinion on the financial statements, the financial statements themselves are the responsibility of the owner. It is the owner's responsibility to maintain adequate books and records and examine or review the financial statements before they are sent to MOHCD.
6. The following financial statement notes and supplemental information are required:
  - a. Capitalization Policy – summarize the project's capitalization policy.
  - b. Ground Lease – for projects with a ground lease, the notes to the Financial Statements must include a summary of the lease terms and conditions including the name of the lessor, identity of interests, whether the annual lease payment is an eligible operating expense or to be paid out of owner's allowable distribution, and if any portion of the annual lease payment is accruable or was accrued for the reporting period. If the lease payment is an authorized operating expense indicate the HUD Account charged.
  - c. Mortgages/Notes Payable – the interest rate, interest expense amount, maturity date, applicable mandatory payment amount, and beginning/ending principal and interest balance must be reported for each loan.
  - d. Distribution of Operating Cash Flow/Surplus Cash – refer to the applicable MOHCD Agreement(s) of the project to determine the distribution of operating Cash Flow/Surplus Cash. The notes to the Financial Statements must include a detailed narrative summary of allowable distributions of Surplus Cash that accurately reflects the requirements under all MOHCD agreements as well as the requirements of other funders and any other agreements that govern. In addition, a computation (showing the same list of allowable distributions included in the narrative summary) must be included that details the operating Cash Flow/Surplus Cash as described in the Regulatory Agreement(s). An adjustment must be made to this computation when withdrawals from the Replacement Reserve Account are greater than the amount capitalized, which indicates some of the withdrawals were included in operating expenses.

- e. Related Party Transactions Including Fees – all related party transactions including fees such as deferred developer fee, asset management fee and similar fees must be broken out in a schedule showing the following:
  - i. Name of the fee and the legal agreement requiring the fee.
  - ii. Fee amount, method of calculation and HUD Account # charged.
  - iii. Description of the Identities of Interest.
7. Upon completion of the audit, the auditor is to:
  - a. Express an opinion on whether the Partnership's (or other corporate owner) basic financial statements, including the notes to the financial statements, the accompanying supplementary information, and the results of its operations and its cash flows for the year(s) then ended, are presented fairly in all material respects. The opinion must state if the financial statements are prepared in conformity with accounting principles generally accepted in the United States of America.
  - b. Report on project compliance with laws, regulations and agreements and internal control over financial reporting in accordance with Government Auditing Standards. Auditors must be alert to situations or transactions in non-compliance with the Regulatory Agreement(s) or indications of waste, fraud, abuse, illegal expenditures and acts.
  - c. Provide a schedule of audit findings as deemed appropriate (including resolutions of prior period findings), comments and recommendations.
8. The auditor must notify MOHCD immediately if a scope limitation is placed upon the auditor in the course of performing the audit.
9. Although the owner may engage an auditor to perform non-audit type services outside the audit, the owner or the owner's representative must perform the management functions and make management decisions. The owner must certify to the completeness and accuracy of the financial statements and the certification in the audit.
10. As a reminder, three other important reporting requirements will remain unchanged:
  - a. AMRs submitted without the accompanying audit will be considered incomplete and will be insufficient to satisfy the reporting deadline. The failure to meet reporting deadlines will reflect negatively on the asset management capacity of the owner when it seeks funding or any other approvals from MOHCD.
  - b. The AMR must also be submitted to MOHCD electronically by the project owner as a separate excel file.
  - c. Residual Receipt payments should not be submitted to MOHCD until invoiced.

MOHCD's audit requirements are not as extensive as those contained in the HCD/CalHFA Audit Handbook. In order to advance the goal of streamlining across funders, MOHCD is deferential to the requirements in the HCD/CalHFA [Audited Financial Statements Handbook](#).

The auditor may contact the MOHCD Asset Management staff if technical assistance is needed pertaining to particular MOHCD programs, regulations or operations, especially if a potential conflict is

found when comparing MOHCD requirements against those contained in the HCD/CalHFA Audit Handbook.

MOHCD staff continues to be receptive to suggestions and appreciate the help provided by the accounting profession.

**Certain HUD Projects May Seek Exemption (Added 3/14/16):**

Some projects that have received certain types of support from HUD are subject to unique HUD reporting requirements. Projects may request an exemption from MOHCD's requirement to include the *"Supplementary Information Required by MOHCD"* in the Supplemental Section of the project's Audited Financial Statement for projects that meet ALL of the following criteria:

- The project has funding or another form of support from HUD that requires the project to annually file electronically with REAC (HUD's Real Estate Assessment Center); and
- The project is not participating in the City's Local Operating Subsidy Program ("LOSP"); and
- The project is owned by a nonprofit organization

Please contact the project's assigned representative from MOHCD's Asset Management Team to request an exemption.