

470 - AUDIT GUIDE POLICY

This policy provides guidance regarding the completion of the annual certified audit process for each development required to submit an annual certified audit to the Authority. The following topics will be covered:

- Purpose of the Annual Certified Audit**
- Audit and Payments Submission Deadlines**
- Developments Requiring a MSHDA Audit**
- Developments Requiring a MSHDA and HUD Audit**
- Developments *Not* Requiring a MSHDA Audit**
- HUD Audits Submitted to MSHDA**
- MSHDA Audit & Payment Submission Requirements**
- Audit Procedures**
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Purpose of Annual Certified Audit

Developments receiving MSHDA or American Recovery and Reinvestment Act (ARRA)-financing must submit an annual certified audit after the end of each fiscal year. MSHDA or “the Authority” administers a variety of housing programs on behalf of the Department of Housing and Urban Development (HUD), the Internal Revenue Service (IRS) and the State of Michigan. As the administrator of these programs and as a lender of money, the Authority requires the independent assessment of each development’s annual financial statements by an independent Certified Public Accountant (CPA).

The audit guide has been arranged to ensure auditors verify the compliance with the various housing program regulations and requirements. The audit criteria described in the audit guide establishes the **minimum** level of review required by auditors. Auditors may supplement the criteria to accommodate their own individual firm’s standards or audit approaches, as necessary.

Audit and Payments Submission Deadlines

April 30th is the Annual Certified Audit and Schedule 1 payments deadline.

January 25th is the tax and/or insurance deficit payments deadline.

Developments Requiring a MSHDA Audit

All developments are to complete and include in the audit report a Schedule 1 and 2 unless otherwise specified below. A Schedule 3 is required for all developments that have a security loan. The following development types must submit an annual certified audit to MSHDA meeting the requirements established in this audit guide:

- MSHDA and/or ARRA-financed developments (including Section 8 and 236), except developments exclusively:
 - Financed under the Neighborhood Preservation Program (NPP)
 - Preserved under the LIHPRHA Program
- Newly Constructed Developments (occupied *prior* to July 1st) - If occupancy occurs *after* July 1st, the partial year audit may be deferred and included in the following year's audit.
 - Developments that are not final closed are not required to submit a Schedule 1 or 2 with the audit unless the development has received a small size and/or security loan.
 - Developments that do not have a construction loan with MSHDA are not required to submit an audit until the permanent loan is closed.
- Preserved developments or developments which have ownership changes from the result of a sale (including Section 8 and 236) - The audit must cover the period from the sale closing through the end of the year. If there are less than 60 days remaining until the calendar year-end, the audit may be deferred and included in the next year's audit.
- MSHDA-owned developments (foreclosure or deed in lieu) – These developments do not need to submit a Schedule 1 or 2 with the audit.
- Rural Development (RD) financed developments that have ARRA financing and/or MSHDA HOME funds.
 - RD developments that have MSHDA HOME funds, and are **not** ARRA financed must submit a copy of the RD audit and submit a MSHDA Schedule 1 and 2.

Developments Requiring a MSHDA and HUD Audit

Section 8 developments that have preserved by financing with MSHDA and have a signed “Assignment of Housing Assistance Payments Contracts” must submit both a MSHDA and a HUD audit. MSHDA does **not** require a copy of the HUD audit.

Developments *Not* Requiring a MSHDA Audit

The following development types do **not** need to submit an annual certified audit to MSHDA if none of the above applies:

- Developments exclusively financed under the Neighborhood Preservation Program (NPP);
- Developments exclusively preserved under the LIHPRHA Program;

- Federally-insured developments;
- Paid-off and don't have any remaining Section 8 subsidies or use restrictions. If a paid off development still has HUD subsidies, refer to the section "HUD Audits Submitted to MSHDA" for the audits submission requirements.
- Rural Development (RD) financed developments that do **not** have ARRA-financing and/or a MSHDA HOME loan).

Refer to the "Developments Not Required to Submit an Audit" (Attachment 5) for developments currently identified in these categories.

HUD Audits Submitted to MSHDA

Paid-off developments where MSHDA administers the Section 8 subsidy and limited dividend payments are restricted must submit a copy of the HUD audit or Annual Financial Statement prepared by an independent certified public accountant. These audits or financial statements must be sent to MSHDA in hard copy within **90 days** of the fiscal year-end or ownership's fiscal year-end.

Submit the original and one copy of the HUD audit to:

MSHDA
 Asset Management Division
 Attn: Mitch Rademacher
 735 E. Michigan Ave.
 Lansing, MI 48912

Note: These developments must comply with Handbook 2000.4 REV-2 CHG-2, "Consolidated Audit Guide for Audits of HUD Programs", dated December 2001. Refer to the "Developments Not Required to Submit an Audit" (Attachment 5) for a list of these developments.

MSHDA Audit & Payment Submission Requirements

The following items must be completed by the designated due date for all audit submissions in order to achieve the *premium management fee factors* for a development:

1. Upload Documents - The following documents must be uploaded by the auditor through the web portal by April 30th. **Upload and submission instructions will be provided under separate cover at a later date.**
 - Excel Audit Template (CSV file) - The CSV tab of the Excel audit template must be saved as a CSV file.
 - Audit Template (Excel file) – The Excel template with all tabs in Excel format.
 - Audit Report (PDF file) – The audit report must include the sections specified in the "Audit Report Requirements and Examples" (Attachment 4).

2. Submit Documents – The above documents must be submitted by the owner through the web portal, once the auditor has completed the upload by April 30th. **Upload and submission instructions will be provided under separate cover at a later date.**
3. Tax and Insurance Deficits - Must be submitted by January 25th for the previous calendar year.
4. Payments Due per Schedule 1 - Any checks and/or MSHDA-held reserve transfer requests determined by the Schedule I must be submitted by April 30th.
 - Management Agents must clearly state the intended purpose of each payment when the payment or transfer is submitted to inform the MSHDA Finance division where to deposit the funds. Unidentified payments will be deposited in the development's Operating Reserve Cash account until the intended use of the funds can be identified. Payments allocated after the deadline will affect the management agent's eligibility for premium management fees or could create an open conditions on the management agent or owner.

Audit Procedures

Attachment 1 includes the audit procedures MSHDA requires to be completed by the auditor.

Audit Procedures – Capitalization of a Development

Attachment 2 provides the auditor with detailed audit procedures for determining the capitalization of a development upon completion of construction.

Compliance Report

The Independent Auditors' Report on Compliance and on Internal Control over Financial Reporting Based on an Audit of Financial Statement Performed in Accordance with Government Auditing Standards ("Compliance Report") is the reporting of any internal control or non-compliance issues.

Questionnaire – The "Compliance Report Questionnaire" (Attachment 3) is completed to determine if any compliance or internal control weaknesses exist which must be reported in the "Compliance Report". Any question answered, "No" represents a compliance or internal control weakness and requires an explanation in the compliance report of the audit.

Schedules 1

The Schedule 1 is a calculation of the surplus funds that are available for distribution and a calculation of certain repayment obligations. Each development is to complete the standard Schedule 1 unless they have been assigned to a revised Schedule 1. A list of the revised Schedule 1's is included in the "Modified Schedule 1 Summary" (Attachment 6).

Schedule 2

The Schedule 2 is an annual summary of the funds available for distribution and the funds received from the first year of operation through the current year including any prior years carry forward. A Schedule 2 must be submitted starting with the year the development final closed. For the purpose of this report, the first (initial) year of operation shall begin on the **first day following the cut-off date** and shall end on the last day of the development's initial calendar year of operation. For the initial year, the limited dividend payment must be prorated from the first day following the cut-off date. **The limited dividend payment cannot be paid until the development has final closed.**

Limited Distribution Payments

- **If cash has been transferred from the development's operating account to the partnership's account, to pay non-operating expenses, or to reduce a payable to the partners, that cash is considered a limited dividend payment paid on Schedule 2.**
- The Authority will determine the maximum limited dividend payment that may be disbursed based on the financial position of the development as of the year-end certified audit. Disbursements for approved limited dividend payments must be made in accordance with the MSHDA-approved Limited Dividend Payment Policy and Procedures.

Schedule 3

The Schedule 3 is an annual reconciliation of the security loan. This schedule is only required to be completed by developments which have a security loan.

Agreed-upon Procedures

“Audit Report Requirements and Examples” (Attachment 4) includes an example of the required format of the Independent Auditor's Report on Applying Agreed-upon Procedures to be submitted to MSHDA as part of the audit submission.

Excel Audit Template Description and Instructions

An Excel audit template is posted on the MSHDA website. A template must be completed for each development and is part of the audit submission process.

Input Tab

The instructions for completing the template are included on the Input tab. This tab populates the calculations performed on the Schedule 1, Schedule 2, and Schedule 3 tabs.

Schedules 1 Tab

The Schedule 1 tab is auto-filled based on the information entered on the Input tab.

Definitions for each of the line items on the Schedule 1 are included on the definition tab of the Excel audit template. These definitions are hyperlinked. A couple of items which require further clarification for the audit submission process follow:

- Replacement Reserve Needs – All Replacement Reserve Needs amounts **must** be reported on the Schedule 1. MSHDA sends a Replacement Reserve Needs Report to the management agent after the end of each calendar year. **Do not use** the Replacement Reserve Needs amount reported on the Activity Statement received from Finance.
 - Comprehensive Needs Assessment (CNA) - Replacement Reserve Needs applies to developments that have a CNA with a Plan 2. The only exceptions to this rule are developments that have some type of workout. Revisions to the Replacement Reserve Needs amount can only be made by MSHDA; Contact Amy Rollis at rollisa@michigan.gov for further information about a replacement reserve needs amount.
- Tax and Insurance Analysis - The tax and insurance analyses are prepared by MSHDA's Finance staff and sent to management agents in December. The analysis reflects the development's current tax escrow, insurance escrow, and the net escrow deficit or surplus. **Revisions to the tax and insurance analysis can only be completed by the MSHDA Finance division staff.**
 - Deficits – If the analysis reports an escrow deficit in either account, the MSHDA Finance division will try to fund the deficit from the: Tax or Insurance Escrow account's surplus, Operating Reserve Cash Escrow, or DCE Interest Escrow.
 - Total Escrow Deficits - If the net of the tax and insurance analysis resulted in a deficit, and there are not sufficient funds from the above escrows to fund the deficits, then the outstanding amount must be funded by January 25th. If the deficit is NOT funded by January 25th, then the deficit is required to be reported on the Schedule 1.
 - Total Escrow Surplus – If the net of the tax and insurance analysis resulted in a surplus, the surplus is automatically transferred by December 31st, to the Operating Reserve Cash Escrow. If the transfer occurred in December, the surplus is not to be reported on the Schedule 1.

Schedule 2 Tab

The Schedule 2 tab is auto-filled based on the information entered on the Input tab. The Schedule 2 in the Excel audit template must match the copy submitted in the PDF of the audit report.

- Developments that use a Schedule 1-B have a Schedule 2 that is revised. The Excel audit template will automatically use the Schedule 2-A for these developments.

Schedule 3 Tab

The Schedule 3 tab is auto-filled based on the information entered on the Input tab. The Schedule 3 in the Excel audit template must match the copy submitted in the PDF of the audit report.

Compliance Tab

The Compliance tab must include an explanation of all items with “No” answers identified on the “Compliance Report Questionnaire” (Attachment 3) or other internal weaknesses or non-compliance issues discovered during the audit process.

The Compliance tab includes the following sections:

- Internal Control Weaknesses
- Compliance Variance Notes
 - General ledger account variance reconciliations
 - Other non-compliance issues

UnadjItems Tab

This tab provides an area to record unadjusted items as specified in the Compliance Report Questionnaire.

Audit Report Requirements and Examples

Attachment 4 included the examples of required formatting and content to be included in the PDF of the audit report.

The PDF of the audit report must include the following:

- Independent Auditors' Report
- Balance Sheet
- Income Statement
- Statement of Owner's Equity
- Statement of Cash Flow
- Notes to Financial Statements
- Schedule of Unadjusted Items
- Compliance Report
- Schedule 1
- Schedule 2
- Schedule 3
- Agreed-upon Procedures

Contact List

Policy - Angie Witt at (517) 335-2010; e-mail: witta@michigan.gov –or – Lisa Espinoza at (517) 373-3276; e-mail: espinozaL@michigan.gov.

Excel Audit Template - Lisa Espinoza at (517) 373-3276; e-mail: espinozaL@michigan.gov.

ProLink Process - Nikki Miller by phone at (517) 373-1975 or by e-mail: millern@michigan.gov

Forms and Attachments List

Forms

Completed as part of the Excel Audit Template

470A1 – Schedule 1

470A2 – Schedule 2

470A3 – Schedule 3

470A4 – Compliance Reporting
470A5 – Unadjusted Item Reporting

Attachments

470 Attachment 1 – Audit Procedures
470 Attachment 2 – Audit Procedures - Capitalization of a Development
470 Attachment 3 – Compliance Report Questionnaire
470 Attachment 4 – Audit Audit Report Requirements and Examples
470 Attachment 5 – Developments Not Required to Submit an Audit (forthcoming)
470 Attachment 6 – Modified Schedule 1 Summary (forthcoming)

470 - AUDIT GUIDE POLICY
Audit Procedures

The following items must be part of the audit procedures completed during the audit process to properly perform an audit for MSHDA requirements.

Procedures	Completed	W/P
	<u>By</u>	<u>Date</u>
		<u>Ref.</u>

General Procedures

- | | | |
|--|--|--|
| <p>A. Review the client’s correspondence file for any significant transactions which have occurred during the current year and discuss with client. Inquire specifically of the client as to:</p> <ol style="list-style-type: none"> 1. Amendments to the Limited Partnership Agreement. 2. Transfers of partnership interest and/or partner address changes. 3. Changes in the estimated construction period. 4. Completion of construction. 5. Cost certification and final endorsement. 6. Additional limited partnership contributions. 7. Loans to partnership (i.e. Small Size/Security). | <p>_____</p> <p>_____</p> <p>_____</p> <p>_____</p> <p>_____</p> <p>_____</p> <p>_____</p> | <p>_____</p> <p>_____</p> <p>_____</p> <p>_____</p> <p>_____</p> <p>_____</p> <p>_____</p> |
| <p>B. Review the client’s permanent binder and update the Regulatory, Partnership, Loan, Workout, and Management Agreements or other such applicable legal documents.</p> | <p>_____</p> | <p>_____</p> |
| <p>C. Discuss all proposed journal entries with the client and obtain agreements thereto. Provide copies of entries and supporting details, as necessary.</p> | <p>_____</p> | <p>_____</p> |
| <p>D. Discuss all unadjusted items with the client and determine that the decision not to record the adjustments is the client’s decision. All unadjusted items must be listed in the Supplemental Schedule – “Schedule of Unadjusted Items”. All year-end differences of ten 10% and a minimum of \$3,000 must be listed.</p> | <p>_____</p> | <p>_____</p> |
| <p>E. Review of Subsequent Events:</p> <ol style="list-style-type: none"> 1. Inquire of and discuss with general partners, the management company and other executives having responsibility for financial and accounting matters as to: <ol style="list-style-type: none"> a. Whether any substantial contingent liabilities or commitments existed at the date of the Balance Sheet being reported on or at the date of inquiry. | <p>_____</p> | <p>_____</p> |

Procedures

Completed W/P
By Date Ref.

- b. Whether there have been any significant changes in the long-term debt, or cash flow to the date of inquiry. _____
- c. The current status of items in the financial statements being reported on, that was accounted for, on the basis of tentative, preliminary or inconclusive data. _____
- d. Whether any unusual adjustments had been made during the period from the Balance Sheet date to the date of inquiry. _____
- 2. Read the available minutes of meetings of partners. As to any meetings for which minutes are not available, inquire about matters dealt with at such meetings. _____
- 3. Make such additional inquiries or perform such procedures as considered necessary and appropriate to dispose of questions that arise in carrying out the foregoing procedures, inquiries and discussions. _____
- 4. Document your findings in a narrative. _____

F. Related Party Transactions

MSHDA considers Identity of Interest and related-party transactions to have occurred if an owner; management agent company or officers of the ownership or management company have an interest (financial or non-financial) in a vendor that provides goods and services to the development.

Identity of interest forms are submitted with the budgets and can be provided to you by the management agent or owner.

- 1. Determining the existence of related parties and identity of interest vendors:
 - a. Review prior year’s work papers for the names of known related parties. _____
 - b. Review mortgagor’s cost certification for disclosure of related parties, if not performed in a prior year. _____
 - c. Inquire of appropriate owner and management company personnel as to changes in related parties during the period. _____
 - d. Review Identity of Interest Disclosure Statements to ensure that all Identity of Interest–related parties that have performed work at the development during the year have been disclosed to MSHDA. _____
 - e. Review maintenance contracts and major contracts and vendor invoices to determine whether there are additional identity of interest relationships with the owner/agent that need to be reported to MSHDA and in the Notes to the Financial Statements. _____

Procedures

Completed W/P
By Date Ref.

- f. Review the Identity of Interest Disclosure forms submitted for the previous five years. If the Identity of Interest vendor had activity in the current year, verify that they included in the related-party section of the notes to the financial statements. _____
- 2. Identifying transactions with related parties:
 - a. Review the extent and nature of business transacted with major customers, suppliers, borrowers and lenders for indications of previously undisclosed relationships. _____
 - b. Review accounting records for large, unusual or nonrecurring transactions or balances, paying particular attention to transactions recognized at or near the end of the reporting period. _____
 - c. Review invoices from law firms that have performed regular or special services for the partnership for indications of the existence of related parties or related party transactions. _____
 - d. Determine source and terms of significant advances to and from the partnership. _____
 - e. Scan cash disbursements and journal entries for evidence of any payments made to the development owners or related parties. Determine whether the owner/management agent paid partnership management fees, asset management fees, incentive management fees and/or write-offs of related party receivables from funds other than surplus cash or distributions. _____
 - f. Scan the bank statements for any deposit, from the development owners and/or related parties, which would evidence that incorrect distributions or payments were made and that those funds were re-deposited into the development’s accounts before the audit. _____
 - g. For payments made to identity of interest vendors, determine whether the amounts exceed the amounts ordinarily paid for such services and supplies. The amounts ordinarily paid can be determined by comparing costs to similar disbursements noted during the cash disbursement analysis or from the auditors’ knowledge of amounts generally paid for services and supplies in the same geographic area, gained through the audits of other area clients. _____
- 3. Disclosure:
 - a. Disclosure in the financial statements of a reporting entity that has participated in related party transactions, individually or in the aggregate, must include the following:
 - (1) The nature of the relationship(s). _____
 - (2) The expense account accrued/expensed. _____
 - (3) A description of the work/services performed, including amounts. _____

Procedures

Completed W/P
By Date Ref.

(4) The dollar volume of transactions and the effects of any change in the method of establishing terms from that used in the preceding period.

(5) Amounts due from or to related parties and, if not otherwise apparent, the terms and manner of settlement.

(6) Provide a listing of amounts accrued/expensed from the development's operating account and the partnership's account. Include:

a. All non-cash transactions.

b. Relationship between the parties.

c. All accounts receivable and accounts payable, current and non-current, with other developments.

d. All receivables/payables between the development's operations and the partnership.

4. Document your findings in a narrative.

All owner transactions must be included in the Notes to the Financial Statements.

G. Discuss with the client and document any significant claims and litigation, both asserted and unasserted. Obtain and review information from partnerships' legal counsel pertaining to these matters.

H. Inquire as to the partnerships' compliance with applicable laws and regulations. Verify all transactions are legal.

I. Inquire as to whether the Owner is receiving any part of the Management Fee or any other compensation, contribution or payment of any nature from the Management Agent.

J. Obtain client representation letter.

K. Make arrangements to have correspondence relative to confirmations, cut-off statements, etc., prepared as of year-end and mailed.

Note: Confirmations of resident rent and security deposits are no longer required.

General Ledger Procedures

A. Review of Accounting System and General Ledger

All Transactions in the areas of revenue and expenses are recorded on the partnerships' books by the management agent. The managing agents typically do not include the general partner's cash activity; thus, the first journal entry should be to record the general partner's cash activity on the partnership's trial balance or general ledger.

Procedures

Completed W/P
By Date Ref.

Substantive testing of interest, property taxes, depreciation, management fees and amortizable items generally results in vouching approximately 80 percent of total expenditures.

Accordingly, this phase of the audit work must be performed at the location where these records are maintained. Additionally the following items must be reviewed:

1. Prepare or update narratives, which describe systems used by the management company in the collection and recording of revenue and in the payment and recording of expenses. _____
2. Summarize control weaknesses noted during the review and discuss the findings with the managing agent and/or general partner as deemed appropriate. Include in the applicable MSHDA compliance letter as deemed necessary. _____
3. Review the general ledger detail and journal entries for the year and investigate any unusual entries. _____
4. Foot the trial balance and trace balances to the general ledger. _____

The trial balance should include activity recorded by both the managing agent and the general partner. If not, a combining trial balance is necessary. _____

5. Reconcile the prior year's statement of partners' equity with the management company's records to ensure all prior years' journal entries were recorded. _____
6. Prepare financial statements for the partnership, making certain that the form and content meet applicable MSHDA reporting requirements. Note that the financial statements are to be prepared on the accrual basis. _____
7. Determine the extent of leasing activity and test compliance of significant leases with the applicable provisions. _____
8. Separate operations and partnership activity on the Balance Sheet and the Income Statement of the Financial Statements. _____

B. Cash

1. Review and test, as deemed necessary, the client's bank reconciliation at year-end for all bank accounts, including the general partner's account. Determine whether the client is reconciling cash monthly. _____
2. Determine the compensating balance or other restrictions applicable to any of the cash accounts and document in the work papers. _____
3. Obtain standard bank confirmations. _____
4. Determine whether all cash reported on the Balance Sheet is separated into the applicable partnership cash or operating cash accounts. _____

Procedures

Completed W/P
By Date Ref.

5. Inquire as to whether the client follows the practice of holding checks for later issuance to payees; consider the need to adjust cash and related account balances.

6. Review development’s operating account to determine that the **operating** account was established at a regulated institution with an office located in Michigan and in the name of the development. Also determine that the funds in the operating account are placed in a deposit account insured by an Agency of the U.S. Government, or invested in direct obligations of the U.S. Treasury.

C. Certificates of Deposit and Marketable Securities

1. Obtain standard bank confirmations.

2. Determine the compensating balance or other restrictions applicable to any of the Certificates of Deposit and Marketable Securities and document in the work papers.

3. Prepare or review an analysis of activity in these accounts for the year.

4. Examine or confirm with holder of securities as of year-end and determine that they are in the name of the partnership.

5. Reconcile interest income and interest receivable to respective accounts and test the reasonableness of same.

D. Accounts Receivable, Residents and Other

Accounts receivable, residents and subsidies should be analyzed with the related revenue accounts simultaneously and accounted for separately on the Balance Sheet.

1. Have the client prepare an aged trial balance of outstanding receivables.

2. Foot the trial balance and reference the total to the general ledger. Prepare entry, if necessary, to convert from cash to the accrual basis.

3. Review with a responsible official the collectability of all the outstanding balances and provide a reserve if required.

4. Have the client list the subsequent cash collections on outstanding accounts receivable.

5. Review the mortgagor/management agent’s formal, written rent collection policy. Determine if the rent collection was enforced with respect to the residents listed on the year-end Aging of Accounts Receivable.

6. Test accounts receivable to determine whether receivables are the result of routine operations and whether development funds have been loaned to the management agent, other developments, employees or the owner.

All accounts receivable on the Balance Sheet must be separated according to whether the receivable applies to the partnership or the development.

Procedures

Completed W/P
By Date Ref.

E. Prepaid Expenses

Prepaid expenses related to amounts paid from escrow should be analyzed with the escrow accounts. Any prepaid balances, which are individually less than \$300, should be expensed when paid.

1. Prepare or review a schedule showing beginning balances, additions, write-offs and ending balances for all prepaid accounts. Exclude from this schedule unamortized mortgage costs/fees, etc., which are considered elsewhere in this program. _____
2. Reconcile pertinent information to prior year's work papers. _____
3. Test additions by examination of invoices or by reference to an escrow disbursement. Examine insurance invoices, tax bills, invoices, etc., where applicable, to determine the propriety of accruals and prepaid balances. _____
4. Test computations of write-offs for reasonableness and reference to amounts charged to expense accounts. _____

F. Fixed Assets and Accumulated Depreciation

If the project was completely capitalized in prior years, the audit procedures in items 1 and 2 apply. If the project was not completely capitalized in prior years, the audit procedures in item 3 apply.

1. Project Capitalized in Prior Years
 - a. Prepare a summary of fixed assets showing beginning balances, additions, retirements, and ending balances. Also show the beginning balances, additions, reductions and ending balances for accumulated depreciation. _____
 - b. Schedule, or have the client schedule, additions and retirements during the year. _____
 - c. Vouch selected additions by examination of vendor invoices or other supporting documentation. _____
 - d. Examine supporting documents for fixed asset retirements. _____

2. Depreciation

If the project has been 100 percent capitalized in the past, calculate, and record depreciation expense for the period. For fixed assets acquired since December 31st, 1980, the appropriate cost recovery method should be used. There may be a significant difference between depreciation expense using the economic useful life criterion for GAAP and cost recovery under ACRS and MACRS. _____

3. Project partially or fully capitalized in the current year.
Use Attachment II procedures to perform the audit review. _____

Procedures

Completed W/P
By Date Ref.

G. Deferred Mortgage Costs

1. If the mortgage closing took place in a prior year, determine that the current-year amortization is in accordance with the accounting treatment which was previously selected. _____
2. If construction for the final mortgage closing took place during the year, vouch amounts recorded for these costs by reference to paid checks and/or copies of the Mortgage Draw Requests which detail the purposes for which funds are advanced. Note that amounts reflected on Mortgage Draw Requests do not necessarily represent amounts “paid.” _____
3. Determine the amortization period for the deferred mortgage costs and calculate the current year’s expense. _____
4. Prepare or update a work paper summarizing the treatment of the various mortgage costs. _____

H. Other Assets

Prepare account analysis where appropriate and examine documents in support of transactions as deemed necessary. _____

I. Mortgage Note Payable, Accrued Interest Payable and Deposits With Mortgagee

Mortgage payable, escrow balances, related prepaid expenses and other expenses should be analyzed simultaneously.

1. Prepare or have client prepare an account showing beginning balances, additions, payments and ending balances. _____
2. Reference beginning balance to prior-year work paper and ending balance to the general ledger. _____
3. Reference any additions to supporting documents. _____
4. Prepare an analysis of accrued interest payable and reference to general ledger. The effect of an interest subsidy must be considered. _____

Section 236 Interest subsidy should not be offset against interest expense on the financial statements. _____

5. Reconcile total principal and interest payments to total expected debt service for the year. _____
6. Test computation of interest expense and accrual for reasonableness. _____
7. Confirm the year-end mortgage note balance, interest payments, escrow account balances and other pertinent details with the mortgagee. For escrow accounts, request mortgagee to provide a detailed listing of all transactions for the year. _____
8. Determine whether the amount required to be paid in monthly to the replacement reserve fund has been paid as required. _____

Procedures

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9. If an allowable distribution was paid and 25% is required to repay a MSHDA-financed HOME loan, verify that:
 - a. A MSHDA-financed HOME loan payment was made; and
 - b. The amount paid equals 25% of the surplus cash for the previous year end. For example, if prior year’s surplus cash was \$100 and the owner is required to pay 25% of surplus cash to the MSHDA-financed HOME loan, verify that they paid \$25 on the MSHDA-financed HOME loan and the owners received a net amount of \$75.

Review the Regulatory Agreement and/or HOME Loan Note for exceptions.

Do **not** include HOME loans provided by local municipalities or counties.

J. Other Long-Term Debt

1. Obtain loan agreement and other supporting documents.
2. Determine that MSHDA approval has been obtained for the borrowing to the extent required by the Regulatory Agreement.
3. Prepare or have client prepare an account analysis showing beginning balances, additions, payments, and ending balance.
4. Test computation of interest expense and accrual.
5. Confirm outstanding balance with lender.

K. Trade Accounts Payable/Owner Advances

Analyze the trade accounts payable and owner advances before completing other Balance Sheet accounts. All payables and owner advances reported on the Balance Sheet must be separated according to its applicability to the partnership or the development.

1. Prepare or have the client prepare a trial balance of the year-end balance and reference to the general ledger.
2. Examine invoices/statements in support of the amounts on a test basis.
3. Perform a search for unrecorded liabilities and describe testing in a brief narrative.
4. For the current year ending, test the completeness of the Trade Accounts Payable/Accrued Liabilities/Surcharges on the MIE, Schedule B for December.
5. Prepare a schedule of unrecorded items. (These items are to be listed in “Schedule of Unadjusted Items” in the financial statements.

_____	_____	_____
_____	_____	_____
_____	_____	_____
_____	_____	_____
_____	_____	_____
_____	_____	_____
_____	_____	_____
_____	_____	_____
_____	_____	_____
_____	_____	_____

Procedures

Completed W/P
By Date Ref.

- 6. Determine if there have been **any** advances to the development’s operating account to pay for allowable operating expenses.

Any disallowed expenditures required to be paid back by the owner are not considered advances to the development’s operating account and are not considered to be repayable from the development’s operating account

L. Trade Accounts Payable – Construction

The balance in this account is the result of the capitalization process described in Attachment II. Prior-year and current-year work papers should contain an analysis of the sources of funds, which are going to be used to find this payable. The major sources are outstanding partners’ capital contributions, which are not specified for tax-deductible payments and the unfunded hard costs remaining to be disbursed under the construction loan.

M. Accrued Property Taxes

If property taxes are paid from escrow, they should be analyzed with the escrow balances.

- 1. Partnerships using the “Lien Date” method for expensing property taxes (Michigan Property Taxes):

- a. In Michigan, property taxes become a lien on the property on December 1 of each year and are usually payable between December 1, and February 15th of the following year.

- b. Examine the current year’s tax bills and record/adjust expense to equal the total of the current year’s tax bills.

- c. Prepare an analysis of accrued property taxes detailing the taxing authority, the fiscal year, the amount of tax, the year to which the tax applies, the beginning balance, additional accruals, payments, and the ending balance.

- 2. Partnerships under tax abatement programs making payments in lieu of property taxes (PILOT Program).

These payments are computed as a percent of shelter rents (gross rental income collected less development-paid utilities) and should be accrued and expensed in the period that the shelter rents arise.

- 3. For partnerships using the “assessment date” method for expensing property taxes:

- a. Property taxes may be accrued on the assessment date of the taxing authority and expensed in the year accrued if this election was made prior to February, 1973. This election is not available for Michigan property taxes after February, 1973, due to an Internal Revenue Service ruling.

Procedures

Completed W/P
By Date Ref.

- b. In order to determine the amount to be expensed, examine tax bills or call the Assessor’s Office of the local taxing authority. Prepare a work paper in connection with your call and be sure to include:
 - (1) Name, title and telephone number of person you talked to. _____
 - (2) The assessment date. _____
 - (3) The amount of the assessment. _____
 - (4) A calculation of the estimated tax, showing source of rates used. _____
- c. Prepare an analysis of accrued property taxes detailing the taxing authority, the fiscal year, the amount of the tax, the year to which it applies, the beginning balance, additional accruals, payments and ending balance. _____
- d. Correct prior year’s estimates of accrued taxes in the current year, as appropriate. _____
- e. If the assessment-date basis has been elected for expensing property taxes for accounting purposes, all taxes accrued during the year should be charged to expense. _____

N. Michigan Business Tax Accrual

- 1. Determine the partnerships’ liability for the single business tax as determined on the Michigan Business Tax Annual Return. If appropriate, ascertain that an accrual has been recorded. _____
- 2. Review reasonableness of expenses and accruals. Ascertain that only that portion of the management agent’s Michigan Business Tax expense directly attributable to the operations of a MSHDA-financed development are an allowable development expense. _____

O. Residents’ Security Deposits

- 1. Determine that the balance in the general ledger is supported by a detailed listing in a subsidiary ledger. _____
- 2. Determine that a separate bank account or a surety bond is used to protect security deposits as required by federal and state statute and MSHDA requirements. _____

A surety bond can be used for all developments with the exception of those financed under the Section 8 Program. _____

- 3. If a surety bond is applicable, verify the surety bond exists and is for the appropriate amount. _____
- 4. Determine that, where appropriate, security deposits have been offset against delinquent accounts receivable or the costs of refurbishing apartments that have been vacated. _____

Procedures

Completed W/P
By Date Ref.

5. Verify that the Security Deposit Liability is accounted for in accordance with MSHDA’s “Guidelines for Completing the Monthly Income and Expenditure Report,” dated **January 2010 or later**. (Obtain MIE Guideline information from the MSHDA website.)

6. For new construction Section 8 developments whose Agreements to Enter Into Housing Assistance Payments Contracts (AHAPS) were executed on/or after **February 29, 1980**, resident security deposits must be placed in a segregated, interest-bearing account and the interest earned on the investment of residents’ security deposits must be allocated to the residents. Determine whether this requirement has been met. Test the computation of the allocation.

P. Other Liabilities

1. Prepare account analysis and trace total to general ledger.

2. Examine documents in support of transactions on a test basis and determine the reasonableness of the accruals.

Q. Partners’ Capital

1. Prepare account analysis showing all activity during the year.

2. Determine the year-end ownership and adjust for any transfers of interest occurring during the year under review.

3. Disclose the names of the current General Partner(s) and percentage of ownership and the names of all Limited Partners with ownership interest equal to or greater than 25% in the Notes to Financial Statement.

Disclose the names of all Board Members’ positions and terms for those developments organized as a non-profit corporation in the Notes to Financial Statement.

4. Obtain supporting documents for any changes in the partnership.

5. Obtain an understanding of the owner/management agent’s procedures for determining surplus cash and making distributions.

6. Scan minutes of board or partnership meetings for discussions authorizing distributions.

7. Determine whether distributions taken during the audit period exceeded the amounts calculated and/or authorized for that period.

8. Determine whether any cash distributions during the year were in accordance with the Regulatory Agreement, other controlling documents and other MSHDA guidelines.

R. Income and Expense

1. Perform a detailed comparative analysis of year-end balances using comparative trial balances with the prior year and investigate any unusual fluctuations.

Procedures

Completed W/P
By Date Ref.

- 2. Determine nature and amount of rent subsidies, including MSHDA resident-based subsidies deposited in the development’s operating account. Check for possible unrecorded receivables. _____
- 3. If the partnership receives Section 236 rent subsidies: _____
 - a. Review Excess Income Reports to ascertain that there is no liability to HUD for excess rents. These amounts are frequently called “surcharges.” _____
 - b. If the owner has elected to retain excess income Pursuant to **HUD Notice H 04-13**, determine if the owner has received HUD approval. _____
 - c. Review the HUD approval letter to determine the appropriate uses and time period for which the excess income is being retained. _____
 - d. Determine if the excess income funds have been retained or used for the authorized purpose and time period. _____
- 4. Review the mortgagor’s/management agent’s formal, written rent collection policy and determine if the policy is being uniformly enforced. _____
- 5. Compare actual rental income to maximum rental income; i.e., 100 percent occupancy, to determine if the rent collections are reasonable. Prepare a reconciliation between rent potential and net rental income. Factors to consider are vacancies and non-rental units. Trace one month’s activity from the MSHDA report to the general ledger rent roll. _____
- 6. Determine whether the management fees expensed or accrued for the year do not exceed the maximum allowable approved by the Authority. The Authority requires an annual submission of a Management Agreement/Addendum with the yearly development budget package. The Management Agreements automatically renews and the management fees and development-assigned staff will be approved via an annual updated Management Agreement or addenda to the Management Agreement. _____
- 7. Verify with the management agent that management fees paid to prepare the **current year’s MIE** Reports were deducted from the management fee. _____

 If the preparation of the MIE Reports is subcontracted, the cost must be recorded as part of the management fee. _____
- 8. Verify no developer/consulting fees are paid from the development’s operating account. _____
- 9. Verify that the all costs associated with the preparation and processing of payroll, including check disbursements and any associated processing fees or service fees are paid from the management fee and not the development’s operating account. _____
- 10. Determine that fees paid to the general partner or developer is in accordance with the Partnership Agreement or Confidential Memorandum. _____

Procedures

Completed W/P
By Date Ref.

- 11. Determine if the staff positions, listed in the Authority-approved **current year's** development budget, are employees of the approved management agent.

The Authority requires an annual submission of a Management Agreement/Addendum with the yearly development budget package. The Management Agreements automatically renews and the management fees and development-assigned staff will be approved via an annual updated Management Agreement or addenda to the Management Agreement.

- 12. Determine the reasonableness of other charge-backs by the management agent.

- 13. Prepare an analysis of miscellaneous income and expense accounts, as deemed necessary.

- 14. Perform a test of at least 10% of the subsidized (**restricted rent rate**) resident files verifying the monthly rent payable by the resident, the amount of security deposit paid by the resident, and the completeness of the resident's eligibility certification forms.

- 15. Verify audit fees are within MSHDA-approved limitations. Refer to annual cover memo for the annual maximums.

- 16. Determine whether vacancy loss is greater than an increase of 15% of total rental revenue or if the change in vacancy loss between the current year and the prior year is greater than an increase of 5% and \$5,000. If so, the following steps should be performed:

- a. Determine whether gross rent potential and vacancy loss were properly calculated.
- b. For all revenue accounts, scan the detailed general ledger. Review the supporting documentation for all material manual entries and unusual entries.
- c. Determine the reason for the increase or cause of the high vacancy rate via discussion with the management agent. You may also want to select a sample of vacant units and perform tests to substantiate the high vacancy rate. Possible tests in the sample include but are not limited to the following:
 - (1) Reviewing the move-out notice from the resident.
 - (2) Reviewing documentation from the move-out inspection.
 - (3) Determining whether the security deposit was refunded to the resident.
 - (4) Reviewing the itemized list of damages and charges provided to the resident, which was used to reduce the amount of security deposit due back to the resident.

- d. Inspecting the vacant unit if the unit is still unoccupied.

Procedures

Completed W/P
By Date Ref.

- e. Determining the period when the unit was vacant by questioning development personnel, including the resident manager and the building manager. _____
- f. Reviewing work orders to determine the period when the unit was vacant. _____
- 17. Determine whether bad debt expense is greater than an increase of 10% of total rental revenue or whether the change in bad debt expense is greater than an increase of 5% and \$3,000 between the current year and the prior year. If so, the following steps should be performed: _____
- a. Obtain an understanding of the owner/management agent’s procedures for collecting delinquent debt and policy for writing off debt. _____
- b. Determine whether delinquent accounts are sufficiently pursued according to procedures. _____
- c. Select a sample of accounts written off to bad debts expense and review supporting documentation to determine whether debt was written off in accordance with policy and generally accepted accounting principles. _____
- d. Determine the reason for any activity on the resident record after the debt was written off. _____
- S. Insurance
- 1. Verify that there is Property & Liability Insurance policies providing coverage for the entire fiscal year. _____
- T. Retirement Plan
- 1. Determine if the management agent has a pension plan for the development’s on-site staff. _____
- 2. Determine if the pension plan has been approved by MSHDA. _____
- 3. Determine if the pension plan is being administered in accordance with the MSHDA-approved pension plan. _____
- U. Tax Credit Expenses (applicable to Section 236/8 developments)
- 1. Tax Credit compliance fees, legal fees, compliance inspection fees and Tax Credit compliance specialist whose duties include auditing of tax credit files, preparation of year-end tax credit report for MSHDA or training of development staff regarding Tax Credit compliance are not allowed for Section 236 or Section 8 developments. HUD has determined that these costs are not an allowable development operating expense. _____
- 2. If these costs have been accrued or expensed, the development’s operating account is required to be reimbursed from the partners. _____
- V. General Ledger Account Variance Testing
- 1. Perform the following testing of general ledger account variances to verify which accounts are required to have the details of their variances included in the Compliance Report. Following is an explanation and example. _____

For year-end, differences of ten percent (10%) and a minimum of \$3,000 in the accounts listed below; provide a reconciliation and explanation in the “Compliance Report.” To compute the ten percent (10%) difference, the difference between the two amounts must be divided by the audited balance.

The reconciliation must begin with the balance reported on the Monthly Income and Expenditure Report (MIE) and reconcile to the amount reported on the Balance Sheet of the audit. The reconciliation must include items not reported on the MIE, all adjustments, etc. Both of the following items will result in an unacceptable audit submission:

- a. An explanation without accompanying reconciliation or
- b. Reconciliation without an accompanying explanation.

The following accounts must be tested for a significant variance:

- a. Operating Cash - Operating Checking Cash (OC), Savings (SC), Certificates of Deposit (CDC), Petty Cash (PC)
- b. Residents Accounts Receivable (A1)
- c. Other Residents Accounts Receivable (A10)
- d. Subsidy Accounts Receivable (A2 & A3)
- e. Escrow Draws Receivable (A11)
- f. Non-Resident Receivables (A12)
- g. Related Party/Affiliate Receivables (A13)
- h. Other Receivables (A14)
- i. Trade Accounts and Surcharge Payable (L1), Liabilities - Accrued Expenses (L2) and Any Other Short-Term Operating Liabilities (L10) and Year-end balances.
- j. Other Long-Term Liabilities (L8 & L9)
- k. Other Liabilities (L10)
- l. Security Deposit Liability (SDL)
- m. Security Deposit Funded (SDC)
- n. Related Party/Affiliate Contributions/Advances (F4 & F5)
- o. Prepaid Rent (L3)
- p. Vacancy Loss (1b)
- q. Marketing Rent Concessions (1e)
- r. Other Income – Other (2i)
- s. Management Fees (4a)
- t. Premium Management Fees (4b)
- u. Payroll:
 - i. Marketing (5b)
 - ii. Administrative (7a)
 - iii. Maintenance (11a)
 - iv. Janitorial (12a)
 - v. Grounds (13a)
- v. Auditing (7h)
- w. Other Administrative Miscellaneous (7k)
- x. ARRA Regulatory Fees (20c)

Cumulative LD payments and premium management fees that have not been approved, real estate taxes, mortgage interest and any other non-operating liabilities are not to be included.

The following provides an illustration of the MSHDA-required reconciliation and explanation for an accounts payable difference of 10% and a minimum of \$3,000:

Trade Accounts Payable/Accrued Liabilities/Surcharges per the MIE:	\$38,422
Operating Trade Accounts Payable/Accrued Liabilities/Surcharges per the Balance Sheet:	<u>\$57,202</u>
Difference	<u>\$18,780</u>
Percentage Difference =	32.83%

The percentage difference was calculated by dividing \$18,780 by \$57,202.

An example of Trade Accounts Payable/Accrued Liabilities/Surcharges and Any Other Short-Term Liabilities Reconciliation

Balance per MIE	\$38,422
Reconciling items:	
<u>Amounts not reported as Trade Accounts Payable on the MIE</u>	
Lansing State Journal	1,116
Management Supply	8,700
Misc. vendor invoices less than \$1,000 each	1,003

Note: Miscellaneous vendor invoices of less than \$1,000 each do not need to be identified separately.

<u>Amounts not reported as Accrued Liabilities on the MIE</u>	
Consumers Power	6,771
<u>ADJUSTMENT</u>	
Error in recording Detroit Free Press payable	<u>1,190</u>
Balance per the Balance Sheet	<u>\$57,202</u>

The amounts identified as not being reported as trade accounts payable on the MIE represent invoices received after the December MIE was prepared.

Procedures

Completed W/P
By Date Ref.

W. Financial Reports

1. The audit must contain the following or its equivalent:

- a. An opinion on the fairness with which the mortgagor's statements show the financial position, the results of operations and changes in financial position of the project. _____
- b. An opinion as to whether the supplemental financial information is fairly stated in all material statements taken as a whole. _____

Procedures

	Completed	W/P
	<u>By</u>	<u>Date</u>
		<u>Ref.</u>
c. The accountant’s report should refer to the accompanying “Compliance Report”	_____	_____
d. The “Compliance Report” MUST report whether or not a Management Letter was issued. If a Management Letter was issued, the letter MUST be included with the audit.	_____	_____
2. A General Partner of the partnership must certify that they have examined the statements and, to the best of their knowledge and belief, they are a true statement of the financial condition as of the statement date.	_____	_____
3. The PDF of the annual financial report must consist of:		
a. Balance Sheet (partnership accounts are to be separated and identified separately)	_____	_____
(1) Verify that all general ledger accounts that are required to be separated per the Balance Sheet example in Attachment 4 are separated.	_____	_____
b. Income Statement	_____	_____
(1) Verify that all general ledger accounts that are required to be separated per the Income Statement example in Attachment 4 are separated.	_____	_____
(2) Verify all apartments or commercial space occupied but not producing income is shown as an expense under the applicable expense classification and a supporting schedule submitted to convey the names of such occupants together with their connection with the development. If none, so state.	_____	_____
(3) Verify extra services, such as the cost of providing congregate, enhanced or assisted service (i.e. food, laundry, housekeeping etc.) are paid from funds other than mortgage loan proceeds, development income or residual receipts. Income/losses from congregate enhanced or assisted services are not to be co-mingled with other income and cannot be deposited into the development’s operating account. If these funds have been co-mingled, state so in the “Compliance Report”.	_____	_____
c. Statement of Partners’ Equity.	_____	_____
d. Statement of Cash Flow.	_____	_____
e. Notes to Financial Statements.	_____	_____
f. Supplemental Data.	_____	_____
(1) Schedule of Unadjusted Items	_____	_____

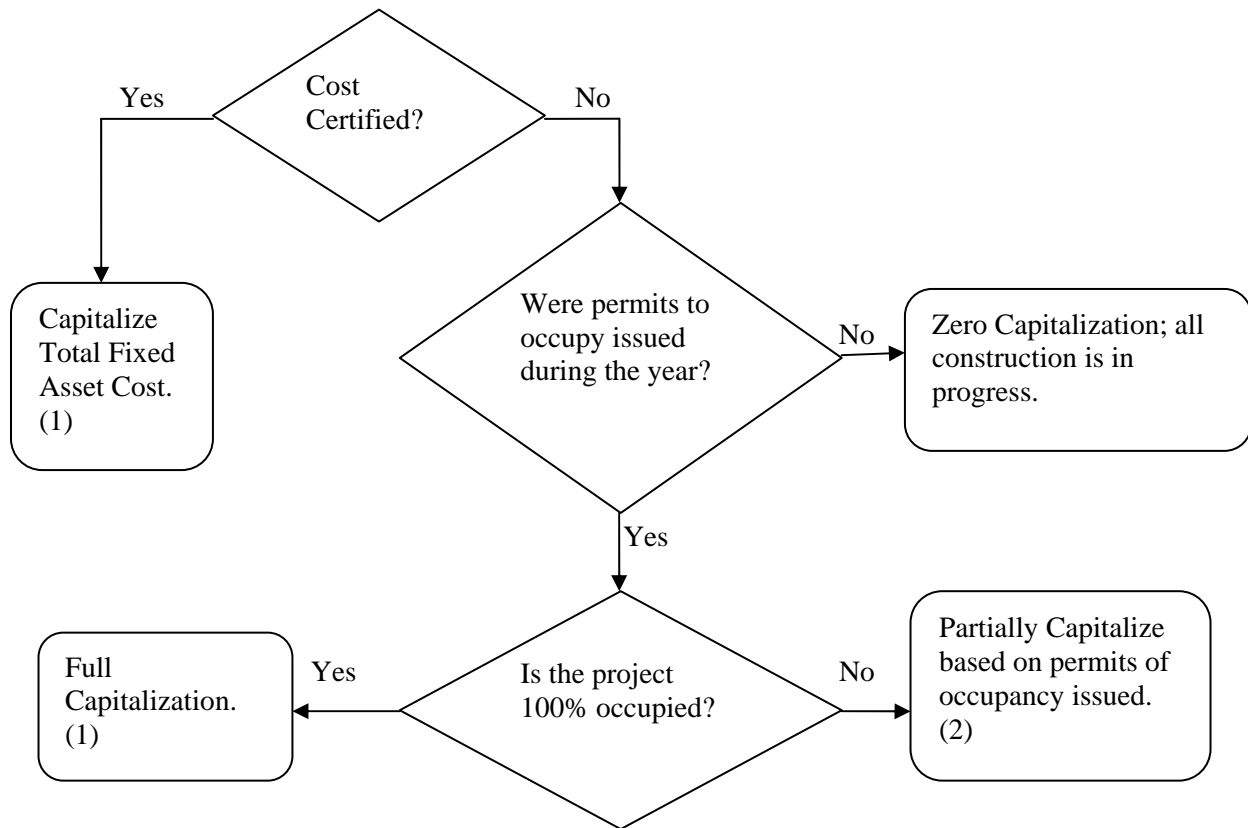
470 - AUDIT GUIDE POLICY
Capitalization of a Development

This attachment includes the following sections:

- Determining Capitalization**
- Capitalization of a Cost Certified Project**
- Capitalization of a Project not Cost Certified**
- Depreciation**
- Construction Period Interest and Other Carrying Costs**

Determining Capitalization

If the project has not been 100 percent capitalized in the past, you must analyze the project as of year-end and determine what amount (if any) must be capitalized. The following “**decision tree**” may assist in evaluating the present status:



- (1) See “Capitalization of a Cost Certified Project” for full capitalization steps.
- (2) See “Capitalization of a Project not Cost Certified” for partial capitalization steps.

Capitalization of a Cost Certified Project

The sum of (a) the partners' capital contributions and (b) the end mortgage proceeds shown below represents the total cost of a completed project to the limited partnership. To determine the ultimate fixed asset cost of the project consider the components of the total costs that have been or will be expensed in a manner other than through depreciation (for example, interest during construction).

Computation of Fixed Asset Cost

Partners' capital contributions	\$ 000,000	(a)
Mortgage proceeds	<u>0,000,000</u>	(b)
Total cost of project	<u>0,000,000</u>	(c)
Less expensed or separately classified project costs:		
(3) Interest during construction	000,000	
(3) Taxes during construction	00,000	
(3) MSHDA commitment fee	00,000	
Title and recording fees	0,000	
(1) Land	0,000	
Legal and organizational	0,000	
(2) Guaranteed payments to partners	00,000	
Operating Assurance Reserve (if applicable)	000,000	
Operating Deficit Reserve (if applicable)	<u>000,000</u>	
Total costs expensed or classified separately from fixed asset or other asset accounts	<u>\$0,000,000</u>	(d)
Total fixed asset cost (c-d)	<u>\$0,000,000</u>	

- (1) Include here the actual cost of the land, which may or may not be the same amount shown on the Commitment Report.
- (2) If identified in the partnership agreement as other than cost of construction (e.g., "for managing the affairs of the partnership").
- (3) See the "Depreciation" and "Construction Period Interest and Other Carrying Costs" sections of this attachment for further clarification.

After computing the estimated total fixed asset cost, compute the portion of the total cost to be capitalized as of the audit date. Use the annexed "decision tree" as a guide in making the computation.

Capitalization of a Cost Certified Project	Completed		W/P
	By	Date	Ref.
1. Prepare a work paper in the annexed format computing the eventual cost to be allocated to fixed assets.	_____	_____	_____

Capitalization of a Cost Certified Project	Completed		W/P
	By	Date	Ref.
2. Use MSHDA Forms 12:003 and PSD 12:004 to compute the allocation of total fixed cost (as previously computed) to the various asset categories. The limited partnership agreement and/ or the project brochure may specify the “types” of asset categories, their useful lives, and the depreciation methods to be used. Prepare a work paper in the annexed format showing the computation.	_____	_____	_____
3. Prepare a journal entry to record fixed assets as computed above. Any residual debit or credit necessary to balance the entry (and clear out construction in progress and any miscellaneous construction-related accounts) should be to the “Accounts Payable-Construction” account. The “Accounts Payable-Construction” account should agree with amounts calculated by the general partner/contractor. Further, you must also determine that the partnership has the resources to make the required payments, principally from limited partners’ subscriptions receivable. For cost overruns, the partnership agreement should be closely reviewed.	_____	_____	_____

Example Allocation of Fixed Asset Cost

	Total	Buildings	Furniture and Fixtures	Land Improvements
Percent to total	100.0%	(3) 93.5%	(3) 1.4%	(3) 5.1%
(1) Total “Hard Cost” per Form PSD 12:004	x,xx,xxx	(2) x,xxx,xxx	(2) x,xxx,xxx	(2) xx,xxx
Cost to allocate	(5) <u>x,xxx,xxx</u>	(6) <u>x,xxx,xxx</u>	(6) <u>x,xxx,xxx</u>	(6) <u>xx,xxx</u>
Total fixed asset cost	(4) <u>x,xxx,xxx</u>	<u>x,xxx,xxx</u>	<u>x,xxx,xxx</u>	<u>xx,xxx</u>

- (1) Total of lines 1 through 41 – exclude lines 42 through 48 for purposes of this work paper.
- (2) Determined by an analysis of lines 1 through 41 of Form PSD 12:004. Group various line items based upon the line item description as it relates to the fixed asset categories.
- (3) Percentage of PSD 12:004 costs as they relate to the total of lines 1 through 41.
- (4) Enter the total fixed asset cost as computed on the “Computation of Fixed Asset Cost” work paper.
- (5) Amount derived (amount needed to make column foot).
- (6) Allocated based on percentages above.

Capitalization of Project Not Cost Certified

Capitalization of Project Not Cost Certified	Completed		W/P
	By	Date	Ref.
1. If the project was not cost certified but there were “Permits to Occupy” issued on some of the units during the year, a partial capitalization of the project is appropriate.	_____	_____	_____
2. Prepare a schedule showing the cumulative number of Permits to Occupy issued through year-end.	_____	_____	_____
3. By reference to the confidential memorandum, determine the estimated total cost per unit.	_____	_____	_____
4. Inquire if cost overruns exist which will impact on anticipated fixed asset cost. If so, revise the estimated total cost per unit.	_____	_____	_____
5. Multiply the estimated total cost per unit by the number of units for which permits have been issued.	_____	_____	_____
6. An anticipated allocation between fixed asset categories can be determined by reference to the confidential memorandum. To prepare the journal entry to set up the partial capitalization, multiply the amount determined in Step 4 above by the percentage allocation obtained from the confidential memorandum.	_____	_____	_____
7. If the project is 100 percent occupied, the project may be considered substantially complete and the above will result in a complete capitalization of the project. However, since the cost certification has not been finalized, it will not be possible to determine the exact allocation of the costs to be capitalized. Accordingly, there may be some minor reclassifications between fixed asset categories in the subsequent year when we have MSHDA Form PSD 12:004 available for the final fixed asset.	_____	_____	_____

Depreciation

A summary of the depreciation review requirements follows:

Depreciation	Completed		W/P
	By	Date	Ref.
1. If the project has been partially or fully capitalized during the current year, a special computation is necessary to determine the current year’s depreciation expense as described below. Reference should be made to the confidential memorandum for depreciation methods and rates (see item #4 below). Particular attention should be paid to the point in time at which depreciation begins. In general, it is permissible to begin depreciating a unit when it becomes ready for occupancy (Certificate of Occupancy has been issued).	_____	_____	_____
2. Compute what a full year's depreciation would be on the fixed assets capitalized as of year-end. (Fixed assets capitalized at year-end represent the cost of all units for which a Permit to Occupy has been issued as of year-end.)	_____	_____	_____

Depreciation	Completed		W/P
	By	Date	Ref.
3. Prepare a schedule of Permits to Occupy, by days, for the year.	_____	_____	_____
4. Prepare a schedule computing depreciation expense for the period.	_____	_____	_____

Construction Period Interest and Other Carrying Costs

"Capitalization of Interest Costs," requires the capitalization of construction period interest with the cost of the related assets. "Accounting for Costs and Initial Rental Operations of Real Estate Projects" deals with various other costs incurred during the construction period. A summary of these costs which have not been discussed elsewhere in this audit program are as follows:

Construction Period Interest and Other Carrying Costs	Completed		W/P
	By	Date	Ref.
1. <u>Pre-acquisition Costs</u> – Such costs are to be capitalized as project costs if all three of the conditions as noted in the pronouncement are met, otherwise, the costs should be charged to expense as incurred.	_____	_____	_____
2. <u>Taxes and Insurance</u> - These costs are to be capitalized during the construction period. Such costs should be charged to expense after the property is substantially completed.	_____	_____	_____
3. <u>Incidental Operations</u> - Revenue from incidental operations in excess of costs of incidental operations should be considered as a reduction of capitalized project costs. Such costs in excess of revenue should be expensed as incurred.	_____	_____	_____
4. <u>Costs Incurred to Rent Real Estate Projects</u> – Costs incurred to rent real estate projects should be capitalized if under operating leases they are related to and their recovery is reasonably expected from future rental operations. Note: The Internal Revenue Code requires the capitalization of construction period interest and taxes, except as they relate to low-income housing, and establishes the amortization periods for such costs.	_____	_____	_____
5. To avoid book/tax timing differences with respect to construction period interest, taxes and other carrying costs, it is suggested that the financial statements be prepared in accordance with the income tax basis of accounting. By doing so, the CPA will be in a position to express an unqualified opinion as to the fairness of the financial statements in accordance with the income tax basis of accounting.	_____	_____	_____

Forms

- PSD 12:003 – Mortgagor’s Certificate of Actual Cost
- PSD 12:004 – Contractor’s Certificate of Actual Cost

**MORTGAGOR'S CERTIFICATE OF ACTUAL COST
MICHIGAN STATE HOUSING DEVELOPMENT AUTHORITY**

TO: Executive Director
Michigan State Housing Development Authority

Development Number: _____
Development Name: _____
Location: _____

This Certificate is made pursuant to the provisions of the Building Loan Agreement dated _____. The cut-off date used for calculation of interest, taxes, and insurance during construction is _____.

The actual cost to the owner of labor and materials and necessary services for the construction of the physical improvements in connection with the subject development, after deduction of all kickbacks, rebates, adjustments, discounts made or to be made to the mortgagor, sponsor or any corporation, trust, partnership, joint venture or other legal entity in which they or any of them hold any interest, is as follows:

Line 1	Construction Costs	\$ _____
Line 2	Incentive Payments to General Contractors	_____
Line 3	Architect's fees	_____
Line 4	Interest during construction	_____
Line 5	Taxes during construction	_____
Line 6	Insurance during construction	_____
Line 7	Title and recording expenses	_____
Line 8	MSHDA fees	_____
Line 9	Legal costs	_____
Line 10	Off-Site costs	_____
Line 11	Tap fees	_____
Line 12	Equipment, furniture and fixtures	_____
Line 13	Overhead allowance	_____
Line 14	Miscellaneous	_____
Line 15	Total of lines 1 through 14	_____
Line 16	Sponsor's profit and risk allowance	_____
Line 17	Letter of credit and guarantee fees	_____
Line 18	Land	_____
Line 19	Total development cost (total of lines 15, 16, 17 and 18)	\$ _____
Line 20	Less – Amount of Authority mortgage loan	_____
Line 21	- Other non-equity funding sources	_____
Line 22	Mortgagor's equity for LD payment purposes	_____

NOTE: This certificate must be supported by a certification as to actual cost by an independent Certified Public Accountant in accordance with the Cost Certification Manual of the Michigan State Housing Development Authority, dated April 15, 1988.

The undersigned hereby certifies that, except as noted on the other side of this form, there has not been and is not now any identity of interest between the mortgagor and general contractor and/or any subcontractor, material supplier, or equipment lessors. It is further certified that, except as noted, there are not and have not been any such relationships between sponsor of this development and general contractor and /or any subcontractor, material supplier, or equipment lessors.

All references to "identity of interest" herein are made in the context of the definition appearing on the reverse side hereof.

(Mortgagor)

By _____

(Date)

Its _____

Identity of interest between the mortgagor and/or sponsor as parties of the first part and general contractors, subcontractors, material suppliers, or equipment lessors as parties of the second part will be construed as existing under any of the following conditions:

When there is any financial interest of the party of the second part; when one or more of the officers, directors or stockholders of the part of the first part is also an officer, director, or stockholder of the party of the second part; when any officer, director or stockholder of the party of the second part; when any officer, director or stockholder of the party of the first part has any financial interest whatsoever in the party of the second part; when the party of the second part advances any funds to the party of the first part; when the party of the second part provides and pays on behalf of the party of the first part the cost of any architectural services or engineering services employed by a general contractor in connection with his or its obligations under the construction contract; when the party of the second part takes stock or any interest in the party of the first part as part of the consideration to be paid them; when there exist or come into being any side deals, agreements, contracts or undertakings entered into or contemplated, thereby altering, amending or canceling any of the required closing documents except as approved by the Executive Director.

The undersigned hereby certifies that" (Cross out inapplicable language). There (has) (has not) been and is not now any identity of interest between ourselves on the one hand and the general contractor or any subcontractor, material supplier or equipment lessor on the other. Attached to and made a part of this certificate is a signed statement fully describing any identities of interest as set forth in the previous paragraph.

Mortgagor

By: _____

Its: _____

Date: _____

**CONTRACTOR'S CERTIFICATE OF ACTUAL COST
MICHIGAN STATE HOUSING DEVELOPMENT AUTHORITY**

TO: _____

Development No. _____

Development Name _____

City and State _____

Development Location _____

Gentlemen:

This Certificate is made pursuant to the provisions of the Construction Contract entered into by and between use under date of _____, and it is understood and agreed by the undersigned that this Certificate is to be submitted by you to the Michigan State Housing Development Authority.

The actual cost incurred in the completion of construction under the above Construction Contract and accepted construction changes, inclusive of all kickbacks, rebates, adjustments and discounts (except as allowed in the Cost Certification Manual) or any other devices having the effect of increasing the true actual cost is itemized below

No	Trade Item	Amount	Payee
1	Concrete		
2	Masonry		
3	Metals		
4	Rough Carpentry		
5	Finish Carpentry		
6	Weatherproofing		
7	Insulation		
8	Roofing		
9	Sheet Metal		
10	Doors		
11	Windows		
12	Glass		
13	Lath & Master		
14	Dry Wall		
15	Tile Work		
16	Acoustical		
17	Wood Flooring		
18	Resilient Flooring		
19	Painting & Decorating		
20	Specialties		
21	Special Equipment		
22	Cabinets		
23	Appliances		
24	Blinds & Shades, Artwork		
25	Carpets		
26	Special Construction		
27	Elevators		
28	Plumbing & Hot Water		
29	Heat & Ventilation		
30	Air Conditioning		
31	Electrical		
32	Community Building		
33	Other Accessory Buildings		
34	Modules		
35	Earth Work		
36	Site Utilities		
37	Roads & Walks		
38	Site Improvements		
39	Landscaping		
40	Unusual Site Conditions		
41	Off-Site Improvements		
42	Site Security		
43	Building Permits		
44	Bond Premium		
45	General Requirements		List Detail on Reverse Side
46	Builder's Overhead		
47	Builder's Profit		
48	Total		

Instructions for Preparation of this Form

1. Complete instructions are presented in the Authority's Cost Certification Manual for Mortgagors, Contractors and Independent Public Accountants, dated April 15, 1988.
2. The detail of expenditures for line items 1 through 45 is required. Line 45 is to be detailed below. If space is insufficient on this form for any line item, attach a schedule. Labor incurred by the general contractor may be shown in total by Trade item. Miscellaneous disbursements by the general contractor of under \$200 each may be aggregated by line item without disclosing payee.

ITEMIZED BREAKDOWN OF GENERAL REQUIREMENTS

ITEM	TOTAL	ITEM	TOTAL
Supervision		Cost Certification Expense	
Field Engineering			
Field Office Expense			
Temporary Facilities			
Temporary Utilities			
Cleaning and Rubbish Removal			
Enter on line 45 the lesser of the total hereon or the amount provided in the trade payment breakdown attached to the Construction Contract.			\$ <u> </u>

The undersigned hereby certifies that: (Cross out inapplicable language). There (has) (has not) been and is not now any identity of interest between mortgagor and/or general contractor on the one hand and any subcontractor, material supplier or equipment lessor on the other. Attached to and made a part of this certificate is a signed statement fully describing any identities of interest as set forth in the previous paragraph.

All amounts shown have been reduced to give effect to the amount(s) of any kickbacks, rebates, adjustments, discounts (except as allowed in the Cost Certification Manual), or any other devices which, if included, would have the effect of overstating the actual cost.

Contractor

By _____

Date _____

Its _____

NOTE: This certificate must be supported by a certification as to actual cost by an independent Certified Public Accountant.

470 – AUDIT GUIDE POLICY

Compliance Report Questionnaire

This attachment provides the parameters for the independent auditor's report on compliance and on the internal control over financial reporting based on an audit of financial statements performed in accordance with government auditing standards. The questions identified below provide the method for recognizing the importance of including specified items on the "Compliance Report".

The CPA is required to:

1. Review, evaluate, and comment on the adequacy of the accounting records, procedures and the system of internal controls maintained; and
2. If disclosed by the review, indicate the mortgagor's (partnerships') failure to adhere to certain specific provisions of the Regulatory Agreement, the Management Agreement, MSHDA directives and HUD regulations and procedures, as included in the HUD subsidy contract.

The mortgagor, in consideration of MSHDA's mortgage, has agreed to various controls and regulations of certain aspects of the development's operation such as limits on rental rates, rates of return, eligibility of residents, fiscal management, etc. These requirements are contained in the Regulatory Agreement which is incorporated in and made a part of the mortgage and the Management Agreement and addenda reviewed and updated annually. MSHDA's monthly reporting requirements are contained in the Monthly Income and Expenditure Policy, dated **January 2010 or later**.

The "Compliance Report" Questionnaire was developed to guide the CPA in his/her audit of compliance and internal control matters that are of particular interest to MSHDA. This questionnaire must be a permanent part of the CPA's working papers, which are subject to review by duly authorized MSHDA representatives.

Answers to the questions should be supported by a review of procedures and/or an actual test of transactions. **Any "No" answer, whether considered to be material or immaterial, is indicative of a potentially adverse condition which must be described in the "Compliance Report" unless the mortgagor has written permission from MSHDA to deviate from the regular mortgage requirements.** The work performed by the CPA is to be done on a test basis.

Compliance Report (CR) Questionnaire

Address any “No” answers in CR.

	<u>Yes</u>	<u>No</u>	<u>N/A</u>	<u>Ref.</u>
A. <u>Regulatory Agreement</u>				
The Regulatory Agreement between the partnership and MSHDA specifies requirements and covenants of the partnership in return for a MSHDA mortgage.				
1. Is the development current in the repayment of its loan obligations?	_____	_____	_____	_____
2. Has the development made distributions in accordance with the limitations specified in the Regulatory Agreement, other controlling documents or other MSHDA guidelines?	_____	_____	_____	_____
3. Has a test of accounts receivable determined that all development receivables are the result of routine operations and no development funds have been loaned to the management agent, other developments or the owner?	_____	_____	_____	_____
4. Related-Party Transactions:				
(a) Have all related-party transactions been disclosed in the format required by MSDHA in the Notes to the Financial Statement?	_____	_____	_____	_____
(b) Have all Identity of Interest entities doing business with the development been properly identified to MSHDA according to the Identity of Interest Policy? Verify this through review of Identity of Interest Disclosure forms.	_____	_____	_____	_____
(c) Have all disallowed expenses been noted in the Notes to the Financial Statement and the “Compliance Report”?	_____	_____	_____	_____
(d) Have all owner transactions not approved by MSHDA’s Board been identified?	_____	_____	_____	_____
(e) Has the owner/management agent paid all partnership management fees, asset management fees, incentive management fees and write-offs of related party receivables from surplus cash or distributions?	_____	_____	_____	_____
(f) Has a scan of the bank deposits identified that all deposits from the development’s owners and/or related parties for distributions are accurate?	_____	_____	_____	_____

Compliance Report (CR) Questionnaire

Address any “No” answers in CR.

	<u>Yes</u>	<u>No</u>	<u>N/A</u>	<u>Ref.</u>
(g) Has a review of maintenance contracts, major contracts and vendor invoices determined that there are no additional identity of interest relationships with the owner/management agent that need to be reported to MSHDA and in the Notes to the Financial Statement and the “Compliance Report”?	_____	_____	_____	_____
(h) Are the payments made to identity of interest vendors within the range ordinarily paid for such services and supplies?	_____	_____	_____	_____
5. Has MSHDA written approval been obtained:				
(a) For conveyance, transfer or encumbrance of the mortgaged property?	_____	_____	_____	_____
(b) For assignment, transfer, disposition, or encumbrance of any personal property of the development or disbursement of funds for other than reasonable operating expenses and necessary repairs?	_____	_____	_____	_____
(c) For conveyance, transfer or assignment of any beneficial interest in any trust holding title to the property, or the interest of any general partner, or any right to manage the property? Transfers must also assume the obligations of the Regulatory Agreement.	_____	_____	_____	_____
(d) For any amendment to the Partnership Agreement?	_____	_____	_____	_____
(e) To remodel, add to, reconstruct or demolish any part of the property?	_____	_____	_____	_____
(f) For the partnership to engage in any other business activity or incur any other liability or obligations?	_____	_____	_____	_____
(g) To permit the development to be used for any purposes other than those originally intended or to greater commercial use than originally approved by MSHDA?	_____	_____	_____	_____
B. <u>Insurance</u>				
1. Has the development’s insurance coverage been maintained as required by MSHDA?	_____	_____	_____	_____
C. <u>Books and Reports</u>				
1. Are the books and records maintained as prescribed by MSHDA and HUD guidelines?	_____	_____	_____	_____

Compliance Report (CR) Questionnaire

Address any "No" answers in CR.

	<u>Yes</u>	<u>No</u>	<u>N/A</u>	<u>Ref.</u>
2. Are the books and records in reasonable condition for potential examination by MSHDA?	_____	_____	_____	_____
3. Does the mortgagor/management agent make frequent postings (at least monthly) to the ledger accounts?	_____	_____	_____	_____
D. <u>Operating Activities</u>	_____	_____	_____	_____
1. Are all operating cash receipts deposited in the name of the development in a bank whose deposits are federally insured and located in the State of Michigan, or invested in direct obligations of the U.S. Government maturing within one year, or in money market funds investing solely in obligations of the U.S. Treasury?	_____	_____	_____	_____
2. Are all cash accounts, Certificates of Deposit and Marketable Securities free from encumbrances, i.e. not pledged or collateralized?	_____	_____	_____	_____
3. Does the management agent have a written policy discouraging the acceptance of cash on site?	_____	_____	_____	_____
4. Are security deposits, rent receipts and general partner's receipts kept separate and apart from each other in accounts maintained in the name of the development?	_____	_____	_____	_____
5. Where a security deposit account is required, does the mortgagor/management agent keep sufficient funds in the security deposit account to equal or exceed the aggregate of all outstanding obligations to the depositors including security deposit interest allocated to residents if the applicable AHAP's were executed on/or after February 29, 1980 ?	_____	_____	_____	_____
6. Where a security deposit account is not required, has the mortgagor maintained a surety bond in accordance with the requirements of the State of Michigan and for the appropriate amount?	_____	_____	_____	_____
7. From a 5% sampling, did the security deposit listed in the resident's file agree with the security deposit listed on the supplementary schedule of the security deposit account?	_____	_____	_____	_____
8. Did cash disbursements from the development's operating account exclude payment for items listed below:	_____	_____	_____	_____
(a) Legal expenses incurred in the sale or proposed sale of the property or the partnership interest;	_____	_____	_____	_____

Compliance Report (CR) Questionnaire

Address any “No” answers in CR.

	<u>Yes</u>	<u>No</u>	<u>N/A</u>	<u>Ref.</u>
(b) Advice to an owner on tax consequences of foreclosure; and	_____	_____	_____	_____
(c) Reimbursement to the owners or affiliates while the mortgagor is in default, under modification, forbearance or provisional workout arrangements for prior operating advance, capital expenditures and/or development acquisition costs?	_____	_____	_____	_____
(d) Developer/consulting fees.	_____	_____	_____	_____
9. Were all the required amounts as calculated by the Schedule I deposited, transfer requests received, or paid to the mortgagor within 120 days after the close of the mortgagor’s annual accounting period?	_____	_____	_____	_____
Exception: The Tax/Insurance Escrow Deficit payments are due by January 25.				
10. Excess Rental Collection in Section 236 Developments:				
(a) Were excess rental collections remitted to HUD each month according to HUD’s excess income reporting requirements?	_____	_____	_____	_____
(b) If the owner elected to retain excess income pursuant to HUD Notice H 04-13 , has the owner received HUD approval?	_____	_____	_____	_____
(c) Have the excess income funds been retained/used for the authorized purpose and in the appropriate time period?				
Note: If excess income funds were not used for the authorized purpose, the funds must be returned to HUD.				
(d) Were Section 236 excess rental collection submissions supported by the lease agreements and recertification documents?	_____	_____	_____	_____
11. Was the amount expensed and or accrued for the preparation of the annual certified audit within the MSHDA approved limits? The current year limits are included in the current years change memo.	_____	_____	_____	_____
12. Does the mortgagor/management agent have a formal, written rent collection policy?	_____	_____	_____	_____

Compliance Report (CR) Questionnaire

Address any “No” answers in CR.

	<u>Yes</u>	<u>No</u>	<u>N/A</u>	<u>Ref.</u>
13. Was the formal, written rent collection policy uniformly enforced with respect to the residents listed on the year-end Aging of Accounts Receivable?	_____	_____	_____	_____
14. Did the vacancy loss increase less than 15% of total rental revenue or was increase in vacancy loss between the current year and the prior year less than 5% and \$5,000?	_____	_____	_____	_____
15. Do resident accounts receivable on the MIE consist exclusively of rents due from current residents?	_____	_____	_____	_____
16. Did the bad debt expense increase less than 10% of total rental revenue or was the increase in bad debt expense less than 5% and \$3,000 between the current year and the prior year?	_____	_____	_____	_____
17. Was the MSHDA-financed HOME loan payment paid and deducted from the total surplus cash available for an allowable distribution?	_____	_____	_____	_____
E. <u>Management Agreement</u>				
1. Has a Management Agreement been approved by MSHDA?	_____	_____	_____	_____
2. Has there been compliance with any modifications to the Management Agreement made by MSHDA?	_____	_____	_____	_____
3. Are the expense charge-backs to the development in accordance with the provisions of the Management Agreement?	_____	_____	_____	_____
4. Was compensation to the management agent limited to the amounts prescribed in the Authority-approved current year’s development budget and/or the Management Fee Structure? Any overpayment/over accrual of management fees, regardless of dollar amount, must be explained in the “Compliance Report.”	_____	_____	_____	_____
5. Was the amount of management fees reported on the General Ledger equal to the annual total amount reported on the MIE Report?	_____	_____	_____	_____
6. Are all of the people on the staff listed in the Agreement or Addendum employed directly by the approved management agent?	_____	_____	_____	_____

Compliance Report (CR) Questionnaire

Address any “No” answers in CR.

	<u>Yes</u>	<u>No</u>	<u>N/A</u>	<u>Ref.</u>
7. Were all costs associated with the preparation and processing of payroll, including check disbursements and any associated processing fees or service fees paid from the management fee and not the development’s operating account?	_____	_____	_____	_____
F. <u>Payroll</u>				
1. Were the payroll tax charges by the management agent reasonable?	_____	_____	_____	_____
G. <u>Tax Credit Expenses</u>				
1. For Section 236 and Section 8 developments, were Tax Credit compliance fees, legal fees, compliance inspection fees and Tax Credit compliance specialist whose duties include auditing of tax credit files, preparation of year-end tax credit report for MSHDA or training of development staff regarding Tax Credit compliance expenses charged to the development’s operations? Repayment of disallowed charges is required from the partnership to the development’s operations.	_____	_____	_____	_____
H. <u>Retirement Plan</u>				
1. If there is a retirement/pension plan, has the plan been approved in writing by the MSHDA, Asset Management Division?	_____	_____	_____	_____
I. <u>Rents and Occupancy</u>				
1. Are dwelling unit basic rental rates and fair market rental rates in Section 236 developments the same as those shown on the rental schedule?	_____	_____	_____	_____
2. Is the rent that the development is receiving from commercial space equal to the amount set forth in the master lease agreements?	_____	_____	_____	_____
3. Are the numbers of non-revenue-producing dwelling units the same as the number shown on the MSHDA-approved operating budget?	_____	_____	_____	_____
4. From the 5% sampling, were rent renewals to residents made for a period of at least 30 days or more?	_____	_____	_____	_____
J. <u>Additional Services</u>				

Compliance Report (CR) Questionnaire

Address any “No” answers in CR.

	<u>Yes</u>	<u>No</u>	<u>N/A</u>	<u>Ref.</u>
1. Was MSHDA’s written approval obtained for the offering of additional services; i.e. individual air conditioners, laundry equipment, etc. not approved at the time of commitment?	_____	_____	_____	_____
2. Were the costs of providing the additional services to residents accounted for separately?	_____	_____	_____	_____
3. Was participation in any additional services voluntary and not a condition for occupancy; i.e. food service, cleaning service, carport rental, cable TV, etc.?	_____	_____	_____	_____
K. <u>Subsidy Payments</u>				
1. Were the amounts requested from HUD supported by the accounting records?	_____	_____	_____	_____
2. Were subsidy payments received and recorded in the proper accounts?	_____	_____	_____	_____
L. <u>Financial Reports</u>				
1. Does the PDF of the audit report and the Excel audit template consist of all items specified in the procedures section of the audit guide?	_____	_____	_____	_____

470 – AUDIT GUIDE POLICY
Audit Report Requirements and Examples

This attachment provides examples of the reporting format and content requirements to include in the PDF of the audit report. Any variation to the format or contents of the reporting requirements detailed below requires prior approval. Contact Lisa Espinoza or Angie Witt at MSDHA to request the approval. The audit report must include the following items:

Independent Auditor’s Report
Balance Sheet
Income Statement
Statement of Owner’s Equity
Statement of Cash Flow
Financial Statement Notes
Schedule of Unadjusted Items
Compliance Report
Schedule 1
Schedule 2
Schedule 3
Agreed Upon Procedures

Independent Auditor’s Report

The audit can be prepared on the accrual method or the income tax method. An example of the report using the full accrual method with an unqualified opinion is shown below. The contents below can be modified to allow the income tax method or the type of opinion:

Example

To the Partners of
(Project Name)
(City, State)

We have audited the accompanying Balance Sheet of (*partnership name of development name*), (a Michigan limited partnership), MSHDA Development No. 9999 as of *December 31, 2012* and the related Statements of Profit and Loss, changes in accumulated earnings and cash flows for the year then ended. These financial statements are the responsibility of the partnership's management. Our responsibility is to express an opinion on the financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit

includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, such financial statements present fairly, in all material respects, the financial position of (*development name*), MSHDA No. 9999 as of *December 31, 2012*, and the results of its operations, the changes in its cumulative income and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Our audit was conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The additional information of (*development name*), MSHDA No. 9999, on pages (*starting page #*) to (*ending page #*) is presented for the purpose of additional analysis and is not a required part of the basic financial statements. This additional information is the responsibility of the partnership's management. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

In accordance with Government Auditing Standards, we have also issued a report dated (*report date*) on our consideration of the partnership's internal control structure over financial reporting and on its compliance with certain provisions of laws, regulations, contracts, grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. This report is an integral part of an audit performed in accordance with Government Auditing Standards and should be read in conjunction with this report in considering the results of our audit.

Firm's Signature _____

Date: _____

Balance Sheet

The following list of accounts must be separated on the balance sheet:

- All partnership accounts must be separated from operating accounts
- Residents receivable
- Related party receivables
- All escrow balances
- Management fees payable
- Related party receivables and/or payables

Income Statement

The following list of accounts must be separated on the income statement:

- Partnership income and expenses must be separated from operating income and expenses

- Congregate services income
- Resident assistance payments
- Section 236 interest subsidy
- Vacancy loss
- Management fees expense
- Premium management fees expense
- Auditing fee expense
- Bad debt expense
- Congregate services expenses
- COE expenses
- Deferred developer fee

Statement of Partner’s Equity

The following is an example of the format required to report the Statement of Partner’s Equity:

	<u>Total</u>	<u>Partners’ Contributions</u>	<u>Accum. Cash Dist. To Partners</u>	<u>Accum. Losses</u>
Balance, beginning of year	\$ _____	\$ _____	\$ _____	\$ _____
Loss				
Subscriptions received during the year				
Cash distributions to partners	_____	_____	_____	_____
Balance, end of year	<u>\$ _____</u>	<u>\$ _____</u>	<u>\$ _____</u>	<u>\$ _____</u>

Statement of Cash Flow

MSHDA does not require any special formatting or contents for the statement of cash flow.

Financial Statement Notes

Required notes and detailed example of the notes follow:

Owner Advance – All owner advances must be noted in the notes and must include the advance amount and the repayment terms. If an owner advance is **not** going to be repaid from the developments operating account, the note must state the intention of non-repayment of the owner’s advance.

Example

Per the letter dated _____, the advance of \$_____ made to the development’s operating account will never be repaid from the development’s operating account during the MSHDA mortgage term.

Ownership Percentages

- The names of all general partners and their percentage of ownership
- The names of all limited partners with ownership interest equal to or greater than 25%
- The names of all Board Members’ positions and terms for those developments organized as a non-profit corporation.

Example

Organization - Under the terms of the Regulatory Agreement, executed in connection with obtaining the mortgage loan, MSHDA regulates rental rates and distributions to partners.

The General/Limited Partners of the Partnership are:

Managing General Partner - James Jones	.45%
General Partner - Ben Brown	.55%
Limited Partner - Sam Smith	99%

Notes Payable – If notes payables exist you must provide footnote disclosure relative to amount, date incurred, purpose, terms, creditor and balance due.

Related-Party Transactions - The following items must be noted in this section:

- Limited distributions, including any incentive management fees paid from the limited dividend payment, must be reported in this section.
 - If the limited dividend payment was disbursed from the development’s operating account during the year and has not been disbursed to the partners by the end of the year, this must be disclosed in the notes to the financial statements.

Example:

On (date), the limited distribution payment was disbursed from the development’s operating account. However, this amount has not been disbursed to the partners as of December 31, 2012.

- Identity of Interest and related-party transactions. This includes the management agent company or offices of a management company that have an interest (financial or non-financial) in a vendor that provides goods and services to the development. These vendors must have prior MSHDA approval in order to provide the goods or services to the development.
- Owner transactions not approved by MSHDA’s Board must be noted.

Example

Messrs. Jones, Brown and Smith, general partners, are officers of Erector Corporation. Erector Corporation and two of its officers own the company which manages the project.

****The required format for reporting related-party transactions is shown below:**

Name of Related Party	Relation-ship	Brief Description of Work/Services Performed	General Ledger Account	Partnership or Operating Account	Transaction Amount	Terms of Settlement
Erector Corp.	General partner is an officer	Painting Units	Painting Expense	Operating	\$ 8,000	Current payable
Erector Corp.	General partner is an officer	Painting Units	Accounts Payable	Operating	\$5,000	Current payable
Erector Mgmt.	General partner is an owner	Mgmt. fee	Accounts Payable	Operating	\$30,000	Deferred until payables are current.
Erector Mgmt.	General partner is an owner	Mgmt. fee	Mgmt. fee expense	Operating	\$12,000	Deferred until payables are current.
Joe Smith	General partner	Loan for operating deficit	Accounts Payable, General Partner	Operating	\$50,000	Deferred until refinancing or sale of development.
Joe Smith	General Partner	Investor Service Fees	Accounts Receivable, Owner	Partnership	\$10,000	Current
Joe Smith	General Partner	Investor Service Fees	Accounts Payable, Owner	Operating	\$10,000	Current

Schedule of Unadjusted Items

These items are to be presented in the PDF of the audit report, and the Excel audit template.

Example

The accounts payable balance per the financial statements is \$5,542. When the auditor tests the completeness of the accounts payable, the test discovers \$3,500 in unrecorded accounts payables. The \$3,500 must be listed on the schedule of adjusted items in the audit.

The auditor is not required to submit details of the variances in the audit report, but the details must be available upon request. Any additional explanation submitted on the schedule is encouraged.

The financial statement presentation would appear as follows:

DESCRIPTION OF VARIANCES	AMOUNT OF OVER/(UNDER) STATEMENT
<u>Unrecorded Accounts Payable (Dec.)</u>	\$3,500

Compliance Report

Independent Auditors' Report on Compliance and on Internal Control over Financial Reporting Based on an Audit of Financial Statements Performed in Accordance with Government Auditing Standards ("Compliance Report") is required to be included in the audit report in the format shown below.

Example

To The Partners of:
(Project Name)
(City, State)

We have audited the financial statements of (*Partnership Name*) MSHDA No. 9999, as of and for the year ended December 31, 2012 and have issued our report thereon dated (*report date*). We conducted our audit in accordance with generally accepted auditing standards and the standards applicable to the financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States.

Compliance

Compliance with laws, regulations, contracts and grants applicable to the (*Development Name*) is the responsibility of the (*Partnership Name*) management. As part of obtaining reasonable assurance about whether the financial statements are free of material misstatement, we performed tests of (*Partnership Name*) compliance with certain provisions of laws, regulations, contracts, and grants including compliance with specific provisions of the MSHDA Regulatory Agreement, MSHDA Directives and HUD regulations and procedures included in the HUD subsidy contract HOME requirements and MSHDA Multifamily Audit Guidelines. However, our objective was not to provide an opinion on overall compliance with such provisions. Accordingly, we do not express such an opinion.

The results of our tests disclosed no instances of noncompliance that we have reported herein under Government Auditing Standards.

However, we have noted certain immaterial instances of noncompliance that we have reported to management in a separate letter dated (*report date*). **(This paragraph needs to state if a management letter was or was not issued.)**

We have compared the December 31, 2012 Monthly Income and Expense Report submitted to MSHDA with balances in the financial statements for the year ended December 31, 2012 audited by us and covered by our report dated (*report date*). The account balances set forth therein are in material agreement (defined by MSHDA as differences not exceeding 10% and 1,000), except as noted on page (*page # of report*) of this report.

Internal Control over Financial Reporting

In planning and performing our audit, we considered (*Partnership Name*)'s internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weakness. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weakness.

Additionally, no management letter was issued in relation to our audit of the financial statement of (*Development Name*) as of and for the year ended December 31, 2012.

This report is intended for the information of the Partners, management and the Michigan State Housing Development Authority. However, this report is a matter of public record and its distribution is not limited.

Firm's Signature _____

Date: _____

Compliance Report Notes:

1. Differences of 10% and a minimum of \$3,000 must be explained and reconciled in this report.
2. Paragraph 2 above must be included in its entirety except for the following:

- Developments, which do not have Federal Government involvement, do not need to include the phrase “HUD Regulations and Procedures included in the HUD Subsidy Contract” into this paragraph.
- Developments, which do not have HOME requirements, do not need to include the phrase “HOME requirements” in this paragraph.

Schedule 1

The Schedule 1 should be the version that is assigned to the specific development. The Schedule 1 included in the audit report is required to match the Schedule 1 in the Excel audit template.

Schedule 2

The Schedule 2 included in the audit report is required to match the Schedule 2 in the Excel audit template. The prior year information does not need to be included in the template, but the current year information is required to match the Schedule 2. All prior years are to be included on the PDF of the audit report.

Schedule 3

The Schedule 3 included in the audit report is required to match the Schedule 3 in the Excel audit template.

Agreed-Upon Procedures

The following is an example of the Agreed Upon Procedures letter that must be included with the Audit Report:

To The Partners of:
(Project Name)
(City, State)

We have performed the procedure described in the second paragraph of this report, which was agreed to by (*Partnership Name*) and the Michigan State Housing Development Authority (MSHDA), solely to assist them in determining whether the electronic submission of MSHDA’s Excel audit template certain financial information agrees with the related information contained in the audit report submitted to MSHDA. (*Partnership Name*) is responsible for the accuracy and completeness of the electronic submission. The agreed-upon procedures engagement was conducted in accordance with attestation standards established by the American Institute of Certified Public Accountants and generally accepted government auditing standards. The sufficiency of the procedure is solely the responsibility of those parties specified in this report.

Consequently, we make no representation regarding the sufficiency of the procedure described below either for the purpose for which this report has been requested or for any other purpose.

We compared the items listed in the electronic submission with the corresponding items listed in the audit report submitted to MSHDA. The results of the performance of our agreed-upon procedures indicate agreement of the electronically submitted information in MSHDA's Excel audit template and related audit report submitted to MSHDA. **(If there are items on the electronic submission that do not agree with the audit report, they are to be specified and explained.)**

We were engaged to perform an audit of the financial statements of (Partnership Name) as of and for the year ended December 31, 2012, and have issued our reports thereon dated (*report date*). Our opinion on the fair representation of the supplemental financial data templates dated (*date*), was expressed in relation to the basic financial statements of (*Partnership Name*) taken as a whole.

We have not performed any additional auditing procedures since the date of the aforementioned audit reports. Further, we take no responsibility for the security of the information transmitted electronically to MSHDA.

This report is intended solely for the information and use of (*Partnership Name*) and MSHDA and is not intended to be and should not be used by anyone other than these specific parties.