

## 470 - AUDIT GUIDE POLICY

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## Purpose of Annual Certified Audit

Developments receiving MSHDA-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 review of each development’s annual financial statements by an independent Certified Public Accountant (CPA).

This policy may also be referred to as the “Multifamily Annual Certified Audit Guidelines” or the “Audit Guidelines” in the developments’ regulatory agreement. The Audit Guide Policy has been arranged to ensure auditors verify compliance with the various housing program regulations and requirements. Audit criteria described in this policy 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

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

April 30<sup>th</sup> is the submission deadline for:

- the Annual Certified Audit,
- Schedule 1 payments, and
- MIE audit adjustments.

Note: If the deadline falls on a day that the Authority is closed (Saturday or Sunday), the submissions will be due on the next business day (Monday) the Authority is open.

## 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 the Authority meeting the requirements established in this audit guide:

- MSHDA-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 1<sup>st</sup>) – If occupancy occurs *after* July 1<sup>st</sup>, 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 following 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 American Reinvestment and Recovery Act (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 a MSHDA formatted audit to MSHDA.

MSHDA does **not** require a copy of the development’s HUD audit, if the development must also submit an audit to HUD.

## 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. E-mail Documents – The Auditor must e-mail the following documents by April 30<sup>th</sup>\* to the [MSHDAAssetMgt@michigan.gov](mailto:MSHDAAssetMgt@michigan.gov) mailbox with the subject line that displays, [Audit Template and Reports, Development Name, MSHDA #]. For example, Audit Template and Reports, Accurate Apartments, #9999.
  - Excel Audit Template (CSV file) - The CSV tab of the Excel audit template must be saved as a CSV file and labeled “CSV Audit template”.
  - Audit Template (Excel file) – The Excel template with all tabs in Excel format labeled “Audit Template”.
  - Audit Report (PDF file) – The audit report must include the reports specified in the “Audit Report Requirements and Examples” section of this policy labeled “Audit Report”.
  - Owner’s Certification – Owner confirmation of the accuracy of the above financial reports labeled “Owner’s Certification”.
2. MIE Audit Adjustments – Must be submitted to MSHDA by April 30<sup>th</sup>\*. E-mail the audit-adjusted MIE templates to the [MSHDAAssetMgt@michigan.gov](mailto:MSHDAAssetMgt@michigan.gov) mailbox with the subject line that displays, [MIE Audit Adjustments, Development Name, MSHDA #]. For example, MIE Audit Adjustment, Accurate Apartments, #9999.
3. Tax and Insurance Deficits - Must be submitted by January 25<sup>th</sup>\* 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 30<sup>th</sup>\*.
  - 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.

\* Refer to Audit and Payment Submissions Deadlines section for further details regarding the due dates.

## 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 developments with or without any remaining Section 8 subsidies or use restrictions unless the HUD Regulatory Agreement or Assignment of HAP states that the contract administrator must receive a copy of the HUD Audit.
- Rural Development (RD) financed developments that do **not** have ARRA-financing and/or a MSHDA HOME loan).

## Audit Process Procedures

MSHDA requires auditors to complete the following items as part of the audit process:

<u>Audit Procedures</u>	Completed	W/P
	<u>By</u>	<u>Date</u>
		<u>Ref.</u>
<b><i>Correspondence Review</i></b>		
A. Review the client’s correspondence file for any significant transactions, which have occurred during the current year and discuss with client. Inquire whether the client has specifically preformed any of the following items:		
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).	_____	_____
<b><i>Binder Review</i></b>		
B. Review the client’s permanent binder and update the Regulatory, Partnership, Loan, Workout, and Management Agreements or other such applicable legal documents.	_____	_____
<b><i>Journal Entry Review</i></b>		
C. Discuss all proposed journal entries with the client and obtain agreements thereto. Provide copies of entries and supporting details, as necessary.	_____	_____
<b><i>Subsequent Events Review</i></b>		
D. Review of Subsequent Events:		
1. Inquire of and discuss with general partners, the management company and other executives having responsibility for financial and accounting matters as to:		
a. Whether any substantial contingent liabilities or commitments existed as of the Balance Sheet date or at the date of this inquiry.	_____	_____
b. Whether there have been any significant changes in the long-term debt, or cash flow through the date of this inquiry.	_____	_____
c. The current status of items reported in the financial statements that were accounted for, on the basis of tentative, preliminary or inconclusive data.	_____	_____

**Audit Procedures**

Completed      W/P  
By      Date      Ref.

- 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. If any meeting minutes are not available, inquire about matters dealt with at such meetings. \_\_\_\_\_
- 3. Make additional inquiries or perform procedures as considered necessary and appropriate to resolve questions that arise in carrying out the foregoing procedures, inquiries and discussions. \_\_\_\_\_
- 4. Document your findings in a narrative. \_\_\_\_\_

***Related Party Transactions***

E. 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 member of the family relationship) in a vendor that provides goods or services to the development.

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

- 1. Determine 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. Inquire of appropriate owner and management company personnel as to changes in related parties during the period. \_\_\_\_\_
  - c. 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. \_\_\_\_\_
  - d. 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. \_\_\_\_\_
  - e. Review the Identity of Interest Disclosure forms submitted and approved for the current year and previous four 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. Identify transactions with related parties:

**Audit Procedures**

Completed      W/P  
By      Date      Ref.

- 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. Verify all limited distributions (cash and non-cash) have been paid from surplus cash as verified from the prior years audit and verify all distributions have been approved by MSHDA. All distributions are to be verified by viewing the approval letter from MSHDA. **All detail of the distributions must be listed in the Supplemental Schedule – “Detail of Surplus Funds and Reconciliation of Variances”** (under the surplus funds tab). \_\_\_\_\_
  - f. 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 LD distributions. \_\_\_\_\_
  - g. 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. \_\_\_\_\_
  - h. 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. \_\_\_\_\_

**Audit Procedures**

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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 income, expenses, accounts receivable and accounts payable, current and non-current for I of I vendors \_\_\_\_\_
  - d. All accounts receivable and accounts payable, current and non-current, with other developments. \_\_\_\_\_
  - e. All receivables/payables between the development’s operations and the partnership. \_\_\_\_\_

***Litigation Review***

- F. 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. \_\_\_\_\_

***Transactions Review***

- G. Inquire as to the partnerships’ compliance with applicable laws and regulations. Verify all transactions are legal. \_\_\_\_\_

***Management Fee Review***

- H. 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. \_\_\_\_\_

***Client Representation Letter***

- I. Obtain client representation letter. \_\_\_\_\_

***Confirmation Correspondence***

- J. Make arrangements to have correspondence relative to confirmations, cut-off statements, etc., prepared as of the year-end and mailed.  
 Note: Confirmations of resident rent and security deposits are no longer required. \_\_\_\_\_

**General Ledger Procedures**

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 By    Date    Ref.

A. Review of Accounting System and General Ledger

Generally all transactions in the areas of revenue and expenses of operations are recorded on the partnerships' books by the management agent. The managing agents typically do not include the general partner's 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.

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.<br>Note: 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.<br>Note: 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 owner's non-operating partnership activity on the Balance Sheet and the Income & Loss Statement of the Financial Statements.   | _____ | _____ | _____ |

**Cash**

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.<br>Determine whether the client is reconciling cash monthly. | _____ | _____ | _____ |
|--|-------|-------|-------|

**General Ledger Procedures**

	Completed	W/P
	<u>By</u>	<u>Date</u>
	<u>Ref.</u>	
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.	_____	_____
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 <b>operating</b> 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.	_____	_____

**CD and Marketable Securities**

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 whether the securities are in the name of the partnership.	_____	_____
5. Reconcile interest income and interest receivable to respective accounts and test the reasonableness of same.	_____	_____

**Accounts Receivables**

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.	_____	_____

**General Ledger Procedures**

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- 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. Note: All accounts receivable on the Balance Sheet must be separated according to whether the receivable applies to the partnership or the development. \_\_\_\_\_

***Prepaid Expenses***

E. Prepaid Expenses

Prepaid expenses related to amounts paid from escrow should be analyzed with the escrow accounts. \_\_\_\_\_

- 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. \_\_\_\_\_

***Fixed Assets and Accumulated Depreciation***

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. \_\_\_\_\_

**General Ledger Procedures**

Completed    W/P  
By    Date    Ref.

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 31<sup>st</sup>, 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.

Refer to the Audit Procedures – Capitalization of a Development to perform the audit review.

\_\_\_\_\_

***Deferred Mortgage Costs***

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.

\_\_\_\_\_

***Other Assets***

H. Other Assets

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

\_\_\_\_\_

***Mortgage and Interest Payables; Escrow Balances***

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

1. Prepare or have client prepare an account showing beginning balances, additions, payments and ending balances.

\_\_\_\_\_

2. Reference beginning balance to prior-year work papers and ending balance to the general ledger.

\_\_\_\_\_

3. Reference any additions to supporting documents.

\_\_\_\_\_

**General Ledger Procedures**

Completed    W/P  
By    Date    Ref.

- |  |              |              |              |
|--|--------------|--------------|--------------|
| <p>4. Prepare an analysis of accrued interest payable and reference to general ledger. The effect of an interest subsidy must be considered.<br/>Section 236 Interest subsidy should not be offset against interest expense on the financial statements.</p>   | <p>_____</p> | <p>_____</p> | <p>_____</p> |
| <p>5. Reconcile total principal and interest payments to total expected debt service for the year.</p>   | <p>_____</p> | <p>_____</p> | <p>_____</p> |
| <p>6. Test computation of interest expense and accrual for reasonableness.</p>   | <p>_____</p> | <p>_____</p> | <p>_____</p> |
| <p>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.</p>  | <p>_____</p> | <p>_____</p> | <p>_____</p> |
| <p>8. Determine whether the amount required to be paid in monthly to the replacement reserve fund has been paid as required.</p>   | <p>_____</p> | <p>_____</p> | <p>_____</p> |
| <p>9. If an allowable distribution was paid and a repayment is required (usually 25%) to repay a MSHDA-financed HOME loan, verify that:</p> <p style="margin-left: 20px;">a. A MSHDA-financed HOME loan payment was made; and</p> <p style="margin-left: 20px;">b. The amount paid equals the applicable percentage 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.</p> <p>Note: Review the Regulatory Agreement and/or HOME Loan Note for exceptions.</p> <p>Note: Do <b>not</b> include HOME loans provided by local municipalities or counties.</p> | <p>_____</p> | <p>_____</p> | <p>_____</p> |

**Other Long-Term Debt**

**J. Other Long-Term Debt**

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

**Trade Accounts Payable/Owner Advances**

**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.

**General Ledger Procedures**

Completed    W/P  
By    Date    Ref.

- |  |       |       |       |
|--|-------|-------|-------|
| 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 December MIE, Tab 12.  | _____ | _____ | _____ |
| 5. Determine if there have been <b>any</b> advances to the development’s operating account to pay for allowable operating expenses.<br>Note: 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. | _____ | _____ | _____ |

***Trade Accounts Payable - Construction***

- L. Trade Accounts Payable – Construction  
 The balance in this account is the result of the capitalization process described in the Audit Procedures – Capitalization of a Development section. Prior-year and current-year work papers should contain an analysis of the sources of funds, which are going to be used to fund 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.
- |  |       |       |       |
|--|-------|-------|-------|
|  | _____ | _____ | _____ |
|--|-------|-------|-------|

***Accrued Property Taxes***

- 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).<br>Note: 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 15 <sup>th</sup> of the following year. | _____ | _____ | _____ |
| a. Examine the current year’s tax bills and record/adjust expense to equal the total of the current year’s tax bills.   | _____ | _____ | _____ |
| b. 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.   | _____ | _____ | _____ |

**General Ledger Procedures**

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

***Michigan Business Tax Accrual***

**N. Michigan Business Tax Accrual**

- 1. Determine the partnerships’ liability for the Michigan 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. \_\_\_\_\_

**General Ledger Procedures**

Completed    W/P  
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***Security Deposits***

O. 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.<br>Note: 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.   | _____ | _____ | _____ |
| 5. Verify that the Security Deposit Liability is accounted for in accordance with MSHDA’s “Monthly Income and Expenditure (MIE) Guide Policy,” dated March <b>2015 or later</b> . The MIE Guide Policy is on MSHDA’s website at: <a href="http://www.michigan.gov/mshda/0,4641,7-141-8002_47708-177124--,00.html">http://www.michigan.gov/mshda/0,4641,7-141-8002_47708-177124--,00.html</a> .  | _____ | _____ | _____ |
| 6. For new construction Section 8 developments whose Agreements to Enter Into Housing Assistance Payments Contracts (AHAPS) were executed on/or after <b>February 29, 1980</b> , 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. | _____ | _____ | _____ |

***Other Liabilities***

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. | _____ | _____ | _____ |

***Partner’s Capital***

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. | _____ | _____ | _____ |

**General Ledger Procedures**

	Completed		W/P
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4. 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.	_____	_____	_____
5. Obtain supporting documents for any changes in the partnership.	_____	_____	_____
6. Obtain an understanding of the owner/management agent's procedures for determining surplus cash and making distributions.	_____	_____	_____
7. Scan minutes of board or partnership meetings for discussions authorizing distributions.	_____	_____	_____
8. Determine whether distributions taken during the audit period exceeded the amounts calculated and/or authorized for that period.	_____	_____	_____
9. Determine whether any cash distributions during the year were in accordance with the Regulatory Agreement, other controlling documents and other MSHDA guidelines/policies. MSHDA policies can be found on the MSHDA website at <a href="http://www.michigan.gov/mshda/0,4641,7-141-8002_47708-177124--,00.html">http://www.michigan.gov/mshda/0,4641,7-141-8002_47708-177124--,00.html</a> .	_____	_____	_____

***Income and Expenses***

**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.	_____	_____	_____
2. Determine the 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, 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 gross 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.	_____	_____	_____

**General Ledger Procedures**

	Completed	W/P
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		<u>Ref.</u>
6. Determine whether the management fees expensed or accrued for the year do not exceed the maximum allowable approved by the Authority and/or the amount approved in the Management Agreement or Fee Addendum. The Authority requires an annual submission of a Management Agreement/Fee 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 Fee Addendum to the Management Agreement.	_____	_____
7. Verify with the management agent that management fees paid to prepare the <b>current year's MIE</b> Reports were deducted from the management fee. Note: 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 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, are in accordance with the Partnership Agreement or Confidential Memorandum.	_____	_____
11. Determine the reasonableness of other charge-backs by the management agent.	_____	_____
12. Prepare an analysis of miscellaneous income and expense accounts, as deemed necessary.	_____	_____
13. Perform a test of at least 10% of the subsidized ( <b>restricted rent rate</b> ) 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.	_____	_____
14. Verify audit fees are within MSHDA-approved limitations. Refer to annual cover memo for the annual maximums MSHDA 450-Attachment 2 located on MSHDA's website at: <a href="http://www.michigan.gov/mshda/0,4641,7-141-8002_47708-177124--_00.html">http://www.michigan.gov/mshda/0,4641,7-141-8002_47708-177124--_00.html</a> .	_____	_____
15. 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.	_____	_____

**General Ledger Procedures**

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- 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. Determining the period when the unit was vacant by questioning development personnel, including the resident manager and the building manager. \_\_\_\_\_
- e. Reviewing work orders to determine the period when the unit was vacant. \_\_\_\_\_
- 16. 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. \_\_\_\_\_

***Insurance***

**S. Insurance**

- 1. Verify that there is Property & Liability Insurance policies providing coverage for the entire fiscal year. \_\_\_\_\_

***Retirement Plan***

**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 certified with MSHDA. \_\_\_\_\_

## General Ledger Procedures

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3. Determine if the pension plan is being administered in accordance with MSHDA's pension plan certification. \_\_\_\_\_

## **General Ledger Account Variance Testing**

### U. 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.

All variances are to be reconciled on the Compliance tab of the Excel audit template and in the Compliance Report. Templates submitted without the reconciliation will not be considered a complete audit submission.

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. An explanation without an accompanying reconciliation and/or a reconciliation without an accompanying explanation will result in an unacceptable audit submission:

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. Tenant Receivable (A1)
- c. Subsidy Receivable (tenant-based) (A2)
- d. Other Subsidy/Grants Receivable (A3)
- e. Other Current Residents Receivable (A10)
- f. Escrow Draws Receivable (A11)
- g. Non-Resident Receivables (A12)
- h. Related Party/Affiliate Receivables (A13)
- i. Receivables from Other Developments (A14)
- j. Other Receivables (A16)
- k. Security Deposit Cash (SDC)
- l. Security Deposit Liability (SDL)
- m. Accounts Payable (L1)
- n. Accrued Expenses (L2)
- o. Prepaid Rent (L3)
- p. Payables to Other Developments (L8)
- q. Short-Term Related Party Advances/Liabilities (L9)
- r. Other Short-Term Liabilities (L10)
- s. Other Long-Term Liabilities (L11)
- t. Other Long-Term Liabilities (L12)
- u. Long-Term Related Party Loans (F14)
- v. Long-Term Related Party Advances (F15)

- w. Long-Term Related Party Advances (non-repayable) (F16)
- x. Deferred Developer Fees (PL1)
- y. Vacancy Loss (1b)
- z. Marketing Rent Concessions (1e)
- aa. Other Income – Other (2i)
- bb. Management Fees (4a)
- cc. Premium Management Fees (4b)
- dd. Payroll:
  - i. Marketing (5b)
  - ii. Administrative (7a)
  - iii. Maintenance (11a)
  - iv. Janitorial (12a)
  - v. Grounds (13a)
  - vi. Security (15d)
- ee. Auditing (7h)
- ff. Other Administrative Miscellaneous (7k)
- gg. 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
<b>Note:</b> 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>	
Consumer's Energy	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.

**General Ledger Procedures (Continued)**

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***Financial Reports***

V. 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. \_\_\_\_\_
  - 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 “Audit Report Requirements and Examples” section of this policy are separated. \_\_\_\_\_
  - b. Income Statement \_\_\_\_\_
    - (1) Verify that all general ledger accounts that are required to be separated per the Income Statement example in “Audit Report Requirements and Examples” section of this policy 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. \_\_\_\_\_

**General Ledger Procedures (Continued)**

	Completed	W/P
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(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) Detail of Surplus Funds and Reconciliation of Variances	_____	_____
(a) Verify that the schedule is in correct format as in the Excel audit template and all variances between the amount approved by MSHDA, amount reported on the MIE, and the amount reported in the audit are reconciled.	_____	_____
(2) Schedule I - Funds Available for Distribution (include the Schedule I that applies to the development).	_____	_____
(3) Schedule II and III (if applicable)	_____	_____
g. Compliance Report	_____	_____
(1) A statement that the auditor, during the “Compliance Report” evaluation, took into consideration the items listed in the “Compliance Report (CR) Questionnaire” section of this policy.	_____	_____
(2) A description of material weaknesses in internal accounting controls.	_____	_____
(3) A description of items of noncompliance with the Regulatory Agreement, Management Agreement, MSHDA directives, and HUD regulations.	_____	_____
(4) A statement that account balances listed in the Monthly Income and Expenditure Report submitted to MSHDA at year-end are in material agreement with the account balances reported in the annual financial statements.	_____	_____
(5) If the account balances listed in the MIE submitted to MSHDA at year-end are NOT in material agreement, they are to be reconciled and included in the “Compliance Report”.	_____	_____
(6) Complete the Compliance tab of the audit template and verify it matches the Compliance report in the audit. (Any template submissions which do not match the PDF of the audit report will not be considered a completed audit submission.)	_____	_____

**General Ledger Procedures (Continued)**

Completed    W/P  
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- h. Independent Accountant's Report on Applying Agreed-Upon Procedures \_\_\_\_\_
  
- 4. The Excel audit template must:
  - a. Verify all tabs are completed. Do not delete or modify any tabs on the template. \_\_\_\_\_
  - b. Match the information in the PDF of the audit report. \_\_\_\_\_

## Audit Procedures – Capitalization of a Development

This process occurs when a development has not received occupancy permits for all the units in the development.

### 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:

Is the development cost certified?

**Yes:** Capitalize total fixed asset costs. (1)

**No cost certification:** Were permits to occupy issued during the year?

**No, permits were issued:** Zero capitalization; all construction is in progress. No annual certified audit is required.

**Yes, permits were issued:** Is the project 100% occupied?

**Yes, 100% occupied:** Full capitalization. (1)

**No, not 100% occupied:** Partially capitalize based on permits of occupancy issued. (2)

(1) See the “Capitalization of a Cost Certified Project” section for full capitalization steps.

(2) See the “Capitalization of a Project not Cost Certified” section 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 (c) 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

		<u>Note</u>
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	\$0,000,000	(d)
<b>Total fixed asset cost (c-d)</b>	<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 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 “decision tree” as a guide in making the computation.

<b>Capitalization of a Cost Certified Project</b>	<b><u>Completed</u></b>		<b><u>W/P</u></b>
	<b><u>By</u></b>	<b><u>Date</u></b>	<b><u>Ref.</u></b>
1. Prepare a work paper in the above format computing the eventual cost to be allocated to fixed assets.	_____	_____	_____
2. Use MSHDA approved Contractor’s and Mortgagor’s Certificate of Actual Costs 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 above 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 approved Contractor's Certificate of Actual Cost.	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 the approved Contractor's Certificate of Actual Costs. Group various line items based upon the line item description as it relates to the fixed asset categories.
- (3) Percentage of approved Contractor's Certificate of Actual 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.

<b><u>Capitalization of Project Not Cost Certified</u></b>	<b><u>Completed</u></b>		<b><u>W/P</u></b>
	<b><u>By</u></b>	<b><u>Date</u></b>	<b><u>Ref.</u></b>
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 an approved Contractor's Certificate of Actual Costs is available for the final fixed asset allocation.			
---	--	--	--

<u>Depreciation</u>	<u>Completed</u>		<u>W/P</u>
	<u>By</u>	<u>Date</u>	<u>Ref.</u>
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, depreciation of a unit begins when the unit 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.)	_____	_____	_____
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:

<b>Construction Period Interest and Other Carrying Costs</b>	<u>Completed</u>		<u>W/P</u>
	<u>By</u>	<u>Date</u>	<u>Ref.</u>
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.	_____	_____	_____

<p>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.</p> <p><b>Note:</b> 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.</p>	<p>_____</p>	<p>_____</p>	<p>_____</p>
<p>5. To avoid book/tax timing differences with respect to construction period interest, taxes and other carrying costs, the financial statements should 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.</p>	<p>_____</p>	<p>_____</p>	<p>_____</p>

## 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") identifies any internal control or non-compliance issues flagged by the audit process and the reporting of any other internal control or non-compliance issues.

This section 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 "Compliance Report Questionnaire" below provides the method for recognizing the importance of including specified items on the "Compliance Report".

The CPA is required to:

1. Include the questionnaire as a permanent part of the CPA's working papers
2. Review, evaluate, and comment on the adequacy of the accounting records, procedures and the system of internal controls maintained;
3. Provide an explanation in the audit compliance report for any question answered, "No" on the Compliance Report Questionnaire (as this identifies a significant compliance or internal control weakness), and;
4. 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 MSHDA's "Monthly Income and Expenditure (MIE) Guide Policy," dated March **2015 or later**. The MIE Guide Policy is on MSHDA's website at: [http://www.michigan.gov/mshda/0,4641,7-141-8002\\_47708-177124--00.html](http://www.michigan.gov/mshda/0,4641,7-141-8002_47708-177124--00.html).

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.

**Yes      No      N/A      Ref.**

***Regulatory Agreement***

**A. Regulatory Agreement**

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. 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 obligation?   | _____ | _____ | _____ | _____ |
| (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?   | _____ | _____ | _____ | _____ |

***Related-Party Transactions***

**B. Related-Party Transactions**

Have all related-party transactions been disclosed in the format required by MSDHA in the Notes to the Financial Statement?	_____	_____	_____	_____
---	-------	-------	-------	-------

**Compliance Report (CR) Questionnaire**

Address any “No” answers in CR.

	<u>Yes</u>	<u>No</u>	<u>N/A</u>	<u>Ref.</u>
1. 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.	_____	_____	_____	_____
2. Have all disallowed expenses been noted in the Notes to the Financial Statement and the “Compliance Report”?	_____	_____	_____	_____
3. Have all owner transactions not approved by MSHDA’s Board been identified?	_____	_____	_____	_____
4. 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?	_____	_____	_____	_____
5. Have all related party transactions been disclosed in the notes to the financial statements and listed as a non-compliance issue if the transaction did not receive MSHDA approval. Non-operating and related party loans and advances are not allowed without written MSHDA approval.	_____	_____	_____	_____
6. Have all disbursements (cash and non-cash) from operations been accounted for through surplus cash transactions (limited distributions), verified from the prior year’s audit (approved by MSHDA)? Have all transactions been approved by MSHDA as verified by the MSHDA Approval letter, and has the detail of the distributions been listed in the <b>Supplemental Schedule – “Detail of Surplus Funds and Reconciliation of Variances”</b> ?	_____	_____	_____	_____
7. Has a scan of the bank deposits identified that all deposits from the development’s owners and/or related parties for distributions are accurate?	_____	_____	_____	_____
8. 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”?	_____	_____	_____	_____
9. Are the payments made to identity of interest vendors within the range ordinarily paid for such services and supplies?	_____	_____	_____	_____

**Insurance**

C. Insurance

1. Has the development’s insurance coverage been maintained as required by MSHDA?	_____	_____	_____	_____
---	-------	-------	-------	-------

**Compliance Report (CR) Questionnaire**

Address any "No" answers in CR.

**Yes      No      N/A      Ref.**

***Books and Reports***

D. Books and Reports

- |  |       |       |       |       |
|--|-------|-------|-------|-------|
| 1. Are the books and records maintained as prescribed by MSHDA and HUD guidelines?                       | _____ | _____ | _____ | _____ |
| 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? | _____ | _____ | _____ | _____ |

***Operating Activities***

E. Operating Activities

- |   |       |       |       |       |
|---|-------|-------|-------|-------|
| 1. Are all <b>operating</b> 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 <b>February 29, 1980</b> ? | _____ | _____ | _____ | _____ |
| 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?   | _____ | _____ | _____ | _____ |

**Compliance Report (CR) Questionnaire**

Address any "No" answers in CR.

	<u>Yes</u>	<u>No</u>	<u>N/A</u>	<u>Ref.</u>
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;	_____	_____	_____	_____
(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 mortgagee within 120 days (April 30 <sup>th</sup> ) after the close of the mortgagor's annual accounting period?	_____	_____	_____	_____
<b>Exception:</b> The Tax/Insurance Escrow Deficit payments are due by January 25 <sup>th</sup> .				
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 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? <b>Note:</b> 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 <b>expensed and or accrued</b> for the preparation of all the annual certified audit(s) (the Authority and HUD) and tax preparation fees 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?	_____	_____	_____	_____

**Management Agreement**

F. Management Agreement

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 <b>current year's</b> development budget and/or the Management Fee Structure? <b>Any overpayment/over accrual of management fees, regardless of dollar amount, must be explained in the "Compliance Report."</b>	_____	_____	_____	_____
5. Was the amount of management fees reported on the General Ledger equal to the annual total amount reported on the MIE Report?	_____	_____	_____	_____
6. 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?	_____	_____	_____	_____

**Compliance Report (CR) Questionnaire**

Address any "No" answers in CR.

**Yes      No      N/A      Ref.**

***Payroll***

G. Payroll

- 1. Were the payroll tax charges by the management agent reasonable? \_\_\_\_\_

***Retirement Plan***

H. Retirement Plan

- 1. If there is a retirement/pension plan, has the plan been approved in writing by the MSHDA, Asset Management Division? \_\_\_\_\_

***Rents and Occupancy***

I. Rents and Occupancy

- 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? \_\_\_\_\_

***Additional Services***

J. Additional Services

- 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.? \_\_\_\_\_

***Subsidy Payments***

K. Subsidy Payments

- 1. Were the amounts requested from HUD supported by the accounting records? \_\_\_\_\_

**Compliance Report (CR) Questionnaire**

**Address any "No" answers  
in CR.**

**Yes    No    N/A    Ref.**

2. Were subsidy payments received and recorded in the proper accounts?

\_\_\_\_\_

***Financial Reports***

L. Financial Reports

\_\_\_\_\_

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?

\_\_\_\_\_

## Excel Audit Template Description and Instructions

An Excel audit template is issued to the auditor and Management Company for each development. The template must be completed for each development and is part of the audit submission process.

### Input Tab

Guidance for completing this tab is provided as comments within the template. This tab populates the calculations performed on the Schedule 1(a through o), Schedule 2, and Schedule 3 tabs.

### Schedule 1 Tab

The Schedule 1 tab is auto-filled based on the information entered on the Input tab. The Schedule 1 in the Excel audit template must match the copy submitted in the PDF of the audit report.

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. If a development has Replacement Reserve Needs, the amount will be reported on the December mortgage activity statement. The Replacement Reserve Needs balance on the December mortgage activity statement reflects actual Replacement Reserve contributions through November, and the month of December is estimated. 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 Todd Miller at [MillerT22@michigan.gov](mailto:MillerT22@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 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 25<sup>th</sup>. If the deficit is NOT funded by January 25<sup>th</sup>, 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 31<sup>st</sup>, to the Operating Reserve Cash Escrow. If the transfer occurred in December, the surplus is not 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” as well as any 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-compliances Issues

### Surplus Funds Tab

The Surplus Funds Tab provides an area to record a reconciliation of the surplus funds transactions. The Detail of Surplus Funds and Reconciliation of Variances must reconcile with the surplus cash from the approved audit from the prior year, the LD distributions approved by MSHDA, and the amount reported in the ‘Adjustments’ tab in the MIE. The schedule in the Excel audit template must match the copy submitted in the PDF of the audit report.

## **Audit Report Requirements and Examples**

This section includes 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 items:

- Independent Auditors’ Report
- Balance Sheet
- Income Statement
- Statement of Owner’s Equity
- Statement of Cash Flow
- Notes to Financial Statements
- Compliance Report
- Schedule 1
- Schedule 2
- Schedule 3
- Detail of Surplus Funds and Reconciliation of Variances
- Agreed-upon Procedures

Any variation to the format or contents of the reporting requirements detailed below requires prior approval. Contact Lisa Espinoza or Ryan Armstrong at MSDHA to request the approval.

## 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

#### Independent Auditor's Report

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

### Report on the Financial Statements

We have audited the accompanying financial statements of (*partnership name of development name*), (a Michigan limited partnership), MSHDA Development No. 9999 which comprise the balance sheet as of December 31, 2016, and the related statements of income and expense, changes in partner's capital, and cash flows for the year then ended, and the related notes to the financial statements.

### Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

### Auditor's Responsibility

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 involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessments of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of (*development name*), MSHDA No. 9999 as of *December 31, 2016*, and the results of its operations, and its cash flows from the year then ended in conformity with accounting principles generally accepted in the United States of America.

Report on Other Legal and Regulatory Requirements

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.

Other Reporting Required by Government Audit Standards

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 in considering *(development name)*'s internal control over financial reporting and compliance.

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, 2016.

- 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	Relationship	Brief Description of Work/ Services Performed	General Ledger Account	Partnership or Operating Account	Beginning Balance 12/31/15	Increase	Decrease	Ending Balance 12/31/16	Terms of Settlement
Erector Corp.	General partner is an officer	Painting Units	Painting Expense	Operating	\$-0-	\$ 8,000	\$-0-	\$8,000	
Erector Mgmt.	General partner is an owner	Mgmt fee	Mgmt Fee Expense	Operating	\$-0-	\$35,000	\$-0-	\$35,000	
			Accounts Payable – mgmt. fees	Operating	\$20,000	\$35,000	\$(30,000)	\$25,000	Deferred until payables are current.
Joe Smith	General partner	Loan for operating deficit	Accounts Payable, General Partner	Operating	\$100,000	\$50,000	\$-0-	\$150,000	Deferred until refinancing or sale of property.
Joe Smith	General partner	Accrue partnership fees	Partnership Mgmt Fee Expense	Partnership	\$-0-	\$5,000	\$-0-	\$5,000	
			Accounts Payable, owner	Partnership	\$10,000	\$5,000	\$-0-	\$15,000	Payable when Surplus cash is available
ABC Inc.	Limited partner	Investor Service Fees	Investor Service Fee Expense	Partnership	\$-0-	\$10,000	\$-0-	\$10,000	
			Accounts Payable, Owner	Partnership	\$20,000	\$10,000	\$-0-	\$30,000	Payable when Surplus cash is available

## Compliance Report

Independent Auditors' Report on Compliance and on Internal Control over Financial Reporting and on Compliance and Other Matters 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, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Governmental Auditing Standards issued by the Comptroller General of the United States, the financial statements of *(Partnership Name)* MSHDA No. 9999, which comprise the balance sheet as of December 31, 2016, and the related statements of income and expense, changes in partner's capital, and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated *(report date)*.

### Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered *(Partnership Name)*'s internal control over financial reporting to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of *(Partnership Name)*'s internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect or correct, misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statement will not be prevented, or detected and corrected on a timely basis. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

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, 2016.

### Compliance and Other Matters

As part of obtaining reasonable assurance about whether *(Development Name)*'s financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements 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 Audit Guide Policy, noncompliance with which could have a direct an material effect on the determination of financial statement amounts. However, providing an opinion on compliance with these provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported 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, 2016 Monthly Income and Expense Report submitted to MSHDA with balances in the financial statements as of December 31, 2016 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 3,000), except as noted on page (*page # of report*) of this report.

#### Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of audit performed in accordance with Governmental Auditing Standards in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

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.

This schedule 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 3) 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.

This schedule is a historical summary of the annual 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. When generating this report, the first (initial) year of operation shall begin on the **first day following the mortgage 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 mortgage 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 annual certified audit. Disbursements for approved limited dividend payments must be made in accordance with the MSHDA's 471 - Limited Dividend Payment Policy.

## Schedule 3

The Schedule 3 included in the audit report is required to match the Schedule 3 in the Excel audit template. This schedule is an annual reconciliation of the security loan and is only required to be completed by developments which have a security loan.

### Detail of Surplus Funds and Reconciliation of Variances

The reconciliation included in the audit report is required to match the reconciliation in the Excel audit template. This schedule is reconciling the amounts recorded on the MIE, amount approved by MSHDA, and the amount reported in the audit report.

Below is an example of an entry of the LD distribution from the 'Adjustments' tab of the MIE.

The previous year's surplus cash for the development was \$52,452. The owner had an approved undisbursed LD of \$12,000 which they had also reported on their Schedule 1 in the prior year's audit. In the current year the owner requested and received approval from MSHDA to receive the distribution of the current year's surplus cash and the approved undisbursed LD ( $\$52,452 + \$12,000 = \$64,452$ ) request

was submitted and approved from MSHDA. Once the owner received approval they decided to pay a partnership asset management fee payable of \$10,000, a partnership asset management expense of \$5,000, a deferred developer fee of \$8,700, and pay the balance of \$40,752 as a cash distribution.

This transaction is required to be recorded on the Adjustments tab of the MIE template. Below is an example of how this transaction would have been reported on the MIE.

Surplus Cash Transactions						
<b>Cash Distributions Paid (balance carries to OE2 on Balance Sheet tab)</b>	Adj6					40,752
<b>Deferred Developer Fees Payable</b>	Adj7					8,700
<b>Related Party Payable</b>	Adj8					10,000
<b>Other Partnership Payables</b>	Adj9					
<b>Partnership Expenses</b>	Adj10					5,000
<b>Operatating Cash</b>	Adj11					(64,452)
<b>Operating Liability including Accrued Distributions Payable</b>	Adj12					
<b>Balance</b>	Adj13	\$0	\$0	\$0	\$0	\$0

For more detail of the reconciliation see the ‘Detail of Surplus Funds and Reconciliation of Variances’ 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 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 (AICPA) 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, 2016, 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.

## Contact List

Policy – Ryan Armstrong at (517) 335-2010; email [ArmstrongR2@michigan.gov](mailto:ArmstrongR2@michigan.gov) or  
Lisa Espinoza at (517) 373-3276; e-mail: [espinozaL@michigan.gov](mailto:espinozaL@michigan.gov).

Excel Audit Template - Ryan Armstrong at (517) 335-2010; email [ArmstrongR2@michigan.gov](mailto:ArmstrongR2@michigan.gov) or  
Lisa Espinoza at (517) 373-3276; e-mail: [espinozaL@michigan.gov](mailto:espinozaL@michigan.gov).

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

## Forms and Attachments List

### Forms

470A – Audit Input Template

470A1 – Schedule 1 (1a through 1p)

470A2 – Schedule 2

470A3 – Schedule 3

470A4 – Compliance Reporting

470A5 – Detail of Surplus Funds and Reconciliation of Variances

### Attachments

470 Attachment 1 – Financial Audit Submission Process (Pending process testing)

470 Attachment 2 – Modified Schedule 1 Summary (forthcoming with the audit template)