Managing Your Housing Portfolio for Success

Finance 101 for the On-Reserve Non-Profit Housing Program (Section 95)

Reporting Requirements:

Revenue, Expenses, Operating Reserve and Replacement Reserve

Revenue

Revenue: Pre-97 program requirements

- First Nation should operate at a break-even position (rent + band contribution + subsidy = expenses)
- Where rent-geared-to-income (RGI) is being used, auditor to confirm the process was followed
- Rental increases should be implemented

Revenue—Pre-97 Program

- Revenue sources:
    - Rental revenue
    - Section 95 subsidy
    - Interest income
    - First Nation contribution

- A revenue contribution must be made to projects in deficit.

When expenses exceed revenues, and First Nations do not have sufficient revenues to cover future expenses, the project's viability and the ability to maintain units at minimum level of health and safety are at risk.

Audited Statement- Example (Pre-97)

Revenues	**Example**	**Corrected version**
Rental revenue	50,000	50,000
CMHC Subsidy	58,200	58,200
Band Contribution		16,815
Total Revenue	***108,200***	***125,015***
Expenses		
Administration	6,540	6,540
Maintenance	12,400	12,400
Insurance	7,875	7,875
Audit	3,100	3,100
Mortgage interest	62,884	62,884
Amortization	15,716	15,716
Replacement Reserve Allocation	15,000	15,000
Services	1,500	1,500
Total Expenses	***125,015***	***125,015***
Current year surplus / (deficit)	**-16,815**	**0**
Surplus / (Deficit) at beginning of year	**(64,218)**	**0**
Surplus / (Deficit) at end of year	**(81,033)**	**0**

In this example, the Band Contribution was listed as an expense, when it is actually a source of revenue. It does not represent a deficit.

Revenue—Post-96: Minimum Revenue Contribution

- The Section 95 operating agreement requires that the First Nation contribute a set amount annually, known as the minimum revenue contribution (MRC)
- This amount is identified and agreed to at the time the project is committed
- The agreement does not prescribe the source of the revenue—it could come from an occupancy charge, a First Nation contribution or both.

Importance of the Minimum Revenue Contribution

- When the MRC is not being funded as per the operating agreement, the impact is insufficient revenue to cover expenses. This threatens project viability and the ability to maintain a project at a minimum level of health and safety.
- When expenses exceed revenue and are being paid by the band, this must be recorded as a revenue contribution, and not as a liability (loan). Otherwise, statements will reflect an ongoing deficit.
- Tip: When reviewing your draft audit, ensure rental revenue and other revenue equals MRC. If not, ensure a band contribution is recorded.

Reasons why the MRC is not funded / underfunded

Vacant units during the year. For example, if a unit is vacant for 2 months, the First Nation must contribute the MRC for those 2 months.

Occupancy charge is lower than MRC. (ex: charge is $300, MRC is $400). The First Nation must then contribute the difference each month to meet the MRC requirement.

The First Nation is using cash-basis accounting—recognizing revenue only when it is paid, instead of when it is earned (accrual)

Audited Statement- Example (Post 96)

Minimum Revenue Contribution	**75,000**	**75,000**
Revenues	Example	Corrected Version
Rental Revenue	50,000	50,000
CMHC Subsidy	58,200	58,200
Band Contribution	0	25,000
Total Revenue	***108,200***	***133,200***
Expenses		
Administration	6,540	6,540
Maintenance	12,400	12,400
Insurance	7,875	7,875
Audit	3,100	3,100
Mortgage interest	62,884	62,884
Amortization	15,716	15,716
Replacement Reserve Allocation	15,000	15,000
Services	1,500	1,500
Total Expenses	***125,015***	***125,015***
Current year surplus / (deficit)	**-16,815**	**8,185**
Surplus / (Deficit) at beginning of year	**12,500**	**0**
Surplus / (Deficit) at end of year	**(4,315)**	**20,685**

Expenses

Expenses

Fire Insurance
Repairs/Maintenance
Heat/Hot Water
Water/Sewer
Administration
Replacement Reserve
Loan Payments
Snow Removal/Garbage Collection
Audit/Legal Fees

Bad debts

- Post-96 Program
  - Bad debt is not considered an eligible program expense given the requirement for the First Nation to contribute the MRC.
- Pre-97 Program
  - Bad debt can be recognized, as long as in compliance with CMHC's guidelines & criteria
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Bad debts expense

Rental arrears should not be recorded as bad debts if the tenant still resides in the unit. There should be an arrears policy and collection process to seek payment of arrears.

Operating Reserve Fund (post 96)

Operating Reserve Fund - Post-96 Program

- The program is designed to generate surpluses in the early years that are to be held in an operating reserve fund.
- This surplus will be available to offset higher operating costs that are expected as the project ages.
- The surplus is invested in a separate interest-bearing account and treated as a restricted account.
- This reserve is for the housing program and the funds are not returned to CMHC.

Impact of Unfunded Operating Reserve

- No money to offset future rising operating costs expected as the project ages.
- If reserves are not established and accumulating in the early years, and revenues do not increase at a steady rate, the community will not have the ability to maintain the houses as costs rise.
- This threatens the future viability of a project and the ability to maintain the project at a minimum level of health and safety.

Audited Statements - Operating Reserve

Operating Reserve	Unfunded	Funded
Opening balance	$15,000	$15,000
Interest earned	$0	$500
Current year surplus / (deficit)	$1,500	$1,500
Closing balance	$16,500	$17,000
Funded bank account	$0	$17,000
Reserve overfunded/(underfunded)	($16,500)	$0

Replacement Reserve Fund

Replacement Reserve Fund

- A replacement reserve is to be held and funded in a separate interest-bearing account.

- It should be used as intended: to pay for the replacement of worn-out building components or for major repairs.

- Under the Post-96 Program, prior approval from CMHC is not required. Under the Pre-97 Program, use of the replacement reserve requires prior approval from CMHC. However, this prior approval can be waived if a community has a capital expenditure plan in place.

Impact of Unfunded or Underfunded Replacement Reserves

- No funds to pay for expensive and/or urgent capital repairs, which may put tenants and units at risk
- No funds available to extend the useful life of homes
- CMHC Section 95 homes are not eligible for other assistance (ex: RRAP)

Maturing units- reporting adjustments

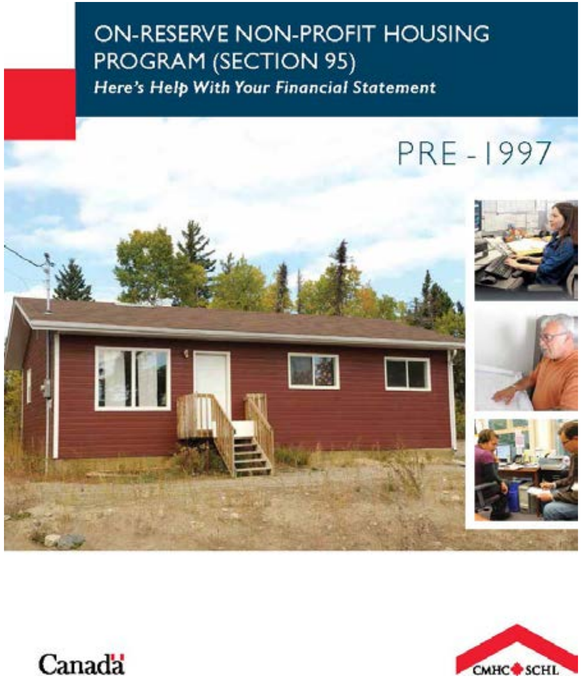
- As units mature / agreements end, adjustments need to be made to ensure that the financial position reported is reflective of the current portfolio.
- CMHC will provide details of adjustments in the audit call letter.

Financial Reporting Process

The Audit Package

- Audited financial statements are due four months from the fiscal year end. *(In most cases, this is four months from March 31, which is July 31.)*
- CMHC will send an "Audit Call Package," which contains:
  - financial data for your housing portfolio
  - resources and information to assist you and clarify audit expectations
  - the *Here's Help With Your Financial Statement* information guide

Here's Help with your Financial Statement guides



What to include in the Audit Package

- Auditor's Report
- Statement of Financial Position *(Balance Sheet)*
- Statement of Revenue and Expenses (*Income Statement)*
- Statement of Cash Flow
- Statement of Funded Reserves *(Replacement Reserve, Subsidy Surplus Fund (Pre-1997) and Operating Reserve (Post-1996))*
- Notes to the Financial Statements
- Auditor's Report on Compliance with the Agreement

Thank You

To be filled in by CMHC staff – contact info, etc.