



# Entry Form 2017 Annual Awards for Program Excellence

**Entry Deadline: Thursday, June 15, 2017, Midnight ET**

Each entry must include a completed entry form. Please complete a form for each entry your HFA is submitting. The completed entry form will become the first page of your entry.

This form is a fillable PDF. Type your information into the entry form and save it as a PDF. Please do not write on or scan the entry form. **Questions: Call 202-624-7710 or email [awards@ncsha.org](mailto:awards@ncsha.org).**

**Entry Title:** Enter your entry's title exactly as you wish it to be published on the NCSHA website and in the awards program.

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**Category:**

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**Subcategory:**

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**Entry Summary:** A 15-word (max) summary of the program, project, or practice you are entering.

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**HFA:**

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**HFA Staff Contact:**

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**Phone:**

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**Email:**

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**Visual Aids:**

Are you mailing to NCSHA 10 copies of any visual aids that cannot be included in your entry PDF?    Yes        No

**Payment:**

My HFA is mailing a check to NCSHA.  
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**MassHousing**  
***Risk Based Financial Statement Review Process***  
**Rental Housing – Multifamily Management**

**Executive Summary**

Over the past year, MassHousing’s Rental Management Department developed a plan of action designed to improve staff efficiency and the way in which the department interacts with its business partners. MassHousing’s newly developed Risk-Based Financial Statement Review Process is an outcome of that effort.

The Financial Statement Review Process enables an Asset Manager, within the Agency’s Rental Management Department, to: monitor the financial viability of a development; verify debt service payments to MassHousing; scrutinize payments to owners; assess compliance with contract documents, and; evaluate the sufficiency of the development’s cash and reserves.

Traditionally, the financial statement review has been conducted as a “one size fits all” process. The audited financial statements were reviewed utilizing the same parameters for each one, regardless of risk rating, program type or history of financial performance at the property. The process has been time consuming, and has not adequately taken into consideration MassHousing’s changing business environment, new lending products, and tenant assistance programs.

While the Agency had made improvements to the process over time, it became clear that a wholly new approach was needed. The new approach described below addresses the above referenced issues by employing a risk-based system coupled with substantive ratio analysis which in all provides a better product for both the Agency and its rental borrowers.

**Process Summary**

At the beginning of each February, the Systems & Technology Team (S&T) now provides the Rental Management Division with a list of developments in the portfolio, which further identifies the Capital and Managerial risk scores for each property based on Asset Management Reviews (AMR) conducted during the audit year and the financial risk score from the prior year. Upon receipt of the current financial statement, a second report is generated to determine if there have been any significant changes in financial rating. This analysis becomes the basis on which MassHousing’s two-tier, risk-based approach is based.

To achieve an overall risk rating of AAA, a development must have:

- Financial – Debt Service Coverage of 1.15
- Capital – Sufficient reserves over the next 10 years or the remaining term of the loan
- Managerial – Satisfactory AMR ratings

Once the three risk ratings are determined, Asset Management employs the Risk Based Financial Statement Review process based on a two-tier system. Steps identified in the first tier are applied to all portfolio properties regardless of risk rating. The steps identified in tier 2 will be applied only to those developments that score less than AAA. An automated ratio analysis will also be conducted for all developments in this group. The development's program/subsidy type will be used to determine the appropriate ratios to be applied.

### **Tier 1**

All developments will undergo the level of financial statement review described below. The steps will be tailored to meet the requirements of the development's specific subsidy and program type.

- Conduct Quality Control Review, this confirms that the financial statement is signed and includes all required reports and schedules.
- Review the auditor's opinion and follow up on any pertinent issues identified in the Notes to the financial statements and the Schedule of Findings and Questioned Costs.
- Using the Project Activity Summary Report in the Agency's database and the Debt Service and Escrow Analysis worksheet, verify that the MassHousing debt service and the development's replacement reserve obligations are reflected correctly.
- Process fast track distribution requests and complete a distribution worksheet, as applicable.
- Generate the Financial Analysis Program.
- **Note:** The new Financial Analysis Program is streamlined to include four sections (1) operating threshold analysis (2) partnership obligations (3) distribution analysis and (4) payments due on outstanding obligations. This Program assists the asset manager in determining the required collection activity identified in the steps below.
- Identify and follow up on any Due To/Due From issues noted in the audit.
- Identify and collect the following, as applicable:
  - Flexible subsidy payments due to HUD
  - Recap obligations
  - Residual receipts payments
  - Excess equity payments
  - Payments on cash flow notes
  - Arrearage note obligations
- Keeping within the parameters of the risk analysis categories, the asset manager develops an "issues report" to document operational and compliance issues, as applicable.
- Staff utilize the findings identified in the "issues report" to generate required monitoring plans which will guide asset management monitoring activities for the balance of the year.

- Generate a close-out letter to the owner and send the financial statement package to scanning for record-keeping purposes.

## **Tier 2**

For all developments that have not achieved AAA risk ratings, the reason for the lessor rating is determined and the financial statement review includes the following additional steps:

- An automated ratio analysis is conducted to measure key performance indicators. This analysis will be used to further investigate operational issues affecting the overall performance of the development. The ratios and benchmarks are established based on industry standards and an analysis of the overall performance of the Agency's portfolio. Program/subsidy type are also taken into consideration as part of the analysis.
- Utilize the Income Statement Comparison Report to generate a report comparing the new audit to the Owner's Submission from the prior year. Review the report looking solely for significant variances and follow up with management as required. This is not meant to be a deep dive into line item specifics. The development's operating budget should also be taken into consideration as the review is conducted.
- The ratio analysis and income statement comparison reports are used to determine if a further review of operations is required. This analysis will be incorporated into the "issues report" and Monitoring Plan, as necessary. These reports will serve as a basis for the formation of the department Risk Report.

## **Positive Outcomes**

Through this risk-based approach, MassHousing has improved its financial statement review process while maintaining the Agency's regulatory role and at the same time, addressing the challenges of the its changing portfolio. The two-tiered risk based approach allows for substantive analysis of those developments that require additional review. With the implementation of the ratio worksheet and program specific benchmarks for performance, MassHousing has enhanced its level of analysis. Issues identified are memorialized as part of the process will inform an asset manager's work on his or her portfolio throughout the year. This new process has become a facet of MassHousing's dynamic and integrated process of asset management.

Based on Agency data, MassHousing has determined that 45% of its portfolio underwent a Tier I level of review. By implementing the new process, the Agency has reduced the amount of staff time required to complete the process and successfully meet a May 31 deadline, an improvement of 30 days from prior years. The change in methodology and streamlined approach has been well received and the Agency anticipates implementing further improvements for an even greater level of efficiency.



Development Name: \_\_\_\_\_ Development ID: \_\_\_\_\_  
 Portfolio Manager: \_\_\_\_\_ Principal Program: \_\_\_\_\_  
 Asset Manager: \_\_\_\_\_

**Property Details**  
 Address: \_\_\_\_\_ Total Rental Units: \_\_\_\_\_  
 Management Company: \_\_\_\_\_ Total Affordable Units: \_\_\_\_\_  
 Site Manager: \_\_\_\_\_ E-Mail: \_\_\_\_\_  
 Regional Manager: \_\_\_\_\_ E-Mail: \_\_\_\_\_  
 2016 Risk Ratings: F: \_\_\_ C: \_\_\_ M: \_\_\_ Tier 1: \_\_\_ Tier 2: \_\_\_

**Auditor Opinion**       Unqualified     Qualified     Adverse     Disclaimer of Opinion

**Cash Flow Notes Payable**  
 Flex Sub Type I: \_\_\_\_\_ Flex Sub Type II: \_\_\_\_\_ Arrearage Note: \_\_\_\_\_ Residual Receipts/  
 Excess Equity: \_\_\_\_\_ Section 8 Recap: \_\_\_\_\_  
 Other: \_\_\_\_\_

● Note any litigation or risk to the asset identified in the audit.  
 \_\_\_\_\_

● Does the Audit contain a Statement of Findings and Questioned Costs?       Yes     No  
 Identify significant items:

\_\_\_\_\_

**Threshold Analysis** \*Minus Replacement Reserve Deposit\*  
 2015 Program per Unit Threshold: \_\_\_\_\_ 2016 Program per Unit Threshold\*: \_\_\_\_\_  
 \*2015 per Unit Trended at 3%

**Program Threshold Analysis**  
 2016 Program per Unit Threshold: \_\_\_\_\_ 2016 Owner's Audit per Unit: \_\_\_\_\_ Variance %: \_\_\_\_\_ <sup>>10%?</sup>  Yes  No  
 2015 Owner's Audit per Unit: \_\_\_\_\_ 2016 Owner's Audit per Unit: \_\_\_\_\_ Variance %: \_\_\_\_\_  Yes  No

**Replacement Reserve**  
 Balance in Replacement Reserve: \_\_\_\_\_ Annual Replacement Reserve Requirement: \_\_\_\_\_  
 (Line 241 - 250A) (Line 53)  
 Number of Years in Escrow Balance: \_\_\_\_\_

**Partnership Obligations and Expenses**

**Partnership Obligations and Expenses**  
**Due From:**      **Due To:**  
 Due From General Partners/Affiliates: \_\_\_\_\_ Due to General Partners/Affiliates: \_\_\_\_\_  
 (Line 225) (Line 287)  
 Decrease in Due From GP/Affiliates - \_\_\_\_\_ Increase in Due to GP/Affiliates - Cash Received: \_\_\_\_\_  
 Cash Provided: (Line 323) (Line 335)  
 Increase in Due From GP/Affiliates - \_\_\_\_\_ Decrease in Due to GP/Affiliates - Cash Used: \_\_\_\_\_  
 Cash Used: (Line 363) (Line 375)

\*Before mailing the letter to the owner regarding clarification a review of all footnotes is required.  
 Comments  
 \_\_\_\_\_

**Distribution Analysis**

● Was a Distribution requested by the Owner?  Yes  No  N/A

If so, please provide provide the following information:

Amount of Approval: \_\_\_\_\_ Date of Request: \_\_\_\_\_ Date of Approval: \_\_\_\_\_

**Stated Equity**

Stated Equity (Document): \_\_\_\_\_ Stated Equity (Line 600): \_\_\_\_\_

● Do the above Stated Equity amounts match?  Yes  No  N/A

Supporting Documentation from the most recently executed document: \_\_\_\_\_

● Has a distribution spreadsheet been previously created and in the "Library" for this project?  Yes  No  N/A

**Distributions**

Distribution %:  6%  10% FC5 Distribution %: \_\_\_\_\_  Quarterly Distributions  Annual Distributions

**Accounts Payable**

Other Trade Payables: (Line 257) \_\_\_\_\_

● Was the requested distribution reduced or rejected?  Yes  No  N/A

Comments:

\_\_\_\_\_

**Payments Due**

Residual Receipts/Excess Equity (Line 700): \_\_\_\_\_  
Flex Sub with MassHousing Letter (Line 696): \_\_\_\_\_  
Flex Sub HUD (Line 696): \_\_\_\_\_  
Arrearage Note (Line 570): \_\_\_\_\_  
Section 8 Recap (Line 570-572>0): \_\_\_\_\_  
Other Cash Flow Note: \_\_\_\_\_

**Issues Report**

Please document below any financial or compliance issues that have been identified in the course of your analysis that require follow-up.

\_\_\_\_\_

● Do the issues identified require a Monitoring Plan?  Yes  No

● Would you recommend this development be placed on the financial watch list?  Yes  No

General Comments/Recommendations:

\_\_\_\_\_

Asset Manager \_\_\_\_\_ Date \_\_\_\_\_ Portfolio Manager \_\_\_\_\_ Date \_\_\_\_\_

## Current vs. New Financial Statement Review Process

Item	Before	After
Overall Financial Statement Review	All Projects reviewed the same way (430 Developments for 2015)	Two tier process: Workload reduced for 45% of the portfolio. <ul style="list-style-type: none"> <li>• Tier I “AAA” -192 developments undergo abbreviated review</li> <li>• Tier II all other -238 developments subject to deeper dive analysis</li> </ul>
Timeline	Process complete by June 30.	Process complete by May 31.
Distribution Requests	Fast Track Distribution completed within 14 days of receipt.	Same
Audit Review Program(ARP)	Comprehensive audit work program included specific line item analysis, recap of informational items and an operational review template.	Financial Analysis Program refined to focus on four key areas: <ol style="list-style-type: none"> <li>(1.) Operating threshold analysis</li> <li>(2.) Partnership Obligations</li> <li>(3.) Distributions</li> <li>(4.) Payments Due on Outstanding Obligations.</li> </ol>
Audit Review Spreadsheet	Data entry of Benedict information into a worksheet to verify the auditor’s numbers and conduct an operational review.	Benedict information used to verify Debt Service and Replacement Reserve Deposits.
Operational Review	The Operational Review contained in the ARP focused on 11 specific line items.	Utilize the Income Statement Comparison Report and compare the new financial statement to the prior year’s statement to identify significant variances.
Additional Payments and Obligations	The ARP was used to identify Flexible Subsidy payments due HUD; ReCap obligations; Residual Receipts; Excess Equity and Cash Flow Note payments and Arrearage Note obligations.	Same
Ratio Analysis	N/A	Use Ratio Analysis and established benchmarks for Tier II developments.
Issues Report	N/A	Utilize new “Issues Report” to generate Monitoring Plans in conjunction with the financial statement review process.
Close Out	Letter, approved FC1 schedule and ARS worksheet sent to the agents indicating audit is closed.	Simplified close out letter sent to agent.

## Ratio Analysis and Benchmarks

Performance Indicator	Benchmark	Basis
Debt Service Coverage	≥ 1.10 DSC	MassHousing Underwriting Standard
Operating Expenses as a % of Total Income	Normative range 57% to 72%	Based on MassHousing Portfolio Performance
Operating Expenses per Unit	Normative range \$9000-\$12,000 per unit	Based on MassHousing Portfolio Performance
Vacancy Rate	Normative range 2.5 to 5%	MH Appraisal and Underwriting Standard
Bad Debt	<1%	Based on MassHousing Portfolio Performance
Accounts Payable per Unit	≤ \$300 per unit	Based on MassHousing Portfolio Performance
Accounts Receivable per Unit	Trend Increasing	Based on MassHousing Portfolio Performance