Affordable Housing Organizations: 10 Reasons to Proactively Alert Your Auditors

By Jennifer M. Galasso, CPA, Partner

Auditors are typically very good at uncovering potential financial issues or oversights that could put an affordable housing project in jeopardy. They stake their reputations on ensuring low-income housing business participants have financial statements that satisfy complex federal and state regulations and meet the specific stipulations of each project's agreements. Good auditors are thorough and meticulous – there's not much that gets passed them.

Yet, when it comes to ensuring timely filings and ongoing compliance, there are many instances where it pays to be proactive in communicating key changes or developments to your independent auditors. Addressing these issues early allows organizations to work with their auditors to minimize an issue's impact down the line. In many cases, auditors will have insights on how best to navigate the situation as an experienced auditor most likely has run into these issues before.

With those goals in mind, here are 10 situations affordable housing organizations should alert their auditors to when they happen.

1. Changes in Key Personnel or Management Agents

Shifts in staffing should be addressed well in advance to avoid any disconnect during the audit process. In many cases, it's prudent to develop a written strategic plan detailing the transition. Changes in third party management agents can be especially troublesome as information from both agents may be needed during the audit and tax preparation process. Depending on the timing of the transition, interim procedures may be beneficial.

2. A New Office or New Leases

Leases are required financial statement reporting items. Letting accountants know about changes in these agreements ahead of time can help head off reporting requirements and avoid complications such as unrecorded liability for deferred rent. It's also important to share how the lease is being amortized, if, for example, rent payments are being straight-lined, so that testing and disclosures are properly planned.

3. Amendments to Operating Agreements

Operating agreements are the fundamental building blocks for organization management and defining the roles and responsibilities of all parties involved. If not disclosed properly, changes can result in inaccurate financial statements and tax returns through improper allocations of net gains and losses or errors in calculating distribution requirements. Here are a few key changes that should be disclosed to your independent auditors when they occur:

- Additions or deletions of members/partners
- Timing of distributions
- Changes to allocation of distributions
- Changes to required capital additions
- Changes to governance roles
- Changes to the business purpose

4. Issues with the Property

There are multiple property issues that should be relayed to an auditor as quickly as possible. If the property is generating low income housing tax credits, any units out of service – for any reason – could result in loss of credits and changes to capital contributions. The auditor can help guide management through these issues.

For a HUD subsidized property, a failed Management and Occupancy Review (MOR) inspection is a key issue. Failing that inspection could indicate non-compliance or financial difficulties that would require submitting monthly reports. Management should be prepared to tell their auditors if they have responded within 30 days of the report and if a Corrective Action Plan has been created. This will alert the auditors of any issues with internal control or compliance and guide planning.

A fire at the property should also be addressed promptly. Delays can cause improper reporting on multiple fronts:

- Understated repair expenses
- Overstated revenues due to insurance reimbursement for repairs or claims
- Improper posting of repairs – expenses posted as fixed assets or enhancements/upgrades or damage repairs posted as expenses even when reimbursement and insurance claims make them not true expenses

5. Switching Banks or Closing Bank Accounts

Auditors need to know when an organization has made banking changes in order to efficiently plan required confirmation procedures. In cases where the bank accounts have been closed or moved, auditors need to make sure the funds have been transferred from the old account to the new account and/or ascertain how the remaining funds were expended.

6. Rent Increases, New Material Grants and Contracts

Any rent increases, new material grants or contracts should be provided before an audit begins. If the audit team begins their planning and field work without that vital information, testing results may be insufficient, and procedures may need to be re-performed. In some cases, auditors may need to revisit their original risk assessment and documentation, costing both auditors and clients more time and resources.

7. Refinancing Debt

Debt refinancing could potentially involve significant adjustments to financial statements beyond simply replacing one loan with another. There are a number of clarifying details that should go along with disclosing refinancing:

- Is the debt considered paid off and new debt taken out or just a refinancing of the current debt?
- How were the debt financing costs reported on both the old and new debt?

Review of the disclosure requirements of the change in terms, including interest rates, repayment requirements and loan covenants, is also important. Many of these points can be discussed prior to the organization’s year end in order to eliminate complications during the audit.

8. Change in Accounting Software or Chart of Accounts

There are times when an organization may benefit from changing or updating its accounting software. Often, this results in a change to the chart of accounts as well. Whether it be account numbers or account names changing, it is mutually beneficial to inform auditors of this conversion. When clients are forthcoming about such a change, auditors can properly plan as this type of change can affect several audit procedures that are typically performed in the planning stages. One way to handle this is to produce a cross-walk document, which bridges the old and new chart of accounts.

9. Litigation in Progress or the Threat of Litigation

Legal challenges and questions around transparency are of interest to all auditors. Losses due to unfavorable litigation outcomes must be recorded in financial statements. That process should begin if the unfavorable outcome is probable and an estimate amount is known. It's critical that auditors have a chance to confirm information with legal counsel and management to ensure financial statements are not materially understated.

Even a threat of litigation may prompt expanded audit procedures or disclosures. By discussing these activities early on, auditors can work with management on reporting and potential adjustments before the audit officially begins.

10. New Projects and Joint Ventures

New undertakings and joint ventures have a way of taking on a life of their own. With proper planning, these new developments can be addressed efficiently and promptly. Giving auditors a heads up allows them to adjust their timing and planning as needed and research any additional disclosure or reporting requirements.

Head Off Risk with Proactive Communication

In all of these instances, getting on the same page with auditors early in the process can help stave off costly rework, delays in report issuance or potential compliance issues down the road. This kind of proactive communication is a good rule of thumb for all interactions, particularly when the audit and advisory team has the experience and expertise to provide value-added insights.

Contact Us

If you require accounting, auditing, tax or consulting assistance with your HUD or affordable housing property, please contact your PKF O'Connor Davies client engagement team or Jennifer M. Galasso, CPA, Partner at jgalasso@pkfod.com.