Financial Management and HUD Compliance

curriculum

supportive housing training series

Corporation for Supportive Housing

U.S. Department of Housing and Urban Development

CUCS
Center for Urban Community Services, Inc.

Financial Management and HUD Compliance

Curriculum

Developed by Center for Urban Community Services

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Financial Management and HUD Compliance is part of the Supportive Housing Training Series. This training series currently includes eleven curricula providing best practices and guidance on supportive housing development, operation and services.

The full series is available for downloading from the Department of Housing and Urban Development website.

For more information:
U.S. Department of Housing and Urban Development: www.hud.gov
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H U D C U R R I C U L U M
FINANCIAL MANAGEMENT AND HUD COMPLIANCE

PURPOSE AND GOALS: The purpose of this six-hour training is to provide an overview of the key principles of financial management for non-profit organizations and provide detailed information on budgeting and compliance issues for supportive housing projects. At the end of this training, participants will have an understanding of key financial management concepts, be able to understand and develop supportive housing budgets and understand the requirements associated with HUD funding programs.

AGENDA

I. INTRODUCTION (20–30 minutes)

II. WHAT IS FINANCIAL MANAGEMENT?

A. KEY CONCEPTS OF FINANCIAL MANAGEMENT (10–20 minutes)

B. THE FINANCIAL AND ACCOUNTING SYSTEM (10–20 minutes)

C. PLANNING AND BUDGETING (20–30 minutes)

D. THE FINANCIAL STATEMENTS (10–20 minutes)

E. THE INTERNAL CONTROL SYSTEM (10–20 minutes)

F. THE PUBLIC AUDIT (20–30 minutes)

G. OTHER AUDITS (10–20 minutes)

H. STATE & FEDERAL TAX RETURN REQUIREMENTS & FILING (10–20 min)

I. STAFFING (10–20 minutes)

III. ACCOUNTING FOR THE SUPPORTIVE HOUSING COMPONENTS

A. INTRODUCTION (10–20 minutes)

B. HOUSING DEVELOPMENT (20–30 minutes)

B1. The Pre-development Budget and Budget Management (20–30 minutes)

B2. The Development Budget — Hard and Soft Costs (10–20 minutes)

B3. Tracking Construction Draws and Payouts (10–20 minutes)

C. OPERATIONS (20–30 minutes)

C1. The Operating Budget (20–30 minutes)

C2. Planning for Reserves and Replacement (10–20 minutes)

C3. Planning for Debt Service (10–20 minutes)

C4. Planning for Capital Expenditures (10–20 minutes)

C5. The Accounting Systems and Procedures (10–20 minutes)

C6. Rent Receivables (10–20 minutes)

C7. Budget Management (10–20 minutes)

D. SOCIAL SERVICES

D1. The Social Services Budget (10–20 minutes)

D2. Fund Accounting for Program Services (10–20 minutes)

D3. Monitoring Expenditures/Budget Variance Reports (10–20 minutes)

IV. THE ANNUAL PROGRESS REPORT

A. INTRODUCTION (20–30 minutes)

B. PROJECT PROGRESS (20–30 minutes)

C. FINANCIAL REPORTING (20–30 minutes)

V. CONCLUSION (10–20 minutes)

HANDOUTS

1. AGENDA
2. FINANCIAL AND ACCOUNTING ACTIVITIES
3. UNDERSTANDING BUDGETS
4. PLANNING AND BUDGETING GUIDELINES
5. INTERNAL CONTROLS
6. OVERVIEW OF AUDITS
7. GLOSSARY OF ACCOUNTING TERMS
8. SUPPORTIVE HOUSING DEVELOPMENT PHASES
9. SAMPLE TIMELINE FOR DEVELOPMENT OF SUPPORTIVE HOUSING PROJECT
10. DEVELOPING SERVICES IN SUPPORTIVE HOUSING: MILESTONES AND ISSUES IN THE FIRST YEAR
11. SAMPLE DEVELOPMENT BUDGET
12. DEVELOPMENT BUDGET WITH TAX CREDITS (NOT IN MATERIALS — TO COME)
13. COMPONENTS OF A MANAGEMENT AGREEMENT
14. SAMPLE OPERATING BUDGET
15. SAMPLE SOCIAL SERVICES BUDGET
16. HUD ANNUAL PROGRESS REPORT
17. COMPLETED SAMPLE HUD ANNUAL PROGRESS REPORT
18. APR FREQUENTLY ASKED QUESTIONS
19. APR DEMOGRAPHIC TRACKING SHEET
20. APR DEMOGRAPHIC TRACKING SHEET LEGEND
21. FINANCIAL MANAGEMENT AND HUD COMPLIANCE: ADDITIONAL READINGS

TRAINER'S PREFACE

I. Brief Summary of Curriculum Content

This curriculum contains at least six hours of verbal content. This does not mean that all of the content must be covered in its entirety. Depending on the intended focus of the training, the nature and job requirements of the participants, and the format (exercises and small group discussions vs. large group presentation), portions of this training can be elaborated, abridged and/or deleted.

The written curriculum contains a great deal of explanatory and background material on principles and practice of financial management. Much of this information is more specialized than most training participants will require. Highlights and group activities have been provided for that material which is more universally applicable. Trainers should familiarize participants with the information contained in this curriculum and invite them to review the material in other settings.

The material as presented addresses two major interrelated topics:

- Financial management for non-profit organizations; and
- Financial management tasks associated with a supportive housing project.

The trainer's first task will be to determine the background and interests of the participants and focus the training session on those aspects of the curriculum that are most appropriate and relevant. Staff with considerable knowledge of financial management will likely be familiar with much of the information in the financial management section and these individuals would most likely obtain greater benefit from a training that focuses on the specific financial management tasks associated with supportive housing projects. Conversely, participants who are directly involved with planning or operating a supportive housing project may have less awareness of financial management concepts and practices and would benefit from more focus on this area.

II. Trainer Qualification

Key to the successful delivery of the curriculum and to participants learning is the qualifications of the trainer. What the trainer brings to the training session—including their knowledge about the subject being taught, their experience in supportive housing, and their training or teaching skills—will impact the quality of the training and the outcomes. This curriculum is intended for use by individuals with the appropriate constellation of talent and ability to manage the learning of others in addressing the issues of financial management and HUD compliance.

III. Good Training Practice

A. How People Learn

People learn through a combination of lecture, visual aids and participation. The more actively they are involved in the process, the more information they will retain. For this reason, eliciting answers from the group rather than presenting material is usually preferable. Additionally, it is important to include exercises that stimulate interaction and experiential learning and not spend all of the time lecturing. Be aware, however, that group participation and discussion takes more time than straightforward presentations and may cut down on the amount of content it is possible to cover. What is minimized or deleted from the curriculum should be based on the assessment of the group's learning needs and the goals initially contracted with the group.

B. Know Your Audience

The type of setting that the trainees work in and their roles will determine the areas of the curriculum that the trainer will focus on. Gathering as much information about the group beforehand is recommended. Some information contained in this curriculum, such as establishing organizational policies for financial management will be within the purview of executive staff and boards of directors only. Other material, such as understanding budgets and how to use budgets in on-going program operations is more universally applicable to participants.

C. Introductions and the Training Contract

Introductions should provide the trainer with more information about the audience. The trainer will want to know the person's name, their program and their role, and what s/he hopes to get out of the training. The trainer should then clarify what will and will not be covered. This is the training contract.

D. Acknowledge and Use Expertise of the Participants

This is important as it allows people to learn from each other, builds group cohesion, keeps people involved and establishes an atmosphere of mutual respect.

E. Flexibility

Throughout the training the trainer should continually assess the needs of the group and revise the amount of time devoted to each specific topic. Responding to the needs and interests of the group must be balanced with the agreement to cover certain topics. It is the trainer's job to respond to the needs that arise and yet stay focused on the subject matter.

IV. Training Content

A. Sequence of Content

This training is designed to help participants to understand the basic principles of financial management for non-profit organizations and then apply these principles to the development and operation of supportive housing and meeting the requirements of HUD homeless assistance grant programs. The initial component provides general principles applicable to all non-profit organizations. The later components talk about financial management in developing and operating supportive housing and the final segment teaches how to comply with HUD homeless assistance reporting requirements. The trainer should assess whether participants are involved in supportive housing development and/or operations and HUD homeless assistance grants and include these components based on applicable needs.

B. Flexibility of Content

The amount of depth that this training allows for depends on the learning needs of the training group. If trainees have basic familiarity with financial management principles, the first section can be dealt with as a quick overview. The sections on development and operating housing and supportive services can be abridged or skipped if the trainees are not involved in one or more of these activities. Similarly, the section on HUD reporting requirements will only be used if the trainees have HUD homeless assistance grants.

V. Time Management of Content

Each section of the agenda has time frames allotted. The trainer should be aware that if a great deal of time is devoted to one topic area, other content areas might be sacrificed. Group exercises can always be abridged if necessary for time's sake. For example, if the group exercise involves dividing into four groups to work on four separate cases, the trainer should consider having each group work on a smaller number of cases. This will shorten the report back time, but will not eliminate the group process. Remember elicitation and discussion takes more time than lecturing but less time than small group exercises. The trainer needs to balance this with the fact that lecturing is also the least effective way to learn.

The trainer will find that each time this curriculum is trained, it will vary. Being mindful of good training practice and making adjustments to the timing and sequence will allow for a tailored training that will be most beneficial to participants.

I. INTRODUCTION (20–30 minutes)

TRAINER NOTE: The following information should be summarized to provide participants with an overall understanding of the milieu and context for the training:

BRIEF LECTURE:

Non-profit organizations operating supportive housing projects provide an essential service that increases the health and well-being of an extremely fragile population. The staffs and boards of directors of these organizations are generally motivated by a profound sense of mission. It is common to enter the profession with backgrounds in human services and much of the executive leadership will have been trained as service providers instead of professional managers.

At the same time, successful supportive housing providers have the potential to rapidly become corporations with annual budgets in the hundreds of thousands or even millions of dollars. The successful management of these financial resources is essential not only to the continued delivery of the human services on which the organizations' tenants depend but also for the well being of the staff who, along with families and dependents, are reliant on the organization's success.

Many organizations solve the financial management problem by hiring professional managers to run the financial side of the organization while the remainder of the organization and staff focus on the mission. Although this approach can address the fundamental financial management needs, it also diminishes the ability of all managers to participate in essential planning for the organization. It might have been effective in a time of increasing resources where the key strategy was planning for growth. In an era of potentially diminishing resources for supportive housing, however, all key staff of the organization must have the basic skills needed to understand budgets and engage in ongoing planning of financial resources. Otherwise, program staff will essentially cede planning to the financial managers.

The goal of this training is to increase the understanding of financial management for program managers of supportive housing organizations. It seeks to broaden their understanding of key financial management concepts and internal control mechanisms. This will facilitate the use of financial information in planning and managing program services.

TRAINER STATES: The specific goals and purpose of this training are:

- To provide trainees with an understanding of the crucial role of sound financial management to the success of their organization and its ability to deliver services to its tenants.
- To assist program staff and financial managers to be able to communicate more effectively on budgetary matters.

- To equip program staff to be able to understand and develop budgets for housing development, housing operations and supportive services delivery.
- To provide program staff with the skills needed to be able to use budgets in the management of their programs.
- To give an understanding of HUD reporting requirements and assist staff in completing HUD reporting requirements.

TRAINER NOTE: Following a statement about the purpose and goals of the training, the trainer should review the agenda. See ***HANDOUT#1: AGENDA*.**

TRAINER STATES: Let's go around the room and find out who everyone is. State your name, agency, role/job and what you hope to get out of today's training.

TRAINER NOTE: The Trainer can either ask people to state their goals after they introduce themselves or ask the entire group to discuss their goals following all of the introductions. Record what the trainees state about what that they want to get out of the training and record on flipchart. After hearing their goals, it is important to discuss what will and will not be covered so that trainees know what to expect — this is the learning contract. If someone mentions something in the go-round that is not on the agenda but related, see if it can be tied to an appropriate point in the training.

TRAINER NOTE: ICEBREAKER: Icebreaker on how people handle personal financial management. Inform the trainees that they will now do an exercise, the purpose of which is to introduce themselves to one another and get to know members of their own community. Instruct the group to find a person in the room whom s/he does not know and spend five minutes with that person. Focus on how the individual deals with their income tax responsibilities. Do they get everything done early in January or wait until the evening of April 14th? How do they keep records and information that they will need at tax time? How are the responsibilities for dealing with taxes divided in their households? Do they have to ask for extensions? Are they surprised by the size of their refunds/tax bills? On the whole, how do they regard their record-keeping responsibilities at tax time? After 10 minutes call "time" and ask each group to pair up with another pair (four persons to a group). Instruct each pair to introduce their partner to the group. Call time after another 10 minutes. Process with the large group how the exercise went. See how the trainees' response to their individual financial management/reporting requirements corresponds to how they react to requirements within their organization.

LEARNING POINT: Program staff at supportive housing programs need to understand the importance of overcoming 'budget-phobia,' learning to participate in the budgeting process and to use budgets as a critical management tool.

II. WHAT IS FINANCIAL MANAGEMENT?

II.A: KEY CONCEPTS OF FINANCIAL MANAGEMENT (10–20 minutes)

TRAINER NOTE: See ***HANDOUT #2: FINANCIAL AND ACCOUNTING ACTIVITIES*.**

Financial management of the non-profit should be geared towards the long-term stability of the organization.

Long-term stability is critical to the non-profit's ability to secure resources to meet its mission and goals. The inability to successfully or adequately manage financial resources will likely preclude non-profit organizations from obtaining and/or renewing government contracts and/or philanthropic support.

For the non-profit organization, long-term stability means having the ability to meet its financial obligations such as, payroll, rent, the cost of implementing and maintaining programs, etc.

To properly perform the financial management function, the Financial Manager must ensure that the organization's financial transactions are appropriately recorded and maintained; perform financial analysis on financial data; utilize this information to inform the organization's plans; make investing and financing decisions based on the organization's plans and financial situation; and manage financial resources to meet the planned objectives of the organization.

TRAINER ELICITS: WHAT ARE SOME KEY TASKS ASSOCIATED WITH THE FINANCIAL MANAGEMENT OF YOUR ORGANIZATIONS? [Expected responses include:]

- Developing, implementing and maintaining an adequate system for recording and maintaining the financial transactions of the organization
- Determining the proper amounts of funds needed to operate the organization's business
- Efficiently allocating funds to programs, administration, capital investment and other assets
- Managing cash flow, inventory and receivables
- Controlling risk
- Reducing excessive costs
- Coordinating the organization's financial planning and budgeting processes

LEARNING POINT: Financial management includes a wide range of activities, including record keeping, developing projections (budgets) and analysis.

II.B: THE FINANCIAL AND ACCOUNTING SYSTEM (10–20 minutes)

TRAINER NOTE: For the most part, the information contained on the financial and accounting system is material that need not be directly covered in the training. Instead, refer participants to their manual and the written information available in it.

BRIEF LECTURE:

Financial information is generated from the financial and accounting system. The activities of the accounting system include:

FINANCIAL ACTIVITIES

Financial activities can be very different from one organization to another depending on the size of the organization and the complexity of its operations. The financial activities of the non-profit organization can be grouped into three general areas:

1. TRANSACTION HANDLING AND RECORD-KEEPING is the bookkeeping/accounting area of financial activity. Checks must be written to pay bills; incoming checks must be deposited; ongoing records of financial activities must be kept. Concerns in this area include:

   - Timely and accurate billing for services performed
   - Timely and accurate payment of bills for goods and services purchased
   - Prompt deposit of receipts
   - Proper authorization of payments
   - Accurate recording of transactions
   - Timely and accurate preparation of financial reports

2. PLANNING AND BUDGETING are processes in which the organization sets goals and objectives, chooses programs and decides how those programs will be operated. The budgeting process relies both on financial information about past performance and the organization's future plans. Concerns in this area include:

   - Involving people appropriately in the budget process
   - Considering both internal and external factors in the budget process
   - Using past and current information to develop realistic projections
   - Securing agreement on the use of the budget in managing ongoing operations

   TRAINER ELICITS: HOW ARE YOU INVOLVED IN THE BUDGET PROCESS IN YOUR ORGANIZATIONS? [Expected responses include:]

- Develop the annual budgets for their units? If yes, what information do they use to develop these budgets?
- Periodically track actual expenses against their budgets
- Change what they do in terms of service delivery or other functions based on budgetary information that they have received

3. FINANCIAL MANAGEMENT is the management of current financial operations based on analysis of financial information and knowledge of the organization's objectives and plans. The financial manager oversees and directs the accounting process and participates in budget development and revision. In addition, the financial manager is responsible for such activities as cash flow management, cost allocations, cost analysis and assessment. Concerns for the financial manager include:

   - Anticipating financial problems
   - Maximizing use of financial resources
   - Ensuring tax compliance and compliance with funder requirements
   - Providing meaningful information to program managers

TRAINER NOTE: The following is an optional topic. Most trainees are not expected to be involved in decision-making regarding the administration of the Fiscal Office of their organizations. If this topic is to be covered in training, trainer should open the topic by eliciting the following:

TRAINER ELICITS: HOW DO YOU INTERACT WITH YOUR FISCAL OFFICE? [Expected responses include:]

- Prepare funding vouchers or progress reports or participate with fiscal office in the preparation of these?
- Develop strategies to increase revenues for your unit or decrease expenditures?

ADMINISTRATION OF THE FISCAL OFFICE

The administration of the fiscal office involves developing the staffing and organization systems to accomplish the above functions. Concerns in this area include:

- Deciding on the structure of the fiscal office. For example: Should a bookkeeper be hired or should the organization contract with an outside service?
- Deciding on leadership of the financial function. For example: Should the executive director also serve as finance director?

- Deciding whether the organization is required to have an audit, whether there are reasons the organization should have an audit, even if one is not required, the type of audit that is best for the organization, and how to choose an auditor as well as using the results of an audit to improve internal processes.

SELECTING ACCOUNTING SOFTWARE

TRAINER NOTE: This section is optional. See note above regarding Optional Topics.

There are various existing automated systems available that will meet the needs of most non-profit organizations. An accounting system can aggregate information in many ways. The level of information and therefore the sophistication of the accounting software must be determined by management.

In selecting a system, the organization must look at the costs of the accounting system versus the benefits of having the information it can provide. It is important to remember that even if a system has the ability to provide information in formats that may be useful to the organization it would not be able to provide the information, if the organization does not have the personnel needed to get information into the system. The purchase of sophisticated software does not mean that there may not be some initial increase in personnel cost. This cost needs to be considered when doing the cost-benefit analysis.

A key factor to consider is whether the organization requires a sophisticated specialty software program such as a program capable of performing Medicaid billing and record-keeping or whether it can manage its finances with an off-the-shelf program such as QuickBooks. Off-the-shelf technology will not only be substantially less expensive to purchase, but it will also be possible to hire staff with experience in operating the program.

LEARNING POINT: Organizations should carefully assess off-the-shelf financial management programs prior to purchasing a high cost specialty program.

II.C: PLANNING AND BUDGETING (20–30 minutes)

TRAINER NOTE: A key theme of this training is the understanding that budgets are not simply an exercise that must be performed but a key part of management and effective delivery of services to tenants. Additionally, the trainees should understand that budgets should not be considered an annual obligation that, once completed, is filed away and not looked at again but vital, on-going tools for the management of the organization and individual components within the organization. See ***HANDOUT #3: UNDERSTANDING BUDGETS*** and ***HANDOUT #4: PLANNING AND BUDGETING GUIDELINES***.

TRAINER STATES: Program planners and fiscal managers speak different languages and often have different priorities and different approaches to the planning and budget processes. These differences can sometimes lead to different perceptions of what is involved in the planning and budgeting processes and different expectations of the outcomes of the processes. Without deliberate care and thoughtfulness, planning and financial management can become activities that divide rather than unite the organization.

Program planning is often viewed as the domain of the executive director, program directors and the board. Fiscal management, on the other hand, is usually assigned to the bookkeeper, accounting and finance directors and perhaps the board treasurer. Fiscal personnel, may at times, view some program planning decisions as failing to recognize economic realities, while program planners may at times feel that fiscal management decisions lack sensitivity to the programmatic mission of the organization. These conflicts are often fought out in the budget process — the very process that should unite these viewpoints.

Budgets are tools of the financial management system used for two central management functions: (1) decision-making and (2) monitoring and controlling.

- A budget is a plan of action expressed in financial terms. In the course of planning, the organization defines its purpose, mission, goals, objectives, strategies and activities.

  Through the budget process, decision-makers look at the financial implications of their plans. They must evaluate how much the program will cost and they must evaluate anticipated revenues for the program. Based on an evaluation of scarce resources, the organization sets priorities and develops budgets.

  A budget describes and estimates the expected income from revenue sources and the expenditures, which the organization will need to achieve its program objectives.

- The budget is also a tool for monitoring and controlling ongoing organizational activities. Once a plan has been developed, the organization needs information to determine whether it is operating in line with its planned objectives.

By itself, an organization going "off track" is neither "good" nor "bad." The implications for the organization must be considered in terms of what is occurring in the organization at the present.

- Since the budget describes the plan in terms of dollars, it provides a basis for monitoring progress by comparing the organization's actual revenues and expenses to the budget. If, for example, a program is costing more than anticipated, it may be necessary to bring costs down, or it may be decided to review the plan to take a higher level of expense into account.

  Since a budget is a planning document, an effective budget is one that accurately anticipates and projects the interplay between program and fiscal activities. An effective budget serves as a guideline that reflects the best estimate by an organization's decision-makers of the anticipated revenues and the costs of operating various program activities.

- Budgets should not be documents that are developed each year, only to be filed away until next year. They should be useful tools used to anticipate problems and to provide a baseline against which actual program and financial experience can be monitored. Budgets should be designed to be modified based on updated information. A budget that is never changed is likely to be a budget that is never used.

- Budgets should not be designed to "look good" to someone else — a funder, a board member, a director or the public. When budgets are designed to create an impression, rather than as expressions of program plans, they lose their ability to assist the organization in planning, monitoring and controlling.

TRAINER STATES: In summary, an organization needs to prepare annual budgets because it helps the organization:

- Define goals for a given period of time
- Monitor progress throughout that period of time
- Point out the significant variances between the financial goals and how resources are actually being used
- Take corrective action as problems arise
- Predict and monitor cash flow
- Illustrate need to funding agencies

LEARNING POINT: Budgets are plans of action expressed in financial terms; to be effective tools, they must be regularly re-assessed and modified based on actual experience and outcomes.

THE PLANNING AND BUDGETING PROCESS

TRAINER NOTE: The section is also optional. Most trainees will not have decision-making roles in establishing policy for the budgeting process.

BRIEF LECTURE:

The budget process is a complex one that can involve the entire organization, executive director, program directors, financial staff, finance committee, board treasurer, the fundraising committee, etc. Involving appropriate individuals in this process provides the opportunity to unite different viewpoints. The following ten-step process can help make the budget process an effective and efficient process:

STEP 1: Establish the budget period and review program achievements and financial performance for the prior period.

- The budget period should be the same as the organization's accounting (fiscal) year. This facilitates comparisons of budget projections to the actual experience of the organization. The budget need not be January 1 to December 31, and often it is convenient to use a similar fiscal year as the major funder of an organization. If, for example, primary contracts are with the state government, then it might be convenient to adopt the state fiscal year for the organization.
- Both staff and board should review the programs achievements and financial performance for the prior year. This would include, but is not limited to, reviewing objectives achieved, program statistics and cost per unit of service or outcome achieved. It should also include reviewing budget to actual comparisons for the prior year.

STEP 2: Identifying major programs and activities of the organization and setting goals and objectives for the budget period.

- This is one of the most important activities in the planning process. Involving staff at all levels in this process helps secure buy-in to the process and the results of the process. It also helps secure commitment to program objectives and goals.
- The major programs and activities of the organization that are identified should be the same as those used by the accounting department to generate financial reports.
- The organization should develop (or review and revise) its long-range plan, and then develop a list of programmatic and organizational objectives to be achieved during the year. By defining measurable objectives the organization can later determine to what extent those objectives have been achieved.

STEP 3: Decide on a method for cost allocation and estimate the cost of required resources (expenses).

- Any organization will have some indirect costs that are not directly identifiable to specific programs/activities. The organization needs to decide how these costs will be allocated to different programs/activities. For example, rent may be allocated based on square footage usage, while insurance costs may be allocated based on the number of employees assigned to a program.

- Determine the number of staff, supplies and other resources needed to attain the objectives of different programs/activities, based on the organization's past experience, the experiences of other agencies and current considerations.

- Remember that in addition to resources directly used for a program, there may be hidden costs required to support the program. For example, if a new program will require ten new staff positions, plans must be made considering time to hire, train and support the new staff, as well as advertising costs, office equipment and furniture and space for the new staff, etc.

- In estimating the cost of required resources, the organization must not only determine the direct costs of running a program, but should determine the shared or indirect costs, such as rent, telephone, accounting, etc.

- The federal government defines indirect costs as: those incurred for a common purpose and therefore benefiting more than one organizational activity ('cost objective') and not readily attributable to specific activities without an excessive level of effort. It isn't possible to determine which costs will be classified as 'indirect' in all situations for all non-profit organizations. Typical indirect costs include: depreciation or use allowances on building and equipment; costs of operating and maintaining facilities; and general administration and general expenses such as the salaries and expenses of executive officers, personnel administration and accounting.

- The federal government also requires that indirect costs be classified in two categories: 'Facilities' and 'Administration.' Facilities is defined as depreciation and use allowances on buildings, equipment and capital improvement, interest on debt associated with certain buildings, equipment and capital improvements, and operations and maintenance expenses. Administration is defined as general expenses such as executive management, personnel, accounting, library and expenses related to these functions. For further information on this topic, please see OMB Circulars A-87 and A-122. (Go to www.whitehouse.gov/omb, click on 'Circulars.')

STEP 4: Estimate anticipated revenue.

- Just as the organization must evaluate its planned expenses, it must also evaluate planned revenues. Again, historic information, the experiences of others and current considerations will form the basis for revenue estimates.
- The organization must make the most realistic assessment possible of revenue estimates. A useful method to maintaining a realist view of revenues is to assign probability of realizing the revenue. For example, signed contacts would have 100% probability, contracts that have been approved and are in the sign-off process may have a 95% probability, while a proposal that is being developed would be assigned a very low probability. Revenue estimates would then make it into the budget depending on the probability of realizing the revenue (90% and over would be more realistic than 80% and over and so on). Budgeted revenues can then be revised as probability of realizing revenue changes.
- It is also useful to develop contingency budgets for more conservative or optimistic projections of revenues. It is difficult to develop contingency plans for revenue when the organization's revenue comes in large chunks from a few sources, such as foundations, corporations and government agencies, because of the significant impact a loss or change in the level of funding would have of the organization's operations.
- As a rule of thumb, it is always best to err in the direction of a very conservative estimate of revenues when a source of revenue is unknown, highly competitive and not intended for ongoing support.

STEP 5: Make necessary adjustments to bring estimated revenues and expenses into desirable relationship.

- Once the initial estimates for revenue and expenses have been made, the organization can see whether it has a balanced budget or whether revenue or expense exceeds the other.
- An organization may choose to incur a deficit during a budget period, realize a surplus or simply "break even." There is no rule that budgets must balance in each budget period; however, large deficits can, of course, lead to bankruptcy and an end to the services being provided. Large surpluses on the other hand, may represent an abrogation of responsibilities for serving the public interest.
- For any given budget period, however, the revenue and expense should be in the relationship the organization chooses for that given period, rather than mechanically "balanced."

- To bring revenue and expense into the desired relation, the organization must re-evaluate its programs and make adjustments. In some cases, the organization may have to increase fundraising goals or reduce program expenditures.
- When reviewing the revenue budget, it is important to avoid the temptation of raising the estimates without changing the plans for generating additional revenue. It is not enough just to say, "We'll try harder to raise more money next year." An organization should have a carefully developed fundraising plan that is reviewed on a regular basis. If the fundraising plans turns out to have been unrealistic, the organization will need to make budget modifications.
- If expenses need to be reduced, it is helpful to determine the costs of each program at different service levels. For example, one might find the cost for providing services for Program A at half the current service level results in decrease in costs by only one-third. Do not assume that benefits and costs move together, with each additional dollar of spending resulting in an additional dollar of service. "Economies of scale" are present in most projects, and beyond a certain point, additional expenses may bring diminishing returns. As a result, there may be some programs where large reductions in expenses will result in less reduction in services than in other programs.
- Cost-benefit analysis is a tool that an organization may find helpful in making hard decisions regarding cutting or increasing costs. Cost-benefit analysis is used to examine the costs required to achieve a certain objective and requires assigning dollar values to the benefits and objectives achieved.

STEP 6: Prepare a cash flow projection and plan for cash flow and cash reserves.

- In addition to planning for revenue and expense to support the organization's programmatic objectives, an organization should prepare a cash flow projection. This involves projecting monthly cash in-flows and cash out-flows for the budget period. For example, even if an organization has a "balanced budget," it may not receive the revenue until the end of the budget period, while its expenses may be spread throughout the period. A cash flow projection will help the organization foresee cash flow problems and plan for solutions.
- If cash flow is a recurring or ongoing problem, it may be wise to set aside funds each year to build a cash reserve. Even if cash is not necessarily a problem, an organization might consider building a cash reserve of at least three to six months of operating expenses to cover the loss of a major grant or for start-up costs for a new program.

STEP 7: Approve the budget

- While the staff is responsible for developing the budget, the board, acting in its governing role, approves the budget.

STEP 8: Implement the plan and the budget

- Staff has the responsibility for implementing the plan and the budget. The executive director and program directors should agree on what line items program directors are responsible for monitoring and controlling.

STEP 9: Compare revenue and expense actual to budget

- Budget to Actual Reports comparing revenue and expense actual to budget should be generated in a timely manner (no later than 2–3 weeks after the close of the month) and distributed to those with budget control responsibility, such as the executive director, program directors, the finance committee and/or the treasurer.

STEP 10: Update cash flows and revise plan and budget as appropriate

- Cash flow projections should be updated monthly based on the actual balance of cash at the end of the last month and updated information on the timing of cash receipts and cash disbursements.

- A budget should be a guide to, not a substitute for, decision-making. Therefore, budget should be used as a tool for assisting managers in their decision-making process. Budgets should be revised to reflect material changes in current financial and program data. A revised budget helps the organization anticipate where it will stand at the end of the year, setting the stage for the next budget period.

TRAINER NOTE: The essential information regarding budget presentation concerns the difference between operating and capital budgets. Trainees should also understand the importance of cash flow projections. Refer to the sample budgets provided to the trainees to provide an understanding of capital and operating budgets.

BUDGET PRESENTATION

TRAINER STATES: The organization should prepare an operating budget and a capital budget. The operating budget and the capital budget should be classified by department, program, activity, grant, etc., as appropriate for the organization.

Documentation supporting each element of each line item in the form of narratives, formulas, as well as assumptions used in calculating numbers and contingency percentages should be prepared and kept.

The overall budget should be presented in a matrix format, by natural classifications as well as functional classifications. Functional classifications include general and administration, fundraising and individual programs whereas natural classifications include salaries, rent, utilities, etc.

Functional classification of budgets gives more depth to the line item budget. Functional budgets are valuable as planning and monitoring tools since each program's costs and revenues can be evaluated separately and considered in prioritizing among programs.

The accounting system of the organization must be able to provide revenue and expense statements for each functional area, similar to the budget format, otherwise monitoring and controlling the budget will become impossible.

The capital budget should be presented listing individual items that the organization plans to purchase and/or improve and their estimated cost.

Non-profit organizations often receive revenue from multiple sources and must prepare budgets for each of those funders. A single line item such as personnel or travel may be partially paid by multiple sources, and the organization may find it advantageous to prepare a source budget that details major funders, and what portion of each line item has been budgeted to that funder. The accounting system, however, should be set up to track revenue and expense by program/activity, not by source. Subsidiary journals may be developed to track an individual funder's budget line items.

CASH FLOWS

TRAINER STATES: It is obvious that if an organization has more expenses than income, sooner or later it will find itself in trouble. It is less obvious, however, when an organization has more income than expense and still finds itself in financial troubles. This occurs if the income and expenses occur at different times, so that there is not enough cash to pay for the expenses when they become due and payable. Most non-profit organizations are constantly fighting the cash flow management battle.

The term "cash flow" refers to the need to have cash come in at the right time to meet expenses. Cash flow can be projected, monitored and controlled. Cash flow projections are typically developed as part of the budget process, so that possible cash shortages or cash surpluses can be anticipated. As the year progresses, cash flow projections can and should be updated as new information becomes available. Cash flow projections may be done weekly or monthly depending on how tight cash is in an organization. Based on cash flow projections, management may decide to postpone a project, borrow money, cut expenses or increase revenues. There is no universal format for cash flow projections, so organizations should establish one that meets their needs.

While in preparing the budget, the focus is on how much revenue and support the organization will earn, how much expense it will incur, and how much of the support will be restricted to specific purposes, in preparing the cash flow projection, the focus is on the timing of receipt and disbursement of cash, regardless of its origins and use. For example, assume an organization has a contract to provide services for a governmental agency during the month of January for a cost of $30,000. In February, the organization prepares and submits an invoice to the agency for the previous month's services, but it does not receive payment on the invoice until March. In this situation, the operating budget will show $30,000 in expected income for the month of January, where the cash flow projection will show an expected receipt of $30,000 in the month of March.

TRAINER ELICITS: WHAT ARE SOME STRATEGIES FOR ADDRESSING CASH FLOW PROBLEMS? [Expected responses include:]

As part of the cash flow management, financial managers consider a variety of responses. A projected temporary shortage can be resolved by:

- Loans
- Lines of Credit
- Speeding up collection of receivables
- Requiring fees to be paid in advance
- Changing the timing of planned fundraising events or campaigns
- Financing the purchase of capital equipment
- Liquidating investments
- Working with funders for a more favorable payment schedule
- Delaying payment to vendors

A projected temporary cash surplus can be taken advantage of by:

- Short term investments
- Changing the timing of planned fundraising events or campaigns
- Making loans
- Buying supplies on sale that won't be needed immediately

Note that these responses address the timing of cash in-flows and cash out-flows, as opposed to increasing income or decreasing expense.

LEARNING POINT: Good financial management includes tracking the overall magnitude of income and expenses (e.g., is the budget balanced?) as well as the timing of when funds are available and when are expenses incurred.

II.D: THE FINANCIAL STATEMENTS (10–20 minutes)

TRAINER NOTE: Financial statements are an optional topic not included unless the group has an extremely high level of interest in financial management.

To perform financial management activities the Financial Manager must have up-to-date, reliable and meaningful financial data to evaluate the organization's operations and its financial status. This financial data should be recorded, reviewed, summarized and reported through the organization's accounting system.

The accounting and reporting requirements for non-profit organizations are provided by Financial Accounting Board (FASB) 116 (Accounting for Contributions Received and Contributions Made) and FASB 117 (Financial Statements of Not-For-Profit Organizations), which is designed to improve the usefulness, understandability and comparability of financial statements.

The end product of an accounting process is a set of financial statements summarizing all the financial transactions of the organization and showing its assets, liabilities, net assets revenue, public support and expenses. A set of financial statements typically includes the following:

- STATEMENT OF FINANCIAL POSITION — The statement of financial position shows an organization's assets, liabilities, unrestricted net assets, temporarily restricted net assets and permanently restricted net assets at a given point.
- STATEMENT OF ACTIVITIES — The statement of activities shows the organization's revenue, public support and expenses classified as unrestricted or temporarily restricted.
- STATEMENT OF CASH FLOWS — The statement of cash flows is a summary of the resources made available to the organization during the period and the uses of such resources. The statement of cash flows looks at the operating, investing and financing activities of the organization and reports on cash flows in these areas.
- NOTES TO THE FINANCIAL STATEMENT — The notes to the financial statements are very integral to the financial statements and are a very important source of information.
- SCHEDULE OF FUNCTIONAL EXPENSES — Many organizations include a schedule of functional expenses as part of their financial reports. The schedule of functional expenses shows the actual expenses compared to budget by the functional categories of the organization for the period. Typically, these functional categories are the individual program areas of the organization plus a management and general category.

LEARNING POINT: The complete financial picture of an organization is presented in the financial statements providing a multifaceted examination of the financial status.

II.E: THE INTERNAL CONTROL SYSTEM (10–20 minutes)

TRAINER NOTE: Internal controls can have direct relevance to most employees of an organization. It is useful to review this topic to assure buy-in with internal controls and to stimulate ideas on how to protect an organization's resources. See ***HANDOUT # 5: INTERNAL CONTROLS.***

TRAINER STATES: Non-profit organizations like all organizations are vulnerable to deliberate theft and misguided use of funds for unauthorized purposes. The same idealism and commitment that bring talented and committed people to the non-profit sector may, however, also make them reluctant to impose controls on trusted staff.

Internal controls not only safeguard the organization's resources, but work to ensure that an organization's plans and policies are implemented as decided upon.

Internal controls are a set of procedures designed to promote and protect sound management practices, both general and financial.

TRAINER ELICITS: WHY ARE INTERNAL CONTROLS NEEDED? [Expected responses include:]

- TO PROVIDE RELIABLE DATA. Managers depend on accurate information to make program and other decisions. Program planning is influenced by the financial performance of the program as demonstrated in the financial statements. Internal controls ensure that this financial information is reliable.
- TO SAFEGUARD ASSETS AND RECORDS. Money and the physical assets of an organization can be stolen, misused or accidentally destroyed unless they are protected by adequate controls. The same is true of non-physical assets such as pledges and accounts receivable, as well as important documents such as contracts, the General Ledger or property ledger.
- TO PROMOTE OPERATIONAL EFFICIENCY. Control within an organization reduces unnecessary duplication of effort and guards against misallocation of resources.
- TO ENCOURAGE ADHERENCE TO PRESCRIBED POLICIES. Management establishes certain procedures and rules to encourage the pursuit of the organization's goals. Internal controls can help to ensure that these procedures are followed by staff members.

TRAINER NOTE: Write "Financial Management Staff," "Executive Management" and "Board of Directors" on respective newsprint.

TRAINER ELICITS: WHAT INTERNAL CONTROLS WOULD BE UNDER THE PURVIEW OF EACH OF THESE GROUPS? [Expected responses include:]

GENERAL PRACTICES

Depending on the size, number, and nature of transactions in your organization, controls may be variously distributed. In a small organization, some overlaps of duties will be necessary. A key principle is the "segregation of duties" — no financial transaction should be handled by one person from beginning to end.

A minimal set of controls might include the following:

- An Accounting Procedures Manual (APM) that describes the administrative tasks of the organization and indicates who is responsible for each task. The APM does not need to be a formal document. It can be a simple description of how functions such as check issuance or transfers among funds are authorized and processed. Writing or revising an APM is usually a good opportunity to see whether adequate controls are in place.

- In many cases, two signatures should be required on checks, or at least for checks of certain amounts (e.g., checks over $500). This policy can help to discourage embezzlement and encourage an atmosphere of accountability.

- Special attention should be paid to cash and check receipts, such as tenant rents or special events ticket sales. The same person should not receive the cash or checks and do the recording of the income and the deposit of the bank.

- The bank reconciliation should be reviewed by someone other than the bookkeeper. Even a small organization can accomplish this by having the board treasurer review the bank statements and cancelled checks at a board meeting. Attention should be given to alterations, authorized signatures and endorsements.

- The board of directors should approve the annual budget, and the board or the board's finance committee should regularly review the financial statements and compare to budget.

- The board of directors should also approve leases, loan agreements, affiliations, grant proposals and other major commitments of the organization.

- The board of directors should approve personnel policies that clearly define salary levels, compensatory time, benefits grievance procedures, severance pay, evaluations and other personnel matters.

AUDIT TRAILS

TRAINER STATE: A system of internal controls provides an audit trail. An audit trail means that a transaction (such as a deposit or a payment) can be followed from one end of the accounting system to the other (e.g., from the source of origin to the final record or from the final record to the source of origin).

For example, from a source document such as a supply order, the auditor should be able to trace how the transaction ended up in the financial statement. Similarly, the auditor can trace any item on the financial statements back to the source documents to verify the nature of the transaction.

An auditor uses the audit trail as a testing mechanism to evaluate the internal controls and thus the reliability of the accounting records. If sound controls exist, the auditor can place more confidence in the accuracy of the accounting records. If the auditor decides that the controls are so weak as to make the accounting records inadequate, he or she may find it necessary to issue a qualified opinion and will list the reasons in the audit report.

Internal controls do not, of course, guarantee that funds will not be taken or misused. Like locked doors, internal controls keep honest people honest. Internal controls also set a standard of accountability and conscientiousness.

Many non-profit textbooks include lists of suggested internal controls, and accounting firms often distribute guidelines for internal control procedures.

TRAINER NOTE: The sections that follow regarding audits, audit reports, selecting an auditor, types of audits and tax filing are primarily included for reference purposes. Trainers should inform trainees that information on these topics is included in the handouts and be prepared to address specific questions that might emerge. See ***HANDOUT #6: OVERVIEW OF AUDITS***.

LEARNING POINT: All non-profits must have a set of internal controls to maintain the integrity of their financial management systems; the basic principle is that no transaction should be followed by only a single person from beginning to end.

II.F: THE PUBLIC AUDIT (20–30 minutes)

BRIEF LECTURE:

Financial reports are used by people within organizations (staff and board) and by people outside the organization (IRS, funders, regulators, contributors and stakeholders).

Accounting standards that are used by all organizations in external reports, share a "common language" to ensure understanding and to make it possible to compare the finances of one organization to those of another. Organizations may choose more informal and unique reports for internal use but must issue standard reports for external use.

WHEN AN AUDIT IS NEEDED

The federal government requires independent audits only for organizations that have expended more than $300,000 in federal funds within one year. While some states require audits for non-profit organizations, most do not. Government agencies may require a government or independent audit for contractors. Some foundations also may require require audits of grantees.

If the people who read your organization's financial statement insist on assurances of an audit, it is clearly a worthwhile expense. Some organizations that are cleaning up messy accounting systems will find an audit invaluable in straightening out problems and setting a clear stage for the future.

ACCOUNTING REPORTS AND AUDITS

An audit is a set of tests performed by an independent Certified Public Accountant (CPA) that results in an opinion as to the accuracy of the financial statements.

Independent accountants (accountants who are not staff members or board members and are not related to staff or board members) prepare three basic types of reports: complications, reviews and audits. Each report is concerned with whether the financial information presented in statements is an accurate representation of the organization's financial operations and status. The different types of reports reflect different levels of assurances from the CPA regarding the accuracy of the information.

1. For a compilation report, the accountant takes financial data supplied by the organization and organizes it into standard financial reporting formats. The accountant does not review the numbers for accuracy nor state an opinion regarding the accuracy of the information.

2. For a review, the accountant performs a limited examination of the numbers prepared by the organization. A review offers limited assurance that the organization's true financial picture does not significantly vary from the information presented.

3. An audit is the most extensive examination of an organization's financial records. An audit may be described as a series of selective tests that gives the accountant a basis for judging whether financial records can be relied upon.

For example, auditors confirm bank balances, look over selected donations to see that they were processed and recorded properly, review grant letters to see that receivables are accurately stated, etc. In addition, the auditor reviews physical assets, bank reconciliations, journals and ledgers, as well as board minutes.

Based on this investigation, the auditor issues a formal opinion about the accuracy of the financial reports of the organization. It should be noted that an audit is not designed to uncover fraudulent activity within an organization.

Auditors can issue different types of formal opinions:

UNQUALIFIED OPINION — Most often, audits are issued with unqualified, "clean" opinions. In these cases, the audit letter accompanying the financial statements includes wording such as the following:

> "In our opinion, the accompanying financial statement *present fairly* the financial position of XYC Corporation as of December 31, 19XX, and the changes in net assets for the year then ended in conformity with generally accepted accounting principles.…"

QUALIFIED OPINION — A qualified opinion is issued when the auditor believes the statements are, in a limited way, not in accordance with generally accepted accounting principles or the auditor is unable to perform sufficient test work in one or more areas. A qualified opinion might include the following wording:

> "In our opinion, except for the omission of the value of donated assets, the accompanying financial statements present fairly.…"

DISCLAIMER OF OPINION — The auditor may issue a disclaimer of opinion if insufficient evidence exists to vouch for the financial statement.

ADVERSE OPINION — The auditor may also issue an adverse opinion if he or she believes that the financial statements are inaccurate.

A management letter may or may not be included as part of auditor's formal report. In this letter, the auditor may recommend stronger internal controls, more emphasis on documenting receipts, or may even comment on the organization's financial history.

SELECTING AND ENGAGING AN AUDITOR

TRAINER STATES: Just as individuals seek doctors or attorneys by asking their friends, organizations usually begin the search for an auditor by contacting similar non-profit organizations for referrals. Ideally, an auditor should be familiar with non-profit accounting and perhaps with the specific field in which the organization works.

Organizations often prepare a brief description of their accounting systems and send out letters to five or six accounting firms asking for bids. It is a good idea to solicit bids from sole practitioners or small offices as well as from large national firms.

Accounting firms that are interested will send a representative to make a bid. The bid will be based on many factors, including the budget size of the organization, the condition of the books, the complexity of the financial reports, the distance the accountant has to travel to the organization, the billing rates of the accounting firm and the deadline by which the audit must be completed.

After receiving the bids, and after checking the firm's references and reviewing the firm's latest Peer Review Report, the organization may select and contract with an auditor.

The auditor usually sends staff to work in the organization's office for a few days or a few weeks. The less work the accountant has to do because the staff has done a complete job, the less costly the audit.

In almost all cases, however, the auditor makes several adjusting entries to the work done by staff before the final financial statements are completed. Such adjustments are a normal part of the audit process and not necessarily a reflection of poor staff work.

PREPARING FOR AN AUDIT

TRAINER STATES: The financial manager or controller should ask the auditor for a list of the tasks that need to be completed before the audit work begins. For example, the auditor may need a list of equipment along with serial numbers and dates purchased, a list of all open bank accounts, documents such as board minutes for the previous year, a copy of the Accounting Procedures Manual or other procedural guides, documentation for accounts receivable and accounts payable such as letters from foundations, award letters, contracts and invoices from companies, etc.

It is a good idea to reconcile bank statements, Accounts Receivable and Accounts Payable schedules, and other asset and liability accounts before the auditor begins work.

Preparing for the audit has two focal points: putting things in order and preparing documentation for items on the financial statements. In addition, accounting staff members should be available to answer questions, retrieve information and prepare documentation the auditor may request.

Working with an auditor is an opportune time to clear up any accounting problems from the year, improve accounting and control systems and to learn more about effective accounting. The auditor can be an important resource to your organization if you choose your auditor carefully and work to develop a cooperative relationship.

LEARNING POINT: Audits are an essential component of financial management systems, providing validation to outside organizations and opportunities for the organization to make improvements in the functioning of their systems; they are generally undertaken to provide outside funders with assurances regarding the adequacy of an organization's financial management systems.

II.G: OTHER AUDITS (10–20 minutes)

A-133 (SINGLE) AUDIT

TRAINER STATES: Non-profit organizations that expend $300,000 or more a year in federal funds, whether direct or indirect, must have an A-133 audit. If all of those funds are expended on just one of the organization's programs, the organization can choose to have the A-133 audit conducted for just that program.

An A-133 audit must be performed in accordance with generally accepted auditing standards and generally accepted government standards. A-133 standards are more comprehensive than the public audit standards.

Generally Accepted Auditing Standards (GAAS) are established by the American Institute of Certified Public Accountants. These standards are established in order to ensure consistency and understandability of audits conducted by Certified Public Accountants. They require that audits not only determine whether financial statements comply with generally accepted accounting practices but also comment on the overall fairness of the financial statements and freedom from material misstatement. These standards are based on the auditor's access during the audit process to financial and related information that is not generally available to third parties.

The auditor's objective for an A-133 (single) audit, in addition to the expression of an opinion of the financial position and the results of operations of an organization, as described above, are:

- To determine that the organization has an internal control structure that provides reasonable assurance of compliance with laws and regulations, not only at the financial statement level, but also with regard to program management.
- To determine that the organization has complied with the laws and regulations that may have a direct material effect on its financial statements and on each major federally funded program.

Non-profits expending less than $300,000 a year are exempted from federal audit requirements, but must keep records available for review by appropriate officials of the federal grantor agency or sub-grantor entity.

PROGRAM AND GRANT AUDITS

TRAINER STATES: In addition to the public audit and the A-133 audit performed by the CPA, the organization may be subject to "program and grant" audits from funding agencies, governmental and private. The funding organization's right to audit the programs and financial records of the organization, as part of the condition of receiving funds, is usually stipulated in the funding contract. The funding agency usually lets the organization know well in advance when an audit would occur and usually outlines the programs and areas that are to be reviewed as part of the audit. These audits are not usually conducted on an annual basis. State and federal agencies usually have specified timetables for program and grant audits.

Funding contacts usually stipulate the type of information and the length of time the information must be retained under the contracts. It is very important that program directors, grants managers, quality assurance or compliance personnel, and fiscal managers read and understand the terms and conditions of the funding contracts and ensure that the organization sets up systems to capture and maintain the stipulated information.

LEARNING POINT: Organizations receiving over $300,000 in federal funds in any year must have an audit performed in accordance with A-133 standards; organizations should be aware of this when interviewing and retaining an auditor.

II.H: STATE & FEDERAL TAX RETURN REQUIREMENT & FILING (10–20 min)

BRIEF LECTURE:

Although non-profits are not subject to income taxes on the income/surpluses from related business activities (i.e., the activities that are related to their exempt purpose), they are nevertheless required to file the federal and state tax returns for monitoring purposes.

The non-profit should check with the auditor or state tax office to find out what returns are required to be filed.

THE FOLLOWING FEDERAL FORMS ARE REQUIRED TO BE FILED:

1. IRS Form 990 (Return of Organization Exempt from Income Tax) and Schedule A to Form 990

   Form 990 and Schedule A are due on the fifteenth day of the fifth month after the close of the organization's accounting year. This return should be filed with the Internal Revenue Service on an annual basis. If not filed on time, a penalty can be assessed. An extension of time to file may be made by filing an IRS FORM 2758.

   Form 990 includes the following information:
   - List of officers, directors and trustees
   - Balance at the beginning and end of year
   - Itemization of revenue and expenses by major activity and/or program such as by fund raising
   - Description of activities

   Additionally, non-profit organizations are liable for payroll taxes, sales taxes and any other taxes that are levied against businesses.

LEARNING POINT: Although non-profits are not required to pay income taxes, they nevertheless must file annual tax returns.

II.I: STAFFING (10–20 minutes)

TRAINER STATES: Each organization has a different mix of resources and each organization will assign responsibilities differently. Some small organizations choose to have transactions handled by staff, with the bookkeeping and accounting done by an outside accountant on contract. Larger organizations more typically keep financial functions on staff, although even very large organizations work with contracted accounting and/or financial management services.

TRAINER NOTE: Use Glossary of Accounting Terms for Quick Review. See ***HANDOUT #7: GLOSSARY OF ACCOUNTING TERMS*****.**

LEARNING POINT: There are no set rules for how to staff a financial management office; non-profits can successfully accomplish these functions using in-house staff and/or contracted services.

III. ACCOUNTING FOR THE SUPPORTIVE HOUSING COMPONENTS

III.A: INTRODUCTION (10–20 minutes)

TRAINER NOTE: The trainer should open this component with a brief introduction based on the materials presented below. Key points to address during the introduction include:

BRIEF LECTURE:

- What is supportive housing?
  - How it differs from both affordable housing and institutionally based care.
- What are the basic components of supportive housing?
  - An appropriate, decent and safe physical facility (SRO for singles, apartments for families, etc.)
  - Supportive services components, including on-site services and linkages with providers in the community
- Roles for non-profit organizations in supportive housing include:
  - Acting as developer
  - Operator of housing
  - Provider of supportive services
  - These functions can be performed by three separate organizations or by one providing all services or any combination in between.

Supportive Housing is decent and affordable housing that is specially planned and designed to serve the needs of families and individuals who would otherwise have difficulty in living independently. Supportive housing provides an appropriate alternative to institutional care, allowing tenants to live with the highest level of independence practicable while providing such services and support as may be needed. Supportive housing has been demonstrated to be a highly cost effective and humane way to provide housing and services to families and individuals with a range of needs and disabilities, including: mental illness, chronic chemical dependency, physical disabilities, histories of domestic violence, HIV/AIDS and other chronic health conditions, as well as many other needs.

There are three components of Supportive Housing: (1) the development of the housing project, which is a time-limited process, (2) the management of the project, which starts when the development process ends, and (3) social services, which provides the supportive structures to the housing project.

Each of these components involves a complex array of programmatic and financial activities. Indeed, there are for-profit and non-profit organizations that perform the activities involved in one and only one of these components, as their sole business function. Supportive housing has brought together these three functions to the benefit of the communities and people served. It means, however, that supportive housing providers are faced with managing three sets of complex activities and issues.

An organization may become involved in supportive housing in a number of ways, which would impact the level of its activities in housing development, property management or social services.

For instance, an organization may be a community development corporation that has been developing affordable housing for many years and has decided that in order to better meet the needs of its tenants it must provide supportive services. Such an organization will need to develop a service component or to partner with a service organization to provide services.

The organization may be a service provider that has decided that in order to meet the needs of its communities it must develop affordable housing. Such an organization would need to develop expertise in housing development and property management or partner with organizations that can provide such expertise.

Whether an organization is directly or indirectly involved in one or all of these components, it is important for the organization to understand the issues involved in managing these components.

The activities of each of these components can be divided into programmatic and financial activities. Each component also has accountability and reporting requirements.

These activities are not as distinct as they may sound and proper accounting of program funds involves sustained and coordinated interaction between program managers and fiscal manager.

This section will deal primarily with the financial activities involved in each component.

LEARNING POINT: There are important financial management tasks in developing, operating and providing supportive services in supportive housing projects, and each has different requirements but accurate and timely reports are key to them all.

III.B: HOUSING DEVELOPMENT (20–30 minutes)

TRAINER NOTE: Introduce the concept of risk. Developing and operating housing may expose non-profit organizations to risks that they have not previously experienced. Trainer should suggest some risks on development end, such as investing money on architectural plans for a project that does not get developed; on the operations end, such as having unanticipated vacancies; and on supportive services end such as government limiting benefits or phasing out a services program.

EXERCISE: Using three sheets of newsprint, write headings, "Development, Operations, Supportive Services" and ask trainees to provide examples of risks that a non-profit developer could experience in these areas. After the initial list is completed, the trainer should then ask the group to provide suggestions on what can be done to reduce these risks. Using the examples given above, the non-profit could arrange with the architect that it would be responsible for fees only if the project proceeded through development; it could minimize vacancy by maintaining waiting lists/minimizing the amount of time it takes to prepare a unit for a new tenant; and ensuring that tenants are enrolled in job training programs to provide options in case benefits are curtailed.

BACKGROUND AND EXPLANATORY TEXT

TRAINER STATES: The mission of non-profit human services providers and the realities of the housing market in many localities compel the non-profits to consider becoming actively involved in housing development. There is often a scarcity of affordable housing or no housing available for individuals and families receiving services from the non-profits. This lack of housing often impedes the non-profit's ability to accomplish its mission. Individuals cannot leave drug treatment programs because there is nowhere appropriate for them to live; mothers cannot be reunited with their children because they have no decent housing; and service providers to homeless people cannot assist their tenants in addressing their needs without adequate housing for them.

The principles and practices of financial management articulated earlier continue to hold true for the financial management of housing development projects. Non-profits undertaking such projects, however, face the very real possibility of experiencing **risk** in either developing and/or operating such housing. Risk in this instance means that the non-profit could potentially face financial liabilities that it does not have the resources to address. The risks the organizations face in the development stage include:

- Spending resources on up-front activities such as professional fees, site control agreements, environmental and/or other surveys and not being able to recoup these funds because the development project does not proceed.

- Experiencing cost-overruns on any aspect of the planning and/or construction that exceed budgeted and funded amounts.

The risks for non-profit housing developers don't end once the project has been successfully constructed. The risks during the operation of the housing include:

- An inability to market the housing units leading to unexpected levels of vacancy and a resulting insufficiency of rental income to meet expenses. Non-profit organizations rarely have the financial resources to sustain an on-going loss.

- The non-profit may be able to rent the units but at a lower rent than projected, leading to the same on-going deficit situation.

- The feasibility of the project may have been based on the availability of governmental subsidies, which might not be renewed after the project has been in operation.

- Insufficiently durable materials or other shortcomings in the construction process or excessive wear and tear by tenants might necessitate costly repairs once the project is operational. These repairs might exceed funds available.

- There could be a loss that exceeds insured amounts or is not covered by insurance.

- And for the supportive services component, the ability to provide these services may have been based on a government grant or funding mechanism that is discontinued. The life of a housing project is measured in the tens of years; the loss of a funding stream for the supportive services component can jeopardize the project and, in turn, jeopardize its non-profit owner.

Non-profit housing developers can take steps to minimize the risks that they will face. Careful and thorough financial management is one of the cornerstones to minimizing risk in housing development. Not every risk can be avoided, but careful planning and sound management of financial resources can minimize risks and, if need be, increase the receptiveness of funders to provide resources to offset losses.

STAGES OF DEVELOPMENT

TRAINER NOTE: Trainer presents handout illustrating a timeline of the development process. Trainer should start by highlighting key milestones: decision to proceed with project, construction, closing, initial occupancy and full occupancy. See ***HANDOUT #8: SUPPORTIVE HOUSING DEVELOPMENT PHASES; HANDOUT #9: SAMPLE TIMELINE FOR DEVELOPMENT OF SUPPORTIVE HOUSING PROJECT*** and ***HANDOUT #10: DEVELOPING SERVICES IN SUPPORTIVE HOUSING: MILESTONES AND ISSUES IN THE FIRST YEAR***. Trainer should return to prior discussion regarding risks and ask the group to link the risks to the key stages in the development process; then discuss the relationship between the stages of development and the availability of funding. Indicate what is necessary for obtaining funding for pre-development activities, how funds are distributed during the construction period, and discuss the rent-up stage of the project, when there are tenants and many expenses but only limited income.

There are three key stages to any housing development project:

- PRE-DEVELOPMENT, which begins with the initial conceptualization of the project and extends through the start of construction. Frequently, non-profits will start pre-development using their own resources. Additional, outside funding, might only become available once the organization has thoroughly demonstrated the feasibility of the project. Accordingly, pre-development should be regarded as a two-stage process:
  - Feasibility determination, which extends from initial concept until such time as the organization has demonstrated that there is the need and demand for the housing; that a suitable site can be acquired, that there are sufficient resources available to develop the project; and that the people to be housed and/or existing subsidy programs have sufficient resources for the project to be operated to serve the target population.
  - Pre-construction, which extends from when the project has been determined to be feasible until construction begins. Pre-construction involves preparing detailed plans for the project, obtaining bids for the construction, and entering into agreements with all members of the development team as well as with those lenders, funders and/or government agencies that are providing financial support to the project.

- CONSTRUCTION, which includes all activities from the start of a renovation or new construction project through the completion of construction as signified by the issuance of a certificate of occupancy by the local government. While the developer has bottom-line responsibility during the construction process, other parties are involved in decision-making, including the contractor, architect and lender. Generally speaking the construction period is when large sums of money are expended in relatively short time frames.
- OCCUPANCY. This phase should also be looked at as a two-step process:
    - Rent up or phase-in, which extends from the issuance of the certificate of occupancy until the project is fully occupied. The project will likely have been planned so as to at least break-even or generate a small surplus when it is fully occupied, but it generally takes time for all the prospective tenants to be identified, screened, certified eligible (if necessary), and to actually move in. During this period, when the project is only partially occupied, it is likely that it will have more expenses than income and the developer will need some other resources to cover this loss.
    - Full occupancy, ongoing operations. This is by far the longest project phase likely to extend for 20 or more years; in most instances, longer than the staff that conceived of the project will be employed by the non-profit that developed it. It is over this long run that the validity of the initial financial projects will be thoroughly tested.

This process involves leadership, market research, public relations, design, construction, financing, accounting and property management, along with a lot of creativity, patience and persistence.

MARKET RESEARCH

TRAINER NOTE: The trainer should introduce and explain the topic of market research and then should elicit innovative ways to conduct market research for the groups that will be served by trainees. Trainer should go around the room and ask participants to identify the populations that they will be serving. Trainer should then ask the group to brainstorm strategies for measuring the demand for supportive housing for the target groups.

BRIEF LECTURE:

The cornerstone of the development effort must be market research. It is the only way the users' needs can be ascertained and evaluated.

When an organization perceives that there is an unmet housing need in its community or among the population it serves, the organization should confirm this perception through market research.

The developer who fails to do adequate market research could over- or under estimate demand, fail to understand and meet the needs of the intended recipients of the service, or fail to properly cost the project.

DECISION-MAKING

TRAINER STATES: Market research will give the organization the information needed to make a decision on whether a development opportunity exists and the resources that would be needed to develop the project.

If the organization determines that a development opportunity exists, it must decide whether it has the expertise, or can hire staff, to develop the project or whether to contract with a development company to develop the project.

A development project of any size tends to be high profile in the community and to funders. Regardless of whether the organization does the development in-house or contracts with a developer, the organization's credibility is on the line and the organization needs to understand what is involved in the development process and to ensure that the development project is soundly managed.

The financial considerations for development project can be quite daunting. The organization must price the project, must determine how it will be funded, and must determine how much equity, if any, is required by the project. The organization must also decide what type of ownership vehicle is appropriate for the project. Ownership vehicles include direct ownership by the non-profit organization or the establishment of a partnership for development or to take advantage of government support through tax credit programs. All of these decisions impact financial systems of the organization.

DEVELOPING COST ESTIMATE SCHEDULES AND FINANCING

TRAINER STATES: After a site has been selected and the type of housing to be developed has been determined, the developer enters into what is called the pre-development phase of the project.

During this phase, the developers must determine the feasibility of the project with respect to design, cost estimates, development economics, financing, further market studies and schedules.

The cost estimates and schedules developed in this phase of the project will be used by the developer to make the "go" or "no go" decision. Therefore the developer must focus on all the factors that can affect the success of the development project. The most important objective for the developer during the pre-development phase is to minimize assumptions and to project the most accurate cost estimates and schedules for the development.

LEARNING POINT: Participating in supportive housing development can entail significant risks; the best tools to avoid risk are sound research and accurate budgeting.

III.B-1: THE PRE-DEVELOPMENT BUDGET (20–30 minutes)

TRAINER NOTE: Refer participants to sample development budget contained in their packages. Begin discussion by reviewing those expense items that will be incurred in the pre-construction period. Using text below as a guide, solicit information from participants regarding strategies to minimize risk to the non-profit developer. See ***HANDOUT #11: SAMPLE DEVELOPMENT BUDGET.*** Trainer should ask participants about the information their organization would require to decide whether to pursue a development project. Please review the bulleted list that appears on the next page. Use it to add information/decision points not raised by the participants.

BRIEF LECTURE:

The pre-development budget is generally developed in stages. The initial budget must have sufficient funding for the preliminary investigation. A sound preliminary investigation is essential to preventing the organization from committing significant resources to a project that is not viable. The revenue for this initial budget will generally come from agency resources or small foundation grants. Individuals already on the staff of the non-profit will conduct much of the initial pre-development work. Pre-development tasks that may require financial expenditures include:

- Professional fees. Legal fees will likely be incurred in drafting agreements; some initial assessments will be required from architects, environmental consultants and zoning/land use experts.
- Site acquisition costs. Often, non-profits developing housing will be required to expend dollars to acquire site control through an option, contract of sale or other instrument.

These initial pre-development tasks represent actual 'risk' to the non-profit. If the project does not proceed, the resources expended will be 'lost.' If the organization was fortunate enough to receive a grant to cover these expenses and the grant was not a 'recoverable' grant, then as long as it operates within the budget established for the grant, it will not have lost any money. If, however, it is funding these expenses out of agency resources or through a 'recoverable' grant and the project does not proceed, then the organization will have lost these resources.

Non-profits, like any other developer, should seek to share these risks with others. It is often possible to convince professionals to agree to provide services 'on contingency,' meaning that they will be repaid for their services, if, and only if, the project is demonstrated to be feasible and funding from other sources is obtained for the development. Similarly sites can often be obtained from public sources, such as municipally or federally owned property. Often, non-profit developers can obtain control over these sites without having to expend up-front capital.

Since the non-profit is often at risk for Phase 1 pre-development expenditures, these need to be managed very carefully. Any expenditure over budget will be extremely deleterious to the organization. To limit costs and properly prepare a detailed budget, the non-profit developer should request a proposal from the various professionals and consultants whose services are required for pre-development tasks. Where possible, existing staff of the non-profit developer should be used for these tasks or to limit the time required by outside professionals.

Depending on project needs, the development team on a housing project could include: the project manager, construction managers, the architect, interior designer, space planner, landscape architect, graphics designer, civil engineer, surveyor, structural engineer, mechanical engineer, plumbing engineer, fire protection engineer, specialty consultants, general contractor, subcontractor, inspectors, mortgage broker/banker or funding agency, financial consultant, appraiser, property manager, attorney and accountant. Organizations should be mindful that it is possible to be 'pound-wise and penny-foolish.' Substituting an inexperienced and potentially over-committed staff member to serve as project manager, for example, could result in lengthy project delays or costly project errors.

Each team member should prepare a proposal listing the scope of responsibilities, costs and schedules for the pre-development phase, as well as for the construction phase. The pre-development budget and cash flows are then developed based on these activities and cost estimates.

At some stage, projects in pre-development will pass from the Phase 1, Risk, to the pre-Construction phase. In order for this transition to occur, some or all of the following will need to be achieved:

- The project will have been demonstrated to be feasible (i.e., sufficient funding can be obtained to develop and operate the project and there is sufficient demand for the projected facility).
- Funding either will be committed to develop and operate the facility or there will be a high likelihood that funding can be obtained.
- An appropriate site for the facility will have been identified, and there will be reasonable assurances that the developer can acquire the site and that there are no major obstacles (environmental, community opposition, zoning, etc.) to the use of the facility for the intended purpose.
- The governing body of the developer (non-profit board of directors) has given its go-ahead for the project.

For the most part, the costs that will be incurred by the developer in the pre-construction phase will be included in the project development budget. It should be noted that government funding programs will frequently maintain funding ceilings for certain kinds of expenditures. Architects and project managers, for example, are usually only reimbursed according to set schedules. Prior to entering into any agreements with outside professionals, the non-profit developer should contact potential funding sources and obtain information on their reimbursement policies for the use of professionals. If the organization enters into an agreement to pay a professional above the established schedule of a funding agency, it might be required to pay the overage from its own funds or it might not be allowed to pay it at all. The non-profit developer should also determine whether government funders are willing to make any advance payments for professional and other pre-development costs or whether the agency will only advance monies when the project is ready to start construction.

TRAINER NOTE: Many of the participants will have HUD homeless assistance grants. Review the following information with the participants to be sure they understand the special HUD requirements.

Organizations receiving support from HUD under the homeless assistance grants programs, specifically the Supportive Housing Program should note some HUD requirements, which directly affect the expenditures of funds for pre-development activities:

- HUD will only reimburse for expenditures that have been incurred **after** the organization has a fully executed contract with HUD. All invoices received must be dated on or after the HUD contract execution date. Therefore, many pre-development expenditures may be ineligible for reimbursement by HUD.
- HUD will advance all funds budgeted for site acquisition at one time. However, organizations that have received funding for acquisition must forward closing documents to HUD within 30 days of the closing on the property.

PRE-DEVELOPMENT BUDGET MANAGEMENT

TRAINER STATES: There is an important principle regarding budget management in a development project: for the most part, payment is only made when tasks have been successfully completed. The project architect, for example, will be paid when he or she delivers to the developer satisfactory, completed plans for the stage of development (preliminary, design development, construction, etc.). The individual responsible for financial management must work closely with his/her counterparts who are responsible for managing the development to assure that payments are not released until the work has been satisfactorily completed.

Effective management of pre-development resources requires a system to expedite approvals among members of the development team, initiate work efforts, control expenditures, approve invoices and accurately track expenditures.

The system should include an approved pre-development budget, a schedule of activities to be performed under the budget, approval procedures, work order requests, work task schedule, invoicing procedures, pay out procedures and cash flow projections developed from the work schedule.

Tracking expenditures and making timely payouts are critical to helping to keep the project on budget. It is important that the development team meet regularly to review how the system is working, to review any changes and the impact on the budget, schedules, etc.

The financial manager's goal is to provide meaningful financial information about the project that will help management in evaluating the soundness of the project as it proceeds. Setting up a sound system of controls and having good communication with the development team helps the financial manager achieve this goal.

LEARNING POINT: Financial management in pre-development requires careful coordination between agency fiscal and program staff to assure that agreements and fees comply with funder's limitations and that payments are only made for work satisfactorily completed.

III.B-2: THE DEVELOPMENT BUDGET — HARD AND SOFT COSTS (10–20 min)

TRAINER NOTE: Refer participants back to the sample development budget. Review principle of payment when tasks are completed as described in text above. Discuss how the development budget is prepared in an iterative process as described in text below.

TRAINER STATES: The developer must create a development budget with the most realistic cost estimates possible. This budget is developed in stages during the pre-development process. For example, it isn't possible to estimate construction costs until a site is chosen, a zoning analysis is performed, the site is analyzed for drainage and environmental considerations, and detailed construction drawings are developed and then priced out. Initially, the pre-development budget will have no information on construction costs, then as a rough count on the number of units and square footage is developed, it will have a 'ballpark' number based on these amounts. Finally, once plans have been completed and bids obtained, there will be actual construction numbers. Even then, the final construction numbers will only be known when the specific construction item has been completed and the project management team has approved the work.

Information gathered during the pre-development phase is used to inform the budget. The budget contains "hard costs" and "soft costs." Hard costs refer to those expenses directly related to acquisition and construction including site costs, site development and actual building/renovation costs. All other costs including professional services, financing, insurance, etc., are known as soft costs. Construction costs are initially estimated by the architects and engineers and then finalized based on bids submitted by the builder. Soft costs estimates are developed by the development manager, the property manager and the financial manager.

The financial manager and the developer are responsible for creating the development budget as well as cash flows using the hard costs and soft costs estimates and schedules developed by the various consultants on the project. The developer must also identify the sources of funds for the project. The project development budget will be finalized prior to the start of construction, signified by the 'construction closing.' Once the budget has been finalized and approved by the project funders, changes in the budget can only be made with their approval. For this reason, most development budgets include line items for both hard and soft costs contingencies. It is in the project and financial managers' interests to have as much money as possible in these contingency lines.

Non-profit organizations handle financial management responsibilities in the development and operational stages in different ways. Some organizations that specialize in housing development will have a development staff that will be responsible for budget development and financial management, from the point of initial project conception through the funding process up to the completion of construction. When the project is ready for occupancy, responsibility for on-going financial management is then turned over to the 'regular' accounting staff. Other organizations, especially those who do not engage in much housing development, will have these tasks handled by the accounting/financial management staff from the outset. Regardless of the approach used by any specific organization, it is important that there be regular communication between the staff and consultants working on the development of a housing project and the financial management staff of the organization.

Supportive housing projects are often developed using Federal Low Income Housing Tax Credits. While this subject is beyond the scope of this curriculum, a sample development budget that uses tax credits is included as Handout #12.

TRAINER NOTE: See ***HANDOUT #12: DEVELOPMENT BUDGET WITH TAX CREDITS*.**

LEARNING POINT: Hard costs include actual construction and acquisition costs; soft costs are all other construction/development-related expenses; development budgets that have been reviewed and approved by outsider funders can only be modified with the approval of those funders.

III.B-3: TRACKING CONSTRUCTION DRAWS AND PAYOUTS (10–20 minutes)

TRAINER NOTE: Present concepts that payments during construction generally involve the approval of a third party (bank or government agency), that the team architect will review each requisition by contractors and certify that the payments are for work that is completed and installed in accordance with the construction plans. See sections below for background information.

TRAINER STATES: Just as in the pre-development phase, in construction, the organization needs to have a system in place to track construction draws and payouts, approval procedures, cash flows. In this phase, the financial manager's goal is to provide meaningful information regarding the financial status of the project to management. Management should be able to determine the project's progress against costs and scheduling estimates.

There is one important difference between construction period financial management and the pre-construction period: After the construction closing, the funders generally reserve authority for approval for any payments under the construction budget. Payments for construction activities are made only after the project architect has certified and the funder verified that the work for which payment is requested has been completed in conformance with approved plans and specifications.

On a monthly basis after draw requests and payouts, the accounting staff should prepare monthly cost reports providing the following information:

- Original budgets
- Revised budgets
- Construction percentage completed
- Actual costs incurred to date
- Unexpended committed costs
- Estimated costs to complete
- Current projected costs
- Variance to revised budget
- Variance explanations

LEARNING POINT: Once construction has started, payment for construction-related activities can only be made after approval by the construction funder (lender); monthly financial reports should track expenditures to budget to percentage of work completed.

III.C: OPERATIONS (20–30 minutes)

TRAINER NOTE: See ***HANDOUT #13: COMPONENTS OF A MANAGEMENT AGREEMENT***. The discussion on property management should address the following themes:

BRIEF LECTURE:

- Clarification of specific tasks associated with property management and operations, as many of these may be considerably different from those that have traditionally been performed by the organizations participating in the training. Use the bulleted list below for this information. Suggestion is that the trainer seek to elicit the various functions from the participants.
- Identification that the function of property management and operations can put the manager and the tenant into a sometimes adversarial relationship, which is not only different from that traditionally entered into between service providers and their tenants but which could impact that relationship. The trainer should present potential areas of conflict between tenants and property manager such as:
    - Late payment or non-payment of rent;
    - Disruptive behavior;
    - Guests that impact the residential setting;
    - And others as may arise
- The trainer should then stimulate a discussion among participants on how these issues would be addressed by a social services organization and how a property manager might address them.
- The final area to discuss regarding property management and operations is what organization should do it, the social services provider or an outside manager. The trainer should get a sense from the participants of the direction their organizations might take with respect to hiring an outside property manager. If there is considerable interest, the trainer should review the list of tasks to be performed by the manager as they are listed in the section below. Otherwise, the trainer should reference the information in the participant's workbook and allow them to review it at their convenience.

Property management and operations is a complex task requiring skills that are somewhat different than those generally employed by non-profit organizations. The fundamental tasks associated with it include:

- Maintenance and repair of the physical plant including routine and scheduled maintenance items as well as emergency repair requirements;
- Maintaining security for tenants and other users of the facility;
- Screening and selecting tenants for occupancy;
- Collecting rents;
- Managing contracts with vendors and contractors;
- When necessary, replacing tenants, ensuring that units are in appropriate condition for new tenants, and renting the units to the new tenants; and
- Maintaining a fiscal system.

A key question that must be addressed by any non-profit considering developing, acquiring or leasing property is how the property will be managed. The organization must decide whether to contract with a third-party management company or to manage the building itself.

In making these decisions, the organization must consider its management philosophy and how this philosophy will be conveyed to staff or to a management company. Managing residential property places demands on an organization that might conflict with other organizational mandates. A property manager, for example, might be required to commence eviction proceedings against a tenant who has failed to pay rent and/or who is disturbing the peace and tranquility of other tenants. Some human services organizations might feel ill at ease in enforcing such sanctions against their tenants.

If the organization decides to select a management company to perform the management services, the organization must ensure that the company has an understanding of the organization's philosophy of service.

If the organization chooses to perform this function in-house, the organization must select a team of personnel who understands the organization's philosophy of service.

If the organization decides to contract with a company, a management agreement should be drawn up that outlines the relationship between the organization and the management company and the expected outcomes. The management agreement should address and describe the following:

- FEE STRUCTURE: Typically, the fee structure is based on a percentage of collected rental income or a flat rate.

- TERM OF AGREEMENT: The term of the agreement should be stated in the management agreement. To ensure continuity, the agreement is typically multi-year, usually up to five years.

- SCOPE OF RESPONSIBILITY: To avoid conflict between parties, this section of the agreement should be clearly defined and should list all the duties of the Management Company.

- COLLECTION OF MONIES: This section of the agreement should define who will collect the rental income and where and when the funds will be deposited.

- EXPENSES OF THE MANAGEMENT COMPANY: This section of the agreement should outline what expenses the property owning organization will pay for and what expenses the Management Company is expected to pay for.

- EMPLOYEES: This section of the agreement should outline who will be employees of the Management Company and who will be employees of the property owner.

- AUTHORIZATION TO SIGN SERVICE AGREEMENTS: This section of the agreement should define who can sign service contracts and, if this authority is delegated to the Management Company, the dollar value of contracts that can be entered into, with and without the approval of the property owner.

- MAJOR REPAIRS: This section of the agreement should outline the procedures the Management Company should take when requesting, bidding and making purchase orders for major items. It typically will specify the amount of money that the Management Company can spend without prior authorization by the property owner. It will also indicate procedures to follow when major repairs are necessitated by an emergency.

- INSUFFICIENT INCOME: This section of the agreement should define how the property owner will fund negative cash flows.

- REPORTING SYSTEMS: This section of the agreement should list all the weekly, quarterly and yearly accounting and management reports the property owner or other parties will require. Funders frequently require annual reports and the responsibility for the initial compilation of the reports should be passed on to the management contractor.

- OPERATING AND CAPITAL EXPENDITURE BUDGET: This section of the agreement should determine when annual operating and capital expenditure budgets are to be completed and how often they are to be updated. It will specify the rights of the property owner to review and approve budgets.

- COMPLIANCE WITH LEGAL REQUIREMENTS: This section of the agreement should require that the Management Company comply with all local, state and federal laws.

- ASSIGNMENT OF CONTRACT: This section of the agreement should define the rights of the Management Company to assign its interests in the management contact.

- TERMINATION CLAUSE AND PENALTY: This section of the agreement should list any reasons for an early termination of the agreement and what, if any, penalty will be paid by the property owner for exercising the clause. In addition, it will define the obligations of both parties after the notice of termination has been given to the Management Company.

Even if the organization decides on in-house management, a document outlining the roles and responsibilities of property management should be drawn up.

LEARNING POINT: Property management is a very different type of activity for most non-profit service providers, potentially placing them in an altered relationship with their clients; organizations should carefully assess whether to use a professional management company.

III.C-1: THE OPERATING BUDGET (20–30 minutes)

TRAINER NOTE: Direct the attention of the participants to the sample operating budget located in their packets. There are several key topics regarding the operating budget that should be reviewed: See ***HANDOUT #14: SAMPLE OPERATING BUDGET*.**

BRIEF LECTURE:

The operating budget covers the income and expenses associated with running a housing project, specifically those costs associated with maintaining the habitability and quality of the housing.

- Projections of revenue. These will likely consist of income from tenant rents and subsidies such as HUD's Section 8 housing assistance payments or operating support grants from HUD's Supportive Housing Program. Income projections require adjustments for vacancies (when apartments are not occupied) and for uncollectable rent (when payments owed by tenants will not be collected by the property manager). Rental subsidies are far more certain than the payments that will be made by tenants. It is important that income projections leave adequate cushions for vacancy and uncollectable rents.
- There is a wide array of operating expenses that need to be projected in the budget. Examples of these expenses are included in the sample budget and in the participant's workbook. It is important that these projections be as accurate as possible. To stimulate discussion, the Trainer should request that participants identify sources of information concerning operating expenses. Answers should include:
    - Existing data on prior actual expenditures;
    - Information from public utilities serving the area;
    - Estimates and quotes from vendors such as maintenance contractors, insurance brokers, etc.; and
    - Public records for taxes, water and sewer charges.
- The importance of establishing reserve accounts to cover current operating expenses and to address scheduled and emergency replacement expenses.
- The debt service component of the operating budget.
- Understanding annual budgets and cash flow projections. As described below, participants should understand that income in a residential building is generally constant across twelve months (as long as occupancy is stable) but that expenses can vary considerably to cover seasonal variations (such as heating/air

conditioning) and because some expenses occur only on an annual basis. Operating budgets require good cash flow projections so as to assure the availability of funds to expenses.

- In maintaining financial oversight, the organization should review the annual budgets, cash flow projections and the **budget variance** report. This report, prepared on a monthly basis, shows how the annual budget translates to a monthly projection and then compares that budget projection to the actual expenditures. Managers should explore significant variations from budget and, when the budget has been significantly exceeded, start to develop plans for either trimming expenditures in other areas to cover the deficit or to raise additional revenue to cover the higher expense*s.*

The Property Manager or the Property Management Company should prepare a property management plan. The plan should include the mission goals and objective of property management, operational considerations, staffing patterns, policies, procedures, routine, preventive and emergency maintenance plans, renting policies and procedures, and operating and capital budgets.

The first step in developing the management plan is to prepare an operating budget for the property. The operating budget lists the income and expenses for the property. The first draft of the operating budget will have been developed in conjunction with the initial plans for a development project or, if the non-profit is acquiring an existing property, as part of the acquisition plans. The property manager will be responsible for updating this initial projection.

These income and expenses for the year are combined into a cash flow statement, which predicts how much net operating income the property will produce annually. Generally speaking, revenues in a residential rental property are fairly constant over a twelve-month period. Expenses will vary. Some, like heating costs in northern areas, will peak over several months during the winter. Other expenses, like insurance, will be based on annual or quarterly payments. What is important is that the cash flow budget accurately reflects these expenses and allows the owner to save surpluses during periods when expenses are lower so as to assure the availability of funds during the periods of heavy expenses. Each month the operator of the housing project should have an accurate estimate of expenses, cash on hand, and cash expected to be received and when. For any month where the cash is projected to be insufficient to meet expenses, the operator will have to develop a plan to raise additional cash (by borrowing or securing additional funds from the owner) or defer expenses.

If the operating budget is prepared after the building is leased-up, the individual tenants and their rents are listed. Expenses are listed per their various categories.

THE REVENUE CALCULATIONS

TRAINER STATES: The first part of preparing the operating budget is to project current revenue items. This means preparing a forecast of rent collections.

The projected rental revenues are calculated by multiplying the total square footage or number of units by total annualized rent per square foot or per unit. Some projects will receive federal rent subsidies. HUD's homeless assistance grant programs allow for rental subsidies under the Supportive Housing, Shelter Plus Care, and SRO Section 8 Moderate Rehabilitation Programs. For these projects, the tenants will pay 30 percent of their income, with the federal government paying the balance of the rent up to the established federal Fair Market Rent ceilings. The income projections would show 100% collection for the federal share and adjusted projections for the actual income that will be received from the tenants.

Additional rental income and miscellaneous income are added to Gross Collectable Rental Income to give Total Potential Income. Examples of miscellaneous income include coin-operated laundry machines or vending machines.

VACANCY ALLOWANCES — Vacancy allowance is the percentage of the gross potential income that is projected to be uncollectable due to space being unoccupied, readied for a new tenant or occupied under a free rental period

UNCOLLECTABLE INCOME — Uncollectable income is income that is uncollectable as a result of tenants having moved out early or being unable to pay rent.

OPERATING EXPENSES — Developing the initial forecast of operating expenses entails detailed research with utility companies, vendors and subcontractors. Costs comparisons with other organizations in the area with similar buildings can help in developing expense projections. When available, the past history of the property's operational costs can also be useful in developing budget forecasts. When using historical costs the percentage of increase that can be expected for each category during the year must be determined.

OPERATING EXPENSE ITEMS TO CONSIDER WOULD INCLUDE THE FOLLOWING:

Personnel Expenses
- Salaries
- Employee Benefits
- Pension
- Payroll Tax
- Unemployment Tax
- Staff Cash Reimbursements

Maintenance and Repairs
- Mechanical, Electrical and Plumbing
- Door Lock Upkeep
- Fixtures and Appliances
- Exterior and Interior Roof Repairs
- Window Repairs
- Window Treatment Repairs
- Finishes (exterior and interior)
- Parking Lots (paving and lighting)
- Signage and Graphics
- Floor Coverings
- Carpentry
- Mirrors
- Masonry
- Landscaping and Gardening

Renewal or Tenant Unit Maintenance (expenses associated with making a space ready for a new tenant)
- Cleaning
- Carpet
- Painting
- Wallpaper
- Sheetrock
- Turnkey
- Furnishings, if provided

Public Utilities
- Electric
- Gas
- Water
- Sewer

Taxes
- Property Taxes
- Personal Property Taxes
- Vehicle Taxes

Property Management Fee

Inventory (expenses for supplies needed for maintaining the property)
- HVAC (heating, ventilation and air-conditioning supplies)
- Plumbing Supplies
- Electrical Supplies
- Appliance Supplies
- Cleaning Supplies
- Painting Supplies
- Fire Safety Supplies

Profession fees
- Attorneys
- Accounting
- Architectural Engineering
- Appraisals
- Feasibility Studies
- Consultants
- Brokers (Real Estate or Mortgage)

Contract Services
- Pest Control
- Trash
- Landscaping and Gardening
- Elevator Maintenance
- Janitorial
- Windowing Cleaning
- Snow Removal
- Security and Guards
- Laundry
- Service of Heating and Cooling Equipment

Administrative Costs
- Attorney's Fees
- Accounting
- Dues and Subscriptions
- Petty Cash
- Office Supplies
- Office Equipment
- Travel and Entertainment
- Fixtures, Furniture and Equipment Rental
- Telephone
- Copier Lease
- Postage
- Interior Plants
- Printing
- Contract Maintenance
- Janitorial

- Equipment Maintenance
- Utilities
- Pagers and Answering Services
- Deliveries
- Licenses
- Uniforms and Cleaning
- Fees
- Artwork
- Credit Bureau
- Training Seminars
- Computer and Processing Expenses

Liability Protection — Insurance
- Property Liability
- Contents
- Fidelity
- Boiler/Machinery
- Vehicle
- Flood
- Rent Loss
- Errors and Omissions
- Health
- Life
- Worker's Compensation

Marketing (expenses associated with leasing the property)
- Agency Fees
- Newspaper and Magazine Advertising
- Business Cards,
- Brochures and Fliers
- Printing
- Postage and Direct Mail
- Signage and Graphics
- Photography (project and aerial)
- Visual Aids (renderings and plans)
- Special Events
- Advertising
- Prospect Lists

Deposits (expenses for deposits or bonds that the property must post)
- Electric
- Gas
- Water/Sewer
- Telephone
- Equipment

Banking (expenses for banking charges)
- Opening Accounts
- Checks
- Returned Checks
- Wire Charges
- Service Charges

LEARNING POINT: Operating budgets should be prepared based on well-researched estimates of expenses. Accurate annual cash flow projections are an indispensable tool, as expenses will vary considerably through the year while income is generally constant.

III.C-2: PLANNING FOR RESERVES AND REPLACEMENTS (10–20 minutes)

TRAINER STATES: Reserves for operations as well as replacement should be calculated. Funds should be set aside on a monthly basis to meet these reserve requirements. Financing institutions and government agencies may also require that certain reserves and/or levels of reserves be kept. The Property Manager and fiscal staff are usually responsible for this task. Replacement reserve items may include the following:

- Flooring
- Roof
- Boiler
- Cabinets
- Plumbing
- Signage

LEARNING POINT: Expect the unexpected; all building systems have a useful life and will eventually require replacement; systems will also break down, requiring expensive replacement without warning, these circumstances must be budgeted for.

III.C-3: PLANNING FOR DEBT SERVICE (10–20 minutes)

TRAINER STATES: Debt service refers to any loans that may have been taken outin order to meet the capital costs of acquiring or improving the property. Not all capital funds must be repaid. A number of sources of capital funds do not require that these funds be repaid provided that the project continues to fulfill the purpose for which it was originally funded. For example, capital funds provided through HUD's McKinney Vento homeless assistance grants need not be repaid provided the project continues to provide housing and/or services to homeless people for at least 20 years. If the project should fail to provide this housing in the first ten years, the entire capital sum (plus a proportionate share of any property appreciation) must be repaid to HUD. The sum due to HUD diminishes ten percent a year for the next ten years so that the liability to HUD is zeroed-out after twenty years.

Many projects, however, will require some form of debt financing to secure the needed level of capital funding to acquire the property and construct or rehabilitate it. Lending institutions will not make loans without first having some assurance that the loan can be repaid. Projections submitted to lenders will have demonstrated that the project will be able to meet all expenses, repaid the loans advanced and have some level of cushion, referred to as 'debt service coverage,' to ensure that the project will be able to make the loan repayments.

As long as there is adequate income to meet the debt service payments, loan repayment is relatively simple to plan for. Loans typically are made in one of two formats:

- Equal monthly payments of principal and interest, whereby the borrower makes identical payments during the life of the loan; over time, the amount of the payment attributable to interest diminishes and the amount attributable to principal increases.
- Equal principal payments, whereby every month the borrower pays down an identical amount of principal and the interest charged each month is based on the unpaid principal balance. These payments therefore decline over the life of the loan.

Debt service is an extremely important obligation. Failure to make loan payments when due will initially result in late payment charges and negative credit reports. Continued failure to make payments could lead to the lender instituting foreclosure proceedings and a resulting loss of the property by the non-profit owner. If the property manager, in reviewing the cash flow projections, determines that it will not be able to make a loan payment, it should contact the lender before the payment is due, explain the situation, and either offer a strategy for making up the missed payment or request help from the lender in developing such a strategy.

LEARNING POINT: The substantial capital costs associated with development projects will frequently necessitate borrowing, which will become a primary obligation of the organization.

III.C-4: PLANNING FOR CAPITAL EXPENDITURES (10–20 minutes)

TRAINER STATES: Capital expenditures are non-recurring costs. If the organization plans to make capital expenditures during the year, a capital budget should be prepared. Capital expenditure items should not appear in the operating budget.

Capital expenditures should be capitalized on the organization's balance sheet as assets and depreciated over some specified period. Depreciation schedules are based on the expected life of the improvement. They should not be expensed currently.

Ideally, funds for capital expenditures can be obtained from reserves (i.e., income that has been saved, for this purpose). There are times, however, when capital repairs may need to be funded from other sources. This will occur when there is a need for emergency repairs that, in order to ensure habitability, must be performed before sufficient reserves have been accumulated. If possible, these can be funded out of operating revenue, provided there will still be sufficient other funding to meet critical operating expenses. If funding the emergency capital need would put too great a strain on operating income, the non-profit owner will have to seek funds from other sources, such as:

- Applying for additional financing from the lender. Lenders may be persuaded to advance additional capital if this is the sole means to assure that the project can remain operational.
- The non-profit owner can undertake a special capital campaign, soliciting contributions to cover this one-time emergency need.
- The non-profit can seek an emergency grant from a foundation or corporation.

It is important that the property manager and the financial manager review the reserves on a regular basis. It is also important that the property manager and the financial manager discuss future needs and plans to meet those needs before they become crises. Examples of capital expenditures include the following:

- New Roof
- New Flooring
- Major Improvements
- Major Appliance Purchases
- Major Plumbing and Electrical Repairs or Improvements

LEARNING POINT: For accounting purposes, capital expenditures must never be combined with operating expenses.

III.C-5: THE ACCOUNTING SYSTEMS AND PROCEDURES (10–20 minutes)

BRIEF LECTURE:

To properly account for receipts and disbursements, the organization should prepare monthly accounting statements. The organization must determine what method of accounting it will use. This should be done in consultation with the organization's accountant. Once decided, the accounting method cannot be changed without IRS approval.

ACCOUNTING METHODS

- CASH METHOD — The cash method of accounting recognizes revenue when cash is received and recognizes expenses when they are paid. Cash accounting gives a clearer picture of the funds that are actually available to the organization.

- ACCRUAL METHOD — The accrual method of accounting recognizes revenue and expenses when they occur, even though they may not have been received or paid. Accrual accounting gives a truer picture of the actual finances of the organization.

ESTABLISHING THE ACCOUNTING SYSTEM

To manage the accounting process, systems should be devised, which result from the unique needs of the project, taking into account the reporting needs of managers, funders and the board.

The accounting system should allow the organization to process and monitor the financial transactions involved in operating the property. It should produce the information needed by the organization to determine the costs of operating the property. The organization should also be able to determine whether the property is operating at a loss or with a surplus.

A chart of accounts that reflects the types of revenues, expense line items, asset and liability and capital accounts of the organization should be established. The following types of reports should be established and monitored regularly as part of the accounting systems:

Monthly Rent Roll Reports

- This report will allow management to ensure that units are rented and rents are collected. It will identify those tenants that have fallen behind in rent payments and allow the owner to determine whether the tenant has an unmet supportive services need or whether sanctions such as an eviction proceeding are appropriate. If units remain vacant for a protracted period, the owner can use this information to determine whether the property manager is doing an effective job in marketing the property, whether the units are targeted to an appropriate in-need population, or whether the rents are not appropriate for the market.

Profit and Loss Reports/Revenue and Expense Reports

- These reports provide an overall picture of the financial solvency of the project. At initial development, the profit/loss report should have shown a slight surplus. If the project is operating at a loss or if it is generating a surplus significantly higher than projected, this will be an indication to management to take corrective action.

Budget to Actual Variance Reports

- Prepared on a monthly basis, these reports will allow the owner to review the extent to which the project has been able to operate according to the established budget. They will provide advance warning of upcoming cash needs and allow decisions to be made to shift resources in order to keep the budget in balance.

LEARNING POINT: Regular financial management reports are an essential tool for property managers and allow for coordination between property managers and social services providers.

III.C-6: RENT RECEIVABLES (10–20 minutes)

BRIEF LECTURE:

Rent collection is extremely important. Management must be consistent in application of rent collection policies to prevent the possibility of tenants falling behind in their payments and to ensure that cash and non-cash receipts are appropriately safeguarded. Projects receiving support from the HUD homeless assistance grants should note that HUD does not require rent payments by tenants but, if the project decides to institute rent payments, it requires that policies be uniformly applied to all tenants. Fiscal and Property Management should have specific processes and procedures in place to ensure control of the rent collection process. The following should be considered:

- Written schedule and procedures for collection
- Written process for non-payment/delinquent cases
- Easily accessible reports on individual payment history
- Written procedures for the deposit of checks
- Early identification of problems of non-payment of rent
- Clear communication mechanisms between Property Management, Fiscal and Supportive Services staff

Supportive housing projects generally adopt a somewhat different response to rent collection problems than typical housing projects. Although it is critical that the importance of on-time rental payments be stressed to tenants, it is also understood that tenants of supportive housing have a number of unique problems that can impede their ability to meet their rental obligations. These can include family crises, medical emergencies, or relapse to addictive behavior patterns. Although there is a fundamental requirement that tenants meet their rental obligations, supportive housing projects will often seek recourse through counseling or referral for supportive services prior to commencing eviction. Well-run projects, however, will not shy from exercising sanctions when they are required.

LEARNING POINT: Organizations must adopt a clear rent collection policy, have it in writing, and apply it uniformly and consistently.

III.C-7: BUDGET MANAGEMENT (10–20 minutes)

BRIEF LECTURE:

Managing the budget involves monitoring actual revenues and expenses against projected revenues and expenses and ensuring the adequacy of funding to operate the property. There are several tools can be helpful in managing the budget, including the following:

THE BUDGET VARIANCE REPORT
The Budget Variance report shows the actual revenue collected and the actual expenses incurred against the budgeted (projected) revenue and expenses. Reviewing this report on a regular basis (monthly or quarterly) helps fiscal and property management to focus on areas of concern and make necessary adjustments to the management plan.

CASH FLOW ANALYSIS
Cash flow to operate the property is Operating Revenue less Operating Expenses, Reserves and Debt Service. It is important that management and fiscal staff monitor monthly and quarterly cash flow in order to avoid deficit spending and to ensure that essential bills are paid

LEARNING POINT: Careful cash management is essential for supportive housing projects as there are limited opportunities by which to supplement cash.

III.D: SOCIAL SERVICES

III.D-1: THE SOCIAL SERVICES BUDGET (10–20 minutes)

TRAINER NOTE: See ***HANDOUT #15: SAMPLE SOCIAL SERVICES BUDGET*.**

BRIEF LECTURE:

The availability of social services is what distinguishes supportive housing from other affordable housing projects. Most supportive housing projects employ a mix of on-site and off-site social services. In some instances, on-site services are provided by a third-party social services provider and therefore service delivery and funding are not the responsibility of the property manager and/or owner. In this case, the owner/property manager must monitor the activities of the third-party provider to be sure that the needs of the tenants are being addressed. In other projects, the owner will provide some services and the balance of the tenants' social services needs will be met through a referral to an outside provider. Generally speaking, facilities that provide one hundred percent of a tenant's social services needs in-house are institutional-type programs such as nursing homes and do not meet the supportive housing definition in terms of encouraging tenants to live with the maximum independence practicable.

Where the owner non-profit is also providing some level of social services, that organization will have a supportive services budget separate from the operating budget for the project. Supportive services are all those that are required for the tenants to be able to live independently in the supportive housing project. Supportive services include but are not limited to:

- Case management
- Life-skills training
- Chemical dependency treatment
- Mental health rehabilitation
- Services for the chronically ill, including those living with HIV/AIDS
- Childcare and parenting-skills training
- Housing placement
- Employment and education services
- Transportation

Funding for social services generally is provided either through:

- Fee-for-services arrangements like those provided by Medicaid, where providers are reimbursed for specific services such as attendance at a clinic. Reimbursement is generally according to a fixed rate (per visit or per day, etc.) and occurs only when an eligible tenant receives the service.
- Through a contract where the organization provides specified supportive services according to an established budget. This is how HUD pays for supportive services in the McKinney Supportive Housing Program.
- Funding raised from private sources such as grants, special events (annual dinners, etc.) or revenues generated from businesses operated by the non-profit organization (such as thrift shops).

TRAINER NOTE: In covering the social services budget, the following topics should be addressed:

BRIEF LECTURE:

- What are social services and what is their importance to supportive housing?
  - Elicit feedback from participants on what constitutes supportive services — use list in section below as a reference.
  - Facilitate a brief discussion on importance of social services to success of supportive housing — obtain comments on off-site vs. on-site services and examples of which services are better provided on- or off-site.
- Introduce concepts on how supportive services are reimbursed, fee-for-service or budget-based. See discussion below for reference information.
- Review sample social services budget to cover range of personnel and non-personnel services included. If appropriate, elicit discussion from group on the implications on the budget of being reimbursed via contract or fee-for-service.
- Discuss the need for financial support for start-up costs and the implications of contract or fee-for-service-based funding on the availability of this funding.
- Finally, review reports needed for adequate financial management, including Profit/Loss, budget to actual and cash flow reports.

The sample budgets included in this training separate out costs for supportive services from those associated with the operations of the project. In many instances — and especially for transitional housing projects — organizations will combine these expenses in a single budget. Often, expenses in these categories will be spread across both budgets. For example, utilities (phone, electric, heat, Internet) are likely to be shared by both supportive services and operations staff. Because HUD in its McKinney Programs requires separate budgets for supportive services and operations, this training curriculum also separates out the two.

As referenced above, the income portion of a social services budget will generally either consist of contract income for the delivery of services or a budgeted reimbursement rate such as $x for a visit times the projected number of visits during the budget period. Contracts are somewhat easier to manage insofar as the income will tend to be more uniform and predictable. The number of reimbursed visits can be affected by events outside of an organization's control such as weather, sickness or simple lack of demand. Contracts will also have budgeted and established schedules of personnel expenditures while fee-for-service arrangements will require that the provider adjust staffing to meet actual demand for services.

The expense portion of a social services budget will generally consist of personnel and other than personnel expenditures. Personnel consists of direct service staff such as counselors, case managers, nurses, etc. and supervisory staff, which can include direct supervisors such as program directors and portions of the overall agency administrative staff (i.e., the executive director and financial manager).

Other-than-personnel services can include supplies and materials directly related to the provision of supportive services as well as general office supplies and support such as office machines, telephone, etc. Other related expenses can include tenant transportation and staff training and recruitment.

Social services budgets will generally require a start-up phase of early operations. During this phase, the organization will have to recruit and train staff, secure space and facilities to provide services, and engage in outreach and screening of potential participants. Fee-for-services payment arrangements generally do not cover these start-up costs; contract arrangements often do. If the reimbursement source does not cover start-up expenses, they will then have to be funded through grants or by loans that will be repaid based on the fee-for-service revenue generated. HUD permits start-up costs to be paid out of McKinney Supportive Housing Program grants.

LEARNING POINT: Supportive housing involves a mix of on- and off-site services; the specific mix at any given project will be based on tenant needs and available funding.

III.D-2: FUND ACCOUNTING FOR PROGRAM SERVICES (10–20 minutes)

TRAINER STATES: Funds for social services may come from many sources and may fund several programs. Categorizing financial information by program helps management identify the costs associated with that specific program. Additionally, accounting activities can be grouped by funding source in the accounting system. This allows management to see how the funds are being spent.

Fund accounting software allows for this kind of accounting. However, management must bear in mind that more complex accounting software costs more. The more complex the accounting system, the more complex the work that has to be done. This impacts the professional level of, as well as the number of, staff needed to do the work. Also, the more highly specialized the software program, the less likely it will be that the organization will be able to identify staff familiar with its operation. This may require more costly staff or more extensive training with subsequent additional costs to the organization when and if staff leaves. Management must look at the costs versus the benefits of providing information in these various formats.

LEARNING POINT: Avoid over-sophisticated accounting systems but be sure that chosen system has sufficient capacity to allow management to analyze and control expenditures.

III.D-3: MONITORING EXPENDITURE/BUDGET VARIANCE REPORTS (10–20 minutes)

TRAINER STATES: Like any other aspects of financial operations, it is important to monitor actual income and expenditures on a frequent basis to ensure that the program is generating sufficient revenues and that expenses remain in line with projections.

Programs that are based on fee-for-service revenue must regularly track actual program income to be sure that it remains consistent with budget projections. If not, the program will need to adjust expenditures by hiring more or less direct services staff to correspond to actual demand. Programs that are not generating sufficient income may, in addition to cutting some expenses, seek to increase outreach and marketing efforts.

Monthly reports for program services should include:

- Budget to actual
- Cash flow analyses
- Profit/Loss — Revenue/Expense

LEARNING POINT: Services planning and delivery need to be regularly adjusted based on actual income and expenses.

IV. THE ANNUAL PROGRESS REPORT

IV.A: INTRODUCTION (20–30 minutes)

TRAINER NOTE: See ***HANDOUT #16: HUD APR; HANDOUT #17: COMPLETED SAMPLE HUD APR*** and ***HANDOUT #18: APR: FREQUENTLY ASKED QUESTIONS***.

BRIEF LECTURE:

The HUD APR is crucial to HUD grantees in many respects:

- Failure to submit timely reports will interrupt the flow of grant funds, potentially disrupting vital program operations.
- The process of compiling, analyzing and reporting the data required for the APR can provide vital information on program operations and outcomes that will be useful in targeting services.

Grantees should try to avoid regarding the APR as a one-time annual requirement and instead use it as an opportunity to continually collect data on their program and to use that data to improve their program. What is essential is that grantees establish a system that allows the collection of data at key points in the service-delivery process, specifically:

- At intake so as to obtain information on the prior living situations of the participants and to establish a baseline from which outcomes can be measured;
- At regular periodic intervals — approximately every 90 days — or whenever there is a significant change in the status of the participant in order to measure services being received by participants, additional services needs, and to identify changes in their status; and
- When participants leave the program in order to assess the benefits for the participants of having been in the program.

To collect this data, grantees should:

- Establish a file for each program participant/family. All information gathered should be considered confidential and should not be shared with or released to other parties without the express consent of the participants.
- The first entry should be an intake form, which will include referral information and documentation that the participant met the appropriate criteria for admission into a homeless assistance program.

- The specific measurable objectives that grantees identified in their grant applications to HUD are an essential component to the APR. Grantees need to include these objectives in the forms that they use to collect data from participants to develop strategies for collecting measurable information on the accomplishment of these objectives.

TRAINER NOTES: If participants have been involved in the APR or initial HUD application process, the trainer should request information on the specific objectives included in the participant's grants or APRs. The trainer should then seek discussion and input from the participants regarding strategies to collect the data required to measure the accomplishment of the objectives.

As a follow-up exercise, where participants report they were unable to achieve certain of their objectives, the trainer should seek input from participants about ways in which participants could modify their objectives to be both ones that their programs can accomplish and that will facilitate the tenants in being able to live with greater levels of independence.

Organizations that receive homeless assistance grants from HUD through the McKinney-Vento programs are required to submit an annual progress report (APR) to HUD. The programs covered by the APR requirement include Supportive Housing Program, Shelter Plus Care, and the Section 8 Moderate Rehabilitation for Single Room Occupancy Dwellings (SRO) Program.

These reports are required to be submitted within 90 days of the anniversary of the "Operating Start Date" of the HUD homeless assistance grant. The Operating Start Date of a homeless assistance program is indicated to HUD by the first date on which a grantee draws down funding from its HUD grant account for operating, supportive services or leasing funds. It is **not** the date on which a site is acquired or rehabilitation or construction activities commence.

Failure to submit the APR on a timely basis will have immediate consequences: the organization will be unable to draw down funds from HUD on its homeless assistance grant until the APR has been submitted.

The key to being able to successfully complete the APR is maintaining current records on individuals and families receiving assistance through the program. Intake forms should be prepared for all individuals and families upon entry into the program. Progress notes indicating services that have been received and accomplishments with specific reference to the goals and objectives set for the homeless assistance program should be prepared for all assisted individuals and families on at least a quarterly basis. Finally, a discharge form should be completed for all those leaving the homeless assistance program for whatever reason. The information for participants should be summarized in "Persons Served Worksheets," examples of which are provided as part of the APR package from HUD. Maintaining current records will dramatically facilitate the process of completing the APR and ensure that the assisted organization will be able to continue to receive HUD homeless assistance funding.

The APR consists of two main sections: Project Progress and Financial Information. Guidance on how to complete these two sections is provided in the sections that follow.

LEARNING POINT: APRs should not be looked at as an annual reporting requirement but as a program management tool, collecting data from participants as a way of focusing service delivery; attempting to collect all required information at year's end will be burdensome and potentially impossible.

IV.B: PROJECT PROGRESS (20–30 minutes)

BRIEF LECTURE:

The McKinney-Vento homeless assistance programs are based on the "continuum of care." The overall goal is to allow homeless people to live with as high a degree of independence and self-sufficiency as possible. For many, an interim period of supportive services and/or housing will be all that is required to get back on their feet and living independently. Others will have long-term disabilities, which require continuing supportive services but which should facilitate living as independently as practicable. In the project progress section of the APRs, grantees will be able to demonstrate that their homeless assistance projects are serving people who are eligible for assistance; that the programs have provided appropriate services and that participants have achieved measurable outcomes as a result of participation; and that the overall program has made progress in achieving the objectives that were set forth for it.

The most important tool that a grantee has in completing the APR will be the participant records prepared for each family and individual served through the program and summary worksheets of this information. The time and effort expended on preparing participant files on program entry — periodically (every 90 days or at the point of significant change in participant status) and when the participant leaves the program — will be repaid by the ease with which the grantee is able to complete the HUD APR. HUD also reserves the right to conduct periodic monitoring visits. The presence of well-documented case records for the individuals and families assisted is important to a successful monitoring visit.

TRAINER NOTE: See ***HANDOUT #19*****:** ***APR DEMOGRAPHIC TRACKING SHEET*** and ***HANDOUT #20: APR DEMOGRAPHIC TRACKING SHEET LEGEND*****.**

COMPLETING PART I: PROJECT PROGRESS

TRAINER STATES: The first portion of the APR requests information on the number, demographic and supportive services needs of the individuals and families served. HUD will compare the information provided with what the grantee had proposed in its initial application and technical submission. Ideally, the grantee will be serving a similar number of people with similar special needs to those proposed in the application. If the grantee has not achieved this, it should be prepared to explain the factors that have precluded it from so doing.

Question 10, which asks about the prior living situation of the program's participants, is particularly important. HUD expects that all individuals and families receiving assistance under the grant will meet its definition of homelessness. Grantees should also have written documentation of this in each of the participants' intake forms. This documentation should take the form of referral letters from referring programs such as homeless shelters, discharging institutions, etc. In some instances, such as individuals and families fleeing from domestic violence, self-certification by the participant is acceptable. With respect to Question 12, Length of Stay in Program, grantees are reminded that for Transitional Housing programs, the length of stay is limited to 24 months.

The information needed to complete the Project Progress component of the APR should come from the participant files, which for convenience purposes can be summarized in forms similar to the "Participant Served Worksheets" that HUD attaches to the APR. Grantees are not required to complete these forms or to use these worksheets. The information requested in the worksheets, however, should represent the minimum information that is included in each participant's records.

Question 16 requests information on the project's success in achieving the measurable objectives that the grantee had specified for the project. For the first year of operations, these are the goals contained in the application and/or modified in the technical submission to HUD. The goals listed in this section should be identical to those previously submitted to HUD. In addition to specifying actual accomplishments, grantees are also asked to specify their objectives for the next operating year. These objectives will then be reported on in that year's APR. Grantees should take this opportunity to revise those objectives that do not accurately reflect project progress.

It should be noted that many local jurisdictions will use the information contained in the APR as one of the factors in deciding whether the project should be ranked for renewal at the expiration of the grant term. Grantees should be mindful of this when preparing the APR.

LEARNING POINT: Periodically collect data on program participants, at entry, every 90 days, at discharge and whenever participants' situations significantly change; program goals can be modified as part of the APR process if the prior year's goals were not appropriate or adequate.

IV.C: FINANCIAL REPORT (20–30 minutes)

BRIEF LECTURE:

COMPLETING PART II: FINANCIAL INFORMATION

There are several key aspects to the financial component of the APR:

- HUD matching requirements. There are statutory matching requirements:
    - Programs receiving funding from HUD under Supportive Housing for acquisition, rehabilitation or new construction must match each HUD dollar with one dollar of non-HUD money.
    - Supportive housing projects receiving HUD funds for operations must provide 25 cents for each 75 cents in HUD funding.
    - Supportive housing projects receiving HUD funds for supportive services must provide 20 cents for each 80 cents in HUD funds.
    - Grantees under Shelter Plus Care must provide supportive services in a dollar amount that matches the funding provided for rent subsidies.

In addition to the statutory matches, applicants will have also identified leveraged funds in their application to HUD. The grantees must report to HUD on the APR's their success in meeting the leveraged funding they indicated to HUD they would achieve.

TRAINER NOTE: EXERCISE: The trainer should divide the participants into groups of four and be sure that everyone has a copy of the sample supportive services budget. The task presented to the group should be to develop an estimate of the cost of provided specified set of supportive services:

Supportive services to include:

- Substance abuse counseling;

- Educational/vocational counseling;

- Parenting-skills training;

- Case management.

Using the line item budget presented for supportive services, the Trainer should ask the group to develop a strategy for reporting to HUD on the costs of delivering the specified supportive services. (The suggested strategy is for the participants to allocate the amount of personnel time required to deliver the services and then apportion the other-than-personnel services according to percentages of personnel time required to deliver the services). However, each group should develop its own approach to the problem and then report back to the entire group.

This section requests information both on the uses of HUD funds received and on matching funds received by the grantee. With respect to the matching funds, HUD will expect the grantee to have received matching funds that equal or exceed those stated in the technical submission. In addition to meeting the matching amounts that the grantee has specified for the project, grantees must also meet the minimum matches that are statutorily required for the McKinney-Vento Programs. These include:

- For the Supportive Housing Program:
    - Funds for acquisition, rehabilitation and new construction must be matched dollar for dollar by other funding sources;
    - Funds for operating costs must be matched 75:25 HUD to other sources of funds; and
    - Funds for supportive services must be matched 80:20 HUD to other sources of funds.
- For the Shelter Plus Care Program:
    - Every dollar of rental assistance from HUD must be matched by a dollar of supportive services from some other source.

It should be noted that HUD in Question 18, Supportive Services, asks for the dollar amount of supportive services provided in a wide range of categories. This is not generally how non-profit organizations prepare budgets or report this information. To provide this information to HUD, grantees should:

- Prepare a supportive services budget, identifying specific personnel and non-personnel services.
- From the HUD technical submission, identify the specific supportive services that are being provided in this homeless assistance project.
- Estimate based on staffing and tenant needs the percentage of effort expended on each of the supportive services. The organization might estimate, for example, that 25 percent of the supportive services effort was devoted to case management. This estimate would be based on the amount of time that the staff assigned to provide supportive services expended on the case management function. Once a percentage has been assigned to each of the supportive services provided, these respective percentages are then applied against the total supportive services budget to arrive at the costs for the supportive services provided.

Question 19 asks for information concerning cash matches for Supportive Housing Program expenditures. Remember that the cash match should at least equal that specified to HUD as part of the technical submission. Although HUD does not require a match for either 'leasing' or 'administration,' if the grantee specified a match in the technical submission, then HUD will expect the specified match.

LEARNING POINT: Financial information presented in APRs must be consistent with information provided in technical submissions; significant variances will require explanation. Also, HUD requires financial data for services to be presented based on the services cost not on the personnel and other-than-personnel costs associated with delivering services.

V: CONCLUSION (10–20 minutes)

TRAINER NOTE: Bring closure to the training by reviewing the highlights of the day. Ask for questions and comments about the content.

BRIEF LECTURE:

Let's review some of what we learned today. We know that financial planning includes:

- Being mindful of the key concepts of financial planning
- Developing a plan and budget
- Ensuring financial statements
- Developing an internal control system
- Responding to audits
- Filing and maintaining complete State and Federal tax returns
- Hiring staff to maintain capacity to sustain a complete financial plan

We also discussed the importance of developing accounting for each component including:

- Housing Development
- Property Management
- Social Services

We finally ended today's training by reviewing the importance of an annual progress report that includes a summary of the project's advancements and an annual financial recap.

LEARNING POINT: Trainer will review significant points of the training and clarify any remaining questions.