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MassHousing's Procedures for Implementing

HUD's Residual Receipts Policy and Method of Calculation

For those developments with the 1980 Form of the Section 8 Housing Assistance Payment (HAP) Contract, Section 2.6(c) (1) of the Contract Provides:

Project funds must be used for the benefit of the project, to make mortgage payments, to pay operating expenses, to make required deposits to the Replacement Reserve in accordance with paragraph (d) of this section and to provide distributions to the Owner as provided in paragraph (c). To the extent the HFA determines that project funds are more than needed for these purposes, the surplus funds must be deposited with the HFA, Mortgagee or other HFA - approved depository in an interest - bearing account. Withdrawals from this account will be made only with the approval of the HFA and for project purposes, including the reduction of housing assistance payments. Upon termination of the Contract, any excess funds must be remitted to HUD.

For developments affected by this requirement, and to be in compliance with a directive from the Inspector General of HUD, the Massachusetts Housing Finance Agency established a system requiring Residual Receipts to be deposited with the Agency. To achieve this objective, MassHousing has defined the following points related to the timing of income recognition, the method for calculation of Residual Receipts, the funding of escrow accounts, and the timing of withdrawals.

- 1) Since Residual Receipts will not be escrowed by the development but rather remitted to the Agency, this amount should not be considered a component of current year's revenue. Similarly, annual interest income earned on the Residual Receipts Escrow will also not be considered income of the development. Revenue should only be recognized when funds are approved for withdrawal from the Residual Receipts Escrow. (See I.R.S. Letter Ruling 9451042)
- 2) The calculation of Residual Receipts will be done in a manner consistent with the way HUD determines this amount, except for the calculation of the Maximum Possible Distribution Earned. MassHousing enabling legislation limits distributions to six (6) percent of Stated Equity (or the relevant percentage agreed upon by the Agency). Consequently, this number will be used to determine the Maximum Possible Distribution Earned. (See Form F.C.-6, Line 697 and Instructions)
- 3) Replacement Reserve escrows will be funded only to the extent originally permitted in the Section 8 Contract document and in any subsequent amendments or adjustments thereto. Excess contributions to the Replacement Reserve escrow will be allowed only in those cases where there is a definable program of capital improvements that cannot be funded from current contributions and accrued interest. *Since it was HUD's intent that the Replacement Reserve Account would be used to fund major capital expenditures, the Agency reserves the right to review the sources of funding for capital items and to impute a replacement reserve withdrawal for those items deemed to have been paid inappropriately from operations.*

- 4) Special Escrows will be funded only to the extent and for purposes sanctioned by the Agency.
- 5) Annual Insurance and Tax obligations will be paid from the Real Estate Tax and Insurance escrow specifically established for these purposes except for any shortfalls in funding that may be paid from the operating cash account.
- 6) Withdrawals from the Residual Receipts Escrow must be approved by HUD and will be permitted for the following purposes:
 - (a) to cover any year-end accumulated deficiencies due to unpaid distributions earned in prior years;
 - (b) to supplement approved additions to Replacement Reserves if funding of the escrow falls below one-year's level;
 - (c) to reduce required Housing Assistance Payments.

Form F.C.-6, which became part of the Audit Requirements in 1987, is designed to quantify the calculation. Essentially, surplus cash will be calculated as of December 31 of each year according to the HUD formula. From surplus cash will be subtracted Distributions Earned but Unpaid. The difference, or Required Deposit to the Residual Receipts Escrow, must be submitted to the Agency no later than 90 days after the close of the fiscal year (i.e. March 31) and in conjunction with the submission of the Annual Audit.

The Auditor for each development must review the calculations and provide appropriate assurances as part of the Report on Supplementary Financial Information.