
CHAPTER 3. INSTRUCTIONS FOR THE PREPARATION OF THE
ANNUAL OPERATING BUDGET - HUD-92547A

3-1. INTRODUCTION

This chapter discusses the purpose, preparation, approval and reporting processes of the Annual Cooperative Budget Form HUD-92547A. (See Appendix 1) One of the primary responsibilities imposed by the by-laws on the initial and subsequent Boards of Directors of a cooperative is to adopt an annual operating budget. The HUD-92547A format is coded to the Uniform System Chart of Accounts and can be expanded to serve the more complex cooperatives.

This form is used to project annual revenue and expenses. The Total Financial Revenue amount assumes all potential sources of revenue by account, and the Total Financial Expenses amount includes administrative expenses, operating expenses, taxes, insurance and financial expenses. The form is completed by the cooperative managing agent with the cooperative Board of Directors and is submitted to HUD on a yearly basis. The report allows HUD to analyze how the cooperative operations are being managed by comparing the current years budget to prior year activity.

The annual cost of operating a cooperative varies with the characteristics of the development, whether it is new construction or rehabilitation, and the services required by its owners.

Budgets should be prepared by listing the annual expenses that result from operating the cooperative development. While the estimated revenues are considered in the budget planning, if the operating expenses are determined by studying similar cooperative projects, the estimates will be more accurate, revenue goals can be set, and the budget becomes a more useful planning tool.

3-2. INITIAL OPERATING BUDGET AND SCHEDULE OF
CARRYING CHARGES DEVELOPED AFTER
OCCUPANCY

A. SCHEDULE OF CARRYING CHARGES

Carrying charges relate to the monthly expenses required to support the cooperative corporation

operations. The initial schedule of carrying charges presents the cooperative Board of Directors' and the management agent's estimate of the first year of the project operations. The initial schedule and the management agent's opinion as to its accuracy must be included in the Information Bulletin. Therefore, the Initial Schedule of Carrying Charges must be prepared considerably prior to actual operations. The amounts in the Current FY column should show expense items reflecting the best judgment of the cooperative Board of Directors and the management agent. The Field Office will reflect any revisions it considers appropriate in the last column, and the schedule reflected in the Information Bulletin must give effect to these revisions.

Note: The expense projections contained in the Project Analysis (Form HUD-92264) are made for a different purpose and should not be regarded as adequate for the cooperative budget.

B. ESTIMATES OF REVENUE

1. Need for Conservatism ("Low" Estimates)

When preparing budgets prior to the attainment of actual operating experience, estimates of revenue must be conservative. During the first years of operation it is important to present budgets that are reasonable and are attainable. Therefore "low" estimates of revenue and "high" estimates for expenses should be presented in the initial budgets.

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2. Limitations on Revenue Estimates for Garage and Commercial Space

In the initial budget, the estimated revenue from garage space must not exceed fifty (50) per cent of the total for this item shown in the Project Analysis (Form HUD-92264). Such a budget should not reflect any estimated revenue from such miscellaneous sources as laundry machines, telephone services, vending machines, etc. Revenue from commercial space may be reflected only to the extent of leases actually executed with Field Office approval.

C. ESTIMATES OF EXPENSES

The fixed charges include all expenses that remain constant throughout the year. The schedule of expenses should be compiled as realistically as possible. Requirements affecting the budget entries on accounts such as Ground Rent, Mortgage Insurance Premium, Interest, Principal, Replacement Reserve and General Operating Reserve are set forth in the Regulatory Agreement and/or the Commitment for Insurance. The Total Financial Revenue amount must be at least equal to the amount of Total Financial Expenses. The revenue from Apartments or Member Carrying Charges must agree with the annual total in the schedule of carrying charges.

D. SOURCES OF ESTIMATES

Tax authorities, insurance companies, utility companies, suppliers and manufacturers of project equipment are good sources of information. Local building owners and managers' associations are also good sources of information. The catalog of a large retail store is useful in estimating the cost of supplies and equipment. Other cooperatives with comparable facilities and services, that have been operating for more than one year, can also be a valuable source of information.

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E. MANDATORY PROVISIONS FOR SECTIONS
221(d)(3) AND 236 CASES AND IN SECTION 213
CASES WITH LESS THAN \$500 DOWNPAYMENTS

1. 2% Provision

In all Section 221(d)(3) and Section 236 cases, and in Section 213 cases in which down payments of less than \$500 are involved, the initial operating budget must contain an allocation for vacancy and collection losses of at least 2% of the budget otherwise projected. If the experience of nearby or comparable projects indicates this to be inadequate, a higher percentage should be required. Budgets prepared after the cooperative is in actual operation should contain such allocations as are justified by its own operating experience.

2. General Operating Reserve

Provision must be made for replacing withdrawals with deposits during the next fiscal

year (or under a previously approved repayment plan). Such deposits, over the amounts required to meet the regular annual requirement must, be included on line 34 of the Operating Budget.

3. Painting Reserve

This is an optional requirement. However, experience has demonstrated the value of establishing such a funded reserve to avoid special assessments.

3-3. BUDGETS USED IN CONJUNCTION WITH
COMPUTERIZED ACCOUNTING

If an automated system is used for preparing budgets a Data Flow Chart should accompany the budget as part of management's plan of operations. The purpose of preparing

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data flow charts is to define how the automated system is integrated in the budget process.

3-4. BUDGETING FOR A SINGLE COOPERATIVE
CORPORATION HAVING SEVERAL MORTGAGE
PANELS

A cooperative that has been developed in sections, wherein each section imposes a separate mortgage obligation on the single corporation, may operate on a consolidated budget reflecting the total operation. The automated Books of Account as previously described, however, must be kept in a manner that will permit financial identification of each mortgage panel.

3-5. SECTION 236 COOPERATIVE BUDGETS

- A. A section 236 cooperative annual operating budget on which monthly charges are predicated is compiled by leaving the charge to Monthly Insurance Premium (MIP) account blank and entering the amount in interest on mortgage payable computed at 1%.
- B. A second annual operating budget with MIP and market interest prevailing when the loan was made should be prepared to present a picture of the budget attributable to units occupied by members paying market interest rates and for computation of year end tax information.

3-6. BUDGET APPROVAL

The budget must be signed by the managing agent, a Director of the cooperative and the HUD Field Office. An approved copy should be available for examination by the cooperative members.

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3-7. PLAN OF OPERATION

Each annual budget must indicate the management plan that will be used to implement it. The plan should cover such items as the following:

- A. Is a staffing plan included in the plan? Does the schedule of personnel to be directly employed by the cooperative include their compensation and duties?
 - B. Have management personnel been instructed in the implementation of data flow to and from the automated system?
 - C. How often will a property manager from the management company visit the project?
 - D. Will the managing agent attend all Board meetings?
 - E. What member committees are organized to assist in management (Budget, Grounds, Collections, Finance)?
 - F. Will the management agent or resident manager contact delinquents in person or in writing?
 - G. Is a delinquent member called before the Board before turning his account over to an attorney or collection agency?
 - H. Have the maintenance personnel been given a maintenance and operations guideline to keep the cooperative's operating costs at the lowest possible level?
 - I. Have the on-premises personnel been given copies of plans, specifications, corporate documents, and been made aware of the requirements imposed by the Regulatory Agreement on the Board and requirements imposed by the Management Agreement on the management firm?
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- J. Has a detailed plan been submitted for any expense items, such as grounds maintenance or painting and decorating, which have been reduced by use of self-help techniques?

3-8. PERSONAL BENEFIT EXPENSE (PBE)

A. DEFINITION

The PBE approach in a cooperative gives the member an opportunity to exercise individual control over some expenses that relate to him personally.

B. APPLICATION

PBE usually includes decoration of the interior of the member's unit and may include other items, such as utilities, which are paid for directly by the cooperative member.

C. PBE EXPENSES VS. CORPORATE BUDGET

The cooperative budget and schedule of carrying charges do not reflect PBE expenses in unsubsidized projects.

D. HUD APPROVAL

The cooperative home ownership concept may lend itself to more extensive self-help than the painting and decoration of unit interiors. If it is used more extensively, e.g., in areas of grounds maintenance, painting of common areas, etc., it must be done under a plan that is approved by HUD.

3-9. PROPORTIONATE FACTOR OF UNIT VALUATION TO TOTAL VALUATION

A. DEFINITION

In the Information Bulletin a valuation is set forth for each unit in the project. A decimal factor may be developed by dividing the valuation assigned each unit

by the total valuation of all units in the project, (e.g., a unit with a \$10,000 valuation in a \$1,000,000 total valuation develops a proportionate factor of .0100 (1%)).

B. APPLICATION

Increases and decreases in carrying charges may be apportioned by the use of this factor. The factor may also be used to determine the proportionate share for each unit of total amounts paid by cooperative for mortgage interest, real estate taxes and other line items on the budget. Interest and real estate tax information is useful to the members in connection with filing of federal income tax returns. The interest and real estate taxes attributable to a unit may need to be broken down further in projects receiving HUD Federal assistance to determine how much an assisted member has actually paid.

C. TAX IMPLICATIONS OF THE UNIT VALUATION

Many states offer homestead tax exemption benefits to encourage urban homesteading. This may affect the unit valuation by the amount of the homestead exemption amount. For example, the District of Columbia offers a 22% homestead tax exemption which decreases the amount of the assessed value of the unit by 22%. For owners that file for homestead exemption, their assessed value will be lower than comparable units that do not take advantage of the tax exemption. All owners should file for homestead exemption whenever they may be entitled to them.

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3-10. BUDGET CONTROLS

The budget process is a critical component in managing operations for cooperative corporations. If estimates for revenue or expenses are inaccurate or unreliable, financial goals will not be achieved and the corporation viability will be uncertain.

Budget controls can establish a framework to provide HUD officials with assurances that cooperative budgets are attainable, daily operations are adequately recorded, and that estimates presented in the budget are reliable.

The following presents criteria for determining adequate levels of budget controls in budget environment, budget preparation,

budget approval process, budget execution, and reporting.

A. BUDGET ENVIRONMENT

Is the budget process clearly documented and available to all cooperative members?

Is there coordination among the board of directors, the cooperative members and the managing agent for preparing and approving the annual budget?

Is there a clear line of authority to modify budgets or present amendments to current budgets?

Are budget review dates and budget approval dates communicated to all parties involved?

Are the responsibilities for budget preparation, adoption, execution, and reporting segregated, where appropriate?

B. BUDGET PREPARATION

Are the individual(s) responsible for the preparation of the budget aware of all budget procedures required by HUD?

Is a "budget calendar" prepared to ensure orderly submission and approval of the budget?

Are outside sources sought to review appropriate sections of the budget?

Are the accounting principles utilized in preparing the budget (including accrual basis) in accordance with the accounting system?

Is the budget prepared in sufficient detail to provide a meaningful tool with which to monitor subsequent performance?

C. BUDGET APPROVAL

Are meetings held to obtain cooperative membership approval?

Is the impact of budget modifications, either increases or decreases, clearly communicated to operating departments or agencies?

Are estimated revenues and expenses recorded in the accounting system for later comparison to actual amounts realized or incurred?

Are budgets published and distributed to all cooperative members?

D. BUDGET EXECUTION

Are procedures formally adopted and communicated for issuing purchase orders or expenditure commitments?

Are requests for supplemental budget changes processed and approved in the same fashion as the original budget?

If liabilities and expenditures are recorded on an accrual basis, are adequate controls in effect to ensure knowledge of outstanding commitments?

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E. BUDGET REPORTING

Are actual expenditures compared to budget with reasonable frequency and on a timely basis?

Are reports discussed with the Board of Directors, and cooperative members and are explanations received for significant variations from budget?

Do procedures exist for timely notification to Board members and cooperative members in the event of budget overruns?

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