



Questions and Answers on S95 Net Operating Revenue

What is net operating revenue?

In general, net operating revenue refers to earnings left over from operations, after all bills and charges have been accounted for. In a housing co-op, it's the revenue that remains after the co-op has met its operating expenses, including a replacement-reserve contribution. "Operating surplus" is another term for net operating revenue.

Why is net operating revenue of special interest to Section 95 housing co-operatives?

In 1995, Canada Mortgage and Housing Corporation (CMHC) began telling Section 95 co-ops that they couldn't keep all of their net operating revenue. Some part of any surplus, CMHC argued, came from the money CMHC provided to reduce the charges of members of low and modest income.

Each year CMHC looked at the relationship between a co-op's net operating revenue and its income from various sources, including income-tested assistance. It then told the co-op what portion of any unspent operating funds it believed had come from the CMHC. For some co-ops, this money was withheld from future subsidy payments; in other cases, the co-op was expected to send CMHC a cheque.

What is the Net Operating Revenue Policy?

Co-ops disagreed with the new practice we have described and the Co-operative Housing Federation of Canada took up the matter with CMHC. This action led to what is now known as the Net Operating Revenue Policy, in effect for

all fiscal years beginning after 1999. The policy applies only to S95 co-ops, although other co-ops may follow it if they wish. It tells a co-op what it should do with net operating revenue, when it has some. The policy lists several possibilities, in order of priority.

Our operating agreement has expired. Do we still have to follow the Net Operating Revenue Policy?

The Net Operating Revenue Policy applies only to Section 95 housing co-operatives that still have a CMHC operating agreement. However, the Agency encourages other co-ops to contribute their operating surpluses to their capital-replacement reserve, even when doing so is no longer required. Read below to find out why.

If we still have to follow the Net Operating Revenue Policy, what is the first priority?

If your co-op is carrying a deficit from past years, any net operating revenue goes first to reduce or clear that deficit.

What does the Agency recommend?

If you have no accumulated deficit, we recommend that you add any net operating revenue to your capital-replacement reserve. There are at least three good reasons to do this.

1. Every year co-ops tell us that they need to borrow money for capital repairs. This is not always easy to do. The net operating revenue you put in your reserve could

mean you don't have to go to the trouble of borrowing or put off needed repairs.

2. With a healthy reserve, you can spruce up your property. All members feel pride when they live in an attractive co-op in good repair. A positive atmosphere makes for a better community.
3. Even if you are following a current reserve plan, a little extra money in this fund will be very useful if a building component fails unexpectedly.

Are there any restrictions?

The Net Operating Revenue Policy does say that your replacement reserve can't grow beyond your co-op's future needs. These needs are set out in your capital replacement plan, if you have one.

The Agency does not see any co-ops putting away too much money, but we see many that are not setting aside enough. Co-op buildings are aging and many co-ops are finding it hard keep up with the anticipated repairs and replacements, let alone the unexpected.

What else can a co-op do with net operating revenue?

If your co-op needs more income-tested assistance than it receives from CMHC, you may wish to put your net operating revenue into the Subsidy-Surplus Reserve. This is actually the second priority under the Net Operating Revenue Policy, but only if "the need is demonstrable." The Agency will agree that your co-op needs to put net operating revenue into the Subsidy-Surplus Reserve if both of the following are true:

1. Your co-op has nothing in its Subsidy-Surplus Reserve, and
2. Without this contribution, your co-op will be short of assistance in the near future.

You may like the idea of putting your surplus here if your co-op is spending a substantial sum

from your own resources to top up the assistance you get from CMHC. But it is important to remember that, once you transfer net operating revenue to this reserve, you can use the money only for income-tested assistance. You cannot take it out later to cover an operating loss, as you are allowed to do with a transfer to your capital-replacement reserve.

In fact, if your membership's needs change, you may not even be able to use these funds for income-tested assistance. As you know, anything in your co-op's Subsidy Surplus Reserve beyond \$500 per unit, plus interest, must go back to CMHC. That includes any amounts transferred from net operating revenue.

Are there any other possibilities?

Yes, there is at least one other. If your co-op has a good reason for setting up a special reserve, you can explain your purpose to your relationship manager at the Agency. The Agency can authorize a special reserve for your co-op if we think your reason is sound.

Prince Edward Island co-ops may have to treat some net operating revenue in a different way. Like all housing co-ops in Canada, they were incorporated under a provincial co-operative act. The act in PEI says that a co-op must put 10 per cent of any operating surplus earned in a year into a reserve. Because this is required under a law, it is known as a "statutory" reserve. However, acts do change from time to time. Before funding this reserve each year, we recommend that these co-ops check to make sure that the requirement is still in force.

Do S95 co-ops ever have to send refunds to CMHC?

Yes, but those refunds are different from the refunds CMHC asked for between 1995 and 2000, although they do involve subsidy money. S95 co-ops are not required to give out every

dollar of income-tested assistance they receive each year from CMHC. As we noted earlier, they can keep up to \$500, plus unspent interest, in a Subsidy-Surplus Reserve for future use. Everything over the maximum is due back to CMHC. These refunds have nothing to do with net operating revenue.

When a co-op has reached the end of its operating agreement, it can keep whatever remains in its Subsidy-Surplus Reserve. This money is to be spent on meeting the co-op's needs.

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