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ASSOCIATIONS INSTITUTE

# Community Association

## BEST PRACTICE

### Finances



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I like to say that the best practices are born out of the trials and tribulations of the worst practices. If you are a board member or community manager of homeowners associations and condominium communities, the way to learn these best practices without suffering yourself is to learn from the mistakes of others. Over the last three years I have researched over twenty case studies of fraud and embezzlement perpetrated by board members, onsite staff, portfolio managers and management companies around the country. In this article we'll discuss the resulting best practices, as well as cover some good housekeeping items.

#### Financial Reports:

One embezzlement scheme where the management company controller stole over \$2.3M from numerous communities was from doctoring the financial reports. The report package did not include a bank reconciliation report which proves what is on the reports matches what is on the bank statements. Besides fraud, getting reports more frequently will help you spot irregularities faster. Use the comparative income and expense report that shows the actual expenses versus budgeted expenses and the variance for the month and year to date. Look at the variances and then ask questions.

#### Best Practice

Get financial reports monthly and make sure they include a bank reconciliation report.

#### Bank Information:

In the case mentioned above, the controller also did not include bank statements with the report package, so the boards couldn't verify the funds in the bank compared to what was shown on the reports.

#### Best Practice

At a minimum get bank statements as part of the boards' financial report package. An even better practice is for boards (more than 1 person) to have online access to view bank accounts so it can spot irregularities faster and for greater checks and balances.

#### Old Bank Accounts:

In some cases, board members changed and an old bank account was not reported on the financial reports and a former board member was spending money from this account. Even when there is no fraud, I've dealt with boards where the original signers on the account moved or died and the new board could not access its money until then it filled out a lot of paperwork and had to go through numerous phone calls and meetings with the bank for over nine months! Plus, fewer bank accounts make the financial reports easier to read and will cost you less to have someone prepare.

#### Best Practice

Close old bank accounts.

**Checks and Balances:**

Another embezzlement case involved a board president who had the community checkbook and wrote out checks, forged a second board member's signature, and pocketed the money. Even having two signers required for checks did not work.

**Best Practice**

Systematize the association's accounts payable. We use an online system where the manager and/or two board members have unique logins to review and approve bills before a payment gets processed. This also increases the board's control over expenses and reduces surprises when reviewing the monthly financial reports.

**Debit & Credit Cards and Petty Cash:**

One onsite manager in Colorado had a debit card and withdrew money from the ATM at the Black Hawk Casino! The Board did not have access to the bank information and this went unnoticed for several years.

**Best Practice**

For debit cards the best practice is to set up a separate account and then limit the amount of money in that account to say \$1,000. Otherwise, someone could withdraw the daily limit every day and that can add up. Credit cards are better as you can put a cap on them but make sure you have a process in place to track the credit cards when board members or staff change. Petty cash is just a bad idea. We recommend not accepting cash as payment as it can easily "get lost." The best way to avoid all of these scenarios is to use a supply house that will invoice the association or if the purchases are infrequent for a board member to make the purchase and then submit reimbursement through an online approval system as mentioned above.

**Payroll:**

A community had onsite staff and chose to "save money" having that staff use Quicken to run payroll. The person doing payroll ended up giving themselves extra pay checks as well as additional bonus checks! Additionally, if withholding rates change and you don't change the rates in your software you may incur a shortfall. Depending on how quick the state is to notice this, the association could be liable to pay the shortfall as well as stiff penalties.

**Best Practice**

Use an outside payroll company to reduce risk.

**Good Housekeeping****Separate Operating Funds from Reserve Funds:**

Many communities use only one bank account. We recommend that your association have a second bank account for its reserve funds. This will help you track these more clearly on the balance sheet monthly to see exactly how much you have put aside for capital replacement projects.

**Operating Expenses Paid from Reserve Account:**

I've seen where communities use the reserve account as a slush fund for operating account shortfalls. If you have to use these funds, we recommend borrowing them for a short term and then replenishing with a special assessment. Levy the special assessment quickly after the cause of the budget shortfall so it is fresh in owners' minds - think more snow than anticipated in a year assessed while it's still cold instead of during mid-summer.

**Collections:**

If your community doesn't have a collection policy that outlines what will be done at what time and the associated fees owners will pay (and you should have this policy, because it is required!) put that on your to-do list. This will help the board, management, accounting staff and homeowners get clear guidance on the association's process. Additionally, a best practice for home loans, car loans and credit cards are reporting delinquent payers to the credit rating agencies and now this is available for community associations. This lights a fire under owners to put their association dues bill on the top of stack of bills to pay and not the bottom.

I hope this opens up some discussion at your community or your management company. 🏠

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*Russell Munz is a Licensed / Certified CAM in 7 states and Founder and President of Community Financials, Inc. a nationwide financial management company that provides monthly accounting services to Community Associations based in Boulder, CO. For more financial best practices and to see the actual embezzlement case studies check out our blog at [www.CommunityFinancials.com](http://www.CommunityFinancials.com).*