



## IT'S 1 A.M. DO YOU KNOW WHERE YOUR MONEY IS?

### TOP TEN POTENTIAL ACCOUNTING AND FINANCIAL PLANNING DISASTERS



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In today's economy, it is crucial that each board of directors have a clear grasp of the financial and accounting aspects of association operations. Even when you have professional management handling

the association's finances, the buck stops with the board.

Here are the top 10 potential disasters facing boards in the current market, in no particular order:

**1. Failure to document approval of contracts, and expenditures for work to be done, in an open board meeting.** It is very important that the awarding of a contract be set forth in the Minutes of the meeting at which it was approved. If you are levying a special assessment to pay for the work to be done, be sure to send out the necessary notices at least 14 days prior to the date of the board meeting at which the assessment is adopted.

**2. Inadequate budgeting to accommodate shortfall caused by foreclosures and delinquencies.** Associations

need to accept that "bad debt" is a reality of life, and you will need to include it in your annual budget; as well as build it in to your annual and special assessments, to cover when less than 100% of the owners pay the assessments. And, bad debt is required to be booked monthly, under generally accepted accounting standards.

While we are talking about budgeting, don't forget to include a realistic estimate of the cost of year-end financials, including an occasional audit, in the annual budget.

**3. Failure to keep receipts and other documentation of expenditures.** Every expenditure should be accompanied by the applicable receipt, and explanation of the purchase. And, the purchases should all be recorded in the accounting records as they occur. If you've ever had the experience of dumping out an envelope full of receipts and trying to reconstruct the purchases at the end of the year, you have first hand knowledge of why that is a poor accounting practice. And, why would you want to subject yourself to possible claims of misappropriation of funds or accounting irregularities?

When the CPA is trying to produce your year-end financial

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report, proper handling of those receipts will be very important. The board should have a strict policy which requires any director, Professional Manager, maintenance person, committee member, etc. who is authorized to spend "petty cash" to produce the receipts before being reimbursed. The policy should also set guidelines for use of petty cash, and set dollar limits, requiring board approval for larger expenditures. The receipts should be kept for reconciliation of accounts, and for inspection by owners who request access to accounting records.

**4. Failure to change account signatories when the Board of Directors changes.** If the board changes, your bank accounts should immediately be updated. The Minutes of the organizational meeting of the board should reflect who is an authorized signatory, and whether checks require two signatures. You should also develop a policy for how accounts payable are to be processed – who reviews and approves the invoices? Who cuts the checks? Who signs the checks, when and where (at a board meeting? In the management office? In the association office?) Keep in mind – if a person is a signatory on the association's account(s), he/she has the authority to withdraw money from the account(s), without further authorization from the board.

Do not forget to have fidelity bond insurance for any person who has access to the association's funds.

**5. If at all possible, budget for and accumulate funds to pay insurance premiums a year ahead, so you have the cash when the policy is renewed.** This will avoid having to scramble to find a loan or levy a special assessment or find other financing (which will add to the costs because of the carrying charges – interest, finance charges, closing costs, and so on).

**6. Whether the board does its own accounting, or you have a management company or a bookkeeping service, or even a CPA company, providing the association with monthly accounting services, it is critical that the year-end financial report be produced by an independent CPA, who has not been involved in the monthly accounting.** This is an important part of checks and balances to ensure financial health of the association. It is never a good idea for the person who writes and signs the checks to reconcile the bank account. These days, stories of theft and mismanagement of accounts are coming in on a weekly, and even daily basis, and they all involve an individual who has sole responsibility for the association's monthly accounting, cuts checks and then reconciles the checking account; and is altering checks after they are signed, issuing checks to themselves or family members, or otherwise juggling the books.

**7. Sorry folks - It is not legal to "borrow" from Reserves.**

The Department of Business and Professional Regulation has ruled that use of Reserve funds for unscheduled purposes is a change of the use of the funds, which requires approval of the association membership (a majority of those who vote at a duly-called membership meeting at which a quorum of members is present). Technically, you cannot take the money from Reserves if it is not for one of the categories for which the Reserves have been collected, even if you plan to pay it back before the end of the fiscal year, unless you get the membership approval. (This applies to condominiums and cooperatives, and for the statutory reserves in homeowner associations.)

Consider obtaining a professional reserve study or the required building inspection report for your association, on a periodic basis, so you have the opinion of an expert on which to rely when one of the owners challenges the board's numbers.

**8. Association credit cards are not a good idea.** I hear from CPA's in the industry that they have become a source of abuse and fraud involving personal purchases. If you want to have a credit card for the local home improvement store, adopt a policy to regulate the use of that card, including who has authorization to use it and under what circumstances. In the alternative, use petty cash.

**9. Never, never, never arrange for or agree to the issuance of an ATM bank card for and of the association's accounts.** (The latest story I heard involved an ATM card for the association's operating account and a machine at the local casino.)

**10. And, last but not least, in a condominium or a cooperative, you must deposit reserves with the same frequency as assessments are paid.** (Florida Administrative Code Rules 61B-22 and 61B-76) This means, if you collect assessments monthly, the reserve funds collected must be deposited within thirty days of the due date. If your assessments are collected quarterly, you still only have thirty days from the due date to make the deposit. You are not permitted to fund your reserves one time annually, or twice a year, or at the end of the quarter, etc.

Responsible minding of other people's money is a basic part of the definition of fiduciary duty. And mishandling other people's money is a fast road to legal disaster. When in doubt, consult with the association's attorney, and with a CPA who does community association work.

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COMMUNITY ASSOCIATION  
LEADERSHIP LOBBY

Participate in our CALL Survey on Community Association Financial Stability, Deadline - October 25th

If you have not done so already, please share your thoughts about the impact of mortgage foreclosures on units/homes on your community association.

Go to:

[http://www.surveymonkey.com/s.aspx?sm=DZD4ue0BIEVb\\_2fG0ZSlluMw\\_3d\\_3d](http://www.surveymonkey.com/s.aspx?sm=DZD4ue0BIEVb_2fG0ZSlluMw_3d_3d)

The deadline for responding is Sunday, October 25, at midnight. We need to show our elected officials that Association concerns deserve top priority in the 2010 legislative session.

# RECOVERING INSURANCE PROCEEDS FROM EMPLOYEE THEFT

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In a recent issue of the Community Update (Vol. IV, 2009), Gregory W. Marler, Esq., discussed techniques by which the Board can protect the associations' assets against fraud. This article will discuss the importance of insurance protection to cover losses from employee theft and how associations may successfully pursue a claim for reimbursement.

## INSURANCE PROTECTION

Fidelity bonding, sometimes called "employee dishonesty coverage," or "crime coverage," is a relatively inexpensive type of insurance designed to protect an association against theft or embezzlement by employees, directors, management personnel, or others who might have access to association funds.

In fact, Florida's Condominium Act requires every Condominium association to maintain insurance or fidelity bonding of persons who control or disburse the funds of the association, which includes, but is not limited to, those individuals authorized to sign checks on behalf of the association, and the president, secretary, and treasurer of the association. The statute also requires that the insurance policy or fidelity bond cover the maximum funds that will be in the custody of the association or its management agency at any one time. The association assumes the responsibility for the costs of the required insurance or fidelity bonding as a common expense of the association.

While general safeguards built into governing documents and the contracts with outside management companies, such as policies requiring two signatories on all association checks, help to provide an extra level of protection against employee theft, insurance protection is essential to ensure replacement of any losses.

## CLAIMS FOR REIMBURSEMENT

Becker & Poliakoff, P.A. ("B & P") recently was successful in recovering a \$50,000 policy limit plus attorney fees from a large insurance company (our settlement contained a confidentiality provision), who would not honor its insurance policy for employee theft with a firm's client. Like many associations, this one contracted with a management company to manage the condominium. An employee of the management company forged numerous checks, which were cashed at the association's bank without a co-signatory from the Board, in violation of the association's policies and procedures.

After approximately eight months, the Board finally realized

that the theft was occurring and made a claim for fraud to its bank. Although the bank made partial reimbursement, there was still a substantial loss to the Association, since the depository contract between the Association and the bank only provided for reimbursement if a claim was made within sixty days of the fraud.

A demand letter was sent to the insurance carrier for reimbursement pursuant to the "employee theft" provision of the policy, but, incredibly, the insurance company denied the claim, stating that the Association had "fraudulently misrepresented" its check cashing procedures in its policy application by not requiring two signatories. Of course, the check cashing procedures were not misrepresented in any way, because the employee of the management company fraudulently circumvented the second signature policy.

The insurance denial was clearly made in bad faith. Therefore, B & P filed a Declaratory Judgment Action, pursuant to Florida Statute §86.021, to recover the value of the policy, in addition to attorney's fees. Two weeks later, B & P also filed a Summary Judgment Motion, under Florida Rules of Civil Procedure 1.150, to have the judge declare, as a matter of law, that this was a covered loss. The purpose of the Summary Judgment Motion was to avoid expensive discovery and put additional pressure on the insurance company by forcing an immediate judicial decision on the merits of the case. Fortunately, within one month of filing the lawsuit, the insurance company capitulated and paid the full policy limits, as well as all of the attorney's fees.

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## Important Considerations:

Fidelity/Dishonesty Insurance Mandatory

Need Check/Balance System for Association Funds

Review Original Invoices

Review Bank Statements Every Month and Compare to Check Register

Review Insurance Denials When You Have a Claim

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## LESSONS LEARNED

The lesson here is simple, an association must first protect itself against losses from employee theft by purchasing necessary insurance. Second it should set forth policies for the handling of association funds, such as requiring two signatories. Finally, in the event of a loss, when the insurance company denies the claim, the Association needs to have its attorney go over the basis for the denial. Denial letters

often contain long recitals of the insurance policy language and multiple irrelevant grounds to deny a claim; such that insurance companies hope that they can either confuse the issue or wear down the insured to avoid paying on the claim. However, with prompt and aggressive legal action, the association could prevail in its efforts to get the denial rescinded and thus recover its losses.

# A FEW REMINDERS FOR COMMUNITY LEADERS

## Condominium Associations

### Staggered Terms:

Did the membership ratify two-year staggered terms? If not, all directors elected in 2009 only serve a term of one-year. If yes, the Firm recommends recording a Certificate evidencing the membership vote in the Public Records. That way there is formal notice of the ratification.

### Building Inspection Reports:

Required by §718.113(6), Florida Statutes. Has the membership voted to waive the required inspection? The inspection report is very useful for calculating appropriate reserve schedules and is helpful in connection with the year-end audit.

### Insurance:

Has your community requested evidence of insurance coverage from the owners? Has an insurance appraisal been performed within the last 36 months? Has your board considered whether or not to ask the owners to 'opt-out' of the Plaza East method of allocating responsibility for casualty repairs?

## Estoppel Certificates

Authority to charge a fee must be in a written resolution adopted by the board or set in a written management, bookkeeping or maintenance contract.

The amount of the charge must be included on the actual estoppel certificate.

## Homeowners' Associations

### Reserves:

Does your community include statutory reserves in its budget? Are you aware of the distinction between statutory and non-statutory reserves? Does the year-end financial report include the required disclosures?

### Litigation:

Considering filing a lawsuit where the amount in controversy exceeds \$100,000? Make sure you obtain the homeowners' approval in compliance with §720.303, Florida Statutes. Do your documents require a membership vote? If so, please consult with your attorney to determine how to proceed.

### Architectural Control:

Does your community have its guidelines in place? What about standards for maintenance and repairs?

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