# DON'T FEAR THE AUDITOR

Audit-Proof Your Property Management Business in **3 Easy Steps**

# Internal Audit Prep Work

Preparing your property management team for an annual audit isn't stressful when you know what to expect. Whether this is your first full-scale audit or you've been through the process a hundred times, understanding what your auditor is looking for will make the process smoother and more efficient.

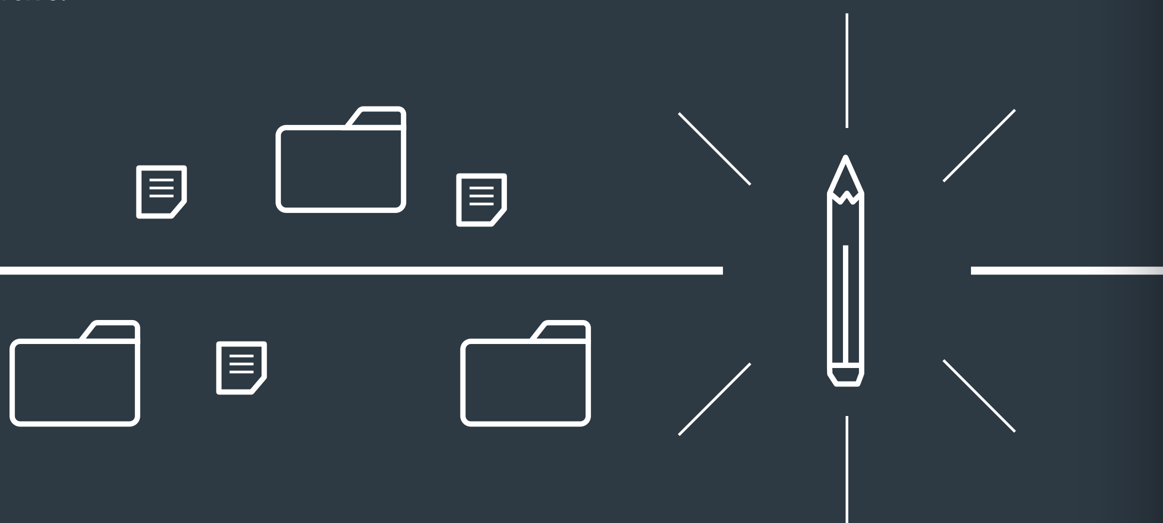
# Auditors Aren’t Enemies

It’s important to understand that auditors don’t come onto your property hoping to find problems; they’re looking for signs that your team follows generally accepted accounting principles and complies with local real estate regulations. During a comprehensive review, they’re also looking for signals that your property is in trouble.

> *Negative cash balances and irregular fee disbursement schedules may indicate process inefficiencies, failure to comply with regulations, or financial mismanagement.*

# Be Prepared

Developing an audit checklist before the auditor arrives will help your management team prepare for the review and spot potential problems. You'll find a downloadable reconcile worksheet in this book, as well as well as a list of the reports you need to prepare your property management company for an audit.



## *3 Essential Steps to Help You Get Started*

Review your financial reports.

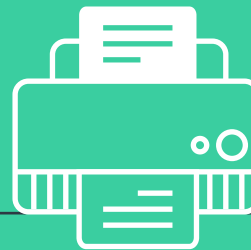
Invest time upfront.

Know your business.

# Step 1

*Review financial reports.*

Reports do more than just track income and expenditures. They convey a property's ability to meet contractual agreements and legal responsibilities. The data in various reports reveal the control systems and processes and identify impacting strengths and weaknesses.



## Come prepared.

Your auditor can give you a complete list of necessary items in advance. At the very least, before your auditor arrives, you'll need to print accounting reports for the audit period like the ones below:

- Trust Account Balance Report
- Trial Balance
- Delinquency Report
- Aged Receivable Detail
- Security Deposit Report
- General Ledger
- Bank Reconciliation

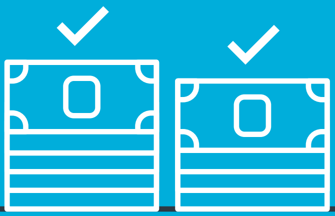
## *Step 2*

*Invest as much time as necessary to balance all accounts and familiarize yourself with individual reports.*

You probably already have a decent working knowledge of all financial reports and accounting policies related to your property management business, but it never hurts to understand them from an auditor's perspective.

Auditors look for seamless continuity. A quick look at the Trust Account Balance Report provides an example of how all financial activities are interconnected.

## Stay ahead of the game.



Properly managing trust account balances is a serious responsibility. Monthly reconciliations ensure funds are available to satisfy all obligations to owners and tenants. Along with funds for pre-paid rents, security deposits, and other reserves or undistributed income, the reports must also include non-refundable deposits accepted during the audit period.

## Auditors might request some of the following supporting documents for review:

**Bank Statements**

(including cancelled checks, deposit slips, and bank receipts)

**Receipts and Disbursement Journals**

(with supporting bills, invoices, and statements)

Disbursement Journal line items should include:

- Total deposit
- Deposit date
- Amount
- Party the funds are held for
- Trust account disbursement names, dates, and amounts

**Owners' Statements**

**Client Ledgers**

(owners' and tenants')

## The 3-Way Reconciliation Process

Your property management auditor will examine checks and balances throughout your accounting system to determine whether your accounting team is using generally accepted accounting processes and balancing your financial transactions each month. Trust account verification uses the 3-way reconciliation process to confirm accurate reporting and account maintenance. If you aren't using property management software that incorporates the 3-way process, here is a manual form you can use.

*This will also be available as a download at the end of this eBook.*

| | | | |
|---|---|---|---|
| Account Name | | Date | |

**Check Point #1:** Bank Reconciliation Report

| | |
|---|---|
| Statement Balance | $ |
| Plus: Deposits and Other Debits | $ |
| Less: Outstanding Checks and Other Credits | $ |
| Available Balance as of | $ |
| **Total** | $ |

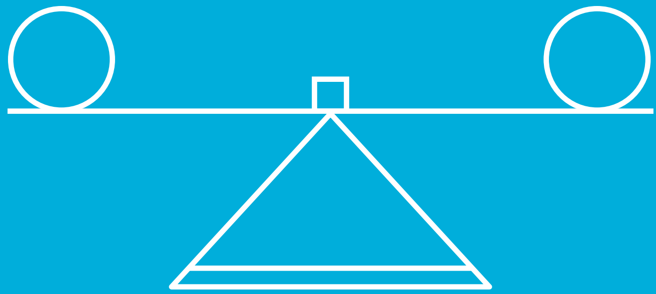
**Check Point #2:** Bank Account Activity Report

| | |
|---|---|
| Ending Bank Book Balance as of | $ |
| Plus: Undeposited Receipts | $ |
| Available Balance as of | $ |
| **Total** | $ |

**Check Point #3:** Bank Balance Detail

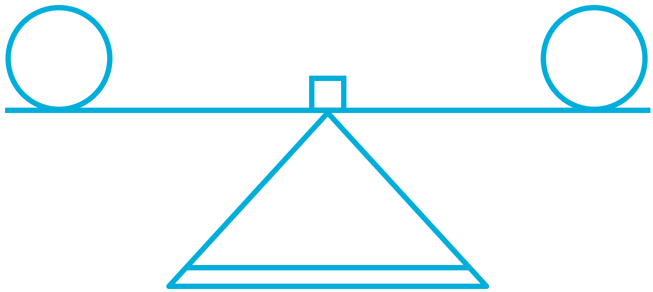
| | |
|---|---|
| Available Balance as of | $ |
| **Total** | $ |

*All 3 checkpoints must be reconciled on the same date and reflect identical totals.*

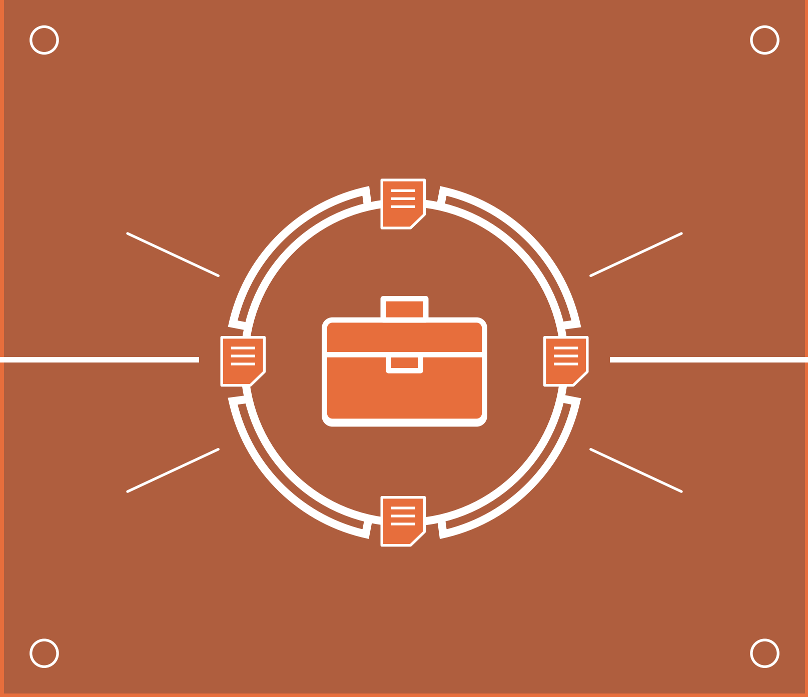


**Balance is extremely important.**

The Trust Account Report provides clues to discrepancies, and running a Trial Balance gives you an instant snapshot of your assets and liabilities. If your accounts don't balance, you know something is missing or incorrectly recorded.



*Bottom line: The worst time to notice you haven't balanced your checking accounts or updated your lease log in 3 months is after an audit has already started.*



## *Step 3* *Know your business.*

**Understand why something may look unusual to your auditor and know the proper documentation to make your case.**

Financial reports work collectively to give an accurate snapshot of your business. Discrepancies on one report usually signal problems in other areas. For example, the aged delinquency report might signal potential tenant screening or rental collection process problems. Reviewing the delinquency report often gives managers opportunities to review policies.

Every property is different, and sometimes what looks suspicious on the surface, is not as bad as it seems at first glance.

**Learn what the delinquency report says about your property.**

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Oftentimes, the delinquency report is accurate, but extenuating circumstances can contribute to a high ratio of past-due accounts. If your property employs a part-time book keeper who only posts receipts once or twice a month, your report could inaccurately show accounts that appear to be past due. With a manual bookkeeping system, making daily deposits won't automatically update A/R accounts, and your numbers may be skewed.

**Non-accounting factors also can influence the delinquency report.**

Some such incidents include:

- Failure to communicate effectively with tenants
- Unresponsive service technicians
- Outdated credit verification policies



Understanding the nuances of your property will help you explain any unusual or suspicious data to your auditor. Just make certain you have the necessary documentation to support your claims.

# Rest Assured

Review your financial reports throughout the year, and you'll always be prepared for an audit.

If you still feel nervous about an upcoming audit, contact your auditing agency to request more information about how to prepare for the process.

**If you're interested in learning more about some of the important topics mentioned in this eBook, check out these additional complimentary resources:**

Boost Your Business into the 21st Century

Guide to Choosing Property Management Software

The 3-Way Reconciliation Process