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Shining the Light on Fraud

Everyone makes mistakes, even property managers. And finding and correcting data entry—or worse, accounting errors made by you or those employed in your property management office can be troublesome; though not nearly as troublesome as discovering fraudulent activity within your ranks.

EMPLOYEE SCREENING

Louie Curry, owner of The Curry Companies in Dublin, Georgia, has encountered a few fraudulent episodes during his 30-plus years in the real estate and property management industries—from managers promising new appliances to tenants in return for sexual favors to bookkeepers pocketing rent payments with bogus receipt books.

“The number one thing is to hire the right people to start with. Check them out. Check with all their former employers,” says Curry, who has eight employees helping manage more than 1,500 properties in southern Georgia. “The second thing is to hold them accountable for what they’re responsible for. You have to verify on a regular basis that they are doing what they’re supposed to be doing. By spot-checking, if you see a red flag, you can jump on it right away.”

The best way to do that, Curry said, is to ask questions if something looks out of the ordinary.

TRANSACTION TRACKING

More property management companies are adopting strict no-cash policies as theft and fraud deterrents. But manipulation of data and/or falsification of entries can still occur without proper oversight.

What every property manager needs most in their accounting system is accountability. A powerful function to utilize is logging of all changes to properties, units, leases, owners and transactions including the date, time, and user ID. This audit feature allows you to trace any suspect transactions and is most effective if you insist that your people always use their own login credentials. If personnel use the same user ID, you will be unable to determine who is responsible for a specific transaction.

Curry, who relies on his CPA firm’s nearly daily reviews of the books, is looking to add an auditing

application as yet another “backstop.” Being able to track changes, including who made them and when they were made, is imperative to detecting—and ultimately preventing—fraudulent activity.

Property manager-turned software trainer Shelly West of Winder, Georgia, has a unique perspective on the importance of transaction tracking. “As a software vendor, we’re sometimes asked to delete transactions. Though we technically can do it, we never want to delete the record. Instead, we recommend reversing transactions so there’s still a paper trail,” said West. “We never want to turn the lights out. We always make sure everything is traceable.”

West also believes owners of management companies should consider being trained in the same accounting and management software applications their employees use. “Knowing what your employees are doing, and having them know that you know what they’re doing, is the best fraud deterrent I can think of,” she said.

At a recent classroom training session, one company owner commented that he felt empowered by the knowledge of what his software can do. Even though he may not use it daily, he now knows what reports and other capabilities are available and can request them specifically. This greater level of engagement puts all of the company’s employees on notice.

COLLECTIONS—CHECKS & BALANCES

One of the more exploited techniques for committing fraud is collecting rent and fees from a tenant and not depositing it in the operating account. A deceitful employee will take this tax free income and use it for personal purposes.

The best practice is to send all overdue accounts to an independent collection agency after a set aging period (30 to 45 days). An employee is much less likely to pocket a payment if he knows an independent collection agent will be following up. Monitor recalls (requests to stop the collection process on a specific account) closely since this is one way a fraudulent employee can counteract this method. Another dishonest practice is to place the overdue accounts in the “collections drawer” but not actually forward the

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accounts to the collection agency. You can thwart this practice with an automated referral process within your software or by manually comparing overdue accounts with the collection agency's active accounts report.

TENANT SCREENING

Just as using a collections agency for past-due rentals is fiscally smart for most property management companies, so is using a third-party screening company to pre-screen all applicants.

"There are a number of third-party companies out there who will do the work for you," said West. "Typically they'll rate the tenants for you, and some even guarantee a percentage of the rent." In most cases, West said the application fee charged by the property management company can more than cover the expense of the screening process.

After getting stuck with a few tenants who were discovered on the national sex offender registry, The Curry Companies began ordering background checks in addition to credit checks on all applicants.

"These days, a background check is just as important as a credit check for new tenants," said Curry. "You don't want to move someone in and then have the sheriff show up to move them out because it turns out they're registered as a sex offender."

AN AUDITOR'S PERSPECTIVE

Pamela Vesper, J.D., C.R.E.I., an auditor/investigator with the N.C. Real Estate Commission, says there are some basic things company owners or brokers in charge can do to deter (and discover) fraud.

The first is to conduct background checks on all employees—even if you've known them for years—and bond any employees who handle the books. Second, conduct monthly reconciliations of the books.


"Most of the embezzlements we see are done by bookkeepers who have no one watching over them," said Vesper. "If some of the brokers had just been more proactive checking the mail and answering the phones, they could have avoided losing a lot of money."

According to Vesper, here are the top 10 signs fraud may be occurring:

1. Excessive Non-sufficient Funds (NSF) and voided checks. "If a bookkeeper is voiding a lot of checks, it may be a sign he/she is stealing from the company."
2. Calls from property owners complaining about late rent payments. "Many times, the bookkeeper has stolen one month's rent and is waiting until the next month to catch back up."
3. Lifestyle changes of employees. "If they are suddenly driving a Lexus and make \$22,000 a year, that's a little suspicious."
4. Employees who never take vacation. "A lot of embezzlements are discovered only when someone is forced to take a vacation."
5. Excessive transfers from one account to another. "I see a lot of security deposit accounts get drained, usually by employees who rationalize it as borrowing."
6. Unusual interest in the mail and/or telephones. "An employee who is so glued to her desk and won't let anyone else answer the phone or get the mail is usually a sign of an employee trying to hide something."
7. Checks for large, round figures. "I've seen some remarkable forgeries over the years. What usually gives them away is the amount of the check."
8. Checks to unknown payees or to employees. (Only paying vendors on an "Approved Vendor List" will help deter bogus businesses from being created by rouge employees, Vesper said).
9. Checks mailed to post office boxes. (Legitimate vendors usually have a physical mailing address).
10. Missing bank statements or cancelled checks. "These must be kept for three years and you should know where yours are. If one is missing, call your bank immediately and request a copy."

In general, Vesper says owners, brokers and managers should follow the old "trust but verify" adage. "Unfortunately it's always the people you trust the most who are going to steal from you. Even if you've known 'Jane' for 20 years and she's your best friend, don't give her carte blanche over your books."

CLOSING THOUGHTS

The advent of computers has helped shine a lot of light on some of the more "shady" business practices of old. And accounting and management software have further illuminated best practices. Consider these simple steps that every property management company can take to ensure fraud is detected as early as possible, if not deterred altogether. 

What every property manager needs most in their accounting system is accountability. A powerful function to utilize is logging of all changes to properties, units, leases, owners and transactions including the date, time, and user ID. This audit feature allows you to trace any suspect transactions and is most effective if you insist that your people always use their own login credentials.