Financial Control Risk Guide

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What is Financial Control Risk?

Financial control risk covers a wide range of financial disciplines and processes that collectively aim to ensure that the Community Scheme follows good practices in the critical area of financial discipline.

This risk arises from a lack of or a breakdown in financial controls and processes e.g. budgetary and expenditure controls, and segregation of duties. It can emanate from HR/People, weak operational controls, poor debit/credit extension and collection, and crime/fraud risks.

The management of financial control risk will ensure that the Community Scheme is better equipped to manage its finances and financial processes ensuring financial stability and sustainability. This will also improve the Community Scheme's reputation as a counterparty for credit and service provision.

Most risks ultimately culminate in financial loss. These can stem from several risk events that could impact a Community Scheme e.g. natural disasters, legal claims, bad debts from levy defaulters, fraud events, uncontrolled/unauthorised expenditure, insurance excess, essential unexpected maintenance/repairs. There is a connectedness between all risks with impacts culminating in an impact on the financial position of the Community Scheme.

Financial control risk covers a wide range of financial disciplines and processes that collectively aim to ensure that the Community Scheme follows good practices in the critical area of financial discipline. Several areas and factors can impact the financial performance of a Community Scheme. These all must be subject to financial control and specific risk management to ensure that the Community Scheme remains financially viable. It will force Office bearers to consider all financial control areas, even those they may not consider as essential or, ultimately, their responsibility. It will also identify the areas that most expose the Community Scheme to loss. A lack of financial controls is probably the most common reason for a Community Scheme to fail.

Several key characteristics dictate the level of financial control required in a Community Scheme to manage financial control risk. These are:

- Number of units.
- Level of monthly levy collections.

- Level of expenditure.
- Value of assets.
- Nature of assets.
- The complexity of the Community Scheme.
- Cash flow – level and volatility.
- Use of banking and financial systems e.g. integrated accounting and payment system.
- Number of bank accounts conducted.
- Financial systems and processes in place - budgeting, monitoring of financial performance, debtor control, reconciliations, segregation/separation of duties, and daily monitoring of bank accounts.
- Level of procurement, number of service providers, and contracts in place.
- Transactions and payments - size, complexity, number.
- State of debtors/levy book – size of debtors, age, number, arrears.
- Number of abandoned units/properties/members interests.
- Use of recognised supporting accounting systems.
- Quality of financial accounts – audited/not audited.
- Level and accuracy of financial reporting.
- Level of financial skills of Office bearers.
- Availability of Office bearers.
- Level of inherent maturity, financial discipline, and personal accountability in the Community Scheme.
- Presence of Managing Agents/Accountants/Third parties providing accounting support.
- Experience and governance processes in Managing Agents.
- Debtor collections – strict processes, billing, collection, level of arrears levies/utility payments, follow-up, legal action.
- Level and extent of delegated authority and the limits of authority.
- Level of debt or borrowings

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- Municipal arrears – amounts outstanding in respect of rates/taxes/utility services.
- Level of financial oversight day-to-day control over the financial affairs of the business or organisation.
- Level of the vulnerability of the Community Scheme to financial upsets, e.g. service provider or supplier failures, reduced economic activity, concentration risk to one debtor, if short-term borrowing facilities or credit were withdrawn, an unexpected tax claim, losses due to the criminal actions of staff or third parties.
- HR/People – skills and expertise levels required, demands on people, skills/resource availability, quality/calibre of employees.
- Regulatory, compliance, and reporting requirements.
- Susceptibility to socio-economic events.
- Level of fraud, theft, criminality.
- Insurance held – fidelity, commercial - buildings/fire/theft, indemnity, cybercrime, riot cover.

Culture

You need to have the following cultural elements in place in the Community Scheme:

- A culture that places a high priority on day-to-day hands-on financial controls and disciplines.
- A culture of fraud awareness and fraud controls.
- A culture of financial risk management that focuses on managing potential financial loss.
- A culture that accepts and embraces accountability, adherence to controls, and disciplines.
- A culture of budgetary and expenditure controls.

The management of financial control risk will ensure that the Community Scheme is better equipped to manage its finances and financial processes ensuring financial stability and sustainability. This will also improve its position as a counterparty for credit extension if need be.

The key elements of financial control that a Community Scheme needs to focus on are financial discipline, financial oversight, budgeting, financial management information, debtor control, cash flow, asset controls, banking and payment controls, IT/Technology controls, disaster recovery/continuity, supplier, and procurement controls, contracting, people/employees, payroll and fraud/crime/criminality.

Financial Discipline

The Help Our Scheme Financial Control assessment will have helped identify critical potential risks and areas of weakness in the financial controls by providing high-level feedback on financial discipline.

Mismanagement and poor governance of a Community Scheme present the biggest risk to their financial stability and survival.

At the heart of financial governance is the need to have robust controls, disciplines, processes, and procedures in all key areas, e.g. HR/People, Operations, Finance, and Administration.

Financial systems need to embrace technology with the highest levels of security and password controls possible. System access and data records need to have integrity, be transparent, be auditable, and provide openness and accountability. It would be best if you eliminated manual processes wherever possible to lower the risk of fraud.

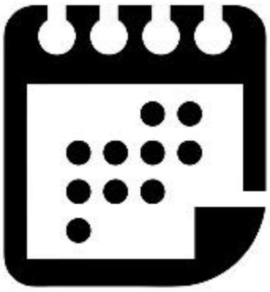
One of the biggest financial risk areas is unauthorised payments and the disappearance or embezzlement of Community Schemes funds. This comes about in many ways, but largely due to no segregation of duties, non-adherence to controls and processes, or shortcutting/ bypassing of controls due to a lack of involvement or availability of Office Bearers. Expenditure not budgeted for, unauthorised expenditure, procurement where no other quotes are obtained, unvalidated expenditure against invoices, or collusion with suppliers or contractors to "extract money" from the Community Scheme are further particular areas of fraud.

Community Schemes with a dominant personality or where reliance is placed on a single Office Bearer for procurement/payment approval are highly vulnerable to fraud. Managing Agents who themselves don't have robust processes around taking payment instructions from Office bearers, act on verbal instructions, or don't have robust due diligence processes around validation of beneficiary bank account numbers add to this risk. These controls need to extend to whether value for money was provided by suppliers or service providers, whether the Community Scheme's expenditure was approved and budgeted for, and whether alternative quotes were obtained. All payment and approval instructions should be independently verified and approved by more than one Office Bearer of the Community Scheme.

All Community Schemes need to have robust controls in place for procurement and payment process controls. These include segregation of approvals, obtaining three quotations, budget approval, robust processes around beneficiary validation, processes around "value" received, and dual release in place for all payments.

General access controls such as biometrics and facial recognition should be used to eliminate theft and criminality within the Communal property wherever possible.

It is important to remember that the Office bearers must maintain adequate accounting records and are responsible for the content and integrity of the annual financial statements and related financial information included in their report.



It is the responsibility of Office bearers to ensure that the annual financial statements fairly present the state of affairs of the Community Scheme at the end of the financial year and the results of its operations and cash flows for the period. The Office Bearers are required to acknowledge that they are ultimately responsible for the system of internal financial control and are required to place considerable importance on maintaining a strong control environment. The Office bearer’s responsibilities are to meet these requirements and set standards for internal control to reduce the risk of error or loss cost-effectively. The standards include the proper delegation of duties within a clearly defined framework, effective accounting procedures, and adequate segregation of duties to ensure an acceptable risk level.

Office bearers have a fiduciary obligation to their owners and employees. A fiduciary duty is a legal obligation of one party to act in the best interest of another. The obligated party is typically a fiduciary, someone entrusted with the care of money or property. Also called a fiduciary obligation.

Fiduciary duties are imposed upon a person or an organisation that exercises some discretionary power in the interests of another person in circumstances that give rise to a relationship of trust and confidence.

Office bearers have fiduciary responsibilities in respect of the Community Schemes they serve, irrespective of their roles being voluntary.

(Section 40(2) of the STA stipulates that the "fiduciary relationship" implies that a trustee shall in relation to the Body Corporate:

i) Act honestly and in good faith (which holds that he shall exercise his powers to manage the affairs of the Body Corporate in the interest and for the benefit of the Body Corporate and shall not act without, or exceed, his powers).

ii) Avoid any material conflict between his own interests and those of the Body Corporate).

These controls should be monitored throughout the Community Scheme. All employees and office bearers should be required to maintain the highest ethical standards in ensuring that operations are conducted in a manner that is above reproach in all reasonable circumstances. Risk management focuses on identifying, assessing, managing, and monitoring all known forms of risk across the Community Scheme. While operating risk cannot be fully eliminated, the Community Scheme must endeavour to minimise it by ensuring that appropriate infrastructure, controls, systems, and ethical behaviour are applied and managed within predetermined procedures and constraints. An operating business or organisation's annual financial statements are typically prepared on the going concern basis (not as a gone concern).

Poor governance and financial controls, including a lack of budgetary management and purchasing/ expenditure disciplines, will contribute significantly to financial risk.

Oversight

Several basic core controls need to be in place to ensure financial control.

Some of the key ones are:

- You need to have clearly defined limits and delegations of authority in place.
- You need to have a specific focus on cash flow, liquidity, and solvency.
- You need to have a specific focus on key expenses and core revenue.
- You need to consistently focus on controllable and manageable costs to achieve the required surplus and enable the accumulation of reserves.

Many financial, administrative control routines should be entrenched in a Community Scheme. These include reconciliations, segregation/separation of duties, audit trails, banking and payment system controls, cash controls, payroll, expenditure, liability, and asset controls.

Specific areas of oversight are:

- Bank Accounts

- You should only deal with credible financial institutions and financial intermediaries whose registrations and ratings have been verified and checked with the appropriate authorities.

- Banking and Accounting Systems

- You need to ensure that there is clear separation/segregation of duties in the key financial areas of your Community Scheme. A clear separation of duties and responsibilities is necessary (e.g. the person loading and authorising the addition of beneficiaries, payments, or payroll cannot release the payments/payroll, or the person preparing the financials/management accounts cannot audit/sign them off or the person doing the reconciliations cannot also sign them off).

- That appropriate access levels and password controls are in place around the use of all accounting, financial, banking, and payment systems.

- Delegation of authority

– You need to ensure that there are clearly defined limits and delegations of authority in place and controls around who can sign contracts or agreements, commit, and bind the Community Scheme, and/or place procurement orders contracts with suppliers. This applies to Office bearers.

- Cash Flow

- you need to have a specific focus on cash flow, liquidity, and solvency. Cash flow forecasting and cash management are critical financial tools. It is important that your Community Scheme is cash flow positive, has the required funding in place where required, is liquid and capable of meeting all its obligations as and when they fall due. The Community Scheme needs to be always solvent and be a going concern.

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- Expenditure

- You need to have a specific focus on costs.

- You need to ensure that all expenditure is budgeted for.

- You need to ensure the accuracy and integrity of your numbers and that they are current.

- You need to consistently focus on controllable and manageable costs to optimise cash savings.

- You need to have strong procurement and purchasing policies and processes.

- You need to have a specific focus on utility charges/consumption and the accuracy of rates/taxes/ utility/energy/power accounts.

- You need to manage ad-hoc essential or emergency expenditures.

- You need to ensure that value for money was received for all expenditures.

- You need to ensure that any expenditure out of reserves meets regulatory requirements and is approved by the resolution of the Office bearers at the AGM.

- Expenditure budgeted in the 10-year maintenance, repair, and replacement plan (“MR&R plan”) must align with the actual expenditure undertaken and the level of specific statutory reserves held for this purpose.

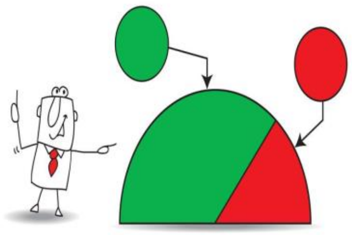
- Revenue

- You need to be acutely aware of the potential loss of revenue/levies or other income under threat due to the prevailing socio-economic situation. A lack of business continuity/ disaster planning cancelled contracts/ agreements or tenders, bad debts, a reputational incident, and/or legal claims.

- Debtors

- You need to have tight control of debtors and overdue amounts due to the Community Scheme.

- Liabilities



- You need to manage the level of liabilities in line with cash flow/cash resources.

- No liabilities should be entered into that might compromise the Community Scheme.

- No contracts or arrangements should be entered, resulting in a contingent liability or unquantifiable obligation of the Community Scheme.

- Business continuity

- You need to have comprehensive business continuity plans in place.

- You need to identify alternate suppliers of key services to the Community Scheme.

- You need to ensure that you are not reliant on a single supplier of services critical to your Community Scheme, whose failure could materially impact its operations.

- Operational

- You need to have a strong focus on the financial impact of general operational activity within the Community Scheme (e.g. efficiency, productivity, stoppages, delays, rescheduling, reworks, etc.) and on the ongoing delivery of quality services to owners/tenants/lessees/residents/visitors.

- Tight controls around the responsibility for the maintenance of owner properties e.g. reporting of problems, assessment, appointment of contractors, account responsibility i.e. Community Scheme or owner, recourse to insurance.

- You need to ensure general risk awareness to aspects that could result in potential financial loss; safety and security, risk of natural disasters such as fire/floods/rockfalls/tide surges or rising sea levels, lack of infrastructure maintenance, water, and power availability, waste disposal, environmental compliance and challenges of climate change or extreme weather.

- The consumption of utility services namely water and electricity need to be closely monitored and managed (especially for leaks/unnecessary usage).

- You need to have the appropriate insurance in place to cover key risks arising from a natural disaster, accidents, damage to property, theft/fraud/robbery, legal liability, Officer bearer's indemnification, and cybercrime.

- Regulatory, Legal, and Compliance

- You need to ensure compliance with the specific regulations applicable to the Community Scheme and general regulations around labour laws, company registration, health and safety, environmental laws, taxation, basic conditions of employment, disaster management and municipal legislation.

- You need to ensure compliance with the house and conduct rules of the Community Scheme.

- You need to have a tight focus on all the contractual obligations and agreements of the Community Scheme.

Budgeting, Monitoring, and Performance

You need to have a culture of budgetary discipline and control in your Community Scheme. This needs to extend from detailed preparation of budgets, justification of spend/expenditure, authorisation of expenditure, appropriateness of the expenditure, prioritisation of the expenditure, and expenditure monitoring. It is also important to remember that the cash flow realities and profitability of the Community Scheme transcend expenditure budgets that may have been approved.

You need to have a clear understanding of the revenue and expense dynamics of the Community Scheme. This requires identifying the major revenue drivers, e.g. levies and the major expenditure items, which costs are fixed and variable. Costs and expenses are controllable or uncontrollable and any relationship between the various expenses.

The objective of a Community Scheme should be to achieve a balanced budget. This requires not just the expenses being covered by core revenue but includes the accumulation of reserves. Special levies should only cover specific essential expenditures and capital improvements or build specific reserves. They should not be used to balance budgets or meet core expenditures. At the same time, levy increases need to be realistic and affordable. Historically low or unrealistic levies are always a problem once a Community Scheme is faced with realistic operating costs and the need to build up statutory reserves.

The timing of expenditure and budget timelines are also critical components of budgetary control. A zero-based budget approach should be adopted where all amounts are justified and set in isolation irrespective of past expenditure or utilisation. Carrying unspent amounts over to the next year just for the sake of it should be avoided unless they are specially earmarked for specific projects or delayed spending. Delaying or deferring expenditure becomes a critical part of budgetary management.

A specific critical area requiring monitoring and discipline relates to the Community Scheme's standing with the local Municipality/Authority/Energy/Power providers regarding rates/taxes and utility services (power/water/refuse/sewerage) and the state of the accounts. It is important that these accounts are strictly monitored and managed and that these accounts are kept up to date to ensure that services to the Community Scheme aren't disconnected and that disputes are nipped in the bud. The levels of consumption need monitoring from a trend/usage point of view to enable early detection of any leaks or abuse and/or wastage of water/power. To ensure that the cash flow situation of the Community Scheme is not adversely impacted, it is important that recoveries for utilities not directly billed/pre-paid e.g. electricity, by owners/tenants, are recovered from owners/tenants in advance of the payment to the Municipal/Local authority/energy/power providers.

An area of friction is where individual owners are in good standing with the Community Scheme/Body Corporate, but where the Scheme has not paid over monies to the Local /Municipal authorities or energy/power service providers. This is tantamount to fraud, and these arrears can rapidly accelerate resulting in service disruption. The costs and time involved in sorting these issues out and paying for re-connection can be considerable.

Adverse trends and negative variances in expenditure need to be looked at critically. More importantly, the likely projected run rates of both revenue and expenditure need to be assessed in light of the actual expense and revenue realities experienced in the Community Scheme. In some instances, the variances are temporary, and the run rate will correct itself in line with the set budget. In some other cases, these might be permanent and will have to be factored into budgets.

Unforeseen or emergency essential expenses which were not budgeted for will similarly have to be factored into budgets. In some cases, cutbacks in other expenditures will be essential to compensate for these and negative permanent variances to ensure budget balance.

Examples of these can be tougher socio-economic conditions resulting in lower levy collections; bad debts, costs associated with abandoned properties, pest control, personal hygiene materials (Covid controls), higher utility charges, higher fuel costs, generator running costs, higher negotiated salaries and wages, higher rates and taxes charges or increases in equipment/technology costs due to a significant fall in the exchange rate. These can often become a permanent feature of the Community Scheme and will need to be countered and managed.

General Budgetary, Procurement and Expenditure Disciplines

- Create an annual zero-based budget with projected income and expenses by:
  - Promoting involvement and responsibility for revenue/expenditure with the relevant individuals, e.g. Office bearers.
  - Ensuring that accurate costings and budgets are drawn up.
  - ensuring that expenditure aligns with realistic cash flow projections.
  - That utility charges align with projected usage and consumption and are based on the projected/latest Municipal/Local/ Power charge increases.
- Once the budget is approved/adopted and in place, continually:
  - Ensure that all expenditure is approved in line with delegated authority.
  - Ensure expenses were included in the budget before approving purchases or spend.
  - Calculate year-to-date figures to identify overspending and/or insufficient income generation.
  - Capture budget variances and subject these to specific scrutiny.

- Adjust the budget periodically in line with actuals or to curb or re-direct expenditure.
- Keep track of the movement of funds, especially large amounts of expenditure and receipts.
- Get written motivations for all non-budgeted expenses.
- Insist on three quotations for ancillary spend.
- Ensure that all suppliers or service providers utilised have been approved in line with laid down supplier evaluation and procurement qualification criteria.
- Insist on obtaining three quotes placing orders.
- Ensure compliance with any preferential procurement policies and requirements where applicable.
- Ensure that governance measures, budget controls and procurement policies are not flouted, influenced, or circumvented entirely to facilitate the overpayment for products and services from pre-selected parties.
- Ensure that regular transactions are diarised so that payment terms are adhered to, discounts optimised and that appropriate funding and/or cash flow is in place.

- ensure that unnecessary interest charges aren't incurred, and that funds use is optimised.
- ensure that cash/funding are available before large, known expenses or payments occur.
- Be relentless on cost controls and efficiencies, prioritise spending and don't overspend on anything.
- Continually monitor expenditure and optimise, change, and rectify where necessary.
- Regularly review both actual revenue and expenses against budgets and take early corrective action where appropriate, in respect of negative variances and excessive expenditure trends.
- Eliminate budget mismanagement, expense/cost over-runs, unexpected costs, maverick spend, negative variances and unbudgeted expenditure approvals.

- Where necessary exercise cut-backs, budget cuts, expanse freezes where needed.

- Review the cash flow projections at least monthly.

- Track from both a year to date and from month-to-month comparative perspective, the level of debtors and current liabilities (creditors) – an ever- increasing rise in the level of debtors is a key trigger that things are going wrong, and that cash needed to pay creditors/meet expenses or being used to build up reserves, is diminishing.

- Include all capital expenditure in the budget and ensure that funds/funding is available to meet these:
    - Ensure necessary AGM and Office bearers' approvals are held and that procurement requirements have been met.
    - Explore optimum financing options – possible cash versus loan finance, e.g. rental, hire purchase, lease.
    - Follow the agreed repayment/finance plan.
    - Make provision for possible situations where this cannot be met.
    - Follow due procurement process by ensuring that the party formalising/authorising the expenditure had the necessary powers, that strict repayment terms are agreed and that the documentation and contracts supporting the transaction/s are in place/held.
    - Ensure that any obligations or commitments entered into do not trigger contingent liabilities on behalf of the Community Scheme.

General Budgetary Controls:

Revenue

- Revenue budgets from levies and other resources need to be realistically set in line with achieving a balanced budget but taking cognisance of inflation, socio-economic realities, likely use of facilities and affordability.
- Levy collections need to be closely monitored to ensure timeous receipt from a cash flow timing

point of view and ensure early identification of defaulters and potential bad debts.

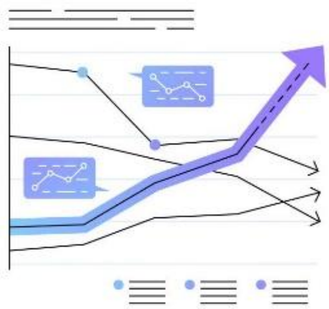
- The collection/recovery of utility charges from owners/tenants where the Community Scheme is liable for payment to the local authorities/municipalities/service providers.
- Many other elements can influence the overall profitability/surplus of a Community Scheme. These can comprise proceeds and profits from the sale of assets, sundry income and revenue, interest/dividend income, accounting adjustments, write-offs and abnormal expenditure, which can have a major influence on whether a surplus or loss is made. However, it remains critical that a Community Scheme is financially viable from its core areas of operation and activities. Where a Community Scheme starts relying on ad-hoc, ancillary income and/or profits from other non-core business operations/use of facilities or once off activities to be "profitable", it is unlikely that the Scheme is viable or that it will be sustainable, at the current level of core levies.
- The Community Scheme needs to understand what its income/revenue break-even levels are/need to be, i.e. the level of levies and other income required to cover fixed costs and the applicable variable costs. These are critical measures if the Community Scheme is looking to undertake additional expenditure and, in particular, capital intensive infrastructural expenditure.
- Building up the required reserves needs a specific focus.
- Material deviations in revenue collections and cash flow need to be countered by immediate cut-backs in expenditure.

Expenditure

- All expenditure should align with the overall strategic objectives of the Community Scheme.
- Expenditure should be justified and supported with clear supporting documentation and quotations. Most expenditure should be zero-based with selected non-discretionary spend based on previous year's levels, rates and taxes, utility charges.
- All budget expenditure is subject to the availability of cash resources or funding. The timing of expenditure needs to coincide with the funding or cash receipts. Therefore, it is no use budgeting for specific

expenditure, including capital expenditure, if the cash resources or funding for this is uncertain, not known or not in place.

- All expenses should be signed off and approved for payment by at least two parties/segregation of duties.
- Run rates of expenditures and revenue must align with one another.
- It is important to ensure that expenditure is going where it is required and intended.
- Expenses in the Community Scheme need to be kept under control, tightly managed against budgets and in line with cash generation.
- Expense growth should be kept below the inflation rate.
- Expense growth needs to be tightly managed, and a Community Scheme needs to ensure that all expenditure is budgeted for and approved before committing.
- A cushion for unexpected costs/expenditure needs to be built into levies to ensure that a surplus is achieved.
- Budgeting and detailed monitoring of performance to budgets is a critical part of financial control. In this way, problems and potential financial risks are identified quickly, and remedial action can be taken almost immediately. In some instances, budget variances may not be permanent and can result from timing differences. In all cases, material variances need to be explained, dealt with, and resolved.
- Trends in expenditure need to be tracked closely. If particular areas are consistently exceeding budgets, they need to be investigated. These can be an indicator of mismanagement, maverick spending, operational inefficiency, and even fraud. Similarly, declining trends in revenue need a high level of focus.



- You need to develop a comprehensive understanding of the relationship between expenses to each other and how they are impacted as levies grow/increase. This includes all operating and overhead costs.
- The Community Scheme needs to clearly understand the nature of its expenses, which expenses are largely fixed, and which are variable, which expenses are controllable, and which expenses are beyond their control/uncontrollable.

- It is also very important to know at what stage or level of operations, fixed costs will increase or need to grow, e.g. rates/taxes, utility charges, additional employees, security costs, back-up power/diesel/petrol costs.
- One of the major benefits for categorising expenditure is to assist in monitoring and managing expenses expenditures against budgets and enabling and ensuring accountability for managing expenses by functional area, e.g. operations, maintenance/repairs, gardens, administrative and security. Use of on-line management portals for incident and general reporting/permissions/complaints/requests etc. has become common to ensure that all parties follow a disciplined process around these issues. Not only do these tools provide clear tracking of issues/requests/complaints and incidents, but there is a full audit trail, records of costs/expenses, and clear accountability for approval and handling of each issue.
- Discretionary spending is a particular area where budgets and expenditure need tight management. Specific examples of this are garden/clubhouse improvements. Any wasteful expenditure must be prevented at all costs. A growing cost to most Schemes is in security related technology (cameras/sensors), cell phone and associated data, and bandwidth expenses e.g. airtime, fibre, hosting services, and cloud storage, which require tight management.

- Ignoring individual expenditure variances merely because "overall' budgets balance or compensate for one another is a recipe for problems from now on.
- Re-allocation of budgets is a practical reality for most Schemes. This comes about from the under-utilisation of budgets and/or from budgeted items or expenditure that is no longer going ahead, discontinued activities/projects and/or specific budget cut-backs. Disciplines around this, however, still need to be maintained. If budgets are re-allocated to cover unbudgeted expenditure or variances in other areas, this can be a negative practice and a bad habit. Again, if cash resources can be saved, resist the cross-subsidisation of areas where expenditure exceeds budgets.
- Extraordinary and/or abnormal items are by their very nature unexpected or unplanned. It is not easy to budget for these, but they can be a reality for some Schemes. It is recommended that a Scheme

budget an amount of 5% of total budgeted expenditure for sundry unexpected expenditure. Examples of these can be extensive litigation and legal fees, pest control measures, Covid control expenses, generator running costs, abandoned property costs, unexpected claims, or uninsured losses. Appropriate insurance for some unexpected losses or expenditure might be a way of mitigating these types of expenses, but of course this comes at a cost.

- Salaries/wages and bonus payments are very sensitive are of expense management and budgeting. Once employees believe that salary increases and bonuses have been budgeted for, these become a right, irrespective of underlying performance, profitability, prevailing economic conditions, and the cash flow position of the Scheme. Given the uncertainty of a Schemes financial situation, undertakings, and specific commitments around these mustn't be given unless they can be delivered upon with certainty.

- Other expenditures linked to annual increases such as electricity and rate tariffs, insurance premiums etc., need to be factored into budgets.
- Expenditure or costs subject to interest rate and/or exchange rate movements need a specific focus. Here conservative rates need to be factored into calculations and budgets based on well informed socio-economic input. Similarly, fuel, diesel, gas and transport costs need to be based on conservative assumptions of crude oil prices and prevailing exchange rates.
- Where a Scheme may avail of borrowings or debt, increases and possible variances in interest rates need to be factored into budgets. Where additional debts are envisaged, this needs to be factored in as well.

- Taxation has a cash flow implication and must be budgeted for in line with prevailing taxation rates and the likely amount subject to tax, e.g. interest income received or sundry income.

Assets

- Assets need to be depreciated and should be provided for at conservative rates. Whilst not having a cash flow implication, depreciation must be included in budgets.
- Bad debts are a specific expense that can have a material impact on profitability and the cash flow of the Community Scheme. These can’t be planned for and are normally unexpected. As such, it is prudent to budget for a level of bad debts against debtors.
- Asset valuations need to reflect the market and realisable value on an on-going basis. This applies to the writing down and revaluation of movable and other fixed assets. This can take the form of an actual write down against profits or the on-going depreciation of assets over their useful life.

- Fixed and movable assets need to be secured, protected, maintained, and insured.
- A specific area of management is abandoned units, properties, or members interest in Community Schemes. Until these assets can be sold, realised, or disposed of to defray costs and arrears, they become the Community Scheme, directors, and trustees' responsibility. The cost of managing and holding these assets needs to be carefully managed.

Financial Information and Reporting

All key decisions must be made considering accurate and current financial information. To do this, you need to have all the financial information you require to manage the Community Scheme (e.g. comprehensive management accounts – budget utilisation, cash flow statements/projections, debtors outstanding, bank statements, accounts payable). This information should be accurate and quickly provided so that problems can be addressed by Office bearers as early as possible. Up to date management accounts are essential for the effective running of the Community Scheme.

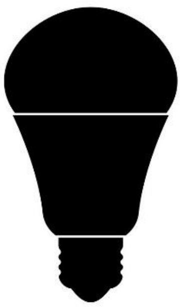
Debtors Controls

The management of the debtor’s book becomes a critical component of Financial Control; it is a dynamic process as the Community Scheme expenditure requires continual funding. The up-front or advance collection of levies or amounts due needs to be pro-actively managed. With budgets being largely balanced and the need to build up reserves, there is very limited scope to accommodate long outstanding debtors or bad debts. The collection of debtors requires that robust billing/invoicing systems, flexible collection processes and admin support systems are in place. Without these being in place and collections not being strictly enforced, the effective management of debtors will not be possible. Bad or irrecoverable debtors/levies are a loss of revenue and a loss of reserves and cash.

Socio-economic conditions can have an enormous impact on owners' ability to pay levies due and then on the overall state of levy collections. The knock-on effect of business failure and employee retrenchment can impact the ability of tenants to pay owners and, in turn, the owner's ability to pay their levies. Budgets should factor in the impact of lower levy collections due to owners' inability to pay and provide for bad debts.

Abandoned units need to be monitored, and appropriate legal action taken as quickly as possible to ensure these properties/interests don't become a financial drain on the Community Scheme.

Stock and Consumable Materials Controls



A Community Scheme holds stock of consumable materials such as paint, fertiliser, light bulbs/fittings, cleaning materials, compost, cement, fencing, pool chemicals, diesel/petrol etc. These need to be both physically managed and use thereof accounted for. You need to ensure good stock management by physically checking and recording stock levels regularly (at least monthly) and ensure stock is secure, protected and adequately insured.

Cash Management and Cash Flow Controls

The control and management of cash flow are at the heart of any Community Scheme's continuity and survival. Managing liquidity is a critical part of cash flow management and ensuring that a Community Scheme remains a going concern.

Cash flow must be budgeted and managed otherwise; all other budgets become meaningless. The preservation and maintenance of cash resources is a key component of cash flow management and sound business planning. Matching of cash flow movements is particularly important to enable the meeting of core operating expenses and meeting liabilities as and when they fall due., salaries and any debt or loan repayments and tax payments.

Banking and Payment Controls

The most critical dimension of handling the monies of a Community Scheme is the monitoring, managing, and controlling of all activities over the

Community Scheme's bank account/s. This needs to apply even where accounts are under Estate Management/Managing Agents/Accountants or a Third Parties' control. The scrutiny of accounts is particularly important for any unauthorised debits or payments, charges, debit orders or unpaid or stopped payments.

While bringing a host of benefits to business operations, the use of the internet and app-based banking applications has also brought a host of risk issues.

There are a number of key control steps that need to be taken to reduce the risk associated with banking applications and payments. These range from risk awareness education (spam/phishing emails/opening of attachments/following links/ransomware), use of anti-virus controls and security patches, strong password controls and disciplines, segregation of duties, transaction alerts and controls of transaction limits. All payment beneficiaries' banking details, including employees, loaded onto the banking system, should be independently verified.

There must be a very structured approach around who is responsible for authorising the addition of beneficiaries, the independent validation of their banking details by making use of direct interface applications with the banks in question and use of verification parties like TPN/Windeed, and the actual making of payments on behalf of the Community Scheme.

No unauthorised amendments to account details should be allowed. Payments should all be under dual release and be subject to validation of the invoices in question, value for money having been received, and budget and spend prior authorisation having been obtained.

With e-commerce growing at exponential rates, so too has the criminal focus and effort shifted. This has seen ever-increasing attempts being made to infiltrate existing business processes, collusion with and among staff, deviation from and/or circumvention of procedures and controls, interception and/or diversion of payments and collections.

The training of all staff/employees involved in the handling and processing of payments should be trained in fraud and cyber risk awareness.

IT and Technology Controls

The role technology and IT play, and their dependency vary for each Community Scheme e.g. for IT systems, access controls, security systems, surveillance, utility usage management, maintenance log/portals, accounting/billing applications, use of banking systems and web-site/messaging/social media/telecommunications platforms.

The level of reliance on technology and IT needs to be assessed by each Community Scheme to assess and quantify the impact of a potential failure or loss arising from these areas. Technology and IT is a complex, ever-evolving environment, and risk controls have to be on-going too.

A culture of awareness and discipline by all people is required to manage the risks emanating from technology use. The Community Scheme needs to clearly.

define what is expected of staff to help mitigate technology risk. On-going risk education and awareness training are essential.

The growing threat and risks of cybercrime and security breaches are set to change the face of business. Cybercrime is generally defined as any form of criminal activity involving the use of computers and the internet. This risk can arise from both external and internal sources.

Attacks can also be malicious, and a form of sabotage and can significantly impact operational continuity.

The role of network, firewall, and security software in eliminating many IT risks (e.g. data theft, hacking, ransomware, ecommerce fraud) is a basic requirement for managing these risks.

Given the integral role that technology and IT plays in every sphere of operations, this key area demands good governance – processes and procedures, policies, disciplines, controls and risk mitigation.

Strong IT and system access controls and strong user disciplines are a key component of financial control.

The main reason for focusing on this area is that cybercrime and fraud committed using technology or via online banking systems pose a massive risk to the financial position of Community Schemes. The majority of fraud in these areas will likely be committed by Trustees/Directors/Estate Management, employees of managing agents, or trusted third parties like bookkeepers or accountants who have access to systems and bank accounts. For these reasons, there needs to be a segregation of duties around the loading, capturing and release of payments, and the addition or amendment of creditor or payroll beneficiary details.

Disaster Recovery and Business Continuity

Even though your Community Scheme may not have experienced a major operational incident, technology outage, failure of a key service provider or natural disaster, e.g. fire or flood, it is imperative that all Community Schemes plan for business continuity and disaster recovery. The impacts of disasters can be both direct or indirect, immediate or take time to manifest. They will invariably have a significant financial impact.

These plans need to cover operational continuity, provision of key utility services such as drinking water, emergencies such as evacuation, security and garden/waste disposal services.

Disaster recovery plans need to be comprehensive and cover most eventualities. Community Schemes need to have a communication plan to enable ready and flexible communication with owners and/or residents. These might involve a few channels, from social media to email notices and message alerts.

Supplier Selection and Procurement Controls

You need to have robust processes and procedures to ensure all suppliers and service providers' credibility and reputation to your Community Scheme. The appointment, selection and verification (due diligence) of all suppliers and third-party service providers need to meet laid down qualification and review processes and procedures.

A Community Scheme cannot allow itself to become vulnerable to a single supplier or service provider. As part of contingency planning, alternative suppliers of goods or services should always be identified. The failure of a key supplier or service provider can impact a Community Scheme both operationally and financially.

It also remains important that alternate quotations are obtained from potential service providers or suppliers. Larger projects or contracts should be subject to transparent tender processes.

HR/People/Employees

Before any staff are appointed, there must be comprehensive vetting of candidates. These will go a long way in mitigating potential problems and risks down the track. This covers their suitability for the post in question, skills, experience, and background and reference checks. The attitude of the party is equally as important.

The use of reputable employment agencies and verification agencies might also mitigate some of the recruitment risks. Still, the final selection and assessment of a potential employee rests with the Community Scheme.

At the heart of the relationship with all employees is their formal contract of employment. This dictates the basis and terms and conditions of their employment.

You need to have employment contracts in place for all employees. Detailed job descriptions should also be in place for all posts. Terms and conditions of employment need to be set out. These, along with HR policies, should clarify that there is a zero tolerance to fraud, theft, and criminality. Clear reporting lines should also be in place, e.g. accountability to Office bearers.

Employees are singularly the most significant risk to a business or organisation. It is imperative that all the necessary background screening and reference checks are performed before employees are placed in positions of trust, deal with monies or be left in control of company assets, e.g. employment history, identity, criminal and credit checks. Once you have a high-risk person in your employ, you open yourself up to potential problems. Lifestyle expenditure is one of the major reasons for driving fraud.

Conflicts of interest are another area that can give rise to corruption, losses, and kickbacks at the Community Scheme's expense. Employees must disclose these in a position of influence. There are always going to be suppliers, contractors, service providers or employees who will look to do business or exploit situations no matter what the cost. Conflicts can influence supplier and service provider selection, unwarranted pricing or sales terms and impact on recourse and objective arms-length with service providers or suppliers.

Where laid down procurement or tender processes are deviated from, bypassed or ignored, the goods or services in question will invariably cost the Community Scheme more than they should have. In some instances, warranties or guarantees will also be nullified, and back up service and support compromised.

Payroll and Statutory Deduction Controls

The payroll often represents a considerable expense in many Community Schemes and should demand specific attention.

It is important that comprehensive and robust controls around all areas of the payroll need to be in place; system updates, tax tables, employee details- personal and banking, salary/wage levels, alterations/additions, termination, over-time, leave pay, sick leave, bonuses, deductions and the reconciliation and payment of statutory and other deductions.

All elements of the payroll should be under dual control. This should apply whether the payroll is run internally, outsourced or run through a bureau. Only reputable well supported payroll systems should be used.

The handling and control around payroll deductions is another critical area of financial control. You need to have processes to ensure that regulated and agreed deductions are deducted and paid over within the specified timelines to the respective authorities and institutions.

Crime, Fraud, and Criminality Loss Mitigation

Fraud, theft, and criminality (economic crime) are endemic to all organisations or businesses where money and people are involved. The size and scale of these can vary greatly and can extend back over a lengthy time period. Criminals are always one step ahead, and Community Schemes need to be permanently on their guard. Trustees/Directors/Estate Management and Office bearers will be responsible for most fraud, theft, and criminality along with employees of the Community Scheme or third parties contracted by the Scheme.

Not only are the number of incidences of fraud, theft, and criminality increasing, but the sophistication of the crimes is also on the rise as technology evolves and employees or people become increasingly involved or implicated in crime syndicate activity. Crimes can range from simple basic thefts to complex accounting frauds involving organised crime syndicates that infiltrate specific industries and business sectors.

All businesses and industries are vulnerable to fraud, robbery, criminality, and theft. The impacts of crime can vary greatly, but most Community Schemes will not survive or recover from a material financial loss.

Socio-economic conditions such as unemployment and poverty can impact the safety and security of the Community Scheme and in turn residents e.g., the extent to which visitors or servants are permitted into the Community Scheme, general crime in the surrounding areas, increased incidents of theft, robberies, and break-ins in general.

To manage these risks, you have to place a specific focus on people, systems, and controls. You have to be extra vigilant around asset controls, cash and bank accounts, the people employed by the Community Scheme, visitors/servants to the Community Scheme, payroll, physical security, banking system access, payment systems, and procurement processes, and undertake the vetting of all the service providers and suppliers to the Community Scheme.

To reduce the risk of fraud, theft, and criminality, Community Schemes need to have a culture that places a high priority on financial controls and discipline and one that endorses financial oversight and accountability at all levels. These include fraud awareness, access controls, IT system controls, tight expenditure controls, clear segregations/separations of duty, and accurate and timeous financial reporting to identify issues quickly.

Community Schemes need to continually ensure that they do not have a high-risk office bearer or employee in their services or employ. This requires on-going monitoring of all employees, particularly those in positions of trust.

A specific area of fraud or funds misappropriation comes about where the financial responsibility is left to a third party such as estate management, managing agents, independent accountants, bookkeepers or tax practitioners. The selection of key service providers needs careful evaluation.

Irrespective of positions, length of service and status, all office bearers, employees and key service providers need to be subject to independent checks and balances.

With office bearers, managing agents, or trusted third parties being the biggest risk to a Community Scheme, they must be vetted; the necessary background screening and reference checks are performed, e.g. references, identity, criminal and credit checks before managing agents are appointed, nominated office bearers are elected, employees engaged or third parties appointed or placed in positions of trust, deal with monies or be left in control of Community Scheme assets. Where relevant, they should be registered with their respective organisational or professional bodies.

Unfortunately, there is also a high level of fraud perpetrated by Office bearers of Community Schemes. In most cases, this is due to controls being circumvented, no segregation of duties, "abdication" of oversight by fellow Trustees/Directors, abuse of procurement processes, matters being dealt with verbally, one party having a strong personality, a lack of oversight over bank accounts, no reference or criminal checks having been performed on Directors/Trustees/Estate Management, conflicts of interest, collusion with managing agents/suppliers/contractors or service providers, deviation of payments due to beneficiary bank account amendment controls being slack.

This people verification process needs to also extend to the appointment of contractors or service providers. These individuals may have the ability and authority to bind or commit the Community Scheme contractually or financially or handle monies on behalf of the Scheme. In all instances, they can impact the reputation and financial position of the Scheme adversely.

A zero-tolerance approach to fraud, theft and criminality needs to be reinforced in employee induction, employment contracts, training and extend into formalised disciplinary processes. There should be a reporting mechanism for fraud/theft and criminality, e.g. a whistle blower line to Trustees/Directors/Executives of Managing Agents/Estate Management being in place. This must ensure confidentiality and no retribution against whistle blowers.

The following are the key risk management governance fundamentals to counter Fraud, Theft and Criminality in any Community Scheme:

- Community Schemes need to have a documented non-negotiable code of conduct that is adhered to and enforced that sets out the values and principles of the Scheme, and that has a specific focus on Crime, Fraud and Criminality.

- Community Schemes need to adopt a zero-tolerance approach to Fraud, Theft and Criminality.
- Community Schemes need to make it very difficult for people to steal from them by having a high focus on financial controls and clear responsibility for assets (fixed and movable assets).
- Community Schemes need to review their security controls, access controls, financial controls and procedures on an on-going basis.
- Community Schemes need to review and analyse all loss and criminal incidents and close any gaps in controls, procedures and physical security.
- Community Schemes need to establish if the controls are adequate and effective and look for continuous improvements.
- Community Schemes need to ensure clear accountability and responsibility for all key areas.
- The Community Scheme needs to enforce ethical standards.
- Community Schemes need to educate employees in fraud and theft awareness.
- As a base requirement, the Community Schemes has to be seen by residents, owners, lessees, employees, contractors, and suppliers as visibly security and crime conscious, compliant with controls, and highly focused on all key security and risk areas.
- Community Schemes through their employees, Trustees/Directors or Managing Agents need to personally champion security controls, adherence to security policies and procedures, and encourage the reporting of Theft, Fraud and Criminal Activity.
- Community Schemes have to send out clear signals of risk awareness, personal accountability, create fraud and crime awareness and be pro-active in countering criminality.