Memo

To: Hot Springs Village Board of Directors
From: George Parker, Audit Committee Chair
Date: January 17, 2018
Re: Discussion - Proposed Revisions to the Audit Committee Charter & Accounting Policies

The Audit Committee spent the past several months reviewing the Accounting Policies and the Audit Committee Charter. The following outlines the Audit Committee’s recommendations for policy and Charter revisions.

Background:
During the Board Retreat held earlier this year, the Audit Committee, CEO and Controller were tasked with reviewing all of the Financial Policies of the Hot Springs Village POA. The Audit Committee was also asked to review its Charter to ensure alignment with the Enterprise Goals. The Audit Committee Charter has not been revised since it was approved in 2007. Accounting Policy revision dates ranged from 2002 – 2016.

Recommendation:
The Audit Committee recommends the Audit Committee Charter and the following Accounting Policies be revised as summarized below:

- **Audit Committee Charter**
  A statement was added to the purpose charging the committee with oversight of the POA’s compliance with GAAP and other legal & regulatory compliance. In addition, a responsibility was added to ensure that complete audit reports are presented to the Board of Directors and property owners. Organization and Appointment, Limitations and Meeting sections were updated per current bylaw guidelines and governance policies.

- **Article 2 – Budget Policy**
  The revised policy combines the former Article 2 – Budget Policy and Article 25- Budget Amendment Policy into one. A purpose statement was added. Changes in policy clarify when the CEO has the authority to amend the budget and which amendments require Board approval. The date which the budget is approved was also changed from November to October, which has been in practice for several years.

- **Article 6 – Audit & Funds Control**
  Revisions added a purpose statement, included the 401(k) Plan in the policy and added reference to the Authority directed in the Bylaws. Wording was also added to ensure that Audit Reports are presented to the full Board of Directors in a public Board meeting.
• Article 8 – Debt Usage and Management
  A reference to the specific section of the Bylaws was changed in the Authority section.

• Article 9 – Contracts Execution Policy
  A purpose statement and reference to the Bylaws were added. The policy was revised to acknowledge contracts that extend beyond one year.

• Article 11 – Delinquent Accounts/Bad Debt Write-Off Policy
  Bylaw references were updated, and the policy was revised to include Utilities and other accounts receivable. The Bad Debt write-off section was revised to include the State of Arkansas statute of limitations.

• Article 14 – Records Availability
  A purpose and specific bylaw reference was added. The section referencing open meetings was removed as it is stated in a separate policy and the confidentiality of employee records is clarified.

• Article 18 – Insurance Claims & Litigation Policy
  Policy was revised to clarify the responsibility of insurance claims and litigation separately and to provide more detail about the different types of litigation. Sections for personnel and Damage claims were added.

• Article 19 – Purchasing Policy
  Policy was revised to authorize the CEO the authority to spend up to $100,000 for budgeted capital items previously approved by the Board and detailed in the budget, while keeping the board apprised of any purchases over $50,000. The CEO’s operating expense authority remains at $50,000.

• Article 22 – Capital Investment Reserve Fund
  Policy is no longer needed as it has been combined with Article 10 – Reserve Funds Policy approved 7/19/17.

• Article 25 – Budget Amendment Policy
  Policy is no longer needed as it has been combined with Article 2 – Budget Policy as noted above.

Additional Information
Article 10 Reserve Funds Policy was approved on 7/19/17 and did not require any revisions at this time.
The Audit Committee has three policies still under review and revision, the Refund Policy, Investment Policy, Records Retention Policy.
In addition, the committee will be working with staff to create a Real Estate Acquisition and Sales policy upon completion of the Comprehensive Master Plan.
I. AUTHORITY

Article XII, Section 1(B) of the By-laws of the Hot Springs Village Property Owners’ Association. The Audit Committee is accountable to the Board of Directors.

II. PURPOSE

Provide approval, oversight and evaluation of the independent auditors. Discuss with auditors the scope and schedule of the annual audits and the discussion of matters relating to the financial operations, controls and financial reporting of the Association.

The committee shall act as liaison between the Board and independent auditors in overseeing the POA’s compliance with legal and regulatory requirements as it relates to generally accepted accounting practices (GAAP).

III. ORGANIZATION AND APPOINTMENT

The committee shall consist of a Committee Chair (appointed annually by the Board Chair), and at least two elected Board members (appointed by the Committee Chair). Preference will be giving to Board members who have financial and/or accounting backgrounds. Vacancies in membership of the Committee will be filled by the Committee Chair. The Treasurer and Controller will serve as ex-officio members of the committee.

IV. DUTIES AND RESPONSIBILITIES

1. Approve the employment of an independent auditing firm to audit the books and records of the association.
2. Evaluate the independent auditor’s qualifications, performance and independence including internal quality control procedures or peer review of the firm.
3. Discuss with the Auditor the schedule and scope for the Annual Audit and any matters relating to the financial operation, controls and financial reporting of the Association’s financial condition, including any areas of concern.
4. Seek assurance from the auditor that the Association’s financial statements are complete and accurate and in accordance with generally accepted accounting practices (GAAP).
5. Meet with the auditor prior to the end of the year and at the completion of the audit to review the audit plan and annual report.
6. Ensures that the auditors make a complete report to the Board of Directors and Property Owners.
7. Oversee adherence to Chapter One, Article 6, the Audit & Funds Control Policy.
8. Ensures that the Board has adequate knowledge and understanding of the Audit Committee and Board’s roles in assessing the overall financial health of Hot Springs Village. Performs more in depth financial analysis if requested by the Board or audit firm.

The independent auditor reports directly to the Audit Committee. The Committee is expected to maintain free and open communication with the independent auditor and management. This communication will include periodic private executive sessions with each of these parties as required.

V. LIMITATIONS
   This committee has no authority to set policy or to take any action on behalf of the Board.

VI. MEETINGS
   As an advisory committee to the Board of Directors, meetings of this committee may be closed sessions due to the sensitivity of the subject matter.

B.O.D. Approved 5-16-07, REVISION DRAFT
ARTICLE 2

BUDGET POLICY

PURPOSE: To establish a structure for the association’s budgeting process and provide a process for making amendments to the budget once approved.

SECTION 1: The staff of the Hot Springs Village Property Owners’ Association will prepare a five-year capital plan, an annual operating and capital expenditure budget and the fee schedule from which the operating budget is prepared, using the Comprehensive Master Plan as a long-range guide in the process.

SECTION 2: The five-year capital plan is to be used for long-range planning and as a guide for capital expenditures, major maintenance and repairs in the formation of the annual operating and capital budget. This is a planning tool and requires input from staff, committees, the Board of Directors, and the Comprehensive Master Plan.

SECTION 3: The operating and capital budget is a management tool to be used as direction for the budget year it represents. The budget along with the fee schedule is to be approved and adopted each year by the Board of Directors at the October Board meeting prior to the budget year.

SECTION 4: Budgets are managed at the Board level, Executive level and the department level. Any amendments that increase or decrease departmental budgets must follow established procedures and coincide with purchasing authority levels. Amendments to the original budget may occur throughout the year for a variety of reasons. There are two types of Budget Amendments permitted under this policy:

1. **No Impact to the bottom line (Net Excess (Deficit) before Depreciation)**
   Intra and interdepartmental adjustments submitted and approved by Division Directors and the COO or CEO with concurrence of the Controller.

2. **Bottom Line Impact**
   Any increase or decrease of revenue or expenditures that impact the overall budget bottom line (Excess (Deficit) Before Depreciation) requires the approval of the Board of Directors.

The Controller manages the budget amendment process, monitors expenses and revenues, adjusts budgets as permitted under this policy, and prepares reports for the CEO. All amendments will be reflected in monthly financial reports.

SECTION 5: Once approved by the Board of Directors, the CEO shall have full authority to align personnel and resources to best meet enterprise goals, except as noted in Section 4.2.

Replaced Guidelines for the Development of the Three Year Financial Plan 2-25-87, 1-12-88, 1-20-88, 4-26-89, 2-6-02, 3-6-02, 3-20-02, REVISION DRAFT
Chapter One General Administration

ARTICLE 6
AUDIT & FUNDS CONTROL

PURPOSE: To safeguard the Association’s assets and financial transactions.

AUTHORITY: Article XI, Section 5 of the Bylaws grants certain authorities and responsibilities to the Treasurer related to the funds of the Association. The Audit Committee’s authority is detailed in Article XII of the Bylaws.

SECTION 1: The Treasurer, CEO, COO & Controller shall be named on all Association bank accounts. Additionally, the Fire Chief and one captain shall be named on the Act 833 account.

SECTION 2: All cash and checks received are to be deposited promptly in the POA’s deposit bank accounts. POA facility managers are charged with the responsibility to assure cash is safeguarded and managed according to established procedures. The POA Controller is responsible for developing and issuing cash receipt reporting procedures for the POA.

SECTION 3: The Association’s books and 401k plan shall be audited annually by an independent firm of Certified Public Accountants as approved by the Audit Committee, and as ratified by the Board of Directors. Audit and tax services shall be reviewed by the CEO/Treasurer and Audit Committee every five years, at a minimum, using the purchasing policies outlined in Article 19.

SECTION 4: Internal auditing procedures shall be directed by the Controller to ensure transactions align with generally accepted accounting principles (GAAP), using the accrual basis of accounting.

SECTION 5: Any irregularity revealed through audit procedures shall be reported immediately to the CEO and Board of Directors for corrective action. The final audit reports shall be presented in a public Board meeting.

Adopted 10-76, B.O.D.
Rev. 5-17-89, 7-22-98, 9-12-01, 10-17-01, 07-15-15, REVISION DRAFT
Chapter One General Administration

ARTICLE 8
DEBT USAGE AND MANAGEMENT

PURPOSE: This policy serves as the Hot Springs Village Property Owners’ Association (HSVPOA) guiding philosophy for analyzing and using debt to ensure adequate funding from which to fulfil its obligations to current and future property owners. As such, it should be periodically reviewed and updated to reflect current market options, best practices, business needs, and regional or national benchmarks.

AUTHORITY: As directed in Article VI, Section 1.6 of the Bylaws, the HSVPOA Board of Directors retains authority to approve debt usage.

The following guidelines shall be used by management to bring forward recommendations, and likewise by the Board, for scrutinizing the debt arrangements.

SECTION 1: PURPOSES FOR WHICH DEBT MAY BE USED
a. Short term debt such as credit cards, lines of credit, or vehicle and equipment leasing programs may be considered to smooth operational cash flow.
   i. Leasing programs may be considered for equipment and vehicles required for routine operations when traditional bank financing options are less favorable. Safety, reliability, and total cost of ownership will guide such decisions.
   ii. Credit card balances must be paid in full each month or their usage suspended.

b. Long term debt should be considered when constructing or improving fixed assets and not to support operating expenses.

SECTION 2: DEBT LIMITS & COLLATERAL
a. When analyzing HSVPOA’s long term debt capacity, the viability ratio shall be calculated. The viability ratio equals (=) expendable net assets divided (/) by total long term debt. Expendable net assets equals (=) total assets minus (-) total liabilities minus (-) net property, plant, and equipment plus (+) long term debt. This ratio is used to determine whether sufficient assets exist to cover debt and should not fall below 1.1.

b. When considering whether HSVPOA can afford to pay debt service from current operational cash, the debt service coverage ratio (DSCR) shall be calculated. The DSCR equals (=) 3 year average net operating income before depreciation divided by (/) total current debt service for one year. This calculation is meant to represent current results, using established or known data. It should be carefully studied and scrutinized to ensure the best course of action is taken before choosing a long term debt arrangement. When significant shifts in net income or additional debt service is readily known, both a current result and a projected calculation should be considered. HSV will strive for a DSCR of 1.25 or higher, but will not fall below 1.1.
c. Both revenues and assets may be used for collateral, as follows:
   i. Assessments, water, and sanitation fees may be pledged. The total pledged amount shall not exceed 25% of the current year’s budgeted or projected revenues, whichever is less. When calculating available assessment revenue, it shall be net of the allowance for doubtful accounts.
   ii. Although revenues are the preferred collateral, assets may be used as collateral when required by the institution or more favorable terms are granted, as a result.

SECTION 3: DEBT STRUCTURING
a. HSVPOA recognizes there are many financing and funding sources available, each with specific benefits, risks, and costs. Bonds, notes, mortgages, and other customarily used financial instruments may be considered, with the most appropriate instrument chosen for the project goals. Cost and benefits have various meanings in debt. Therefore, the goals of a particular debt arrangement shall be clearly understood; i.e. 1) to fund construction while minimizing monthly debt service, 2) to fund construction while expediting repayment, 3) to refund bonds in order to take advantage of favorable net present value savings; 4) other business needs
b. Bonds may be issued under public or private offerings.

SECTION 4: SERVICE PROVIDER SELECTION
a. Either competitive sourcing or direct negotiation with known local or regional industry leaders may be used to identify the appropriate debt solution. Depending upon the instrument chosen, various service providers may comprise associated fees, such as attorneys, underwriters, trustees, investors, CPAs, financial advisors, and other professionals or experts.
b. Professionals chosen by direct negotiation and internal research shall be subject to competitive sourcing every 3-5 years to ensure the organization continues receiving the highest level of service, most qualified professionals, and competitive pricing.
SECTION 5: COMMUNICATION AND COMPLIANCE
a. Debt recommendations will be made in a public forum with the appropriate external professional presenting and answering questions. Afterwards, summary information to include provider credentials, total fees, interest rates, and repayment terms will be posted on the HSVPOA website. Full details will be provided confidentially to the Board prior to the meeting and may be reviewed afterwards by members in good standing in accordance with the Declaration and Bylaws.

b. Although the Declaration grants the Board ultimate authority for debt approval, keeping property owners apprised on matters impacting the organization’s overall net worth is important. Therefore, a member comment period between recommendation and Board approval will occur, with the length between the two determined by market conditions and urgency of need.

c. A local or regional legal firm possessing industry leading experience in the debt instrument under consideration shall be engaged to develop related documents and guide the organization on related laws governing its issuance and future management.

d. Arbitrage and other financial analysis or audit requirements will be performed by the audit firm engaged at the time of such requirement, as prescribed by Article 6 of the General Administration policies.

Sources Used or Cited


BOD 07/18/07; 01/20/16, REVISION DRAFT
Chapter One General Administration

ARTICLE 9
CONTRACTS EXECUTION POLICY

PURPOSE: To establish authority for contract agreements.

AUTHORITY: The authority to execute contracts and/or agreements shall be vested in the officers of the Association as stated in Article XI, Section 6 of the Bylaws.

SECTION 1: CONTRACT LIMITATIONS
Any and all contracts and/or agreements obligating the Association to an expenditure over $50,000 for the life of the contract must be approved by the Board of Directors. The CEO approves contract expenditures below this amount or contracts allowing for termination at any time and with a maximum annual obligation of $50,000.

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ARTICLE 11
DELINQUENT ACCOUNTS/BAD DEBT WRITE-OFF POLICY

PURPOSE: To outline action to be taken when assessments, utilities, fines, fees or any other receivable become delinquent.

AUTHORITY: Various authorities are stated throughout the policy that reference the Declarations & Bylaws.

SECTION 1: ASSESSMENTS

A. All assessment accounts become delinquent on the 15th day of the month and will be placed on the delinquent list with written notifications, penalties, and collection procedures enacted. As per the Declaration (Article X, Section 7), assessments are due on the first day of each month. This 15-day window is merely a reprieve from delinquency communications and is not intended to circumvent the assessment due date or counting of days for collection actions.

B. On the last day of the month due, balances shall incur the Board approved late payment penalty which will be charged each subsequent month of delinquency.

C. As provided in Article X, Section 7 and Section 10 of the Declaration, beginning with the second year of assessments, monthly assessment payments that are more than 45 days outstanding will be subject to the following payment stipulation: “In the event of default as to a monthly payment, and if the default is not remedied within 30 days, the Association shall have the option of declaring the assessment for the entire year due and payable.” If this action is taken, “the assessment shall bear interest from the date of delinquency at the rate of 6% per annum, and the Association may foreclose the lien against said property, or may bring an action at law against the individual(s) or entity personally obligated to pay the same”.

D. Penalties on delinquent assessments will be established by the Board of Directors of the Hot Springs Village Property Owners’ Association.

SECTION 2: UTILITY BILLS

A. Any unpaid balances on utility bills are considered past due 21 days after the billing date.

B. On the 21st day after the billing date, all utility accounts with balances shall incur the Board approved late payment penalty, which will be charged each subsequent month of delinquency and late notices will be mailed.

C. Utility services will be shut off for non-payment (and charged related shut off/on fees as approved by the Board) 30 days after the billing date.
SECTION 3: USAGE FEES, FINES, ETC.

A. Any unpaid balances of other receivables, including fines, fees, lease payments, or any other accounts due to the Association will be considered past due 31 days after the billing date.
B. Past due notices will be sent after 31 days and for each month thereafter.

SECTION 4: DELINQUENT ACCOUNTS

A. On the 61st day from the billing date, the property is no longer in good standing and subject to the suspension of privileges as described in the Declaration (Article XIV, Section 1) and Bylaws (Article I, Section 9).
B. On the 120th day, the property will be subject to third-party collection action, which may include credit bureau reporting, foreclosure proceedings, and any other legal recourse available to HSVPOA.
C. To avoid repeat delinquencies, the POA will not sell any POA owned lots to property owners that are not in good standing as defined in Article XIV, Section 1 of the Declaration.
D. The POA staff, under the guidance of the CEO, may to adjust down any penalty charges in its efforts to collect delinquent accounts or to facilitate the sale of property in inventory.

SECTION 5: BAD DEBT WRITE OFFS

A. In accordance with accrual accounting, a provision for bad debt shall be included as a separate line in the approved annual budget. It shall be calculated and recorded monthly as 100% of all balances that are more than 365 days outstanding and any other assessments deemed “uncollectable”.
B. The Controller shall prepare and review an aged trial balance of accounts receivable monthly and provide summary balances during the monthly financial presentation to the Board.
C. The CEO will evaluate delinquent accounts each June and December to identify and write off all balances outstanding beyond the statute of limitations, currently 5 years. The bad debt write-off will only occur after all measures of debt collection have been exhausted, such as in-house and outside third-party collections and when debts have reached the statute of limitations set by the State of Arkansas (Arkansas Code Ann. 16-56-111).

Adopted B.O.D. 2-21-01, 8-5-09, 1-18-12, 10-15-14, REVISION DRAFT
Chapter One General Administration

ARTICLE 14
RECORDS AVAILABILITY

PURPOSE: To provide appropriate transparency to property owners in good standing.

AUTHORITY: As stated in the Bylaws, Article XV, Section 1 the books, records, and papers of the Association, with the exception of personnel records, shall at all times, during reasonable business hours, be available for public inspection by any member in good standing of the Association.

SECTION 1: Certain records of the Association, such as membership name and address listings, membership payment records, etc. shall not be distributed to any person without the written consent of such members. Likewise, members will not be permitted to copy such records for removal from the Association office.

SECTION 2: All personal information, relative to a member or employee, in the possession of the Association shall be held confidential to that member and will not be made available for general public scrutiny.

SECTION 3: Upon proper identification, all federal, state or local agencies authorized by law shall have access to the Association records without protest.

Adopted 10-76, B.O.D., Amended 11-76, REVISION DRAFT
ARTICLE 18
INSURANCE CLAIMS AND LITIGATION POLICY

PURPOSE: To establish authority for handling insurance claims and litigation.

AUTHORITY: Article 9’s contract execution policy and related spending limits shall govern decisions to enter into agreement or litigation under this policy.

SECTION 1: INSURANCE CLAIMS

Through its daily operations, the Corporation is subject to claims being filed against it which exposes the Association to a direct liability or a liability against its insurance. The COO is assigned the responsibility to manage and control the disposition of claims.

SECTION 2: LITIGATION

1. Delinquent Assessments - All legal action necessary to pursue the collection of assessments is to be administered by the CEO under the provisions of applicable federal and state law, the Declaration, Bylaws and policies.

2. Enforcement of Declaration and Governance Policies - Any legal action required to pursue the enforcement of the protective covenants, Bylaws, and policies of the POA must receive the prior approval of the Board of Directors. Enforcement of Operational Policies shall be administered by the CEO.

3. Personnel – All legal action related to personnel under the CEO’s authority shall be pursued by the CEO, in coordination with the HR Director and an Employment Law attorney. Legal matters relating to the CEO’s employment are pursued by the Board of Directors.

4. Damages – All legal action necessary to pursue the collection of damages is to be administered by the CEO under the provisions of applicable federal and state law and within the spending authorities stated in Article 19.

5-15-89, 9-12-01, 10-17-01, 6-11-03, Approved 7-16-03 BOD, 04-15-15, REVISION DRAFT
Chapter One General Administration

ARTICLE 19
PURCHASING POLICY

PURPOSE: To obtain maximum value when acquiring materials and services for the benefit of the HSV Property Owners Association (POA). This policy shall extend to all levels of procurement activity. The CEO or designated staff are herein referred to as the purchasing authority (P.A.), as determined by commitment authority levels.

SECTION I: DELEGATION OF AUTHORITY
The board of directors shall delegate the total purchasing responsibility to the CEO whom shall extend subordinate authority to staff as defined in established procedures.

Commitment Authority of Approved Budgetary Spending
1. CEO, up to $50,000 for operating expenses
2. CEO, up to $100,000 for budgeted capital items previously approved and noted in the budget. The CEO will keep the board apprised of any purchases over $50,000.
3. COO, up to $25,000
4. Division Director, up to $10,000
5. Supervisor, up to $5,000
6. The board of directors shall approve any expenditures not delegated to the CEO as noted above.

SECTION II: CONTRACTS
Board approval of the annual budget is not to be presumed as sufficient authorization for the CEO or staff to enter into contractual agreements obligating the POA beyond this policy. Advance notice of contract awards over $50,000 is prohibited until approved by the board of directors and related purchasing procedures have been completed. Additional policies on contracts are found in Chapter One, General Administration, Article 9, Contracts Execution Policy.

SECTION III: PROJECT APPROVAL
Projects, unlike general ongoing maintenance efforts, shall be defined as repurposing or procuring buildings, amenities, or other infrastructure and capital.

The CEO (or COO as designee) shall approve all expenditures over $50,000 that have been authorized within a board approved project. At any time that project costs are projected to exceed the original project authorization, such increase must be presented to the Board for approval within 30 days.

SECTION IV: EXCEPTIONS
The following expenditures are exceptions to this policy: utilities, taxes, insurance premiums, or legal fees incurred to enforce current policies or to pursue board approved litigation. The CEO has authority to re-direct line item spending up to the CEO’s commitment authority, as deemed appropriate for accomplishing the Enterprise Goals and without perpetuating infrastructure neglect. The Board retains approval authority for spending in excess of the approved total annual budget.

Adopted BOD 1-15-14; 12-16-15, REVISION DRAFT
ARTICLE 22
CAPITAL INVESTMENT RESERVE FUND

Policy previously combined with Article 10, RESERVE FUNDS POLICY on 7/19/17

Adopted 11-19-03
ARTICLE 25
BUDGET AMENDMENT POLICY

Combined with Article 2 – Budget Policy