BIZCOMMUNITY

Why next-level trust fund separation is vital in rental property management

By Jan Davel

29 Jul 2020

No estate agent or property manager needs to be reminded of the legal specification that trust funds must be held separate from business funds. The reason for it is well known too - it is to ensure that third-party funds are only ever used for the purposes they were intended for. The upshot is that this imposes a strict duty on estate agents, including property managers, to keep such funds - for example rent monies, tenants' damage deposits and landlord reserves - safe and separate.


Jan Davel, CEO, Payprop

In my opinion, even complying with Section 32 of the Estate Agency Affairs Act is not necessarily enough to have truly segregated trust funds that keep tenants, landlords and agents safe. Levelling up when it comes to the detailed segregation of funds will make a lot of business sense for agents wanting to position themselves as trusted custodians of tenant and landlord funds.

A trust fund isn't like water in a bucket

All agents must have a separate trust account into which tenant funds are paid. In addition, they must keep an accounting record, which may include a system of reconciliation to match rent payments received to tenants on the incoming side, as well as landlords and other beneficiaries on the outgoing side.

Some property management systems can even automate the settlement of these amounts by pulling funds from a trust account, putting them into a settlement account, and then pushing all payments out. It all sounds fairly simple, but the risk becomes clear when you imagine your trust account without next-level fund separation as a bucket full of water.

All tenant funds flow into the bucket, and each month funds are scooped out and distributed. The trouble is, you no longer know which money belongs to which property – it's all water. You could be paying property A's expenses with property B's money! It can easily happen when a cheque bounces or a debit order fails – you think you have the money and you pay, but the money is never really there. Worse still, you end up paying the landlord or supplier who is making the most noise – hoping that when the tenant eventually pays, the imbalance will sort itself out. In the long run, these little exceptions create a trust account that is almost impossible to reconcile down to each property.

And that goes double for funds on retainer

It is becoming increasingly common for some water to be left over in the bucket at the end of the month. Retaining some of the landlord's money (with their permission) in the trust account to cover approved property expenses is a very healthy practice and helps when there is a problem with the property. If a fixture breaks or maintenance to the property is needed, the landlord is responsible for fixing it and must have money available to do so. When landlord money has not been retained and the landlord fails or neglects to make funds available, agents may feel compelled to use the security deposit.

But, as we all know, the damage deposit belongs to the tenant. It is not the agent or the landlord's money. Using the tenant's deposit to pay for repairs or maintenance that are for the landlord's account, even by accident, can ruin an agent's relationship with the tenant and landlord – especially when the deposit money is needed at the end of the lease term to pay for damage to the property or to refund the tenant.

The case for next-level separation of trust funds

Using a proptech platform, like PayProp, ensures that there is separation of funds. Imagine that within your trust account bucket, there is a little bucket for every property into which only funds that belong to that property can go. Each little bucket is further subdivided, with space for funds held for the landlord and funds held for the tenant.

Next, there is the matter of the funds actually being there. Through our platform's integration with the banking system, we can guarantee that beneficiaries are only paid once funds are actually received and cleared, that a property's expenses are only paid with money meant for that property, and that any money retained is separately 'tagged', stored and accounted for. We also ensure that outgoing payments do not exceed the amount received in respect of a particular property, and we ensure that each agent's trust account is reconciled to the last cent daily.

All accounting, banking and property management tasks related to these funds are automated, leaving no room for human error, while a proper audit trail remains available for every user and every action they take.

Unfortunately, many estate agencies struggle to achieve detailed segregation of funds. As a result, their business and their clients may be exposed to significant risk of misuse of funds – often in error. Efficient use of proptech can solve this problem, while helping with agency compliance.

ABOUT THE AUTHOR

Jan Davel, CEO, [[https://za.payprop.com/ PayProp]]