

BEFORE THE REAL ESTATE COMMISSION
OF THE STATE OF IOWA

IN THE MATTER OF:)	CASE NO. A05-009
)	DIA NOS. 06DOCRE006
LARRY R. STEWART)	
Broker (B17081))	
)	FINDINGS OF FACT,
LARRY STEWART REALTY)	CONCLUSIONS OF LAW,
503 Kelly Street)	DECISION AND ORDER
Charles City, IA 50616)	

On May 26, 2005, the Iowa Real Estate Commission (Commission) found probable cause to file a Statement of Charges against Larry R. Stewart (Respondent). The Statement of Charges alleged that Respondent engaged in practices involving his trust account which are harmful or detrimental to the public, in violation of Iowa Code sections 543B.29(3), 543B.34(7)(2005) and 193E IAC 13.1(6), 13.1(6)(a)(3) and 18.14(5)"e" by the following:

- a. Failing to maintain adequate trust records at all times.
- b. Failing to perform monthly reconciliation of the general ledger with individual ledgers and bank records to ensure agreement.
- c. Failing to maintain the general ledger and individual ledgers to reflect current balances, and
- d. Showing an overage in the individual ledgers resulting in commingling of funds.

A prehearing conference was held by telephone on September 8, 2006. The hearing was held on September 14, 2006 at 1:30 p.m. Respondent Larry R. Stewart appeared and was represented by attorney Judith O'Donohoe. Assistant Attorney General John Lundquist represented the state of Iowa. The following Commission members presided at the hearing: James Hughes, Broker, Chairperson; Don Marple, Broker; Dan Berry, Broker; Patty Daniels, Salesperson; and Laurie Dawley, public member. Administrative Law Judge Margaret LaMarche assisted in conducting the hearing. A certified court reporter recorded the proceedings. The hearing was closed to the public at the election of the Respondent, pursuant to Iowa Code section 272C.6(1)(2005).

After hearing the testimony and examining the exhibits, the Commission convened in closed executive session, pursuant to

Iowa Code section 21.5(1)(f)(2005), to deliberate its decision. The Commission instructed the administrative law judge to draft Findings of Fact, Conclusions of Law, Decision and Order, in conformance with their deliberations.

THE RECORD

The record includes the state's Prehearing Conference Report; testimony of the witnesses; and the following exhibits:

- State Exhibit 1: Statement of Charges, Notice of Hearing, Proof of Service
 - State Exhibit 2: Respondent Licensing Information
 - State Exhibit 3: Audit Narrative
 - State Exhibit 4: Trust Account Examination Deficiency Report, 5/10/05
 - State Exhibit 5: Relevant Statutes and Administrative Rules
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- Respondent Exhibit A: Larry Stewart Realty Sales Listing Recap by Year
 - Respondent Exhibit B: Summary of How Error Occurred with attached documentation

FINDINGS OF FACT

1. Respondent is a licensed Broker Officer and designated broker in charge of Larry Stewart Realty in Charles, City, Iowa. Respondent's Iowa real estate broker license (B17081) was first issued on September 23, 1975 and is in full force and effect through December 31, 2007. Respondent has owned Larry Stewart Realty since 1987. In the time period relevant to this decision, June 2004-May 2005, Respondent employed his son as a broker-associate and also employed four licensed sales associates. (Testimony of Respondent; State Exhibit 2)
2. In 1987, Respondent retained Ralph Anderson of the Anderson Agency of Forest City to set up a computer based accounting system known as "Escrow Ledger." Since that time, Ralph Anderson has continued to work with Respondent to incorporate any necessary updates to the accounting system. Every sales transaction is coded by year and transaction number and is stored in the system's hard drive. All closing documents are computer generated. Respondent maintains a trust account for client funds.

Prior to 1995, Respondent personally performed all accounting functions related to the trust account, including monthly reconciliation using the computerized data system. In 1995, Respondent hired an experienced executive secretary to serve as his office manager. After Respondent trained the office manager, she assumed all accounting responsibilities, including responsibility for monthly reconciliation of the individual ledgers with the general ledger and the reconciled trust account balance (aka "three-way tie"). However, Respondent's system did not provide a separate written worksheet for performing the three-way tie. In June 2004, Respondent hired a new office manager when the prior manager resigned for family reasons. Respondent and the departing office manager trained the new office manager on the computerized accounting system. (Testimony of Respondent; Jeff Evans; Respondent Exhibit A)

3. The Commission has employed Jeffrey Evans as a Trust Account Auditor for 3 years. In that time, Evans has performed numerous unannounced trust account audits. On May 9, 2005, Jeffrey Evans arrived during regular business hours to audit Respondent's trust account. Respondent and his office manager were very cooperative and provided Evans with the current trust account ledgers, bank statements, reconciliations, check book, and deposit slips. Evans quickly noticed that the trust account records did not include a monthly reconciliation of the individual ledgers to the general ledger and to the reconciled bank total (three-way tie). Since the records were up-to-date, Evans attempted to reconcile the account. Evans was able to tie the general ledger balance and the reconciled bank balance total but was unable to tie the total of the individual ledgers. After rechecking his calculations numerous times, Evans determined that the total of the individual ledgers was \$9,969.68 more than the general ledger total and the reconciled bank balance total.

Respondent's office manager called Evans later that same evening to report that they had found errors in the accounting system. Evans returned to Larry Stewart Realty the next day. With the corrected information provided by Respondent's current and prior office managers, Evans again tried to perform the three-way tie. This time, he was able to reconcile the total of the individual ledgers to the general ledger balance but found that the bank balance was short \$10,062.00. This indicated a substantial shortage of funds in the trust account. (Testimony of Jeff Evans; State Exhibit 3)

4. Upon further investigation, it was determined that the \$10,062.00 shortage in the trust account was the result of an accounting error involving a sales transaction in June 2004. The transaction involved the sale of a 148 parcel of land to a buyer who had been renting the parcel for a number of years. The seller agreed to give the buyer a credit of \$10,062.00 for rental payments that the buyer had already made to the seller in 2004. However, Respondent's office manager erroneously treated the rent credit as though it had been a cash deposit, when in fact no cash was received or deposited in the trust account. The closing documents were then computer generated, based on this bookkeeping error. As a result, the seller received \$10,062.00 in cash proceeds at closing that was not owed to him. This caused the \$10,062.00 shortage in Respondent's trust account.

In August 2004, Respondent's office manager had recognized that there was a \$10,062.00 discrepancy between the QuickBooks balance and the bank balance. On September 10, 2004, Respondent's office manager made a general journal entry of \$10,062.00 to debit the sellers' ledger account and credit the seller expense account. This reconciled QuickBooks with the bank balance but did not correct the problem of the trust account shortage. (Testimony of Jeff Evans; Respondent; State Exhibits 3, 4; Respondent Exhibit B)

5. From June 2004 until May 2005, neither Respondent nor his staff was performing monthly reconciliation of the individual ledgers total with the general ledger total with the reconciled bank statement (three-way tie). If the three-way tie had been performed, the accounting error and the trust account shortage would have been discovered in the month following the transaction. The \$10,062.00 trust account shortage persisted, undiscovered, from June 2004 until Evans' audit in May 2005. Consequently, trust account funds were commingled, i.e. trust account funds from other clients were necessarily used to cover the shortage created from the sales transaction involving the 148-acre parcel. Since Respondent has a high volume of business and always had a substantial balance in his trust account, there was always sufficient money in the trust account to pay the checks that were presented to the bank. (Testimony of Jeff Evans; State Exhibits 3, 4; Testimony of Respondent; Respondent Exhibits A, B)

6. Immediately following Evans' audit, Respondent went to his bank and took out a note to cover the shortage in the trust account. Respondent also contacted the buyer's attorney and the

seller's attorney from the sale of the 148-acre parcel to notify them of the error. The seller did not have the funds to repay Respondent but agreed to give Respondent a \$10,062.00 note secured by a mortgage encumbering a ten-acre building site that he owns. (Testimony of Respondent; Jeff Evans; State Exhibit 4)

7. Since Evans' audit, Respondent has revised his accounting process to ensure that the individual ledger totals are reconciled to both the general ledger total and the reconciled bank balance each month. The monthly reconciliation is documented and preserved as part of Respondent's permanent trust account records. (Testimony of Respondent; Respondent Exhibit B)

CONCLUSIONS OF LAW

I. The Violations

A. Applicable Law

Each real estate broker is required by statute to maintain a common trust account in a bank, savings and loan association, savings bank, or credit union for the deposit of all down payments, earnest money deposits, or other trust funds received by the broker or the broker's salespersons. Iowa Code section 543B.46(1)(2005) In addition, brokers shall not commingle the broker's personal funds or other funds in the trust account with the exception that a broker may deposit and keep a sum not to exceed five hundred dollars in the account from the broker's personal funds, which sum shall be specifically identified and deposited to cover bank service charges related to the trust account. Iowa Code section 543B.46(4)(2005).

The legislature has specifically authorized the Commission to adopt rules to ensure implementation of Iowa Code section 543B.46. Iowa Code section 543B.46(8)(2005). Pursuant to this authority, the Commission has adopted the following relevant rules:

193E IAC 13.1(6) provides, in part:

13.1(6) Each broker required to maintain a trust account shall maintain *at all times* a record of each account, as required by these rules, in the place of business, consisting of at least the following:

a. A record called a journal which records in chronological order all receipts and disbursements of moneys in the trust account.

(1) For receipts, the journal of each trust account must include the date, name of the depositor, the check number and the amount deposited, and the name of principal or identify the property.

(2) For disbursements, the journal for each trust account must include the date, name of payee, name of principal or identify the property, the check number and the amount disbursed.

(3) The journal must provide a means for *monthly* reconciliation on a written worksheet of the general ledger balance with the bank balance and with the individual ledger accounts to ensure agreement.

b. Real estate sales transactions shall additionally require an individual ledger account identified by the property or the principal, which records all receipts and disbursements of the transaction and clearly separates the transaction from all others. The individual ledger account shall include the date, check number, amount, name of payee or depositor or explanation of activity with a running balance.

...

(emphasis supplied)

193E IAC 18.14(5) provides, in relevant part:

18.14(5) *Violations for which civil penalties may be imposed.* The following is a nonexclusive list of violations for which a civil penalty may be imposed:

...

e. Maintaining inadequate transaction records such as:

(1) Failing to maintain a general ledger.

(2) Failing to maintain individual account ledgers.

(3) Failing to retain records on file.

Iowa Code section 543B.29(3) (2005) provides, in relevant part:

543B.29 Revocation or suspension.

A license to practice the profession of real estate broker and salesperson may be revoked or suspended when the licensee is guilty of the following acts or offenses:

...

3. ..engaging in...practice harmful or detrimental to the public. Proof of actual injury need not be established.

Iowa Code section 543B.34(7)(2005) provides, in relevant part:

543B.34 Investigations by commission.

The real estate commission may upon its own motion and shall upon verified complaint in writing of any person, if the complaint together with evidence, documentary or otherwise, presented in connection with the complaint makes out a prima facie case, request commission staff or other duly authorized representative or designee to investigate the actions of any real estate broker...and may suspend or revoke a license issued under this chapter at any time if the licensee has by false or fraudulent representation obtained a license, or if the licensee...is found guilty of any of the following:

...

7. Failing, within a reasonable time, to account for or remit any moneys coming into the licensee's possession which belongs to others.

B. Discussion

Real estate brokers have essential statutory and fiduciary duties to maintain proper trust account books and records, to properly account for the public's money, and to submit to audits. Unless proper accounting procedures are utilized in a timely manner, it is impossible to ensure and verify that brokers are fulfilling their obligation to protect and preserve client moneys that they hold in trust and that they are not commingling trust funds. As the licensed broker, Respondent is legally and ethically responsible to timely account for all trust account funds that he receives and disburses and to comply with all of the Commission's rules pertaining to trust accounts.

At the time of Jeffrey Evans' audit on May 9-10, 2005, neither Respondent nor his staff had been performing a monthly reconciliation of the trust account records to show the required three-way tie between the reconciled bank account, the general ledger, and the individual ledgers. In addition, Respondent did not have a written worksheet for monthly reconciliation of the general ledger balance with the bank balance and the individual ledger accounts, as required by 193E IAC 13.1(6)(a)(3). Moreover, Evans' audit revealed a \$10,062.00

shortage of funds in Respondent's trust account as a result of an accounting error in June 2004. When issuing checks from the trust account over the course of the year, Respondent necessarily used the funds of other clients to cover this shortage. This constitutes commingling. Because of the shortage in the trust account, there was a risk that checks issued on the account could be returned by the bank due to insufficient funds. However, due to the large volume of closings handled by Respondent and high balances in the trust account, there was always sufficient money to cover the checks that were written.

As the state points out, this case keenly illustrates the importance of performing a monthly reconciliation establishing the three-way tie. Monthly reconciliation is essential to identify any inaccuracies or mistakes in the trust account record keeping and to protect client funds. If a proper monthly reconciliation had been timely performed, the accounting error would have been discovered in July 2004.

The preponderance of the evidence established that Respondent engaged in a practice that is harmful or detrimental to the public by failing to maintain adequate and up-to-date trust account records, in compliance with Iowa Code sections 543B.29(3), 543B.34(7) (2005) and 193E IAC 13.1(6) and 18.14(5)(e). As of the date of the audit, Respondent did not have accurate records of his individual ledgers and had a substantial shortage in his trust account. Respondent had not performed the monthly reconciliation required by 193E IAC 13.1(6)(a)(3) for nearly a year.

II. Sanction

In determining the appropriate sanction, the Commission considered the factors outlined in its rules, including the relative seriousness of the trust account violation and the potential for harm to the public. 193E IAC 18.14(6). Respondent has had a distinguished career as a broker without a prior violation. The violation was neither willful nor intentional. Respondent and his staff were very cooperative with the auditor and promptly provided all requested documentation. When the error was identified, Respondent promptly deposited his own funds in the trust account and took immediate steps to ensure that the deficiency in his accounting process was corrected. For these reasons, the Commission believes that the violations are adequately addressed by an educational requirement and a civil penalty.


ORDER

IT IS THEREFORE ORDERED that the Respondent Larry R. Stewart, Broker License (B17081), shall personally complete the eight-hour Commission approved broker pre-license education course "Iowa Real Estate Trust Accounts." The original certificate of attendance must be submitted to the Commission office with a cover letter to the Commission's Executive Officer, referring to Case No. A05-009. These hours shall be in addition to any real estate continuing education required by law for license renewal and must be completed within six (6) months of the date of this Order.

IT IS FURTHER ORDERED that Respondent shall pay a civil penalty to the Commission in the amount of \$500 no later than thirty (30) calendar days after the issuance of this Decision and Order. The civil penalty must be submitted with a cover letter to the Commission's Executive Officer, referring to Case No. A05-009.

IT IS FURTHER ORDERED, pursuant to Iowa Code section 272C.6 and 193 IAC 7.41, that Respondent shall pay \$75.00 within thirty (30) days of receipt of this decision for fees associated with conducting the disciplinary hearing. If the Commission issues a separate order assessing additional costs or expenses, the Respondent shall promptly comply with the terms of that order.

Dated this 2 day of November, 2006.


James Hughes, Chairperson
Iowa Real Estate Commission

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Judicial review of the commission's action may be sought in accordance with the Iowa administrative procedure act, from and after the date of the commission's order. If a party does not file a timely application for rehearing, a judicial review petition must be filed with the district court within 30 days after the issuance of the commission's final decision. 193 IAC 7.37.