MAGAZINE FOR COMMUNITY ASSOCIATION LEADERS

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by kenneth m. arnold

Bad Debt

IT'S NOT HARD to imagine your condominium or homeowners association having trouble collecting assessments. It's been a reality for many associations lately, and it's having a damaging effect on all aspects of community life.

What can an association do to address delinquencies? The first step is understanding the complexity of the problem.

Delinquencies aren't just about dollars and cents, but about common sense and sensibility, too. Debt starts to hurt when an owner makes that first decision, on any given month, that he or she is not going to pay on time. It hurts even more when that owner makes a strategic default.

Delinquencies damage real lives in real time. Owners who pay on time begin to carry more of the burden. In addition, association management and governance can devolve into a series of impossible decisions. Payments to vendors might be late, leading to the loss of amenities and services. Infrastructure suffers and aesthetics are neglected. Associations can experience declines that may take years to correct. In short, it's paradise lost, and the goal of maintaining and increasing property values is dashed.

So how can an association get back on track? What can be collected and when can collections be expected?

Just as with any other commercial enterprise, money owed to an association is called accounts receivable and should always be considered recoverable until proven without a doubt to be uncollectable or economically unjustifiable. Community association boards need to be more positive and confident that accounts receivable are collectible. It's simply not good business practice to throw one's hands in the air and exclaim, "There is nothing we can do." The truth is there is plenty to be done. Associations need to craft an action plan and begin addressing the issues of bad debt when they first appear.

ANTICIPATION

In the past, the first mortgagee would take the first step to resolve the problem. During these times of overwhelming toxic assets, banks have made associations full partners in their misfortunes. Banks aren't coming to the rescue to salvage their collateral, take their losses and put qualified owners or renters in units; they are waiting to act until they are in the most optimal position. Unfortunately, banks' best interests don't always coincide with those of the association. Boards need to be proactive and distinguish accrual income from anticipated income in order to be prepared to face potential cash flow issues.

HIERARCHY

Delinquent assessments—aka accounts receivable—have many faces and come to associations at different times. There are owners who are habitually late but don't default; there also are investors who walk away from underwater units. Both cause damage, but the latter is far more pernicious. Associations should put the variable types of delinquent accounts receivable into a hierarchy. It gives a board the ability to address each case appropriately.

The end of the line for accounts receivable is when it becomes absolutely clear that money cannot be col lected under any circumstances. Fron the perspective of the association, a fi mortgage foreclosure is not the end c the collections process. When an owi loses his or her property to the lendei the debt to the association does not simply go away. Foreclosure does not terminate the former owner's obligati to the association. Boards should reta collection help at this time.

LEGAL OPTIONS

Many associations rely on legal remedies, which vary from state to state and include: demand letters, lawsuits, assessment liens, foreclosures and the appointment of receivers.

Demand letters. These letters include the amount alleged to be pasi due, late charges, interest and legal cc They ask the owner to contact the as: ciation attorney to make arrangemen for payment. They can state whether lien will be filed and can indicate thai the association will take further legal action if payment is not made on time.

Lawsuits. Under most association declarations, owners are personally liable for paying assessments. The association can file a lawsuit and potentially obtain a judgment that requires the owner to pay unpaid assessments and—if governing documents and state statutes allow—late fees, interest, court costs and attorney fees.

Assessment liens. Many owners pay when they learn that an assessment lien has been recorded because it clouds the title to the unit.

Foreclosure of assessment liens. Foreclosure is a last resort. It results in the association taking title to the property or the owner (or other lien holder) paying the lien.

Appointment of receivers. A court-appointed receiver manages the property and pays any rent that is collected to the association to help cover the mi ing assessments.

COLLECTION PROFESSIONAL

Associations also now have another option—a cottage industry of specialized firms that focus exclusively on co munity association collections. These qualified, trained and adequately insu professionals have had great success recovering money.

The business of professional collec tions is no different from any other di cipline, science or art. Adhering to th federal Fair Debt Collection Practices Act and applicable state laws should r be left to chance, and selecting a collections firm should require a thoroug review of the company's credentials. This new breed of service providers a collections firms recognizes that community associations are cash poor; an as a result, they have developed innov tive compensation packages that give homeowners and condominium assoc tions a plethora of options.

Specialty finance firms also have evolved and have introduced ways for associations to monetize their ledger as The fact is that accounts receivable are a liability, but rather an asset that can b leveraged for cash flow at zero or limite interest. Private sector companies have identified the problem, realized an opp tunity and are now providing new solutions. These qualified collections servic pursue debts on a contingency fee basis

Associations need to fight tooth a nail for every cent they are owed. Bac debt is a condition that needs to be treated like an illness. Associations n to develop the proper treatment plan and write the correct prescriptions. C

KENNETH M. ARNOLD is co-founder and (of Association Financial Services, a Miam based company specializing in debt colle tions, specialty lending and other financia solutions for condominium and homeow associations. Go to www.associationfinan services.com for more information.

RESOURCES: *DELINQUENCIES: HOW COMMUNI ASSOCIATIONS COLLECT ASSESSMENTS*, BY LOUR K. SANCHEZ, ESQ., AND THOMAS J. HINDMAN, ES RETAIL: $25. CAI MEMBER: $15.

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