

Community Association Management *Insider*

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Strengthen Association's Finances with Effective Collection Policy

A community association can face a serious financial crisis if even a small percentage of members don't pay their assessments on time. All too soon, reserves start to get depleted and the community has to start making trade-offs about what bills to pay and what services to forgo.

Fortunately, most communities' members do pay on time. And in many cases, the few members who don't pay are the ones who simply don't understand why they have to pay and how their delinquencies affect everyone else.

How can you educate these holdouts and motivate them to make good? By communicating clearly the reasons it's important for them to pay, the fact that you have a legal duty to collect, and the progressively more serious steps you'll have to take if a member lets things go too far. The best way to do this is to adopt a tough—but fair—written assessment collection policy and distribute it to all association members.

Even if you have a policy, it may have holes in it. For instance, it may have you marching straight into court after you send a late notice, rather than taking some less aggressive, and perhaps more effective, steps first. Below, we tell you what should go into an effective collection policy. And we've worked with an attorney and a community association consultant to create a Model Policy (see pp. 3-4) that you can adapt for your association's use.

Benefits of Good Policy

A member who delays paying his assessment probably doesn't perceive that payment as fulfilling a basic human need. "Most people consider food and housing to be essential, so they pay the mortgage and grocery bills first. They put other payments, like assessments, down the list," says consultant Richard L. Thompson. And real estate attorney Thomas C. Schild says that's because there are typically no direct consequences to their late payments, such as cutting off credit or services or reporting late payments to credit agencies.

To get your assessments into the "essential" category, you need a fair but tough assessment collection policy. Your policy should impose consequences for late payment that are both financial (such as late fees, interest charges, or returned check charges) and nonfinancial (such as suspension of voting rights, restricted access to amenities, or shutoff of association-provided utilities), says Thompson.

Also, it's important to remember that most members will never suffer any of these consequences. The point is to have effective tools at your disposal that have already been communicated to the entire community. That way, when it's time to take action, there are no surprises over what you're doing.

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COLLECTION POLICY (continued from p. 1)**What to Put in Policy**

Putting together an effective policy is easy. Your community may already have the basics in an existing board resolution. But many resolutions are filled with legalese and are difficult to read. For our Model Policy, we've combined the best elements of several model resolutions and translated the result into easy-to-understand language. Adapt it to your community's needs. Your policy, like ours, should do the following:

Explain how late payments affect the community. Appeal to members' sense of community. Tell them that assessments represent shared costs they would have to bear alone if they weren't part of a community association. Remind them that nonpayment threatens their neighbors' property values as well, not just theirs [Policy, preamble].

Explain board's legal authority to collect assessments. Make members understand that you *must* pursue delinquent accounts and that state laws and your governing documents will back you up when you do [Policy, preamble].

List all charges the policy covers. A member who pays regular assessments on time may delay paying other charges, such as special assessments, fines, and bills for common area damage the member caused. Your policy—and the consequences it sets for late payment or nonpayment—should cover these other charges, too. Also, it should state that any charges you bill to a member will be considered common expenses. This puts all delinquencies on an equal footing come enforcement time [Policy, par. 1].

Give remittance address. It may seem like overkill, but tell people where to send the check [Policy, par. 2].

Set "annual assessment" with monthly payments. It may help to have members realize that they owe a total amount for the year for their regular assessment and that you're allowing them to pay in monthly installments for their convenience. So, instead of thinking they owe \$200 per month, they should be thinking they owe \$2,400 per year. Looking at the big picture may help some people realize how important their contributions are and make them more inclined to pay those monthly installments on time [Policy, par. 3].

Insider Says: Schild, who practices law in Maryland, says he drafts most of his clients' policies this way. But check with your attorney to make sure your state permits this approach.

Set clear due dates. Set due dates for regular assessments (in most communities, usually the first of the month), as well as due dates for other charges. Also, state that any common expense becomes delinquent the day after its due date [Policy, par. 3].

Set consequences for late payment. Set progressively more serious consequences for a payment as it becomes more overdue. You must do this within the bounds of the law, so check state law and your governing documents. They may prohibit some of these consequences altogether and impose penalties on you for using them. They also may set deadlines and time frames that are different from the examples in our Model Policy. To stay out of trouble, get the association attorney's approval before adopting these methods.

With your attorney's okay, here's what we recommend:

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MODEL POLICY

Set the Consequences for Delinquent Payments

Here's a collection policy we've developed with the help of consultant Richard L. Thompson and real estate attorney Thomas C. Schild. The policy will help members understand the consequences of late payments and show them that you intend to apply

your collection policy uniformly, fairly, and consistently. Don't adopt the policy without showing it to your association's attorney. State law and your governing documents may dictate changes and deletions.

ROLLING GREEN COMMUNITY ASSOCIATION COLLECTION POLICY

One of the many advantages of living in a community association is sharing with other members the costs of certain maintenance, repairs, and amenities that are often too expensive for a single-family homeowner. All Rolling Green members are legally bound to share those costs.

WE'RE IN THIS TOGETHER

To properly maintain Rolling Green's common areas, it's imperative that all assessments, whether regular or special, be paid in full and on time. Delinquencies throw the association's entire budget off course and negatively affect all members' property values and lifestyles.

KEEPING UP OUR END OF THE BARGAIN

To adequately maintain our community, state statutes and our governing documents give Rolling Green's board of directors the authority to impose and collect assessments and other allowable charges from members. In fact, the board owes a duty to all members to make sure everyone pays. The board has adopted the following policy to fulfill its duty in a fair, systematic, and impartial manner.

1. Common Expenses

The term "common expense" refers to any amount a member must pay to Rolling Green. Among the charges it includes are regular annual assessments, special assessments, rules violation fines, late fees, common area repairs, and any other fees, interest, or charges imposed under this policy.

2. Where to Send Payment

Deliver all payments to the management office:

ROLLING GREEN COMMUNITY ASSOCIATION
MANAGEMENT OFFICE
1234 Rolling Green La., Jackson, NJ 00000

3. When Common Expenses Are Due

Annual assessments are due the first day of January and apply to that calendar year. For convenience, members may pay their annual assessments in equal monthly installments on the [insert day—e.g., first, 15th] day of each month. Unless otherwise stated, other common expenses are due [insert time period—e.g., within 30 days of, on the first day of the month following] notice of members' obligation to pay. If a member does not pay in full any common expense by its due date, that payment is delinquent.

4. Late Payments

Once a common expense is delinquent, Rolling Green may take any or all of the following actions:

- a. **Accelerate the balance for the rest of the year.** If payment is not received by the due date, Rolling Green will send a written delinquency notice to the member within

[insert time period—e.g., 10, 15, 30] days of the due date. If Rolling Green does not receive full payment of the amount owed within [insert time period—e.g., 10, 15, 30] days of the date on that notice, the delinquent member may not take advantage of Rolling Green's monthly payment plan for the rest of the year. The member will have to pay the entire remaining balance of the annual assessment immediately.

- b. **Late fees and interest.** If Rolling Green does not receive payment for any common expense in full on or before the [insert day—e.g., third, fifth, 10th, 15th] day after it becomes due, the delinquent member shall pay liquidated damages for Rolling Green's time, inconvenience, and overhead in collecting the late payment, as follows:
 - i. a \$[insert #—e.g., 25] late fee; and
 - ii. interest at a(n) [insert #—e.g., 12, 18] percent Annual Percentage Rate from the original due date until the date of payment.

These charges will be treated as common expenses.

- c. **Returned check fees and bank charges.** In addition to any late fee that may be applicable, for each check to Rolling Green that is returned by a bank for any reason, the member who wrote the check shall pay the following charges:
 - i. liquidated damages in the amount of \$[insert #—e.g., 25]; and
 - ii. any related bank charges that Rolling Green incurs because of the returned check.

These charges will be treated as common expenses.

- d. **Suspend privileges and access to amenities.** If an account contains delinquencies for more than [insert time period—e.g., 30, 45, 60] days or has an outstanding balance of \$[insert #—e.g., 200, 500] or more, Rolling Green will give the member [insert time period—e.g., 10, 15, 30] days' notice of intent to suspend any or all of the following privileges:
 - i. Voting privileges;
 - ii. Use of pool, playground, park, club facilities, lake, tennis courts, golf course, and other recreational amenities;
 - iii. Use of common laundry facilities;
 - iv. Use of storage facilities;
 - v. Parking privileges; and/or
 - vi. [optional—discuss with your attorney] Association-provided utilities.

Unless Rolling Green receives full payment by the end of the notice period, the privileges or amenities listed in the notice will be suspended.

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- e. **Account referred to an attorney.** Rolling Green may, in its sole discretion, refer a delinquent account to an attorney for further action. The attorney may do any or all of the following:
- i. File a lien against the unit in accordance with state law and Rolling Green's governing documents;
 - ii. File a lawsuit to collect the amount owed;
 - iii. Foreclose on the property;
 - iv. [optional—discuss with your attorney] Notify the mortgage lender of any lien and/or lawsuit Rolling Green has filed; and/or
 - v. Take any and all other appropriate legal action.
- f. **Attorney's fees and costs of collection.** The delinquent member shall be responsible for all of Rolling Green's attorney's fees and costs of collection, including court costs. These charges will be treated as common expenses.

5. Crediting Late Payments

All delinquent accounts remain delinquent until paid in full. No partial payments will waive Rolling Green's right to pur-

sue full payment and/or to enforce the provisions of this policy. Rolling Green will apply partial payments to the outstanding balance in the following order:

- Fines, late fees, and interest;
- Court costs, attorney's fees, and other costs of collection;
- Special assessments; and
- Regular assessments, with payment being applied to the oldest balance first.

6. Notices, Payments, and Consequences of Nonpayment

Unless otherwise required by law, all notices will be sent by first-class mail, postage prepaid, to the delinquent member's address as shown in Rolling Green's books and records on the date the notice goes out. All amounts due must be paid in full before the notice period expires. If the notice period expires without full payment, the consequences set forth in the notice and/or in this policy shall apply.

COLLECTION POLICY

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► **Accelerating balance.** Give yourself the right to demand payment of the outstanding amount of the entire annual assessment if monthly payments are not made on time. This can be a powerful incentive. Faced with the prospect of paying a whopping annual assessment all at once, the member won't find the smaller monthly bill so bad. But note: Because this is a severe remedy, our Model Policy requires you to give written notice of your intent to invoke it. The policy also gives members a grace period from the time they get the written notice to pay the monthly installment and avoid balance acceleration [Policy, par. 4(a)].

► **Charging late fees and interest.** Charge a late fee for any common expenses that a member doesn't pay by a set time after the due date. The late fee should be high enough to be an incentive but not so high that a court will find it an unenforceable penalty. Unfortunately, there's no magic number here. What's reasonable varies from state to state and even from court to court. Speak to your attorney about what amount to set.

To improve the chances that a court will enforce your late fee, your policy should state that late fees are so-called liquidated damages. This means that the fee you've set is a reasonable approximation of the expected damages you'll suffer if members pay late. In other words, you're seeking reimbursement for the time and expense of record keeping, sending notices, making phone calls, and meeting with the delinquent member.

Charge interest, too, retroactive to the date the assessment became delinquent. State law will tell you the highest annual percentage rate you can use. Go for that top number, but don't go over it. If you do, you could face charges of usury (a legal term for charging an illegally high rate of interest) [Policy, par. 4(b)].

► **Charging for returned checks.** Paying on time with a bad check is as bad as not paying at all. To avoid this scenario, say that in addition to whatever late fee applies, the member must pay you for your trouble if the check is returned. Our Model Policy contains two charges for returned checks: a set fee that covers your administrative hassles—say \$25—and reimbursement for what-

ever bank charges you incur as a result of the returned check. Again, call the set fee liquidated damages to increase the chances that a court will enforce it [Policy, par. 4(c)].

► **Suspending privileges and amenities.** Members' assessments pay for or make possible a number of privileges, including voting privileges, use of recreational facilities, and parking privileges. Why should a delinquent member get a say in association business and enjoy privileges that everyone else has paid for? Suspend those privileges until the member pays. But again, make sure you're on sound legal footing to get the courts on your side in case of a challenge. If you are, courts should be sympathetic to your case. For instance, an Indiana appeals court recently ruled that a condominium association's governing documents supported its decision to suspend a member's voting rights after he refused to pay his assessments [Lynn v. Windridge Co-Owners Assn., Inc.].

As with balance acceleration, because these are extreme remedies, give the member notice and time to make good before suspending anything. Check your governing docu-

ments and state law, too [Policy, par. 4(d)].

One particularly effective strategy is termination of association-supplied utilities. Certain states and localities prohibit the practice. But if it's allowed, Thompson recommends using it as a last resort because it generally gets immediate results [Policy, par. 4(d)(vi)].

► *Referring matter to attorney.* Let members know you'll hire an attorney when you have to. Describe what you may have the attorney do—file a lien against the member's unit, sue the member for payment, and/or foreclose on the unit [Policy, par. 4(e)]. Tell members that if this becomes necessary, they'll be on the hook for attorney's fees and collection costs if allowed by your governing documents and state law [Policy, par. 4(f)].

Insider Says: Many policies we've seen state that the association will notify the delinquent member's mortgage lender about any liens or legal actions filed. Though we've included this as optional language in our Model Policy, Schild leaves it out of his clients' policies. He says that notifying a third party about a debt

could violate the federal Fair Debt Collection Practices Act. Not all courts agree on this point, however, so check with your attorney [Policy, par. 4(e)(iv)].

Set how partial payments will be applied. Tell members how you'll apply partial payments to what's owed. As a general rule of thumb, regular assessments should be the last thing paid off. That's because you have the clearest legal authority for collecting assessments; courts may be less willing to award you other charges.

Most policies we've seen put fines, late fees, and interest first. Next come legal fees, collection costs, and court costs. Then come special assessments, and finally regular assessments. When you start applying a partial payment to regular assessments, you should start with the oldest month's delinquency first. With this setup, members have a greater incentive to pay everything they owe. If they don't, they'll keep facing new late fees as each deadline goes by [Policy, par. 5].

Set method of notice. Make giving notices easy on yourself. Unless

the law requires you to do otherwise, use first-class mail. State that you'll send notices to the most current address on record, and encourage nonresident members to give you updated information [Policy, par. 6].

Adopting, Communicating, and Enforcing the Policy

Have your board pass a resolution adopting the policy. Once passed, distribute the policy with assessment bills, print it in your association's newsletter, and post it on the association's Web site. According to Thompson, swift and uniform (nobody is exempt) enforcement is the best way to prevent delinquencies. Thompson also recommends having a professional manager or bookkeeper handle the job. "Neighbors should never be put in the position of having to collect delinquencies from other neighbors. It's too emotional, and the negative consequences are long-lasting," he adds. ■

Insider Sources

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