

THE COLLECTION OF ASSESSMENTS-A MUST FOR EVERY ASSOCIATION

By: Gabriella Comstock of Knuckles, Keough & Moody

It happens in every association, whether you are a condominium, townhome or homeowners association, at some point, a member within the association will fall behind on the payment of assessments. In fact, at some point, many members within an association may fall behind on their payments. It will also happen that the same member, who is not paying the association, is also not paying his/her mortgage company and other creditors. Therefore, the mortgagee may file a foreclosure action against the member. This may even lead the member to file for protection under the Bankruptcy Code. What then? How does an association then pay its bills, especially in a smaller association? What can the Association do to protect its interest and collect the money due and owing to it? While every forcible entry and detainer, foreclosure and bankruptcy matter are different, the purpose of this article is to provide the board of directors with a general overview of what it can do to best protect the association's interest.

The Collection of Unpaid Assessments

The assessments are the life line of every association. A declaration for the association imposes the obligation to pay assessments on the members. The first thing that a board of directors must do is become familiar with what the declaration states as it relates to the obligation to pay assessments. The Board should confirm whether the payment of assessments are monthly, quarterly or annually. The Board should also be familiar with what remedies the declaration provides if an owner fails to pay. A declaration may create an automatic lien, which is perfected upon default by the unit owner. This language is similar to that within the Illinois Condominium Property Act (hereinafter "the Act"), which states that a lien is created in favor of the association, which includes the amounts due and owing for unpaid assessments, fines, interest, late charges, attorney's fees and costs. 765 ILCS 605/9(g). Pursuant to the Act, the lien is created upon default by the unit owner, and the lien is created, even if the Association does not record a separate lien against the property with the Recorder of Deed's Office, where the property is located. 765 ILCS 605/9(g). For a non-condominium association, the board should determine if the association's declaration requires the lien to be recorded with the Recorder of Deed's Office, to be valid.

It is not uncommon that an association, that is professionally managed, seeks the assistance of its property manager to collect unpaid assessments. It is also not uncommon that the management company may charge a fee to the association for sending any letters or taking necessary steps to collect the amounts due and owing for assessments. Ordinarily, an association assesses to an owner's account all fees and costs, including those incurred by the management company, to collect the unpaid assessments. Ordinarily an association assesses to an owner's account all fees and costs, including those incurred by the management company, to collect the unpaid assessments. However, in January, 2006, the law in Illinois changed, and in order for an association to assess this amount against the unit owner's account and include it in the lien created in favor of the association, the contract between the managing agent and the association must identify the fees that will be charged to the association and the association's governing documents must state that the association will assess the management fees incurred, to the owner's account. 765 ILCS 605/9.2(c). Hence, before assessing this charge to an account, the Association should confirm with legal counsel that it has the authority to do this.

It is also not uncommon that the declaration will state that the board can charge interest or impose a late fee when a balance remains on the account. The Act authorizes the imposition of a late charge. 765 ILCS 605/18.4(l). The declaration typically identifies the percentage of interest that can be assessed. However, as to late charges, the board, even for

condominium associations, must then go the next step and be sure that the association's governing documents specifically identify the amount of the late fee and the date that it will be assessed. This information is usually included in the Association's Rules and Regulations. While the declaration should state that the board has the authority to assess the late fee, I recommend that the amount and the date that the late fee will be assessed be included within the Association's Rules and Regulations. After all, what is considered to be a reasonable late fee today, may change tomorrow. It is much easier, and less expensive, to change the association's Rules and Regulations, than the declaration.

The declaration will also state what remedies are available to an association to collect the amounts due and owing. Typically, the declaration will authorize the board of directors to initiate an action pursuant to the Forcible Entry and Detainer Act, 735 ILCS 5/9-101, et seq.. If it does not, the Board should seek the opinion of legal counsel to confirm the association is a common interest community as defined in the Forcible Entry and Detainer Act; thus, subject to it. It may also state that the board can pursue a foreclosure action to foreclose upon the lien against the property, in its favor. A foreclosure action will be governed by the terms of the Illinois Mortgage Foreclosure Act, 735 ILCS 5/15-1101, et seq.. Because a foreclosure action can take nine (9) to twelve (12) months to complete, and can be very expensive, I recommend that the association pursue a Forcible Entry and Detainer action (hereinafter "forcible").

The Forcible Entry and Detainer Act must be strictly complied with by the association. The advantage to filing such an action is twofold. First, it is a much faster process than a foreclosure, as it can be completed as quickly as four months, and it is much less expensive. Second, and most importantly, if the association is successful in obtaining a judgment in a Forcible action, against the member, the order will also include a provision that grants the association possession of the unit, if the judgment is not satisfied. For example, the order will state that a certain dollar amount is due and owing to the Association. It will also state that if the monetary judgment is not paid by a date certain, which will be no less than sixty (60) days from the entry of judgment, the association will have the right to take possession of the unit on the sixty-first day. That is, the association can take the order to the County Sheriff's Office and ask the Sheriff to go and evict the owner. Please note that the association only obtains the right of possession, not the right of ownership. Also, its right to possess the unit, only exists until the judgment is satisfied. Rarely do associations evict an owner. However, the threat of an eviction is very powerful and encourages compliance by a non-compliant unit owner.

Once the board has confirmed the contents of their governing documents as it relates to assessments, and is familiar with the remedies available to it, it is very important for the Board to adopt a collection policy. The collection policy must be strictly enforced, against all members. That is, the board cannot treat any member differently. Illinois law is clear that an association's restrictions must not be arbitrary in their application. See, Scott v. York Woods Community Association, 329 Ill. App. 3d 492, 768 N.E.2d 847, 263 Ill. Dec. 766 (2d Dist. 2002). The collection policy can be incorporated within a Board Resolution or the Association's Rules and Regulations. The collection policy should include the following:

When the board of directors or the association's property manager will send a notice to the owner requesting payment in full.

When the board of directors or the association's property manager will refer a delinquent account to legal counsel to initiate legal action.

Whether payment plans will be accepted and under what terms. The policy should identify how payment plans will be treated for first time offenders and repeat offenders.

Once an owner is in legal, all communications should only be between the owner and legal

counsel. This avoids confusion and promotes consistency.

All payment plans, either entered into prior to or after entry of judgment, must be in writing and signed by the member.

As stated, the collection policy for unpaid assessments should be in writing so that all owners understand their options. It must be strictly complied with by the board. A collection policy sends a message to the members of the association that the board will work with the members, to a certain extent, but that the board is also serious that it will collect the amounts due and owing to the Association.

Collection of assessments against a member whose unit is the subject of a foreclosure action

But what happens to the collection policy for unpaid assessments when a mortgagee files a foreclosure action against the member? Should the association ignore its policy? The answer is no. The board should simply then look to comply with its policy related to foreclosure actions.

Most of the time, the mortgagee's lien against the property will be superior to that of the association's lien. For purposes of this article, we will address the fore-closure action where the mortgagee's lien is superior to that of the association's. The association should be named as a defendant in the foreclosure action as it is an interested party to the action, based on the recording of the association's declaration. Therefore, the association will be served with a summons and complaint in the foreclosure action. Once it is served, it should file an answer and appearance as this will ensure that it continues to receive notice of the events in the case. Also, the filing of an answer ensures that the association will be included in any Judgment of Foreclosure. This is very important if a surplus results from a judicial sale.

From the sale proceeds, the mortgagee will be paid first. If there is any money left over, this represents the surplus. The remaining defendants in the case, who preserved their lien against the property, can petition the court for a distribution of the surplus proceeds. The way to preserve the association's lien is to be included in the Judgment of Foreclosure. Like the forcible act, the terms of the Illinois Mortgage Foreclosure Act, as it relates to a petition for distribution of surplus funds, must be strictly complied. Some of the counties in Illinois have adopted local rules on such a distribution, that must also be strictly complied with. Failure to comply with the local rules, can result in the denial of a petition, even if there are no other lien holders and the borrower is not asking the court for a distribution. Further, if an association does not take affirmative steps to preserve its lien against the property, *i.e.* file an appearance and be included in the judgment of foreclosure, it will be within the Judge's discretion whether to grant the request for distribution.

To avoid this, like a policy to collect unpaid assessments, the board should also adopt a policy as to how to address foreclosure actions. The policy should state the following:

All foreclosure actions will be forwarded to legal counsel, if the attorney is not the association's registered agent.

If the member's account with the association has a balance, the attorney will be directed to file an appearance and/or answer, to preserve the association's lien in the Judgment of Foreclosure.

The attorney will be directed to monitor the foreclosure action until it is completed.

The association's collection of assessments against the members, should not cease, unless directed by legal counsel.

Collection of assessments when a member files for bankruptcy

The association's collection policy for unpaid assessments can be complicated when a member files for protection under the bankruptcy code. A member can file for protection either under Chapter 7 or 13 of the Bankruptcy Code. Regardless of the Chapter, the filing of a bankruptcy, imposes an automatic stay which ceases all collection activity against the debtor. That is, the association cannot continue with its efforts to collect unpaid assessments. However, there is an exception to this stay, as collection proceedings can continue when the creditor obtains relief from automatic stay. While this article does not address how and when the automatic stay should be lifted, it does address what steps can be taken to collect the money due and owing to the association.

The filing of a bankruptcy by a member of an association does *not* mean that the association will never see the money due and owing to it. In fact, just the opposite can be true. If an owner files for Chapter 7, he/she is seeking to liquidate his assets. He/she is asking the Court to discharge him/her from his/her personal obligation to pay all assessments incurred prior to the entry of an order of discharge. If the Court grants this request of the debtor, the association will be prevented from going after the member personally to collect on its debt. Yet, it is not prevented from pursuing its lien against the property. This means that the association can record a lien against the unit in the amount due and owing prior to the entry of the order of discharge. Once the member sells his unit or looks to refinance, the lien will have to be satisfied. Hence, while the association cannot seek to collect this amount personally against the owner, in a forcible action, it can see the money when the lien is satisfied.

When an owner files for bankruptcy under Chapter 13, the debtor is looking to reorganize or "catch his breath". A plan will be created which requires the debtor to pay the trustee a certain amount each month. The trustee will then pay each secured creditor a specified amount which should be applied to the pre-petition arrearage or balance on the debtor's account with the creditor. In other words, the trustee will forward payments to the creditor to payoff the debtor's debt that accrued prior to the filing of bankruptcy. Then, the debtor is responsible for making current payments to the creditor for his/her obligations that accrued after the filing of bankruptcy, *i.e.* assessments which came due and owing after the filing. To receive payments from the trustee, the association must file a proof of claim with the bankruptcy court. It must also take affirmative steps to monitor the bankruptcy to ensure that payments are being made to the association by both the trustee and the debtor. If the association is not receiving payments regularly, the Bankruptcy Code provides a mechanism to the Association that allows it to seek relief from the automatic stay.

Consequently, just as the association created a policy related to the collection of assessments and fore-closure actions, one must be adopted on how to handle bankruptcy matters. The policy should include the following:

Legal counsel will be advised of the filing of bankruptcy by any member of the association.

Legal counsel will be directed to monitor all Chapter 7 filings, when the member has a balance on his/her account with the Association.

Upon the order of a discharge in a Chapter 7 proceeding, the association will direct legal counsel to record a lien against the property.

Legal counsel will be directed to file a proof of claim in all chapter 13 bankruptcy matters.

Legal counsel will be directed to monitor all Chapter 13 matters, until completed.

Conclusion

It can be very difficult to collect money from your neighbors. A clear, consistent policy will make it easier for the board. Collection policies send a very loud message to members that the collection of assessments is very serious to the board. It also protects the association to ensure that as much money as possible will be collected from all members. There will be times when the association cannot collect all that is due and owing to it. Yet, strict compliance with collection policies should make those instances rare.

Knuckles, Keough and Moody is a member of ACTHA

630-369-2700* grc@knucklesassociates.com

* www.condoattys.com