

DOUBLE TROUBLE

Foreclosures and Bankruptcies on the Rise

By Thomas Schild, ESQ.

Community associations throughout the Washington, DC and Baltimore region will continue to feel the financial strain of unpaid assessments in 2008 as the number of lender foreclosures and owner bankruptcies continue to rise.

Although the "mortgage crisis" is now front page news on a daily basis, the general news media rarely report the impact that the sharp increase in foreclosures has on the ability of community associations to collect assessments.

Foreclosures Hit Record Levels

A recent state study of Maryland foreclosures found there was a 344 percent increase in foreclosure activity in the second quarter of 2007 compared to the same period in 2006, with foreclosure activity rising from 920 properties to 4,092 properties.

In 2008, more foreclosures are expected as adjustable-rate loans obtained in 2005 and 2006 will reset to higher interest rates. In the current real estate market with falling property values, there typically is no equity in the property and the property is purchased at the foreclosure sale by the lender. The association lien is extinguished by the foreclosure. However, the lender who purchases the property is responsible for paying assessments from the date of the foreclosure sale.

Additionally, an owner whose mortgage is foreclosed is still personally responsible for the assessments and related charges due prior to the foreclosure sale date. The association can file suit to collect those fees.

Bankruptcy Stops Collection Action


However, all collection action must stop if an owner files bankruptcy. Faced with a lender foreclosure, some owners will file a Chapter 13 bankruptcy to stop foreclosure and the owner will re-pay debts owed prior to the time the bankruptcy is filed with the United States Bankruptcy Court. A person who files a Chapter 13 bankruptcy is required to keep current on future payments. Other owners who cannot repay existing debts or keep current on future payments may file a Chapter 7 bankruptcy. Upon approval by the Bankruptcy Court, the owner will no longer have personal liability to pay the debt.

Uncollectable Assessment Debt

Lenders lose more than \$50,000 per home sold in foreclosure, according to the recent study of Maryland foreclosures. In 2008, most associations should also expect to write off some assessment debt as uncollectable.

To minimize the amount of uncollectable debt, the board of directors should take the following actions:

- Maintain clear and complete owner account records showing all charges and payments.
- Take prompt collection action against delinquent owners, such as filing liens against the property and/or suit against them personally.
- Review notices regarding lender foreclosures and homeowner bankruptcies and take appropriate action.
- Consult with the association's attorney and accountant as to when and how to write off uncollectable assessments and related charges.

Although association boards cannot prevent delinquent association assessments, every board should plan now to monitor and respond to the expected increase in lender foreclosures and owner bankruptcies. 



Thomas C. Schild, ESQ., of Thomas Schild Law Group, LLC in Rockville, Maryland, is a member of CAI's National Faculty and chairs the Maryland Legislative Action Committee. He represents community associations in Maryland and Washington, D.C.