THOMAS SCHILD
LAW GROUP, LLC

401 North Washington Street, Suite 500
Rockville, Maryland 20850

Tel: 301-251-1414 law@schildlaw.com
Fax: 301-251-6636 www.schildlaw.com

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Community Association LawLetter

DOUBLE TROUBLE: FORECLOSURES AND BANKRUPTCIES ON THE RISE

Community associations throughout the Washington D. C. 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 the 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

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bankruptcy is required to keep current on future payments.

Other owners who can not re-pay 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.

Uncollectible Assessment Debt

Lenders lose over $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 uncollectible.

To minimize the amount of uncollectible 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; and

- Consult with the association's attorney and accountant as to when and how to write off uncollectible 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.

CONDOMINIUM RESALE DISCLOSURE STATEMENT RESULTS IN $1 MILLION COURT JUDGMENT

A trial court in Cecil County, Maryland has ruled that a condominium association and its management company violated the Maryland Consumer Protection Act by failing to provide information about future repair costs.

The owners of 25 of 93 condominium units filed suit against the condominium association and its management company, alleging that the resale disclosure statements included false, misleading and incomplete representations and non-disclosure of material facts regarding the need for extensive repairs to the Condominium common elements. The resale disclosure statements, including the operating budget, were prepared by the management company and issued by the Condominium before the full extent and cost of repairs was known and before a special assessment to fund the repair was approved by the Condominium board of directors.

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RESALE DISCLOSURE
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The Condominium and its management company contended that all disclosures and documents required by the Maryland Condominium Act were provided and that no additional disclosures were required by the Maryland Consumer Protection Act regarding potential repairs and future assessments.

The trial court concluded that the Consumer Protection Act did apply and found that the resale disclosure and current operating budget included false and misleading statements and that material facts were not disclosed regarding needed repairs and possible assessments. The parties stipulated to damages of $1 million if the Consumer Protection Act had been violated.

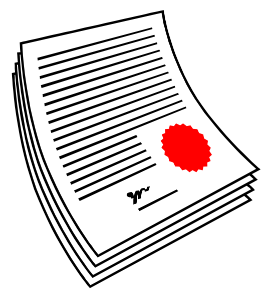
The Condominium and its management company have appealed the trial court ruling.

BUSY LEGISLATIVE SESSION EXPECTED IN 2008

With taxes and slots already acted on by the Maryland General Assembly during its Special Session in November, 2007, a variety of proposed bills affecting governance of community associations will be considered during the 2008 Maryland legislative session.

Among the proposed legislation expected to be introduced are bills to require registration and bonding of management companies; establish requirements for studying and funding the estimated costs to replace association common property components; and establish procedures for homeowner association governance transition from the developer to the homeowners.

Other expected bills will facilitate amendment of homeowner association covenants; aid associations in the collection of unpaid assessments; exempt amateur radio antennas from association restrictions on making changes to an owner's property; and modify the procedures regarding owner review and copying of association records.



The Maryland General Assembly will also consider numerous proposals offered in response to the significant increase in lender foreclosures now occurring throughout Maryland. These include bills to strengthen the laws and enforcement against fraud in mortgage transactions and to require additional notices and extend the redemption period before a foreclosure sale can occur.

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THOMAS SCHILD LAW GROUP, LLC represents condominiums, cooperatives, and homeowner associations in Maryland and Washington, D.C. The firm advises community associations on all aspects of association operations including covenant enforcement, assessment collections, developer warranties, maintenance and management contracts, and association document interpretation. Thomas Schild Law Group also represents community associations in court litigation and administrative hearings.
