

AN OPPORTUNITY FOR RECOVERY IN DIFFICULT ECONOMIC TIMES

By: **BRIAN D. MORENO, ESQ.**

It goes without saying that a majority of community associations in California are struggling with unprecedented increases in delinquent assessment accounts. Some associations spend thousands of dollars chasing unpaid assessments. A significant portion of these delinquent owners are leasing their properties and collecting rent while not paying their assessments.

But the homeowners association is not without options.

First, an association can pursue a lawsuit and after judgment is entered, file a motion for an assignment order. Second, the association could amend its CC&Rs and/or rules and regulations to include a restriction that requires all tenants to personally agree to be bound to the association's governing documents, thus exposing the tenant(s) to personal liability in the amount of the delinquency. The third option and focus of this article is enforcing the assignment of rents provision contained in the CC&Rs prior to filing a lawsuit.

In California, Civil Code Section 2938 regulates the formation and enforcement of the assignment of rents and profits generated by a lease agreement relating to real property. It provides that "[a] written assignment of an interest in leases, rents, issues, or profits of real property made in connection with an obligation secured by real property... shall, upon execution and delivery by the assignor, be effective to create a present security interest in existing and future leases, rents, issues, or profits of that real property..." Once a written assignment of rents is properly authorized and formed, the law creates a security interest (i.e., lien) against the rents and profits paid by a tenant.

The question then is whether the association's CC&Rs, by itself, creates an assignment of the right to a tenant's rent payment in favor of the association. Indeed, Section 2938(b) provides that the assignment of an interest in leases or rent of real property may be recorded in the same manner as any other conveyance of an interest in real property, whether the assignment is in a separate document or part of a mortgage or deed of trust. Since a homeowners association's CC&Rs is a recorded document and contains covenants, equitable servitudes, easements, and other property interests against the development, it follows that the assignment of rents relief provided in Section 2938(b) can be extended to community associations provided the CC&Rs contains an appropriate assignment of rents provision.

Section 2938, however, does not clarify whether the CC&Rs document on its own creates a lien and enforceable assignment right.

Moreover, a deed of trust is much different than a set of CC&Rs, in that the deed of trust creates a lien against the trustor's property upon recordation, while a home-owners association would not have a lien until an owner becomes delinquent with his or her assessments and the association records an assessment lien against the property. Therefore, depending on the scope of the assignment of rents provision in the CC&Rs, a homeowners association would likely need to record an assessment lien first before pursuing rents from a tenant. Moreover, even after a lien is recorded, homeowners associations should consider adding a provision in the assessment lien giving notice to the delinquent owner that an assignment right is in effect upon recordation of the assessment lien.

Nevertheless, association boards should consult with legal counsel to ensure proper compliance with the law.

Once the assignment right becomes enforceable, the next issue is how the association can and should proceed. Section 2938(c)(3) allows the association to serve a pre-lawsuit demand (a sample of which is included in the statute) on the tenant(s), demanding that the tenant(s) turn over all rent payments to the association. This can be a powerful tool for homeowners associations. Moreover, if the tenant complies, the association will receive substantial monthly payments that can be applied towards the assessment debt, and collecting the funds does not appear to preclude the association from pursuing judicial or non-judicial foreclosure proceedings at a later time.

While homeowner associations have the option of pursuing a lawsuit against the delinquent owner and seeking to collect the rent payments after a judgment has been obtained, there are obvious advantages to enforcing the assignment of rents provision prior to pursuing litigation. A pre-lawsuit assignment of rents demand may prove to be more effective and cheaper. Additionally, the tenant affected by the assignment of rents demand may place additional pressures on the delinquent owner/landlord having received such a demand. Given this, the options available pursuant to Section 2938, including the pre-lawsuit demand for rents, should at least be considered and analyzed before action is taken.

Truly, the initial pre-lawsuit demand for rents may persuade the landlord-owner to resolve the delinquency with the association in the face of the potential disturbance of the landlord-tenant relationship. Even if the tenant fails to comply with the demand and/or the owner fails to bring the account current, the association could nonetheless pursue foreclosure remedies and/or seek to have a receiver appointed to specifically enforce the assignment of rents provision.

In sum, if a delinquent homeowner is leasing the property to a tenant, the homeowners association should consider making a pre-lawsuit demand for rent payments. If the association's CC&Rs does not contain an assignment of rents provision, the board of directors should consider amending the CC&Rs to include an appropriate provision. Without

question, the pre-lawsuit demand for rents could provide an excellent opportunity for recovery of unpaid assessments during these difficult economic times.

Brian D. Moreno is a Senior Associate with Richardson & Harman, PC, specializing in the representation of Community Associations and Assessment Collections.

© All Rights Reserved