



Community Association Management Insider®

Helping You Run Your Condo or Homeowners Association Legally and Efficiently

SEPTEMBER 2017

FEATURE

Ensure your association's financial sustainability by undertaking a reserve study that provides a plan for funding the repair and replacement of capital items.

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Use Reserve Study to Keep Contributions at Pace of Deterioration

No matter how high the quality of the homes and amenities in your community is, it's inevitable that over time they'll need maintenance to keep up their appearance and performance. Ultimately, some will need to be replaced—and members will be required to pay for the expense. It's tempting to put off contributing to repairs; members, and especially those who are feeling a financial pinch, might argue that the replacement and maintenance of items that are currently in fine working order is an issue that can be dealt with in the future. Members may have a sense of urgency only about immediate problems that need to be addressed. But that's a losing argument, and one that could spell financial disaster down the road. Four tenets of association living have been time tested:

1. Expenses always happen;
2. The board is responsible;
3. Delays usually get expensive; and
4. Homeowners always get stuck paying the bills.

So what can you do to set your association up for financial stability? A reserve study will identify the components the association is responsible to maintain, calculate the strength of the current reserve fund, and calculate the contributions necessary to fund reserves so these predictable reserve projects can get done on time.

Review Basics of Reserve Accounts

To understand what a reserve study can do for you, it's important to understand the nuts and bolts of association reserve accounts in the first place. Community associations maintain reserve accounts as a way to fund their long-term needs for repair and replacement of major capital items. These items typically include all common property under the association control, such as roads, roofs, swimming pools and pool decks, sidewalks, and clubhouses. Reserves are not intended to fund the association's everyday operating expenses, which are set forth in its annual budget.

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Reserve Study

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Reserves are tied into other serious issues of governance. Properly funded reserves are a critical component of a board's fiduciary duty. Without necessary reserve funding, an association can face painful financial realities that will almost certainly pinch the pockets of current homeowners and negatively affect the value of all the properties in the community. But it can also throw shade on the board's judgment.

For example, if an association has insufficient reserve funds to replace an item in the community, it faces several tough decisions. It may have to enact a substantial assessment increase for the year in which the roof must be replaced, it may be compelled to levy a costly special assessment to fund the replacement, or, even worse, the board may elect to defer necessary replacement to the future, making the replacement even more costly when it finally happens—a decision that indicates the board is not properly handling their duties.

Seek Proper Expertise

Board members are volunteers and, although it's ideal if they bring useful professional experience to the job—for example, if members are accountants, finance professionals, or architects—professionals should be called in for certain projects. A reserve study is an item that should be handled by a specialist. After all, the board, and the community, are looking for an organized, black and white plan to handle repairs and maintenance, and a reserve specialist can provide an objective, accurate strategy. But there are also variables that a specialist will know should be taken into account.

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Reserve Study

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“A reserve study is the art and science of anticipating and preparing for major common area repair and replacement expenses in an association,” says Robert Nordlund, PE, RS, founder and chief executive officer of Association Reserves, a California-based company that performs reserve studies for associations. Collecting from members “as needed” for repairs and replacements just doesn’t work. Major expenses are predictable and boards have a responsibility to run the association in a businesslike, not cavalier, manner, Nordlund stresses. “Guessing or wishful thinking is not an effective plan,” he says about the idea that it’ll be easy to collect maintenance and replacement costs at the time they need to be done.

Keep Process in Perspective

A reserve study will start by identifying the components the association is responsible for maintaining, calculate the current strength of the reserve fund, and calculate the contributions necessary to fund reserves so predictable reserve projects can get done on time. It can show the association whether its reserves have kept pace with deterioration, and offer a plan to make sure that enough money is in the reserve account to do so going forward. Namely, a reserve study will recommend contribution amounts.

While an association might be concerned about the price of a reserve study, generally only one full, detailed study is necessary, with less expensive updates performed periodically thereafter.

Adjust Member Mindset, Craft Payment Plan

Sometimes, board members are shocked when they look at the reserve study, Nordlund notes. He encourages them to see it as a regular expense and not a future expense. “A roof will still fail right on time, whether a board sets aside funds or not,” he points out. But it’s easy for members to rationalize that reserve account contributions are just putting money away for the future. Nordlund emphasizes how important semantics are in this scenario. He couches it in terms of “paying the ongoing bill of deterioration—not putting money away for the future.” He explains that reserve contributions are as real as any other bill, like the cost of electricity or landscaping services. Nordlund tries to equip association managers with the right tools to address reserve contributions. Words, strategies, and numbers are an effective approach, he says.

As far as setting up a realistic plan for members to contribute to reserves, it sometimes helps to increase payments over time until the payments reach the ideal number that’s been identified in the reserve study. When recommended contributions are still too steep, consider the \$10 solution, says Nordlund. For example, if the member monthly reserve contribution is set at \$17, but the reserve study pinpoints \$85 as the necessary number, and members can’t or won’t pay the steeply increased amount, bump it up by \$10. “And plan to do it again the next year, and for a few more years, until gradually the reserve contributions are where they should be,” he says.

“Associations in an underfunded reserve account situation have gotten there over a number of years, and it’s important to remember that it won’t be solved

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Reserve Study

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immediately,” says Nordlund. He points out that giving managers and boards a plan they can implement and reassuring them that they don’t have to solve the problem today, just start heading in the right direction, makes the challenge doable. In that way, reserve studies help the association successfully get to the future by treating reserves as a priority today. ♦

Insider Source

Robert Nordlund, PE, RS: Association Reserves, Inc., 5000 N. Parkway Calabasas, Ste. 308, Calabasas, CA 91302; www.reservestudy.com.

DEALING WITH MEMBERS

Bring Out the Best from Members Campaigning for Board Seat

The 2016 presidential election involved an unprecedented level of negative campaigning for office, including vitriol and attacks on candidates and their political parties. Campaigns aren’t limited to just political office, though. Association boards are comprised of elected members—which means campaigning is something managers will have to help handle.

In most associations, any member in good standing has the right to run for the board of directors. But just because a member follows community rules and pays assessments on time doesn’t mean that he’ll run an above-board campaign and treat his opponents respectfully. While they’re excellent examples of democracy in action, community association campaigns for the board of directors can turn vicious, with candidates using negative speech and advertising to discredit their opponents. And there are other consequences besides candidates having their reputations questioned. Members who become disillusioned by candidates’ immature behavior might withdraw from association life altogether, costing your association qualified volunteers for the board and committees.

Setting a code of campaign conduct and asking all board candidates to voluntarily sign a written pledge to abide by that code can minimize damage to candidates’ reputations and repercussions for your association.

Carefully Consider Using Code

Instead of engaging in a spirited, fair debate about community issues, candidates may resort to name-calling, rumor-mongering, and personal insults. But before you go to the trouble of setting a code of campaign conduct, decide whether such a code is right for your community and understand that to be effective, members must sign a pledge to follow it. Otherwise, they aren’t bound to abide by those rules.

Although enforcing the code against candidates who violate it could be difficult, if it’s written and applied fairly, a code of conduct could have a positive effect on communities. For example, it will make clear to the voting community the types

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of behavior that are and aren't appropriate, which could help discourage inappropriate behavior. Also, setting a code will give first-time candidates a guide to use for their campaign.

Be aware that certain aspects of your code could be subject to interpretation and lead to problems. For example, if the code asks candidates to behave in accordance with basic rules of civility and respect, someone will have to decide what's respectful and what isn't, which could cause problems if others don't agree with that person's decision. You'll have to weigh your options: Even though campaigns can get disorderly and even vicious, setting and enforcing the code could cause a different kind of tension that has the potential to linger long after the campaign is over. Think about whether, in the long run, it's best to let the opposing candidates police the process through their campaign literature and speeches, and let the members decide through their votes whom they want representing them.

Ultimately, you'll have to decide for yourself whether to establish a code of campaign conduct at your community. Your decision will, in part, depend on how badly candidates at your community behave, and what you think the cost of such behavior is to community participation and leadership. Ask your attorney for his or her opinion. He or she may have had personal experience with this type of issue or be able to offer advice about how to draft a code and pledge.

What Pledge, Code Should Say

If you decide to set a code of campaign conduct and to ask candidates to sign a written pledge to abide by it, your pledge, like our *Model Policy: Ask Board Candidates to Sign Code of Conduct*, should ask candidates to follow seven rules during the campaign:

Rule #1: Behave in accordance with basic rules of civility and respect. This is the most important principle to infuse into candidates' campaigns. But your association must be equally diligent in ensuring that all candidates—incumbents as well as challengers—are held to the same standard. Fair enforcement and a true commitment to democratic ideals are essential if you want to transform your community elections into something better than they are now [Policy, par. 1].

Rule #2: Stick to the issues and avoid negative behavior. It's okay for campaigns to be spirited and competitive. But they should focus only on community-related issues. Toward that end, candidates should avoid rumor-mongering, name-calling, and personal insults. If a candidate believes that another candidate is, or has been, involved in wrongdoing, she should be willing to substantiate her allegations before making them public.

But keep in mind that it's equally important for the association to be reasonable in its interpretation of this part of the code. Sometimes, a candidate's character traits are relevant to community issues—for example, if a candidate for treasurer was once convicted of embezzlement. On the other hand, character traits that are personal and unrelated to community issues should be off-limits as campaign topics [Policy, par. 2].

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Rule #3: Include name on campaign material. Just as candidates for public office are required to do, candidates for your association's board of directors should place their names prominently on any campaign material they wish to disseminate. That way, members can consider the source when reviewing such material [Policy, par. 3].

Rule #4: Use membership list for association-related matters only. In most states, members are entitled to access the association's membership list, which usually includes members' contact information, such as their addresses and phone numbers. Sometimes, members run for the board of directors to get this list for other reasons—for example, to sell their business's products. If your state allows members to access the association's membership list, you can give candidates access to the list, but you should ask them to agree to use it for association-related matters only [Policy, par. 4].

Rule #5: Abide by established rules for phone calls, personal visits. Board candidates might want to call or visit association members to get their message out. Some states let associations keep members' phone numbers confidential from other members. Think about prohibiting door-to-door solicitation after a certain hour of night as a security measure, also. If your association has rules regarding phone calls and personal visits, you should ask candidates to agree to abide by them [Policy, par. 5]. Get your attorney's advice before setting any such rules.

Rule #6: Refrain from having other people do things banned by the code. Candidates may try to circumvent their pledge to abide by the code of campaign conduct by asking others to do things that the code bans the candidates from doing. So ask candidates to agree not to do anything through others that they can't do themselves. And ask them to promise that if anyone violates the code of campaign conduct on their behalf, they'll publicly reject that person's support [Policy, par. 6].

Rule #7: Act professionally and courteously at "Meet the Candidates Night." Many associations host a "Meet the Candidates Night" to give candidates a chance to address the community directly and state their case for why they should be elected to the board of directors. Such events can quickly get out of hand if the participants don't conduct themselves in a professional, courteous way. So ask candidates to agree to behave appropriately at such an event. In particular, ask them to agree to remain seated and quiet while other candidates speak [Policy, par. 7].

Don't Force Signature

Setting a code of conduct and asking all board candidates to pledge to follow it may reduce negativity, but remember that you shouldn't try to require candidates to sign it. An association board has no authority to impose requirements for board candidates other than being in good standing, such as agreeing to a set of campaign standards. If you try to force candidates to sign the pledge or you disqualify candidates who refuse to sign the pledge, you may leave the association vulnerable to a lawsuit and maybe even liability.

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So after you write up your pledge and code of campaign conduct, ask candidates to voluntarily sign the pledge. A voluntarily signed pledge should be legally valid, as long as the code included in it is fairly written.

Also, if a candidate refuses to sign the pledge or violates the pledge after signing it, don't publicize that fact to members. If you do, you'll give the appearance that the association is taking sides in the election. But a candidate's refusal to sign the pledge or violation of it after signing it can become an issue for the campaign that other candidates can publicize to the membership. Because such publicity could hurt a candidate's election chances, the threat of it could encourage candidates to sign and follow their pledge.

If your association's governing documents say that the association can regulate campaign behavior (or if you amend your governing documents by a member vote to say so), you could probably require candidates to sign the pledge. But check with your attorney before doing so. ♦

MODEL POLICY

Ask Board Candidates to Sign Code of Conduct

The following Model Pledge, which spells out a code of conduct, asks candidates for the association board of directors to abide by the association's code of campaign conduct. And it recites the components of the association's code of campaign conduct. Show this to your attorney before adapting it for use at your community.

BOARD OF DIRECTORS CANDIDATE PLEDGE

[Insert date]

As a candidate for the ABC Community Association Board of Directors, I promise to abide by the association's Code of Campaign Conduct, as follows:

1. I will behave in accordance with basic rules of civility and respect.
2. I will strive to stick to the issues and avoid rumor-mongering, name-calling, and personal insults.
3. I will not disseminate any campaign material or message in which I am not prominently identified.
4. I will use the association membership list for association-related matters only.
5. I will abide by established rules for phone calls and personal visits.
6. I will not, through other people, do anything that the Code of Campaign Conduct forbids me to do myself. I will publicly repudiate support from any individual or group who does so.
7. I will comport myself at the ABC Community "Meet the Candidates Night" in a professional, courteous manner, including, but not limited to, remaining seated and quiet while other candidates speak.

SIGNATURE _____ DATE _____

PRINT NAME _____

IN THE NEWS

► **Arizona HOA Bristles at Artificial Turf**

Many people are switching from real grass landscapes to artificial turf because of lower water usage and less maintenance. Residents of one Arizona homeowners association who switched to artificial turf cited the climate—specifically scorching sun and temperatures—as making it nearly impossible to grow green, healthy grass year-round; others were concerned about water bills. Homeowners at this association are required to have 50 percent of the front yard and 50 percent of the backyard covered by grass, and two trees, which can use large amounts of water.

But after some residents installed the fake grass, they learned that it went against the association's design guidelines. Even though the city offers rebates for low water use landscaping, the association rules provide that any type of artificial flower, plant, tree, or turf is not permitted when it's visible from a neighboring property.

A neighbor who put the synthetic grass in his backyard, which was allowed because it's out of view, said his water bill went down 50 percent. A petition that's currently circulating has several signatures, but residents who have gone to war with the association have lost in the past. One homeowner spent \$40,000 on a court battle that he lost.

Arizona state senator John Kavanagh has gone to bat for residents. He introduced a bill last session saying that HOAs couldn't prohibit artificial grass, but "the association may reject or require the removal of a member's artificial grass if the artificial grass creates a health or safety issue that the member does not correct." The bill died in committee.

The association has taken the position that a member in an association has entered into a contractual relationship, and should obey the rules no matter what. Senator Kavanagh said he may try to introduce the bill again once committee leadership changes.

► **Flag Mailbox Puts Spotlight on HOA's Violation Notification Process**

A mailbox decorated like an American flag is causing two kinds of controversy within a Florida homeowners association. The 82-year-old owner of the mailbox—a retired Navy veteran—was upset when the association sent him a letter apprising him that the mailbox violated a covenant and was allegedly reducing property values. The homeowner is gearing up for a fight with the association, which he has accused of bullying him.

For its part, the association claims that there are ongoing conversations regarding the issue and that the association isn't unpatriotic, but rather honors

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servicemen and women. It pointed out that homeowners are permitted to fly two flags at their properties: an American flag and a U.S. military flag.

The homeowner stated that he isn't just upset by being asked to remove the flag. He is also offended at the method the association uses to notify covenant violators. He noted that the letter he received made him feel as if he were going to jail for the violation. He says that he wishes the first step when a homeowner is doing something wrong is to have an informal discussion. ♦

DEALING WITH CONTRACTORS**How to Negotiate a Favorable Laundry-Room Service Contract**

Some condominium buildings have a shared, central laundry room for members, instead of washing and drying appliances in units. Even in planned communities with freestanding homes, the association may decide to use a common laundry room. But it's not as easy as buying washers and dryers and installing some method for charging members for the services. It's more involved than that. Having a well-maintained laundry room in a condominium building or a community is important for both residents and associations. Associations benefit from ancillary income, and members don't have to find off-site laundromats, where they may have to spend hours waiting for machines.

But a laundry room can quickly turn into a management headache if machines break down, service calls are ignored, and members start complaining. As a result, engaging a service provider to handle your community's laundry facility is an important process, and the contract you negotiate should be thorough. It should outline the expectations of both parties during the time period of the contract, including maintenance, service, and payment.

The money you may earn is an important negotiating point. Most laundry-room contracts are on a concession basis. This means that the laundry-room service company installs the machines at its own expense and pays you a flat fee, a percentage of the receipts, or a flat fee plus a percentage of the "override." The association pays for the utilities. Typical leases are five to 10 years in length, and the term is mostly driven by the equipment cost and the return that the laundry company can expect from collections.

But besides money, there are many other critical factors to raise and resolve when negotiating with a laundry-room service company. You will need a specific agreement written for the particular needs of your community. The following are some important points to consider when negotiating a laundry-room service contract.

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Consider Ancillary Uses to Laundry Room

Laundry rooms may be used not only for washing and drying. If you negotiate a contract with only these activities in mind, you may forgo other potentially profitable activities that you, or someone else, could perform.

When members spend time in the laundry room, they may get hungry and thirsty. Or they may get bored waiting and may want to buy a newspaper or a paperback. Of course, there are vending machines that will satisfy these members. If your service contract grants the laundry company unrestricted use of the laundry room, you may not be allowed to participate in these potentially lucrative activities.

Choose Convenient Location

The operator may push for a central location for your laundry room because it's easier to service the machines. But the association has to consider what's convenient for the members. If the community is spread out over multiple buildings such as in a townhouse garden-style arrangement, you may want to provide laundry facilities at each building, rather than in one centrally located laundry room. Or if you manage a large high-rise condominium, you may want to provide laundry facilities on every floor or in several locations in the building.

Ensure Sufficient Number of Machines

Be aware that a laundry-room service company may want to reduce its initial capital outlay by installing fewer machines. The operator may offer you a higher percentage of the gross if he puts in fewer machines. While this may give you an immediate benefit, it's not a good idea for the community in the long term. With too few machines, members will eventually get fed up with waiting for machines and take their laundry elsewhere. Also, these machines will wear down faster. This will create more of an inconvenience to you and your members due to increased service calls from malfunctioning machines.

It's important to have the correct ratio of equipment to members. This will depend on both the size of your community and its member profile. Working-class families and families with children may do five or more loads of wash each week, while young professionals send more clothing to the dry cleaner. Elderly members, who are less active, may do only one load of laundry per week.

Get Speedy Service Commitment

The biggest complaint you're likely to get from members about your laundry room is that the machines break down too often. Since breakdowns are inevitable, the length of time it takes the company to respond to your repair call is crucial.

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In negotiating a laundry-room contract, a solid maintenance and service agreement is more important than the amount of revenue you'll receive. Don't settle for less than a 48-hour response time.

Your contract should contain a clause defining "satisfactory" service in terms of response hours and specifying what action you should take if this time isn't met. If the time isn't met, give the company notification of a default of the contract by certified mail. The end result should be that you have the ability to cancel the contract if the service company doesn't meet the specified terms.

Negotiate Rate Control, Refunds

One thing that may seem small but is a great source of annoyance to members is losing money in the washer or dryer and having to wait three weeks to get a check for 75 cents from the operator. The operator should give the association manager the authority to make on-the-spot refunds to members on its behalf.

You'll also want some control over cost increases to the members. Most laundry-room service companies will want total control over this provision, but you can ask for a mutual-consent clause. The operator will then have to get your approval before it increases prices on the machines.

Get Paid Monthly

Frequency of collection is also important. Some laundry-room service companies won't formally agree to a specified frequency of payments and may even try to pay you rent only once a year. But every month is ideal, since collections are made at least that frequently.

Beware of any contract provision that suspends rent payments to you if collections fall below a set dollar amount per machine per day. Since you're giving a laundry-room service company the privilege of using your space on a continuous basis, it should pay you regularly, without interruption.

Require Adequate Liability Insurance

Make sure the operator carries liability insurance over and above what's provided for in your association's insurance policy. If the laundry-room equipment malfunctions and causes a flood, you want to be sure you're fully compensated for damages that may have occurred to your building's structure.

Beware of Automatic-Renewal Trap

Most laundry-room service contracts contain automatic-renewal clauses. With these clauses, unless, before a specified deadline, you notify the operator that you don't want to renew, the contract is automatically renewed. Your notification usually must be received a certain number of days or months before the contract is set to expire.

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The problem with such “negative option” arrangements is that you’re likely to overlook the deadline. As a result, you’re trapped into an automatic renewal. That may be for one additional term. Or, in some contracts, automatic renewal can recur indefinitely, term after term, as long as you keep forgetting to say no by each successive deadline. Obviously, if you’re dissatisfied with your laundry-room service company, or just want the freedom to get competitive bids, automatic renewal is a big problem.

To complicate matters, some operators will seek not only automatic renewal, but also a right of first refusal. Thus, even if you do prevent the contract from renewing, the operator has the right to continue providing laundry service for another contract term if he can match any competitive bid you may have obtained from another company.

Check with your lawyer to see whether automatic-renewal clauses are enforceable. New York, for example, has a law that invalidates such clauses unless the company gives you proper advance notification that a deadline is coming up and warns you to exercise your rights.

If you do agree to an automatic-renewal provision, make sure it gives you ample opportunity to cancel service before the contract ends. Give yourself at least 30 to 90 days to find another laundry-room service company with which you can do business. ♦