

A Property Manager's Liability for Acts of Owners or Asset Managers

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We are occasionally confronted with the issue of whether or not a property manager can be liable for the

acts or omissions of the owner or asset manager. The issue often arises when a tenant makes a claim such as: damage to personal property caused by unrepaired roof leaks, loss of business income due to failure to make repairs, and, most frequently, for failure to timely and properly refund a security deposit.

HOW TO PROTECT YOURSELF

There are a few ways a property manager can protect against these risks. First, request that each lease require the tenant to name you, the property manager, as an additional insured on their liability policy. Also ask the owner to give you the same coverage. Don't forget to follow up and make sure the coverage is actually in place throughout the entire lease term.

The best form of protection for many of these claims, other than the insurance mentioned above, is a strong indemnification provision in your property-management agreement. A good indemnity places financial responsibility on the owner or asset manager for wrongs they cause. The indemnity should also protect the landlord and property manager for any tenants' acts that injure a third party. However, because of economics and bargaining

power, or the lack of it, indemnification agreements are often one-sided in favor of the owner or asset manager. Worse yet, they are often not properly drafted. The bottom line is that often the property manager is saddled with risks that are not within their control. This could leave the property manager out in the cold if a claim arises.

REFUNDING A SECURITY DEPOSIT

Typically, the owner holds the security deposit and is the final arbiter of whether all or a portion will be refunded. This decision is usually based on the property manager's walk-thru of the premises and a collection of bids for any repair work. As a result of the property manager's involvement, the risk of sanctions for violations of applicable law should be shifted to the owner or asset manager when decisions are made that are not consistent with the reporting of the property manager.

Most property managers are familiar with the Texas Property Code's requirements to refund a security deposit upon lease expiration. If you are not, you need to

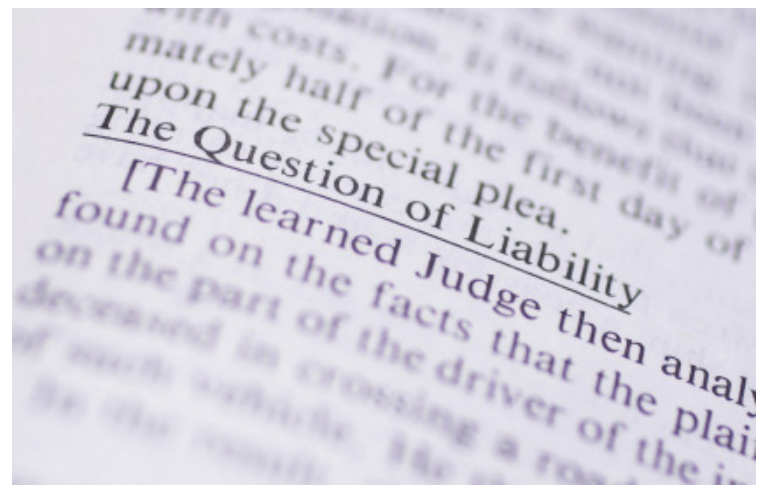
be. Following is a summary of these sections. Take note of the provisions that insulate property managers from liability, and impose sanctions

against the landlord for failure to comply. These provisions should be read in conjunction with the indemnity clauses in the property-management agreement

TYPICAL ALLEGED VIOLATIONS OF TEXAS PROPERTY CODE ANN. §93.005 REGARDING SECURITY DEPOSIT RETURNS

The most commonly alleged violations of Property Code Sections 93.005 include: (a) a failure to return the security deposit to a commercial tenant before the 60th day after the tenant vacated the Property; (b) a deduction of amounts from the security deposit for items which were "normal wear and tear"; and (c) a failure to provide an itemized list of deductions. The penalties for violation of the statute are three times the amount of security deposit wrongfully withheld, plus \$100 and payment of the tenant's attorney's fees. In order for a tenant to show that a property manager directly violated the Property Code, the tenant must show: (a) the property manager was a "landlord"; (b) tenant provided the security deposit to the property manager;

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(c) the property manager had an obligation to return the security deposit to the tenant; (d) the property manager unlawfully deducted amounts from the security deposit for "normal wear and tear"; (e) the property failed to timely return the security deposit to tenant; and (f) the property manager failed to timely provide an itemized list of deductions to the tenant. Since the property manager is not the landlord but may be the landlord's agent, the most likely source of liability for a property manager is the indemnification of the owner who is a landlord and is the person statutorily responsible for returning the deposit.

FIRST LINE OF DEFENSE: THE LEASE

It is advisable that all your owners' form leases contain a waiver of the requirements and applicability of Tex. Prop. Code §§ 93.005 - 93.011, and only obligates the landlord to return to the tenant the balance of the security deposit not applied to satisfy the tenant's obligations within a reasonable time after the term ends and only if the tenant has performed all of its obligations under the lease. This will override the statutory time scheme.

SECOND LINE OF DEFENSE: THE PROPERTY CODE

The Texas Property Code provides a defense to such claims unless the lease is drafted in such a manner as to make the property manager a "de facto" landlord. The code, in Section 93.001 (a), provides that its requirements apply only to the relationship between landlords and tenants of commercial rental property so a property manager should have no direct liability for failure

to return the deposit. Also, Section 93.005 provides that notice of the tenant's forwarding address can be sent to either the landlord or the landlord's agent which shows the Texas legislature distinguished between the landlord and the property manager.

OTHER ISSUES

Many times owners will forgo security deposits for letters of credit. This is a critical area of potential liability for a property manager. Letters of credit can be advantageous to a landlord (instead of a security deposit) in certain situations, like when the tenant files bankruptcy. The liability can arise in a number of areas:

(i) making sure the letter of credit is actually issued and received before the tenant is allowed to occupy the space; (ii) making sure any replacement letters of credit are timely obtained; (iii) reacting to a notice that a letter of credit will not be renewed by the issuing bank; and (iv) not sending a notice to the bank before each expiration inquiring if the letter of credit will be renewed. It is this last item that has been the subject of litigation since in some cases the notices sent by the issuer of the letter of credit that stated the bank would not renew were not received by the property manager. The property manager's obligations with respect to the receipt and management of letters of credit should be specifically spelled out in the property management agreement so that each party to it will know who is responsible for what actions. It is also important to establish a reliable calendar or "tickler" system to keep track of important dates, such as expiration dates for letters of credit, or deadlines to return the security deposit to a tenant.

IREM CALENDAR



JUNE 14, 2011

Membership Luncheon
Doubletree Hotel
LBJ & Midway Road

JUNE 20-23, 2011

Track B – Property Operations II
Spectrum Center
5080 Spectrum Drive #122W
Addison, TX 75001

JUNE 24, 2011

ACoM Exam
Spectrum Center
5080 Spectrum Drive #122W
Addison, TX 75001

**NO LUNCHEONS IN
JULY & AUGUST**

AUGUST 15-19, 2011

Track C – Asset Analysis
Spectrum Center
5080 Spectrum Drive #122W
Addison, TX 75001

AUGUST 26, 2011

IREM® On-Site Open
Bridlewood Golf Club
Flower Mound, TX
10 am shotgun start

SEPTEMBER 13, 2011

Membership Luncheon
Maggiano's NorthPark

OCTOBER 11, 2011

Membership Luncheon
Location TBA

OCTOBER 17-21, 2011

Track D – Capstone Courses
Spectrum Center
5080 Spectrum Drive #122W
Addison, TX 75001

OCTOBER 21, 2011

CPM® Exam
Spectrum Center
5080 Spectrum Drive #122W
Addison, TX 75001