



HOW BIG IS YOUR BAD DEBT PROBLEM?

SECURITY DEPOSIT ALTERNATIVES CUT UNRECOVERABLE LOSSES

By Brian Alexander of SureDeposit

Rental owners suffered over \$1 billion in bad debt losses in 2004 alone. That means for a typical 250-unit property, it is common to see bad debt write-offs of \$18,000 each year, and much more in many cases. That's a staggering amount of money for a property and the industry to leave on the table under the wrongful assumption that there is little that owners could actually have done to adequately protect themselves against such losses.

For too long, owners have merely resigned themselves to the fact that a certain percentage of all move-outs lead to bad debt. In fact, 12% do. They also have had to live with the reality that only 18% of all money referred to collections agencies is recovered and can take up to 5 years to recoup.

Apartment owners of more than 3,300 communities nationwide, however, have learned that they do not have to take bad debt lying down. By offering residents a security deposit alternative at move-in as an option in place of a traditional security deposit, these owners have learned that they are much better protected against financial losses from damage to a unit or skipped rent. The most widely accepted form of a security deposit alternative is found in the form of a surety bond and is in place at more than one million units across the country.

How do security deposit alternatives work? At lease signing, the renter is given the option to purchase either the surety bond or pay the traditional security deposit. To select the security deposit alternative the prospective resident signs a short form acknowledging the purchase of the bond and makes payment directly to the surety. The surety in turn assures the property owner or management firm that the renter will fulfill the lease obligations at the end of the lease term.

The security deposit alternative offers the owner a minimum coverage of \$500, with coverage in \$250 increments thereafter, providing the owner with the flexibility to set a bond level appropriate to local market conditions and to the perceived credit risk of the prospective resident. For example, for \$500 worth of coverage, the resident need only pay an \$87.50 security deposit alternative premium.

The one-time, non-refundable premium remains in effect for as long as the renter resides at the leased apartment. In addition, the bond continues to provide coverage at no additional cost if the renter moves to another apartment within the owner or management firm's portfolio anywhere in the country.

If the resident meets his rental obligations and returns the apartment in good condition, he moves out without further obligation. If, however, the apartment suffers physical or monetary damages at move-out, the owner files a claim with the surety for direct payment. The surety then collects reimbursement for the claim from the resident, who, under the terms of the bond, remains fully liable for his lease obligations. As part of the claims procedure, the surety assumes all collection and recovery activity, saving owners and managers valuable human resources and administrative time.

The benefits of security deposit alternatives to owners can be substantial. The security deposit alternative discourages renters from failing to pay their rent or leaving their units in poor condition when they move out. This is because the renter remains fully liable for his lease obligations under the terms of the surety bond. In addition, the resident's lower up-front costs required to move into a new apartment make it easier for a leasing agent to close the sale. But arguably, the most dramatic benefit to owners can be found in their enhanced level of protection and the subsequent and significant impact on a property's bottom line, particularly in markets where requiring full cash deposits puts a property at a competitive disadvantage.

According to Cameron Omoto, Program Manager for Alliance Residential Company, which has already deployed security deposit alternatives throughout 40% of its portfolio to date, "Security deposit alternatives are a no-lose proposition, especially in softer markets where move-in specials prevail. Our bad debt picture has markedly improved."

The claims process typically associated with security deposit alternatives is superior to the old collections methods. The speed with which claims are reimbursed and the lessened administrative burden are also key benefits to the owner. Some multifamily companies report that SureDeposit's security deposit alternative program saves them two or more hours per file to dispose of a case.

From a pure dollars and cents standpoint, security deposit alternatives give property owners more ammunition to combat bad debt. Since the premiums for the surety bond paid by the renters are pooled, property owners are left with a higher level of payment assurance than a single security deposit of a lesser amount. The premiums, coupled with the amount that is recovered from the resident by the surety in the event of a claim exceeds the amount recovered from the resident alone to cover the claim with the use of a reduced security deposit.

Improving a property's NOI has become a greater business imperative to both onsite staff and the corporate office alike. Security deposit alternatives can play a critical role in helping property owners recover bad debt for a healthier NOI.

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Brian Alexander is the regional marketing director for the western region of SureDeposit.

With more than one million units in nearly 3,300 communities under agreement, SureDeposit is the nation's leading provider of alternatives to traditional security deposits.

For more information, call 1-800-531-SURE (7873), or visit online at www.suredeposit.com.

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