



Past Due Rent - The Real Estate Implications

by Chris Hitler

"I wish buying and selling real estate was easier" is a common sentiment I hear from my clients as they engage in the transaction process to buy or sell a storage facility. Consummating a real estate deal is tough. Besides agreeing on the most salient transaction terms such as price, earnest money, and financing, there are less prominent details that have to be sorted out. One of these items is past due rent – who gets to keep it, the Buyer or the Seller?

There are a few approaches to resolve this issue. The first two offer a clean break at closing:

1. Give the Seller a credit of a fixed amount

The benefit of this approach is both transparency and definitiveness. Both Buyer and Seller know exactly what will be credited at closing. The downside is the high potential of unfairness. One side gets compensated more than is actually collected.

2. Give the Seller a percentage of past due rent at closing

Although this approach is not quite as definitive as the previous one (i.e., knowing exactly what will be credited to the Seller), transparency is good because Buyer and Seller know how the credit will be calculated and it reduces the risk of over/under crediting the Seller.

At the other end of the spectrum are two options that focus on fairness while sacrificing transparency and expediency:

3. Buyer passes on to Seller all collected past due rent

From a fairness perspective, Seller gets only what has been paid. Unfortunately the Buyer has no incentive to collect past due rent since it will be given to the Seller. Furthermore, the Buyer may consider every tenant current the day of closing and simply ignore past due amounts thus eliminating the chance for the Seller to collect anything.

4. Buyer passes on to Seller past due rent collected within 30 days of closing, but keeps anything collected after 30 days

Although the Buyer has an incentive to collect past due rent, this incentive may not necessarily help the Seller because the Buyer may choose to wait until the 30 days are up before trying to collect.

There are numerous other approaches and none are perfect. They all have benefits and tradeoffs. One way to mitigate the amount of past due rent (assuming tenants are on a First of the Month rent payment schedule) is to be strategic about the timing of when the deal closes. Picking a closing date after the first of the month will cause a high percentage of tenants to still owe rent for the month. Conversely, closing a deal towards the end of the month greatly reduces the percentage of tenants still owing rent for the month.

The more fundamental mitigating approach and frankly, just good business, is to consistently stay on top of your tenants and not let

them fall behind on their rent. So, how do good storage operators keep tenants current?

1. Contact them: Send letters, postcards, emails, text messages and get on the phone. Having a sense of urgency can be contagious with your tenants.

2. Be empathetic but firm: A willingness to listen goes a long way to getting your rent paid versus some other bill. However that should be coupled with being clear on the cost and consequences of not paying rent on time.

3. Follow through on consequences: Rather than waive late fees, make tenants pay them and ultimately use your lien rights and conduct auctions if tenants fail to meet their contractual obligations.

Fortunately steps 1 and 2 go a long way in keeping tenants current, but if you are forced to conduct a lien sale you will want to take steps to maximize the storage unit's auction price:

- **Advertise the event:** the price a unit sells for is directly correlated with the number of Buyers attending the auction. Post a sign at the facility; put a notice on your website; and most importantly advertise on a storage auction marketing website where thousands of savvy Auction Buyers have begun to look for lien sales.
- **Provide some advance notice:** Posting an auction ad the day before will not help your cause. Auction Buyers need time to organize their schedule to ensure they are available, so get the advertising in place at least one to two weeks in advance.
- **Be transparent:** Notify Auction Buyers when units and especially the entire auction get canceled. Many Auction Buyers are professionals and showing up to an auction unnecessarily wastes their time and money. Fortunately a good storage auction marketing website can do notifications automatically so you can spend time on more pressing issues like marketing your facility to new customers.

Staying on top of receivables is a critical task for any Owner. It can also ensure you get the maximum amount in your pocket when it comes time to hand over the reins to a new owner and reduce the chance a deal may be tripped up over a relatively small issue like who gets the past due rent. **MM**

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