

Modern Real Estate Practice in Illinois, 6th Edition
Filmore W. Galaty, Wellington J. Allaway, Robert C. Kyle
Laurie MacDougal, Consulting Editor

Chapter 18: Property Management

Learning Objectives

After reading this chapter, students should be able to:

- Identify the basic elements of a management agreement.
- Describe a property manager's functions.
- Explain the role of environmental regulations and the Americans with Disabilities Act in the property manager's job.
- Distinguish the various types of insurance alternatives.
- Define the following key terms: Americans with Disabilities Act; construction life cycle costing; management agreement; multiperil policies; property manager; risk management; surety bonds; tenant improvements; workers' compensation acts.

Why Learn About Property Management?

There are more than six billion square feet of commercial real estate in the United States, and each and every one of those square feet is managed by a property manager or a property management company. That's a lot of responsibility. If you plan a career in property management, the reason you need to know the information in this chapter is obvious: it's your job description. But, even if you don't plan to become a property manager, you may find yourself managing properties on a temporary basis anyway. Even if you never manage a property, you may well have an office in a building that is managed by a property manager. Knowing what his or her responsibilities are will help you protect your business interests.

Suggested Items to Bring To Class

1. Copies of sample property management agreements from various sources so that they can be compared.
2. Information on professional property management associations, their membership requirements, designations, educational programs, etc.
3. Copies of professional associations' building inspection checklists, maintenance schedules, maintenance reports and other documents used in the property management function.
4. Sample insurance policies from various sources so that they can be compared for their similarities and their differences.

Lecture Outline

I. The Property Manager

Property management involves the leasing, managing, marketing, and maintenance of real estate. The property manager has three principal responsibilities: financial management, physical management, and administrative management.

- The property manager is responsible for maintaining the owner's investment and making sure the property earns income.

IN ILLINOIS...*property managers must be licensed real estate brokers. This is because they engage in rent collections, lease and rental negotiations, and the procuring of tenants among other functions. However, the Illinois Real Estate License Act specifically exempts resident managers of apartment buildings, duplexes and apartment complexes from licensure requirements when their primary residence is on the premises being managed.*

Illinois permits individuals whose real estate practice is limited to leasing or renting residential property, collecting rent, negotiating leases and similar activities to obtain a special leasing agent license instead of the broader-scope broker or salesperson license.

A. The Management Agreement

Creates an agency relationship between the owner and the property manager: the property manager is considered the owner's general agent.

- The manager's first responsibility is to realize the highest return on the property in a manner consistent with the owner's instructions.

B. Rental Commissions

Residential property managers often earn commissions based on the property's annual rent.

II. Management Functions

A. Budgeting Expenses

The property manager should develop an operating budget that is based on anticipated revenues, expenses, and the owner's long-term goals and includes allocations for fixed expenses and a cash reserve for variable expenses.

1. Capital expenditures

The manager should budget money to cover costs of modernization or remodeling. The expenses may be spread over several years.

B. Renting the Property

Effective rental of the property is essential, but the manager must primarily be concerned with the long-term financial health of the property.

1. Setting rental rates

Rental rates are influenced by supply and demand. The rental income must:

- be sufficient to cover the property's fixed charges and operating expenses.
 - provide a fair return on the owner's investment.
 - be in line with prevailing rates in comparable buildings.
- a. Current vacancy rate** is an indicator of how much of a rent increase is advisable.

2. The rental rate for residential space is usually stated as the monthly rate per unit, while commercial leases are usually stated according to either annual or monthly rates per square foot.

C. Selecting Tenants

The manager should be sure that the premises are suitable for a tenant in size, location, and amenities and that the tenant is able to pay for the space.

- If a commercial tenant is likely to expand in the future, the manager should consider the property's potential for expansion.
- The residential property manager must comply with all federal, state, and local fair housing laws in selecting tenants.

1. Collecting rents

A property manager should accept only those tenants who can be expected to meet their financial obligations.

- The terms of rental payment should be spelled out in the lease agreement.

D. Maintaining Good Relations with Tenants

A high tenant turnover rate results in greater expenses for advertising and redecorating. It also means less profit for the owner due to uncollected rents.

E. Maintaining the Property

To maintain the property efficiently, the manager must be able to assess the building's needs and how best to meet them.

1. Preventive maintenance includes regularly scheduled activities such as painting and seasonal servicing of appliances and systems.

2. **Repair or corrective maintenance involves the actual repairs that keep the building's equipment, utilities, and amenities functioning.**
3. **Routine maintenance includes such day-to-day duties as cleaning common areas, performing minor carpentry and plumbing adjustments and providing regularly scheduled upkeep of heating, air conditioning, and landscaping.**
4. **Construction**

Commercial or industrial property managers may have to make tenant improvements (alterations to the interior of the building to meet a tenant's particular space needs). The renovation of a building often enhances the building's marketability and increases its potential income.

F. Handling Environmental Concerns

A variety of environmental issues, from waste disposal to air quality, must be addressed by the property manager.

G. The Americans with Disabilities Act

- Title I of the ADA provides for the employment of qualified job applicants regardless of their disability.
- Title III of the ADA prohibits discrimination in commercial properties.
- The ADA recommends reasonably achievable accommodations to provide access to the facilities and services.

III. Risk Management

One of the most critical areas of responsibility for a property manager is risk management. The property manager must decide whether it is better to avoid, control, transfer, or retain a risk.

A. Security of Tenants

Recent court decisions have held owners and their agents responsible for physical harm that was inflicted on tenants by intruders.

B. Types of Insurance

Some common types of coverage are:

- Fire and hazard: coverage against direct loss or damage to property from a fire or other hazards such as windstorm, hail, smoke damage, or civil insurrection.
- Consequential loss, use, and occupancy: covers the consequences of a disaster including the loss of rent or revenue.

- Contents and personal property: covers building contents and personal property during periods when they are not on the premises.
- Liability: covers the risks assumed when the public enters the building.
- Workers' compensation: covers claims for medical or hospital payments for injuries sustained by building employees hurt in the course of their employment.
- Casualty: coverage against theft, burglary, vandalism, and machinery damage as well as health and accident insurance.
- Surety bonds: cover an owner against financial losses resulting from an employee's criminal acts or negligence while performing assigned duties.
- Multiperil policies: an insurance package that includes standard types of commercial coverage, such as fire, hazard, public liability, and casualty.

C. Claims

Two methods can determine the amount of a claim under an insurance policy:

- Depreciated or actual cash value: the property is insured for what it was originally worth, less depreciation.
- Current replacement cost: the property is insured for what it would cost to rebuild or replace it today.

IV. The Management Profession

- Most metropolitan areas have local associations of building and property owners and managers that are affiliates of regional and national associations.

Discussion Questions

1. What types of property management firms, or departments within real estate or other firms, are located in your area?
2. How would you evaluate a property manager? By looking at the physical condition of the buildings managed? By interviewing tenants in these buildings? By examining the books or the management agreements for these properties? Are these all valid methods to use in finding a property manager?

Classroom Exercises

1. Have small groups of your students discuss the similarities and differences in the property management agreements you have brought to the classroom.
2. Arrange to have someone from a local IREM or BOMA chapter speak with your class about the property management profession.
3. Arrange to have an insurance representative speak with your class about the types of coverage required on investment properties.