CP-15 – Leasing and Property Management

(Recodification adoption June 7, 2022: CP-27 Commission Position on the Performance of Residential Leasing and Property Management Functions recodified to CP 15 - Leasing and Property Management)

Property Management is one of the leading sources of complaints received by the Commission. This position statement is designed to identify common issues in Property Management found during a complaint investigation or an audit; however, it does not encompass all potential issues associated with Property Management. Any Broker interested in performing Property Management Services is strongly encouraged to complete educational offerings specific to Property Management, co-list with a Broker experienced in Property Management, and familiarize themselves with Chapter 5 of the Commission Rules.

State and local laws have been rapidly evolving with regard to the obligations and rights of landlords and tenants. Significant modifications that were adopted in 2021 include restrictions on late fees (*see* C.R.S. § 38-12-105) and monetary penalties for violating these restrictions. There are also limitations on a landlord's ability to increase rents (*see* C.R.S. § 38-12-702) and specific prohibitions on certain lease provisions (*see* C.R.S. § 38-12-801). There are also statutory penalties for unlawfully removing a tenant from a property. (*see* C.R.S. § 38-12-510). These are only a sampling of revised state guidelines and several jurisdictions, including Boulder and Denver, have specific licensing requirements for rentals and additional notice requirements.

License Requirements:

Pursuant to section 12-10-201(6), C.R.S., the leasing and subsequent management of real estate for a fee or compensation is included among the activities for which a License is required. Given the rapidly evolving law, the number of complaints received, and the issues identified in investigations and audits, the Commission considers Property Management to be a complex area of practice. Section 12-10-217(1)(q), C.R.S., and Rule 6.2. require that a Broker be worthy and competent when providing Real Estate Brokerage Services. If the Broker does not have the competency necessary to fulfill and perform leasing and/or subsequent management of the real estate, the Broker must comply with Rule 6.2.B. before providing such Real Estate Brokerage Services. Property Management Services must be performed and contracted in the name of the Brokerage Firm. A Broker who agrees to lease a property or perform Property Management Services must review the Brokerage Firm's Office Policy Manual, and have permission from the Broker's Employing Broker. Similarly, the Employing Broker has the responsibility to ensure that they are also competent to supervise an Associate Broker that performs leasing and/or Property Management Services.

Leasing v. Property Management:

While leasing and Property Management are similar, they are two distinctively different services. Leasing is a one-time activity in which the Broker acts as a special agent, while Property Management is an ongoing relationship in which the Broker is a general agent. If a Broker is performing leasing with a Commission-Approved Exclusive Right-to-Lease Listing Contract, the Broker may list a property for lease, advertise the property, help screen tenants, and/or help negotiate a lease. The lease should be signed by the owner and tenant. Once the lease is signed, the Broker's duty/relationship with the owner or tenant is over. Conversely, with Property Management, a Broker's obligations continue beyond the formation of the lease. Therefore,

a Broker performing Property Management Services may also perform leasing services. A Broker who only performs leasing services is not performing Property Management Services.

Generally, a Broker will function in one of three capacities with regards to rental properties. In the first scenario, the Broker may provide leasing services only for an owner where the Broker is involved in procuring a tenant and negotiating the lease terms (i.e., Commission-Approved Exclusive Right-to-Lease Listing Contract). In the second scenario, the Broker may provide leasing services on behalf of the tenant in locating a suitable rental property and negotiating a lease (i.e., Commission-Approved Exclusive Tenant Listing Contract). In the third scenario, the Broker agrees to provide leasing services and is also responsible for one or more of the following: maintaining the property's physical condition, communicating with tenants, collecting rent, and/or collecting security deposits (i.e., Management Agreement and Commission-Approved Brokerage Duties Addendum to Property Management Agreement). In the first two scenarios, the Broker's services are completed once the lease is executed and thereafter the Broker is not involved in the transaction any further. In the third scenario, the Broker's duties are ongoing; therefore, the Broker is conducting Property Management Services. Regardless of whether the Broker is working with the owner or the tenant, the Broker must establish clear expectations regarding the services the Broker agrees to provide and communicate these expectations to the Consumer.

Supervision:

Before engaging in Property Management or leasing, the Associate Broker must discuss with their Employing Broker whether the Associate Broker is capable of and allowed to perform Property Management or leasing services. The Brokerage Firm is responsible for maintaining all Trust or Escrow Accounts and all transaction records, and the Employing Broker is responsible for exercising authority, direction, and control over the Associate Broker's conformance to statutes and Commission Rules. (*see* Rule 6.3.). This includes ensuring all contracts are reviewed to maintain assurance of competent preparation and ensuring all transaction files are reviewed for the required documents. If the Employing Broker does not allow Brokers to perform leasing and/or Property Management Services as part of their employment and in the name of the Brokerage Firm, the Office Policy Manual should clearly state that the Broker needs to refrain from leasing and/or Property Management Services or seek employment elsewhere. If the Brokerage Firm does allow leasing and/or Property Management, regardless of how minor, the Employing Broker must ensure that the Office Policy Manual addresses these activities, including management of the Associate Broker's own property. (*see* Rule 5.11.). Both the Associate Broker and the Employing Broker need to be aware of state and local laws that impact the performance of Property Management Services, which include, but are not limited to, laws about security deposits, habitability, carbon monoxide alarms, asbestos, lead-based paint, handling of confidential information, zoning, and agency.

Forms:

A Broker may complete Standard Forms pursuant to section 12-10-403(4)(a), C.R.S., and as set forth in Rule 7.1. including those promulgated by the Commission. The appropriate disclosure document must be provided to the owner or tenant before performing Real Estate Brokerage Services for the owner or the tenant.

There are no Commission-Approved leases or Management Agreements. These forms must be drafted by an attorney engaged by the specific Brokerage Firm as set forth in Rule 7.1.B. Therefore, obtaining and using a copy of a Management Agreement and/or lease from another Brokerage Firm does not comply with the requirements that these forms be drafted by an attorney. However, if the owner provides the lease, as set forth in Rule 7.1.C. (i.e., Client Form), the Broker must maintain written confirmation that the lease form was provided by the owner. In all situations, Brokers need to provide copies of executed contracts to the Consumers. Tenants need to be provided with copies of leases and owners need to be provided with copies of the Management Agreements.

Brokers performing leasing services for either an owner or a tenant may draft Letters of Intent (e.g., Brokers specializing in Commercial Real Estate); however, the Letter of Intent must comply with Rule 7.1.H. which states that the Letter of Intent is nonbinding and that the form has not been approved by the Commission.

If the Broker is going to provide Property Management Services, the Broker needs to provide a Management Agreement drafted by a licensed Colorado attorney. The Management Agreement should outline the duties and responsibilities of both parties. The Management Agreement should, at the very least, address:

- Duration of the relationship;
- The parties;
- Identify the lease form (i.e., Attorney Form or Client Form);
- Identify the authority to execute leases (i.e., Owner or Broker);
- Identify the property to be managed;
- General duties performed by the Broker, including interior walk-through expectations and exterior drive-by expectations;
- Fees for the manager's services, including disclosure of any mark-ups. (*see* Rule 5.17.). Before a mark-up can be charged, the Broker must obtain prior written consent to assess and receive mark-ups and/or other compensation for services performed by any third party or affiliated business entity;
- A unilateral clause allowing fee changes are prohibited;
- Tenant selection criteria. If the decision to lease will be based on criminal history or financial worthiness, the Management Agreement should indicate who is responsible for collecting this data and what sources will be used. Be aware of the restrictions on screening of tenants laid out in the Rental Fairness Act. (*see* C.R.S. § 38-12-901). Additionally, the Broker must ensure compliance with the Fair Housing and Fair Credit Acts;
- Posting of eviction notices. If a Forcible Entry and Detainer (also known as an eviction) is necessary, an attorney should represent the owner or Broker in the filing of the Forcible Entry and Detainer. Special attention should be given to any local requirements that may be in effect, that

modify the eviction process. A Broker that files a Forcible Entry and Detainer without the assistance of an attorney may be practicing law without a license;

- Ownership Interest. The Broker must disclose a Broker's direct or indirect ownership interest in any company which will be providing maintenance or other services to the owner, and any other conflicts of interest (*see* Rule 6.17.);
- Identity of the entity responsible for holding the security deposit, and if interest or credits are earned on security deposit Trust or Escrow Accounts, who benefits from such interest and consent to transfer the interest to the beneficiary;
- The process to be followed for any subsequent transfer of the owner's monies, security deposits, keys, and documents (*see* Rule 5.8.A.); and
- Date that the owner receives regular monthly accounting of all funds received and disbursed.

While these general duties should be addressed in the Management Agreement, it is not an all-inclusive list of all the duties that may be performed by a property manager or that should be addressed within the Management Agreement. Brokers are encouraged to pay close attention to Commission Rules and changes to state laws and local ordinances.

Regardless of whether the Broker is acting as a leasing Broker or a property manager before engaging in any of the activities that require a License, the Broker is required to disclose in writing the different Brokerage Relationships that are available to the tenant. (*see* Rule 6.5.). The Commission-Approved Brokerage Disclosure to Tenant must be used to disclose the Brokerage Relationships available.

Trust Accounts and Record-Keeping:

Any Broker performing Property Management Services in which the Broker is responsible for the collection and distribution of rent or security deposits needs to be especially cognizant of the Commission Rules pertaining to the management of Money Belonging to Others and records retention contained in the Chapter 5 of the Commission Rules. Section 12-10-217(1)(h), C.R.S., requires that a Broker account for and remit, within a reasonable time, any monies coming into the Broker's possession that belongs to others. All Money Belonging to Others which is received by a Broker acting as a property manager must be deposited in the Brokerage Firm's Trust or Escrow Account within five (5) business days of receipt. (*see* Rule 5.7.A.).

If a Broker is going to deposit rent or security deposits into the Brokerage Firm's Trust or Escrow Account(s), the Broker is required to keep records relative to these monies. Rule 5.10. requires that all Money Belonging to Others that is accepted by the Broker be deposited in one or more accounts separate from money belonging to the Broker or Brokerage Firm. Separate Trust and Escrow Accounts must be maintained in the name of the Employing Broker or Independent Broker acting as a sole proprietor or the name of the licensed business entity. Additionally, the maintenance of the separate accounts is the responsibility of the Employing Broker or Independent Broker. (*see* Rules 5.3. and 5.6.). This includes rent checks. Rule 5.5. requires that "[a] Brokerage Firm who engages in Property Management must deposit rental receipts and security deposits and disburse money collected for such purposes in separate Trust or Escrow Accounts, a minimum of one for rental receipts and a minimum of one for security deposits." As an alternative to Trust or Escrow Accounts, a Broker may perform "conduit" Property Management by

depositing rent monies or security deposits directly into an account solely owned and controlled by the owner.

Rule 5.8.A. prohibits a Broker who receipts for security deposits from delivering such deposits to an owner unless the tenant's written authorization is given in the lease or written notice is given to the tenant. The notice must identify who is holding the security deposit and the procedure the tenant must follow to request the return of the deposit. If the security deposit is held by or transferred to the owner, the Management Agreement must specify that the owner is responsible for the security deposit's return and that, in the event of a dispute, the Broker is authorized to reveal the true name and current mailing address of the owner. The Broker may not use any portion of the security deposit (e.g., late fees, tenant charges, or owner charges) for the Broker's benefit.

Rule 5.14. requires an Employing Broker or Independent Broker to maintain a record keeping system, at the Brokerage Firm's licensed place of business that consists of a journal, a ledger, and a bank reconciliation worksheet. All Trust or Escrow Accounts must be reconciled on an ongoing monthly basis. The Employing Broker must also maintain supporting records that detail all cash received and disbursed under the terms of the management and rental agreements. If personal funds have been deposited into the Trust or Escrow Account to open and maintain the Trust or Escrow Account, the journal and ledger must contain entries documenting this money. (*see* Rule 5.14.D.). These personal funds must also be included in the bank reconciliation worksheet. All deposits of funds into a Trust or Escrow Account must be documented, as must all disbursements of funds from a Trust or Escrow Account.

Absent a written agreement that indicates otherwise, the "cash basis" of accounting is required for maintaining all required Trust or Escrow Accounts and records. Funds from one owner cannot be used to supplement operating capital or to finance expenditures of other owners or a Broker. An owner's ledger may never have a negative balance. (*see* C.R.S. §§ 12-10-217(1)(h) and (i), and Rules 1.34. 5.9., 5.11., 5.18., and 6.3.B.). The Broker and Brokerage Firm is required to retain accurate, ongoing records which verify disclosure of and consent to any mark-ups assessed or received, and fully account for the amounts or percentage of compensation assessed or received, (*see* Rule 5.17.). For Commission purposes, Brokers and Brokerage Firms may maintain their records in electronic format as long as the records are stored in a format that can be continually retrieved and legibly printed. (*see* Rule 6.24.). Section 12-10-217(1)(k), C.R.S., requires Brokers to maintain possession of their records for four (4) years.

Security Deposits:

Brokers have to be very careful how they handle security deposits. The security deposit law is complicated and legal assistance is advisable. Wrongful withholding of a security deposit may result in the owner, and the Broker as the owner's agent, being liable for treble the amount wrongfully withheld, plus reasonable attorneys' fees and court costs. Section 38-12-103, C.R.S., requires that the security deposit be returned to the tenant within one (1) month after a lease is terminated or the premises have been vacated and accepted, whichever occurs last. The lease may indicate a longer period to return the security deposit to the tenant; however, state law does not allow this extension of time to exceed sixty (60) days. Security deposits cannot be retained to cover normal wear and tear. Section 38-12-102, C.R.S., defines normal wear and tear as:

> "deterioration which occurs, based upon the use for which the rental unit is intended, without negligence, carelessness, accident, or abuse of the premises or equipment or chattels by the tenant or members of his household, or their invitees or guests."

Normal wear and tear are at the core of most security deposit disputes. Security deposits may be retained for nonpayment of rent, abandonment of the premises, or nonpayment of utility charges, repairs or cleaning contracted for by the tenant in the lease. If there is cause to retain any portion of the security deposit, the tenant must be provided with a written statement listing the exact reasons why all or a portion of the security deposit is being retained. The statement must be delivered with the difference between the amount of the security deposit and the amount retained. The Broker or the owner is deemed to have complied with this requirement by mailing the statement and the payment to the tenant's last known address. Payment may also be sent electronically to the tenant's account. If the Broker or the owner fails to provide the statement to the tenant as required by law, the owner may forfeit their right to retain any portion of the security deposit to offset amounts owed. The owner does not lose the right to pursue amounts due, they just lose the right to utilize the security deposit to offset amounts owed. Furthermore, if the tenant pursues court action regarding any portion of the security deposit being retained, the owner bears the burden to prove that retention of any portion of the security deposit was not wrongful.

If a lease is nullified and voided due to the owner's failure to repair a condition covered by the Warranty of Habitability laws (*see* C.R.S. §§ 38-12-501 - 38-12-511) or otherwise, the owner or the Broker must by Colorado law deliver all, or the appropriate portion of, the security deposit plus any rent rebate owed to the tenant for the period that the tenant vacated the premises. If a portion of the security deposit is retained, the tenant must be provided with a written statement listing the exact reasons why all or a portion of the security deposit is being retained and payment of the remaining balance of the security deposit. If the tenant does not receive all or a portion of the security deposit with the statement within the required deadlines, the tenant may be entitled to three (3) times the amount of the security deposit and reasonable attorney fees (*see* C.R.S. § 38-12-103).

Transfer of Services:

If a Broker no longer will be managing a property, the Broker must transfer a copy of the entire file to the owner or, upon written authorization from the owner to the new Broker engaged to perform the Property Management. At a minimum, the entire file should include:

(a) Copy of existing lease
(b) Copy of check-in condition report
(c) Keys, access codes, passwords
(d) Outstanding tenant balances
(e) Tenant(s) security deposit(s)
(f) Accounting of owner's funds (subject to outstanding obligations)

Although the Commission Rules do not specifically address the transfer of Management Agreements, the Rules do specify when and how to transfer the tenant's security deposit to either the owner or the new Brokerage Firm (*see* Rule 5.8.). The previous Brokerage Firm must give written notice to the tenant that the security deposit has been transferred to the owner or new Brokerage Firm along with the owner's or new Brokerage Firm's contact information. The new Brokerage Firm must also notify the tenant of its

receipt of funds. (*see* Rule 5.8.B.). Timely transfer of the deposit protects the Broker from getting caught between the owner and the tenant regarding the accounting of the deposit. The Brokerage Firm must also provide the owner with a final accounting of all trust funds held by the Brokerage Firm. Although the Brokerage Firm may delay the transfer of the owner's funds until all outstanding invoices or debts have been resolved, the transfer of the owner's funds needs to occur within a reasonable amount of time. A Brokerage Firm that fails to transfer funds in a reasonable amount of time may be subject to discipline by the Commission. Likewise, the new Brokerage Firm must give written notice to the owner and tenant of the status of any security deposit held by the previous Brokerage Firm, to include the amount, within thirty (30) days of receipt of the security deposit.

For additional requirements regarding the transfer of Management Agreements, see Commission Position 7 – Assigning Listings, Relationship and Commissions. When one managed portfolio is purchased by another Brokerage Firm, a new Management Agreement, or an assignment of a Management Agreement along with the assignment of any Trust or Escrow Accounts must be executed. (*see* CP 7 – Assigning Listing Contracts, Relationship and Commissions).

Managing Broker's Own Property**:**

Brokers are subject to the license law and Commission Rules when they participate in real estate matters as principals (*see* CP 1 – Contracts provided by Principals Selling Real Property and CP 14 – Commission Position 14 - Broker Buying Property), including managing the Broker's own property. (*see Seibel v. Colorado Real Estate Commission*, 530 P.2d 1290 (Colo. App. 1974)). A Broker who manages their own rental property must disclose known conflicts of interest and that the Broker possesses a Colorado Real Estate Broker's License (*see* Rule 6.17.). The Broker also needs to use a lease drafted by an attorney for the transaction, along with disclosing in writing to the tenant the Brokerage Relationships under the license law. (*see* Rule 6.5.).

If the Broker is an Associate Broker, it is important for the Broker to consult with their Employing Broker regarding the Brokerage Firm's requirements or limitations regarding managing a Broker's own property. When a Broker personally manages and receipts for a security deposit on their own property, the license law requires that the security deposit be placed in a Trust or Escrow Account. (*see* Rule 5.11. and CP 29 – Holding Money Belonging to Others for Activities not Involving Real Estate Brokerage Services).