

LEGAL ISSUES IN ARKANSAS RESIDENTIAL LEASES

By: Daniel Goodwin

Slow sales of single family homes built “on spec” have lead many builders to lease their unsold inventory. Tightening credit and job markets coupled with increased home foreclosures have lead many families to lease, instead of purchase, homes. This increased demand for rental property has turned many builders into landlords. This article will summarize common issues arising in the landlord-tenant relationship.

Just like a banker making a mortgage, a landlord must evaluate the creditworthiness and “tenant-worthiness” of its prospective renters. That requires the landlord to properly identify each tenant signing the lease. Many landlords require a prospective tenant to complete a tenant application detailing work and residential history and listing references. This type of background information can help measure the tenant’s income and relationship with past landlord’s. Furthermore, if the tenant leaves owing money, having additional contacts may help the landlord in a collection action against the tenant. If the prospective tenant’s creditworthiness seems poor, the landlord should consider having someone else “co-sign” or guaranty the tenant’s obligations on the lease. Finally, properly identifying the tenants and limiting occupancy of the premises only to those tenants can help ensure that the occupancy complies with existing restrictive covenants and zoning requirements. It may also prevent undesirable elements from taking up residence.

The lease should provide clear commencement and termination dates. If there are early move-in dates or free-rent periods, those should be clearly stated in the lease. Clearly indicating these terms will avoid disputes over the term of the lease and potential “holdover” problems.

Arkansas law governs the collection and administration of “security deposits.” However, the law does not apply to landlords who own five or fewer units unless they pay a third party to manage the property. If the statute applies, the security deposit may not exceed two months’ rent. After termination of the lease, the landlord must return the balance of any security deposit to the last known address of the tenant by certified mail within thirty days. If the landlord has applied a portion of the security deposit to pay rent or repair damages, the landlord must also provide the tenant with an itemized list of such expenses. If the tenant can not be found within 180 days using reasonable efforts, the security deposit becomes the property of the landlord. The lease should provide that the security deposit must be replenished if any portion is applied to cure a lease default during the term of the lease.

The lease should clearly state who is responsible for each utility service and for maintenance of the premises. There are some items that a landlord may prefer to maintain and repair itself, especially if they are capital improvements and the landlord has access to contractors through its construction company. The lease should also prevent the tenant from making any alternations to the premises without the landlord’s prior written consent.

The lease should address the condition of the premises. The landlord may require the tenant to perform a pre-lease walk through to provide a baseline condition of the premises. This baseline condition can then be compared to the premises at move-out. The landlord can also use the walk-through to have the tenant waive any defects not discovered at that time. The landlord can also disclaim various warranties implied by law.

The landlord should require the tenant to comply with all zoning requirements, neighborhood covenants, the landlord's rules and regulations and all other governmental regulations. The landlord's rules and regulations could cover numerous items such as requiring the tenant to mow the lawn, restricting pets, controlling guests on the premises and prohibiting other activities that create a nuisance and/or devalue the property or the neighborhood.

The landlord should prohibit the tenant from assigning or subletting the premises without the express written consent of the landlord. If the landlord has underwritten the credit and character of a tenant, it does not want a new, less desirable tenant taking over the property.

The landlord may also want to carefully draft a default and termination section that clearly defines the landlord's rights and obligations. The landlord may give the tenant notice and cure opportunities for some defaults and not others. Some tenant conduct may be so undesirable that the landlord must terminate the lease and evict the tenant. These provisions should also spell out the way in which notice must be given. For the landlord, it is usually preferable to provide physical notice at the rented premises.

In Arkansas, there are a couple of legal ways to remove a tenant who is in default. It is not legal to engage in "self-help" repossession of the premises (i.e. using physical force to eject a tenant). The most efficient method is called an unlawful detainer action. That procedure requires providing a 3-day "notice to quit" to a tenant who is occupying the premises without a legal right to do so (because the lease has expired or been terminated). If the tenant has not left the premises in three days, the landlord may file an unlawful detainer action in court. If the tenant does not respond to the complaint within three days, the court will order the sheriff to oversee the removal of the tenant and its possessions. If the tenant does respond, the judge will set a prompt hearing date. Assuming the tenant does not have a right to remain in the premises, the judge will then order eviction. In most instances, the notice to quit results in the tenant leaving the premises.

In addition to standard leases, some landlords have also turned to "lease-purchase" transactions to help move unsold inventory. In these transactions, the landlord simply provides another form of seller-financing, like a rent-to-own store. In a typical transaction, once the tenant pays a certain amount of rent, the landlord will deed the property to him. In many cases the monthly rent exceeds fair market value because it contains a built-in finance charge. Landlords in lease-purchase transactions have an important issues to consider in addition to those listed already. Namely, any built-in finance charge must comply with Arkansas' very strict usury law. That usury law is tied to the Federal Reserve's "primary rate" of credit, which is usually very low in poor economic times. The result is that the maximum allowable rate of interest for non-bank lenders is often lower than what a bank would charge on a typical mortgage loan.

There are many other issues that a well-crafted residential lease should address to provide maximum protection and comfort to the landlord. However, by covering these core issues, a landlord should have a legally enforceable lease that will protect the property, its right to receive the rent and the right to get the property back upon a default.

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