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CONDOMINIUM CONSUMER PROTECTION ACT OF 1975

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HEARINGS

BEFORE THE

COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS UNITED STATES SENATE

NINETY-FOURTH CONGRESS

FIRST SESSION

ON

S. 2273

TO PROVIDE MINIMUM NATIONAL STANDARDS FOR DISCLOSURE AND CONSUMER PROTECTION IN CONDOMINIUM SALES AND CONDOMINIUM CONVERSIONS, AND FOR OTHER PURPOSES

OCTOBER 6, 7, AND 8, 1975

Printed for the use of the Committee on Banking, Housing and Urban Affairs

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CONDOMINIUM CONSUMER PROTECTION ACT OF 1975

MONDAY, OCTOBER 6, 1975

U.S. SENATE,
COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS,
Washington, D.C.

The committee met at 10:20 a.m., pursuant to call, in room 5302, Dirksen Senate Office Building, Senator William Proxmire (chairman of the committee) presiding.

Present: Senators Proxmire and Morgan.

OPENING STATEMENT OF CHAIRMAN PROXMIRE

The CHAIRMAN. The committee will come to order.

The committee begins today 3 days of hearings on S. 2273, the Condominium Consumer Protection Act of 1975. This bill is jointly sponsored by myself, Senator Brooke, and Senator Biden.

We will hear testimony from witnesses representing the Federal Government, State governments, condominium owners, and various parts of the condominum industry. As our leadoff witness, we are pleased to have with us today the Honorable Carla A. Hills, Secretary of the Department of Housing and Urban Development.

One year ago, in response to numerous complaints about condominiums from around the country, the Housing Subcommittee of this committee held hearings on condominium consumer protection legislation. Many of the witnesses at those hearings stated there was a real need for Federal legislation to clear up problems in this area.

Since that time, the Department of Housing and Urban Development has done a study of problems, difficulties, and abuses in condominiums and cooperatives, as mandated by section 821 of the Housing and Community Development Act of 1974. The report of the study was issued as scheduled on August 22, 1975, and, Mrs. Hills, I congratulate you on your promptness and on the excellent job done by you and your Department in compiling this study.

The legislation we are considering today, S. 2273, is designed to clear up the condominium problems and abuses that we found in our hearings and you confirmed in your study. It is a substantially revised and, I think, substantially improved version of last year's bills.

The major change is that we take HUD out of the business of registering condominiums altogether. Instead, the bill calls for HUD to set minimum standards for consumer protection and disclosure in condominium sales and conversions, but it leaves enforcement of the law to the States or, alternatively, to individual action through the courts.

Mrs. Hills, you and I have met and discussed this legislation and there has been substantial communication between your staff and committee staff. I know we agree on the basics—that we want to help consumers while holding cost and paperwork down to an absolute minimum.

So far as the specifics of the bill are concerned, I think we have a working draft in front of us, but there is certainly plenty of room for changes and improvements, based on your suggestions and on the testimony of other witnesses at these hearings.

Now, before we continue, Senator Biden has an opening statement.

OPENING STATEMENT OF SENATOR JOSEPH R. BIDEN, JR.

Senator BIDEN. Today the Senate Banking Committee begins 3 days of hearings on legislation to provide full disclosure and fair enforcement of purchases and sales of condominiums.

Despite the deep recession that most of our housing industry is experiencing, the sales of condominiums seems to be going as well as ever. Whether used as a principal residence, a vacation retreat, or a retirement home, the condominium has become the fastest growing sector of the housing market.

And with this rise in sales has been a rise in problems. Low quality construction, misappropriation of funds, and insufficient warranties are all too commonplace.

Some of these abuses were documented very well during hearings before this committee last year. The recently completed study of condominiums by the Department of Housing and Urban Development also provides instances where consumers have been defrauded.

The legislation which we consider today will hopefully correct and prevent much of this abuse. S. 2273, introduced by Senators Proxmire, Brooke, and myself, provides certain basic standards which must be met before a condominium can be sold. It also provides standards for disclosure so that the purchaser knows what he is getting into.

S. 2273 differs from previous condominium legislation in two important respects. First, it does away with the bureaucracy that was required by last year's legislation. Instead of requiring HUD to scrutinize every condominium offering, we rely on the "private atttorney general" concept and provide an incentive for a defrauded consumer to sue, not only for himself, but on behalf of the entire class of people who may have been cheated.

Second, this bill recognizes the fact that certain States have made great legislative strides in this area. Consequently, S. 2273 provides an incentive for States to enact legislation to protect the condominium purchaser. If a State passes legislation which meets or exceeds the minimum standards in S. 2273, it will have the responsibility for enforcing the law rather than the Federal Government.

With these two important changes, as well as other suggestions which will come from the hearings, I am hopeful that we will be able to produce legislation to correct and control much of the abuse in condominium sales.

The CHAIRMAN. Mrs. Hills, please go ahead with your statement.

STATEMENT OF CARLA A. HILLS, SECRETARY, DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

Secretary HILLS. Thank you very much, Mr. Chairman.

Mr. Chairman and members of the committee, good morning. Thank you for the opportunity to be here today to discuss S. 2273, a bill which has been introduced by members of this committee to protect purchasers and prospective purchasers of condominium units. We understand that this bill is an extensively revised version of bills with similar objectives considered by the committee last year.

My prepared statement is more than 40 pages in length and is divided into two parts: First, a summary of the background and principal findings of the recently completed comprehensive study of condominiums which we submitted to Congress on August 22; and second, our comments on S. 2273 and our recommendations for an appropriate Federal response to the problems of condominium housing. In the interest of conserving time and with the permission of the committee, I would ask that the full statement be entered into the record and I will summarize our comments and our recommendations.

The CHAIRMAN. Without objection, that will be done.

Secretary HILLS. Thank you.

[Complete statement of Mrs. Hills and a copy of S. 2273 follow:]

STATEMENT OF CARLA A. HILLS

SECRETARY OF HOUSING AND URBAN DEVELOPMENT

Mr. Chairman and members of the Committee.

Thank you for the opportunity to be here today to discuss S. 2273, a bill which has been introduced by members of this committee to protect purchasers and prospective purchasers of condominium units. We understand that this bill is an extensively revised version of bills with similar objectives considered by the Committee last year.

You will recall that when we appeared before you to discuss these earlier bills last October 9, we recommended that consideration of federal condominium legislation be postponed until HUD had completed the national study of condominiums and cooperatives mandated by Congress in Section 821 of the Housing and Community Development Act of 1974 (P.L. 93-383). Section 821 directed HUD to conduct a "full and complete investigation and study, and report to Congress not later than (August 22, 1975), with respect to condominiums and cooperatives, and the problems, difficulties, and abuses or potential abuses applicable to condominium and cooperative housing." Section 821 was a response to Congressional concern over the reported problems and abuses accompanying the recent rapid growth in condominium development. I am happy to report that the study called for in Section 821 was

transmitted to Congress as scheduled on August 22, 1975. I am pleased with the quality of the report, and I trust that you have had an opportunity to peruse it.

In order to carry out the broad mandate of Section 821 within the time available for the study, we felt that the study should at a minimum include the following major elements:

1. Documentation of the growth and impact of condominiums and cooperatives in the U.S. housing market.
2. A review of the nature and extent of problems and abuses related to these forms of homeownership, with particular attention to conversion projects and the factors behind conversions.
3. A survey of the present activities of state and local governments in regulating condominiums and cooperatives
4. A review of the present role and impact of HUD and other Federal and Federally-sponsored agencies with responsibilities in the condominium field, and
5. An assessment of the economic impact of proposed substantive Federal disclosure and regulatory requirements on developers, consumers, and public administrative agencies.

To accomplish these related yet diverse objectives, HUD for the past year has undertaken a major and exhaustive study

of condominiums and cooperatives. A Department-wide Condominium Task Force was established under the leadership of Michael H. Moskow, Assistant Secretary for Policy Development and Research, with David M. deWilde, Acting Assistant Secretary for Housing Production and Mortgage Credit, and Robert R. Elliott, General Counsel, serving as co-chairmen. William Lilley III, Deputy Assistant Secretary for Policy Development, served as vice chairman in charge of day-to-day operations.

The study included the following components:

- Four days of public hearings in Washington, D.C., and Fort Lauderdale, Florida
- Interviews with housing officials and industry representatives in states with substantial condominium activity
- Preparation and circulation for comment of a draft state statute governing condominium sales and conversions as a technical drafting service for state legislatures
- Review of the FHA Section 234 (condominium) and Section 213 (cooperative) mortgage insurance programs to identify program strengths and weaknesses
- Consultations with representatives of other federal agencies with current responsibilities for condominiums
- Compilation of a statistical profile of condominium and cooperative development in the United States; surveys of condominium

unit owners and associations of co-owners; intensive area housing market research; and legal analysis. (This portion of the study was conducted under the supervision of HUD by Arthur D. Little, Inc., of Cambridge, Massachusetts, and its subcontractors, ICF, Incorporated, and Arnold & Porter, both based in Washington, D.C.)

In addition, we received dozens of unsolicited letters from consumers who related their experiences in condominium and cooperative housing. These letters provided a valuable indication of the nature and extent of consumer problems.

As we anticipated last fall, the study provided a wealth of useful information which has helped us to better understand the scope of, and forces behind, the condominium boom of the past few years and the problems which have accompanied it. In that sense, the study represents the first attempt on a national basis to examine the recent explosive growth in condominium development. The report contains the most detailed data available on national condominium development since the 1970 Census. In addition, the study contains a comprehensive survey of State laws applicable to condominiums and the only extensive analysis of the nature, extent, and severity of problems and abuses that is based on actual surveys of unit owners and their associations.

I want to note at this point that even though cooperatives were an important part of our study, most of my remarks today are confined to our findings with respect to condominiums. In brief, we found that most cooperatives were built prior to 1970, that they have not been subject to the same degree of problems as condominiums have been in recent years, and that, for various reasons, their growth rate has actually declined in the past five years. Consequently, we decided to concentrate our efforts on condominiums in order to be able to address some of the more pressing problems. Several prominent authorities in the field of cooperatives who testified at our hearings in Washington, D.C., last February supported this decision.

Today I want to begin by summarizing very briefly some of the principal findings and conclusions of the study with regard to characteristics of the industry, related consumer problems, and the status of efforts of state and local governments. Finally I would like to comment on S. 2273 and discuss our recommendations for an appropriate federal response to problems which trouble the condominium housing market.

RAPID GROWTH

First, our study documented the explosive growth in condominium construction during the past five years. From a

mere 85,000 units in 1970, condominiums as of April 1, 1975 accounted for 1.25 million units nationwide, a phenomenal 15-fold increase. In 1973 and 1974, 25 percent of all for-sale housing starts in the United States were condominiums. There has been tremendous impact on housing markets in certain metropolitan areas which had rapid increases in housing starts. In certain markets, condominiums constitute a substantial portion of all increments to the housing supply. For example, the Fort Lauderdale, Florida, SMSA has experienced a 1,000 percent increase in condominium construction since 1970. In the Washington, D.C., SMSA, only 7.4 percent of the total building permits issued in 1970 were for condominium units; this figure jumped to 44.5 percent in 1974. In the State of California the number of condominium units registered with the state increased from 5.5 percent of all registrations of new for-sale housing in 1970 to 34.8 percent in 1974.

The conversion of rental properties to condominiums has proceeded on a much smaller scale, with an estimated 100,000 units nationwide during the five year period ending in March 1975.

In some areas, there has been a direct relationship between the increase in condominiums and the decline in the construction of multifamily rental housing. In certain areas, and especially those with rapidly expanding housing

markets, condominium construction has virtually replaced multifamily rental construction. For example, in the Washington, D.C., SMSA in 1970, 7.4 percent of all building permits were for condominium units and 39.4 percent were for multifamily rental units; by 1974 only 6 percent of the permit authorizations were for multifamily rental housing, whereas condominiums accounted for a share of 44.5 percent.

Not all of these units were easily absorbed. As a result of overbuilding, unfavorable economic conditions, and other causes, some markets are glutted with unsold condominium units. There currently are an estimated 250,000 completed but unsold units, half of which are located in the Fort Lauderdale, Florida, SMSA.

In the wake of this impressive growth pattern, condominium and cooperative units now account for 2.4 percent of all occupied housing and house approximately 4 million people. Although a precise breakdown is not available, the majority of these persons reside in condominiums.

The study further shows that outside of retirement and resort communities, condominiums appeal primarily to young childless couples and couples of 45-64 whose children are no longer living at home. Although the

research indicates that these are the groups who are most likely to purchase condominium units, most demographic groups find benefits in condominiums and are represented among the purchasers.

We also found that condominium development to date has been a highly regionalized phenomenon, with most of the development occuring in the West and South. Nearly 50 percent of all condominium and cooperative units are located in Florida, California, and New York. Of all the States, Florida and California have by far the largest inventories of condominiums. Ten States (Florida, California, Ohio, Texas, Illinois, Michigan, Arizona, New York, Pennsylvania, and Maryland) have accounted for nearly two-thirds of all new condominium construction in the past three years. These ten States were also responsible for most of the activity prior to 1970, as the concentration of condominiums and cooperatives has not shifted significantly throughout the 1970's.

FACTORS UNDERLYING THE GROWTH OF CONDOMINIUMS

Our study confirmed a number of widely-held, though previously undocumented, beliefs concerning the factors which have contributed to the growth of the condominium industry and the appeal of condominiums to consumers, developers, and local public officials.

First, we found that condominium units cost slightly less than conventional single-family homes. In 1974, 40 percent of condominium units fell into the $20,000 to $30,000 category, compared with only 28 percent of single family homes in that category. In that year, the median prices were $32,100 for a condominium unit and $34,750 for a single family home.

Although condominiums have brought the possibility of home ownership within reach of a wider population, condominium units are usually smaller in size than conventional dwellings of equal value. Furthermore, the life cycle cost of a condominium (mortgage, utility and maintenance costs) may be equal to or in some cases greater than that of other forms of housing.

In addition to the economic advantages of home ownership, including tax benefits and the opportunity for equity appreciation, a great number of condominiums provide amenities such as swimming pools, tennis courts, and other recreational facilities which individual purchasers otherwise would be unable to afford. In addition, the condominium unit owner has fewer maintenance responsibilities than the owner of a conventional residence.

Since condominiums often are located at prime locations in or at the fringe of urban areas, they can offer greater convenience than single family tract developments to jobs, public facilities, shopping, and other urban services.

Condominiums can also be attractive to local public officials. In addition to expanding the supply of affordable middle income housing, condominiums provide for more efficient land use through their higher density development. In addition, increasing the supply of units for homeownership has traditionally been encouraged by local communities because of the increased neighborhood stability which accompanies resident ownership.

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The economic, social and environmental factors which have stimulated new condominium development also have encouraged the trend toward conversion of existing apartments to condominiums. This trend has received additional impetus, moreover, as apartment owners for various reasons--local rent controls, market factors, and tenant resistance to increased rent costs, to name a few--have not been able to raise rents rapidly enough to keep up with rising costs. In addition, recent changes in the tax laws have enhanced the attractiveness of conversions for apartment owners.

Conversions can help to preserve and rejuvenate neighborhoods in areas with little developable land. In some areas, local officials have encouraged conversions through preferential tax treatment and other means because of their potential for upgrading the housing stock and the greater tax revenues to be gained as a result of the increased property value.

Developers have also turned to higher density housing such as condominiums as an alternative to the single family detached home because of rapidly increasing land costs. As the cost of materials, labor and supportive services (e.g., marketing, financing and legal services) increased as a percentage of the price of conventional homes, condominium units have provided a competitive alternative because of their lower price. Condominiums often offer the only economical and affordable opportunity for home ownership in many high density metropolitan areas.

The future prospects for condominium development appear favorable. Although the feverish boom of the 1970-1974 period appears to have subsided, many of the factors which served to promote the unparalleled growth during this period still exist and are expected to continue to exist. Specifically, these factors include those which I mentioned previously, namely, the scarcity of developable land in major urban areas and the ever-increasing cost of constructing conventional single family dwellings due to sharply rising land values.

In addition to these factors, however, we expect that continuing affluence and increased discretionary income will enable more people to purchase housing and stimulate the market for retirement homes and/or second homes in recreation areas, traditionally popular markets for sales condominium units. Additionally, consumer confidence is expected to increase as consumers learn more about condominiums and as problems and abuses in the industry subside.

PROBLEMS RELATED TO THE SALE AND PURCHASE OF CONDOMINIUMS

I next would like to describe some of the problems in the condominium industry which we discovered during the course of our study. A number of problems arose early during the period of recent condominium growth because of the newness of the condominium concept and the lack of experience of consumers, developer/builders, attorneys, and government officials. These problems were further exacerbated by the legal and conceptual complexity of the condominium form of property ownership. Secondly, as the industry matured, a number of problems have surfaced in connection with difficulties inherent in managing and operating jointly-owned property.

Although the HUD study generally found that the problems have not been severe in terms of their impact at the national level, we found that some of them have had a serious impact on those directly affected. Furthermore, some problems which are common to other types of housing, such as poor quality construction, are aggravated in condominiums because of the interdependence of the unit owners and the need to obtain the approval of a majority of owners before remedial action can be taken.

SPECIFIC PROBLEMS

The ten most significant problems for consumers of condominium housing were found to be recreation leases, poor construction quality, complex legal documents, tenant displacement in conversions, association operating problems, problems of community living, loss of consumer deposits, nonpayment of association dues by the developer, warranties and engineering reports, and underestimated operating expenses. I want to discuss each of these briefly.

Recreation Leases

A recreation lease is a device by which the developer of a condominium project retains title to certain of the development's amenities and leases them to unit owners or to their association under a long-term--typically 99 year--lease. Many recreation leases, and those which have been the primary object of consumer complaints, contain provisions for automatic adjustments based on cost-of-living indices. Under the terms of most of these leases, owners who fail to pay are subject to liens on their units. In some cases, the existence of the lease and its full implications are not fully disclosed to prospective purchasers. In addition, a number of the leases cover facilities that are of smaller

size or poorer quality than the buyer originally expected.

The study found that the leases can be severe in terms of their long-term cost and ultimate financial impact on the owners--particularly those owners who are living on fixed incomes. However we found that these leases were limited almost exclusively to Florida, and that even in Florida few of the new projects employ such leases because of the adverse reaction of consumers and lenders to leases in existing developments. We found that although recreation leases are controversial and have caused some problems, they are not without some benefits, as they may reduce the initial cash outlay required for purchase and provide access to a larger complement of amenities than otherwise would be available.

This is not to understate the problems of those persons who have purchased units unwittingly in projects with these leases, for whom the only recourse at present appears to be private litigation. We understand that the Federal Trade Commission, the only Federal agency with current authority to respond, has recently reopened its investigation of this problem. We have maintained contact with the Commission throughout our study, and will continue to cooperate with them by sharing data

which we have collected during the HUD study.

Poor Construction Quality

Another source of buyer complaints concerned the quality of condominium construction. These complaints included settlement cracks, improper drainage, roughly finished interiors and poor soundproofing. We found that although the problem of quality is not unique to condominiums nor to housing in general and is often a matter of subjective judgment on the part of the consumer, construction defects can have a more serious effect on the condominium owner because of the difficulty of obtaining the required agreement of a majority of unit owners to correct the deficiencies,especially if higher monthly owner assessments will be required. The study also found some evidence that condominium purchasers, particularly in multifamily buildings, place greater emphasis on the quality of construction than renters in the same type of facility.

Complex Legal Documents

The legal documentation required for creation of a condominium regime is costly to prepare and voluminous, running

frequently in excess of several hundred pages. An even greater problem is the intricate and complicated language of the documents, which is difficult even for lawyers to understand. As a result of the complexity of the documents, lawyers often charge between $750 and $1,000 for a review involving a single unit. The complexity of the documents contributes to problems in other areas, since consumers often fail to comprehend the ramifications of their decisions to purchase condominium units.

Tenant Displacement in Conversions

The displacement of existing tenants in rental buildings converted to condominiums has been a problem which has received wide publicity and has led to moratoriums on conversions in several cities, as well as other local ordinances which indirectly limit conversions. The study found that an average of only 20 percent of rental tenants buy in a conversion. Those who do move can find it difficult to find substitute housing, particularly in areas where the available supply of suitable housing is inadequate or unaffordable.

Association Operating Problems

A wide variety of problems associated with condominiums occur after the developer leaves. The study shows that a number of operating problems for condominium associations are causing significant problems now and will cause even more serious problems in the future. These include improper insurance coverage, unworkable bylaws or organizational structure, and inadequate budgeting for long term operation and replacement of common facilities.

The study shows that the long term operation and maintenance of a project and its ultimate viability depend to a great degree on the presence of experienced and well trained managers, particularly in the larger condominium developments. There are few professional property management firms with condominium experience, however, and their cost may be prohibitive to smaller developments. Many developments are managed by officers of the association of co-owners, whose experience can vary widely. Almost every association contacted during the course of the study indicated a need for more experienced management, though professional management is no panacea.

Before most key actions affecting management, maintenance, and operation can be undertaken, it is necessary to achieve a consensus, in some cases unanimity, of the

unit owners. The difficulty in obtaining agreement and the time that it can take to reach agreement can seriously threaten the proper operation and maintenance of condominium developments.

A third serious problem impeding proper operation and management is the lack of adequate reserves for major repairs and replacements. Many associations do not establish adequate reserves and have no incentive to do so because of a recent IRS ruling which taxes replacement reserves as ordinary income to the owners association. Several bills have recently been introduced in the Congress which would reverse this ruling as it applies to the membership income of certain homeowner associations. HUD supports this effort.

Problems of Community Living

We found that some of the most widespread problems arose as a result of the communal and close-quarter living required in most condominiums. Many owners are unable to adjust to the differing lifestyles of their neighbors. Interestingly, the third most often-cited problem affecting condominium owners was the problem of pets. These problems can be compounded when the association is

unwilling or unable because of bylaws or organization to respond to owner complaints.

Loss of Consumer Deposits

In many jurisdictions, developers are not required by law to place buyer deposits in escrow. The most common reason for consumer loss of deposits was developer bankruptcy. The boom years of condominium development appear to have fostered a disproportionate share of developer bankruptcies because, for various reasons, those years created an environment which allowed experienced developers to overcommit themselves and allowed inexperienced and underfinanced developers to rush into the industry. Intentional and criminal misuse of deposits, however, was rare. Although this problem is limited in its extent, its impact is nonetheless severe on the individuals affected.

Nonpayment of Association Dues by the Developer

Although many States require the developer to pay association dues on units which have been completed but not yet sold, a severe problem is created for unit owners if the developer, directly or through various loopholes, avoids his share of association assessments. This was not found to be a widespread problem, but it was serious in those cases where reported. It appears, however, that this practice is less prevalent now than in the past.

Warranties and Engineering Reports

It is difficult for purchasers of condominium units to judge the quality and adequacy of such structural components as heating and electrical systems. Developers do not ordinarily provide facility and equipment warranties, and many consumers believe that a unit purchaser should be provided a basic engineering report on the project and that warranties should be provided on key elements. Some states have enacted laws to this effect. Costs of engineering reports and warranties tend to be passed through to unit owners.

Underestimated Operating Expenses

A significant number of respondents to our surveys reported that original cost estimates underestimated future maintenance costs. The extent to which this was intentional is debatable. Low estimates of these expenses may require major unexpected increases in monthly assessments or a special assessment by the homeowners' association. For political reasons or because of impediments in the association's by-laws (such as a requirement for unanimous consent), association officers may be unable to raise the funds necessary for the proper operation and maintenance of the project.

Despite these problems, 95 percent of unit owners who responded to our survey replied that they were satisfied or very satisfied with their condominium units. The sample which we surveyed comprised 602 unit owners in six different areas including 80 owners from Fort Lauderdale, Florida, which has been widely known as a problem area.

GOVERNMENT INVOLVEMENT

Our comprehensive survey of state and local legislative activity clearly demonstrated the diversity of statutory approaches and the local nature of real estate and development practices. Since the condominium concept was first introduced in the United States in the early 1960's, every state has enacted basic enabling legislation to allow for the creation of condominium regimes. In response to the problems and abuses which have accompanied the recent surge in condominium construction, a number of states have amended their basic statutes or turned to other devices such as general subdivision statutes, land sales registration, or securities statutes to develop disclosure or regulatory controls.

The HUD study found that more than half of the States amended their basic enabling statutes to include consumer protection requirements. While many of the states which are operating under these basic statutes have little or no condominium activity, others, such as Texas, Pennsylvania, and the Commonwealth of Puerto Rico, do. The remaining states have enacted some form of disclosure provisions or regulatory laws with respect to condominiums. Thirteen states (Alaska, Connecticut, Idaho, Minnesota, Missouri, Nebraska, Nevada, New Jersey, North Dakota, Ohio, Tennessee, Vermont, and Washington) have partial regulation or disclosure.

However, it should be noted that with two limited exceptions, these State laws govern only out-of-state condominiums advertised in that State.

Nine states (Arizona, California, Florida, Hawaii, Michigan, Montana, New York, Oregon, Virginia) and the District of Columbia have full regulation. These ten jurisdictions account for over 50 percent of all condominium units in the United States. The jurisdictions which have most actively regulated condominiums are, for the most part, those in which the greatest condominium development has occurred.

The impact and effectiveness of these stronger laws have yet to be fully assessed because the laws are so recent. However, there is convincing evidence that some states have done an exceptionally good job through various devices of protecting consumers and deterring abuses.

The variety of statutory approaches undertaken by the states appears to be an informed response to numerous factors. For example, the State of Maryland chose, after long and careful consideration, not to institute detailed regulations. Policymakers in Maryland determined that the costs to consumers and the State outweighed the benefits to be derived from such legislation.

Other states have prohibited certain questionable practices through strong administrative positions which may not be explicit in their statutes. For example, California and Hawaii require a prospective condominium developer to complete a very detailed questionnaire which is closely scrutinized and investigated for accuracy.

OBJECTIVES

From the knowledge gained from our study of the condominium industry and our analysis of the problems and their effects on consumers, the status of current state and local efforts, and our expectations about future trends in the condominium industry, we believe that some additional degree of consumer protection is necessary. However, we also believe that we at the federal level must be exceedingly careful about the extent of our involvement. We stongly feel that adherence to the following objectives is critical for a conscientious, appropriate and effective response at the federal level:

1. Federal involvement in any regulatory scheme involving condominiums should be kept to a minimum. Jurisdiction over real estate matters traditionally has been a concern of state and local government. The condominium industry is still relatively new and in its formative stages. A high level of federal involvement might retard a very innovative and flexible young industry that can provide homeownership opportunities to a wide spectrum of Americans. Federal involvement should not discourage the further development of this of any other useful,

innovative, and desired form of housing.

2. States must be allowed to continue to develop their own legislation and administrative mechanisms required to deal with condominiums within their jurisdiction.

3. The benefits of protection must be carefully weighed against the costs for such protection. Increased costs to the industry--and ultimately to the consumer--resulting from bureaucracy and red tape should be avoided.

4. It is imperative that there be a thorough understanding by all concerned parties of potential problems and the complexities of owning and managing condominiums.

We applaud your recognition in drafting S.2273 of the need to keep the Federal role to a minimum and to minimize any adverse economic impact on consumers. In particular, we welcome those changes from the previous bills which give the states more opportunity to act and which minimize the need for additional HUD regulatory authority and additional HUD bureaucracy. We are especially supportive of your decision not to require registration or review of any condominium documents by the Federal Government.

COMMENTS ON S. 2273

At this point I would like to discuss in detail the Administration's views on your legislative proposal. These views are based upon the results of our study and careful analysis over the past year.

We have carefully reviewed the bill and its major provisions: national standards for consumer protection and disclosure; assistance to the States to enforce these standards, and civil and criminal penalties for non-compliance, with HUD empowered to conduct investigations and seek injunctions.

We agree that there is a need for promulgation of national minimum standards for disclosure and consumer protection in the sale of both new and conversion condominiums, as long as these standards are kept to a minimum and do not involve registration with HUD or direct regulation by HUD. Thus, we believe that the basic approach proposed in S. 2273 is the correct one.

However, there are certain provisions of the bill that we feel are unworkable or unnecessary at the Federal level. In keeping with our objective of keeping the Federal role to a minimum, there are certain modifications which we believe would strengthen the bill and provide an added measure of assistance to consumers. These are our specific comments and recommendations on S. 2273:

Consumer Protection Standards

Certain substantive protective standards should be left to the states in order that these requirements might be tailored to the nature of the condominium market within their jurisdiction. Thus, we do not believe that Federal preemption of state regulatory authority is needed in the following areas as proposed in S.2273:

1. The bill unnecessarily contains a prohibition against developer retention of interest in common elements (e.g., recreation areas) after control has been transferred to the owner association. The condominium study found that the problem of long-term recreation leases is not an extensive one outside of Florida and that few new condominium projects are currently being sold with these leases. The negative public reaction to these long-term leases has and will continue to discourage abuse. Furthermore, these leases can provide certain additional benefits for the purchaser at a lower cost if they are properly used and if their implications are fully disclosed to the purchaser. The HUD condominium study estimated that recreation leases can reduce purchase prices in a typical condominium project by $2,000 to $8,000 per unit. We therefore support only mandatory disclosure of all leases, liens, encumbrances affecting condominium units and

their common properties. We believe that the states are capable of dealing with whatever abusive practices may accompany these leases. For example, the State of Florida, where most of the abuses involving these leases have occurred, now prohibits escalator clauses, which tie lease payments to the cost of living, in future recreation leases -- the most abusive use of long-term leases.

2. The bill provides that transfer of control from the developer to the owners' association be made at a specific time based on the date of initial occupancy or the percentage of units occupied. Our study has shown that there are many cases in which transfer after one year would not be beneficial to consumers, developers or lenders. Continued control by the developer or his agent would, for example, be beneficial in resort, time-sharing and some retirement condominium in which few owners tend to be active in the owners' association.

There are other important reasons why mandatory transfer as specified would be harmful. A developer would be taking a big risk if he were to build a project knowing that, regardless of how sales were proceeding, he must quickly relinquish control of his project to the unit owners, be they one or one hundred. It is quite likely that such risks would drive developers away from the condominium

market and would force developers in the direction of very small projects and it would certainly raise the price of a condominium unit

An appropriate time of transfer varies from project to project, depending on its size and the expertise of the unit owners. Premature transfer of control has caused and will continue to cause problems for unprepared owners' associations.

3. S.2273 would require a two year warranty on common elements and a one year warranty on individual units. We strongly oppose a Federal requirement for such warranties. The requirement for warranties would add substantially to the purchase price of a condominium unit. Our study found that the typical sales price for a condominium unit in 1974 was just over $32,000. We have estimated that warranties on new condominium units might raise that price by as much as $1,600, and, in older buildings, the price increase could be twice this amount.

Warranties of the stringent kind specified in the bill are more expensive than can be justified by the benefits. They are in any event not required for other types of construction, and imposition of such a broad warranty requirement on condominiums alone would probably force developers away from condominium projects and thereby reduce the availability of this lower-priced homeownership opportunity. We would be happy to explore with the Committee the possibilities for a narrower and more appropriate warranty.

4. S.2273 would require that a developer assume all rights and obligations of a unit owner for unsold units prior to transfer of control to the unit owners.

The major effect of this provision would be to require a developer to pay, for all unsold units, his full pro rata share of all common expenses of the condominium project.

While the HUD study found some evidence that developers have avoided paying reasonable assessments, the effect of requiring full payment can be a higher purchase price since developers must pay for unused facilities and services. We recommend that the developer be excused from paying his pro rata share of utilities and certain maintenance costs on unsold, unoccupied units. The developer would be responsible for a full share of costs of contracts or costs otherwise

unavoidable, for example, heating the halls in a partially occupied building--and for contributions to various reserve accounts.

In this way, the actual costs of operating and maintaining a project are appropriately divided between the developer and the unit owners for occupied and unoccupied condominium units. Detailed regulation of condominium assessments should remain within the authority of the States.

5. The bill would require that contracts and agreements are voidable six months after control is transferred to unit owners. The State of Virginia recently amended its law to eliminate a similar requirement, because it caused all contracts including such beneficial agreements as service contracts on elevators to be voided. A requirement such as this adds an element of risk to such service contracts and thereby increases costs to consumers. We believe that it would be preferable to devise a prohibition which is narrowly-drawn to regulate "sweetheart contracts."

In summary, we support only those Federal consumer protection standards which are needed to prevent fraud and protect against clearly abusive practives. Any Federal condominium law should contain simple and explicit consumer protections that have as limited an economic impact as possible on the consumer, do not unnecessarily restrict the industry, and permit the states to act to the extent they deem appropriate to provide additional protections which might in their judgement be necessary.

In this regard, we fully endorse the following consumer protection provisions contained in S.2273:

1) The 15-day "cooling off" period. This would allow the consumer to review the information provided and to carefully evaluate his decision to purchase.

2) The minimum period of 90 days in which tenants are offered the right of first refusal on purchasing a unit in the project and the minimum 120 day notice of the requirement to vacate the premises. These periods are essential in order to provide existing tenants an adequate opportunity to locate suitable alternative housing. Since 80 percent of all tenants do not purchase, Federal protection is warranted to protect the rights of the tenants and offset potential hardships.

3) The requirement for escrow of consumer deposits. The loss of deposit monies was one of the most severe problems encountered during the course of the condominium study in terms of its impact on the individuals affected. This requirement can eliminate the possibility of such losses without imposing major costs or constraints upon consumers or the industry.

National Standards for Disclosure

We are concerned that Federal disclosure requirements also be held to a minimum. Highly technical and voluminous disclosure statements are complicated, costly, and, as we found during the study, often not read by the buyer. Disclosure requirements should be kept simple and limited to provision of information essential to a prudent purchase decision by consumers. Compliance with these requirements should not result in substantial additional cost for consumers or discourage future condominium development. We strongly oppose any requirements for registration or review of condominium documents by the Department.

I would like to comment specifically on two provisions of S. 2273 which may not be consistent with this objective:

1. S.2273 requires a two-year budget projection and certification by a CPA. These requirements are excessive and, in the case of smaller projects, could add significantly to the cost of a unit.

The condominium study found that the underestimation of future common expenses is a widespread problem, resulting from both limited deliberate "lowballing" and, in virtually all cases, unanticipated cost increases. We feel that this problem is serious and widespread enough to warrant a Federal standard. However, we feel that the standard proposed in S.2273 is unworkable and would not solve the problem it addresses.

In discussing the requirement for certification of the budget projections with certified public accountants and industry experts, it became clear that CPA certification would be unworkable. CPAs would not be willing to certify budget projections, in some cases, no matter what fee were to be charged.

We recommend that a one-year or two-year budget be required to be disclosed. Along with this requirement, the short Federal disclosure model form would contain a warning, clearly displayed, that common expenses may well increase substantially in the future.

2. Similarly, the mandatory provision for an engineering report prepared by a certified engineer, though desirable, would be expensive.

   The cost of a typical engineer's report, including the five year estimate required in S. 2273, would vary greatly depending on the size, age, condition and amount of proposed rehabilitation to the building. We estimate that such reports might cost about $75 per unit for the typical 100 unit project.

We concur in the other items required to be disclosed by S.2273. Each is a piece of basic information, essential to a prudent purchase decision. The provision of such basic information, which does not impose a great impact on developers and is understandable to buyers can and will provide major protections to potential purchasers. These provisions have been utilized by many of the States. As such, they represent proven methods of consumer protection.

Included in the mandatory Federal disclosure requirements would be:

1) the name and address of the condominium project and its developer and project manager;
2) a general narrative description of the project;
3) disclosure of construction status, zoning or other requirements and expected expansions of the project to inform the buyer of the expected size and structure of the completed project;
4) the significant terms of financing offered by the developer;
5) description of warranties, completion bonds or other projections provided by the developer;
6) terms and provisions of management of the project;
7) a clear statement of the purchasers right to review the condominium instruments and the existance and nature of the "cooling off" period; and
8) the existence and contents of a reserve fund to finance repairs or replacement of major common elements.

As I indicated previously, in place of outright prohibition of long-term leases, we recommend disclosure of all leases liens or encumbrances on the condominium. This requirement is essential to protect purchasers and will not entail the major expense required by warranties.

A Federal disclosure law could be a vehicle to solve one problem which became quite clear in our review of State condominium laws. There are a number of overlapping and contradictory requirements which make it difficult and, in some cases, impossible for developers to offer condominiums in certain States. At present, eighteen States have laws that regulate to varying degrees the sale of out-of-state condominiums in their State. Some of these States regulate only sale of out-of-state condominiums and exclude those built and sold within that State.

The multiple filings that can be required under current law are expensive, and most of the expense is passed on to the consumer. For example, a Florida developer wishing to offer his units for sale across the nation would be required to make seventeen filings in addition to his registration in Florida. A conservative estimate of the annual cost to the industry and, in the end, to the consumer is $13.5 million. This amounts to an additional $333 for each out-of-state condominium sold between 1970 and 1974.

The use of a single, uniform disclosure form for all condominium projects subject to the Act would essentially eliminate the problems caused by multiple and conflicting disclosure requirements.

We recommend that HUD develop a model disclosure form to be used by developers in preparing the disclosure abstract, as required in S. 2273. The Federal model form would be mandated for the sale of all condominiums subject to the provisions of the Act. A State could not require disclosure in addition to the Federal form and the disclosure statement required by the State in which the project was located.

The State could, however, place a warning on the Federal or Federally-approved disclosure form indicating which disclosure requirements of that State's law were not met by the out-of-state condominium.

Even more problematic than differing State disclosure requirements are direct conflicts in State laws. Such conflicts mean that a developer might be prevented from selling his project in another State because the out-of-state requirements differ from those of the State in which the project was located. For example, in

California the voting power of the unit owners is distributed on a one vote per unit basis. In New York, on the other hand, voting power is distributed on the basis of the ratio of the size of each unit to the total project square footage. A one unit/one vote division is not permitted. As a result, a California unit cannot be marketed in New York and vice versa.

We therefore recommend that a State not be permitted to prohibit the sale of out-of-state condominiums if the developer has complied with the recommended Federal requirements and the laws of the State in which the condominium is located. However, the State of New York, for example, could indicate on the disclosure form for the sale of a California unit in New York that "if this condominium were to be located within the State of New York, the voting rights of the unit owners could not be divided as indicated herein but would be divided on the following basis . . . ." and then set forth the basis.

EDUCATIONAL AND TECHNICAL ASSISTANCE

S.2273 does not include a provision for specific educational and technical assistance to the various sectors of the industry in addition to purchasers. We believe this is a serious oversight and does not address an important need in an area in which we believe a Federal response is appropriate.

We strongly recommend that such a provision be included in the bill, based on the recommendation of virtually everyone contacted during the course of our study.

Developers, lenders, and consumers alike agreed that such assistance improves the viability of condominium projects and reduces the problems and abuses affecting consumers.

The educational and technical assistance package would have two facets. First, a series of documents would be designed by HUD to inform potential purchasers (as provided for in the bill), lenders, sellers, and other participants of the basic definition of condominiums, of potential pitfalls involved in condominium ownership, and other information required to assist in making a wise and knowledgeable purchase decision. A second focus would be directed toward

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providing the homeowners association, developers, and individual unit owners with information relating to the proper management and maintenance of the condominium.

An informed public and experienced and knowledgeable managers and developers will do much to eliminate the recurrence of problems and abuses in the future. We believe that this combination of disclosure, regulatory and educational provisions will prevent the recurrence of the blatant and pervasive problems and abuses. Responsibility for administration is lodged at the most appropriate and responsive level, and there is sufficient flexibility to allow for differences within the several States.

OTHER PROVISIONS

S.2273 intends that the implementation and enforcement of the consumer protections contained in the bill be undertaken by the States. The Administration, while concurring in the objective, contends that this goal can be obtained without the involvement of the Department of Housing and Urban Development in certification of State condominium programs or the provision of cost sharing grants to the States.

Promulgating national minimum standards for condominium sales, and providing for the enforcement of those requirements through the courts, are, we believe the most efficient and least expensive methods of ensuring consumer protections. Certification of State programs would not add significantly to the consumer protections provided in the bill but would add significantly to the cost and level of Federal involvement necessary.

The Administration is opposed, for the same reasons, to the provision of grants to States which have received HUD certification. The benefits to the consumer do not warrant the expenditures that would be necessary. Further, as indicated in our condominium study, the distribution of condominium units and regulatory activity as well, is very localized. The grants to States would result in a transfer of tax monies from the least populated States, where there are few condominiums, to the most populated, where virtually all condominiums are located.

In addition, the Administration does not concur in the requirements of Section 12 of S.2273 dealing with investigations, injunctions and prosecution of offenses. All criminal and civil actions and other investigations should be left to the appropriate offices within the Federal Trade Commission and the Department of Justice.

I want to assure you that we are most willing and anxious to work with the committee in improving S. 2273. We agree that condominiums are here to stay, and that our concern for the health of the industry and the protection of the consumer has been warranted. We agree that the Federal role should be limited and the State role should be encouraged in order that differences among the States in local property law and in condominium development can be accommodated.

Again, thank you for the opportunity to appear before you today. I would be happy to respond to your questions.

94TH CONGRESS
1ST SESSION

S. 2273

IN THE SENATE OF THE UNITED STATES

AUGUST 1 (legislative day, JULY 31), 1975

Mr. PROXMIRE (for himself, Mr. BROOKE, and Mr. BIDEN) introduced the following bill; which was read twice and referred to the Committee on Banking, Housing and Urban Affairs

A BILL

To provide minimum national standards for disclosure and consumer protection in condominium sales and condominium conversions, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That this Act may be cited as the "Condominium Consumer Protection Act".

DEFINITIONS

SEC. 2. For the purposes of this Act, the term—

(1) "Secretary" means the Secretary of Housing and Urban Development;

(2) "condominium project" means a residential

development consisting of real property and any improvements thereto, in which individual dwelling units, together with undivided interests in the common elements, are offered for sale;

(3) "unit" means that portion of the condominium project designated in the condominium instruments for exclusive ownership and use by the unit owner;

(4) "condominium unit" means a unit in a condominium project, together with the appropriate undivided interest in the common elements;

(5) "common elements" means all portions of the condominium project, other than the units to which the condominium unit owners receive a right of exclusive use, enjoyment, and access;

(6) "condominium instruments" means all documents or instruments establishing or controlling the ownership or control of a condominium project or unit;

(7) "leasehold condominium project" means a condominium project in which each unit owner owns an estate for years in his unit, or in the land upon which that unit is situated, or both, together with an individual leasehold interest in the common areas, with all such leasehold interests due to expire at the same time;

(8) "conversion condominium project" means a condominium project containing structures wholly or

partially occupied prior to the time that the condominium instruments are drawn up and the condominium units offered for sale;

(9) "interstate commerce" means trade, traffic, transportation, communication, or exchange—

(A) between a place in a State and any place outside of such State; or

(B) which affects trade, traffic, transportation, communication, or exchange described in subclause (A);

(10) "Federally related condominium housing loan" means a loan which is made to finance the sale of a condominium unit to an individual or family and which—

(A) is made in whole or in part by a lender, the deposits or accounts of which are insured by any agency of the Federal Government, or is made in whole or in part by a lender which is itself regulated by any agency of the Federal Government; or

(B) is made in whole or in part, or insured, guaranteed, supplemented, or assisted in any way, by the Secretary or any other officer or agency of the Federal Government or under or in connection with a housing or urban development pro-

gram administered by the Secretary or a housing or related program administered by any other such officer or employee; or

(C) is made in whole or in part by any "creditor", as defined in section 103 (f) of the Consumer Credit Protection Act of 1968 (15 U.S.C. 1602 (f)), who makes or invests in residential real estate loans aggregating more than $1,000,000 per year;

(11) "sale of a condominium unit" means the transfer for consideration of a condominium unit, or in the case of a condominium unit in a leasehold condominium project, the long-term lease of a condominium unit;

(12) "developer" means any person who, directly or indirectly, offers for sale condominium units in a condominium project;

(13) "agent" means any person who represents or acts for or on behalf of a developer in selling or offering to sell any condominum unit in a condominum project, but such term does not include an attorney at law whose representation of another person consists solely of rendering legal services;

(14) "State" includes the several States, the District of Columbia, the Commonwealth of Puerto Rico,

and the territories and possessions of the United States;

(15) "purchaser" means an actual or prospective purchaser of a condominium unit; and

(16) "offer" includes any inducement or solicitation to encourage a person to acquire a condominium unit in a condominium project.

EXEMPTIONS

SEC. 3. Unless the method of disposition is adopted for the purpose of evasion of this Act, the provisions of this Act shall not apply to—

(1) the sale of real estate not pursuant to a common promotional plan to offer or sell ten or more condominium units in a condominium project;

(2) the sale of a condominium unit solely for commercial or industrial purposes or uses;

(3) the sale of real estate under or pursuant to court order; or

(4) the sale of real estate by the Federal Government or by any State or local government or any agency thereof.

PROHIBITIONS

SEC. 4. (a) It shall be unlawful for any developer or agent, directly or indirectly—

(1) to make use of any means or instruments of

interstate commerce or of the mails to sell or offer to sell any condominium unit in a condominium project; or

(2) to sell or offer to sell any condominium unit in a condominium project the purchase of which will be financed by a federally related condominium housing loan;

unless such developer or agent complies with the provisions of section 5 of this Act and furnishes the information required by section 6 of this Act.

(b) Any contract or agreement for the sale of a condominium unit which is subject to subsection (a) shall be voidable by the purchaser for a period of not less than fifteen days after the later of the execution of the contract or agreement, or the date on which the purchaser is furnished with the other information required by section 6. Upon the exercise of any right under this subsection, the developer or his agent shall refund fully and promptly any deposit or other prepaid fee or item to the purchaser.

NATIONAL STANDARDS FOR CONSUMER PROTECTION

SEC. 5. A sale or offer to sell a condominium unit in a condominium project which is subject to this Act may be made only if—

(1) any deposit or downpayment made in connection with the sale will be held in trust or escrow pursuant to regulations of the Secretary until delivered

at settlement or returned to, or otherwise credited to the purchaser, or forfeited;

(2) except in his capacity as an owner of unsold condominium units, the developer or agent will not retain an interset in any common element (including any recreational area or facility) after control of the condominium project is assumed by the owners' association unless, in the case of a leasehold condominium project, he will also retain that same type of interest in the entire condominium project;

(3) the unit owners will assume control of the common elements and of the condominium owners' association not later than one year after initial occupancy of the condominium project, or as soon as 80 per centum of the units are occupied, whichever is earlier;

(4) the condominium owners' association or the unit owners will not be subject to any management contract or other agreement enforceable against them after the expiration of six months after control of the common elements by the condominium owners' association becomes vested in such owners' association or owners, unless such a contract or agreement is renewed by a vote of the unit owners in accordance with the by-laws;

(5) the developer has furnished, as a minimum, a

two-year warranty (from the time of initial occupancy of the project) covering the full cost of labor and materials for any repair or replacement of roof and structural components, and mechanical, electrical, plumbing, and common service elements serving the condominium project as a whole, and a one-year warranty (from the time of initial occupancy of any unit thereof) covering the full cost of labor and materials for any repair or replacement of structural, mechanical, and other elements which pertain to such unit;

(6) the developer will assume the rights and obligations of a condominium unit owner in his capacity as owner of condominium units not yet sold prior to the assumption of control under clause (3); and

(7) in the case of a conversion condominium project, all tenants were offered an option, exercisable within not less than ninety days after notice, to purchase a condominium unit in the condominium project, and such tenants were given written notice of not less than one hundred and twenty days prior to being required to vacate the premises to facilitate the conversion.

NATIONAL STANDARDS FOR DISCLOSURE

SEC. 6. (a) Each developer of a condominium project which is subject to this Act shall disclose fully and accu-

rately to prospective purchasers of condominium units all material circumstances or features affecting such project, by preparing and providing to each prospective purchaser an abstract which shall contain—

(1) the name and address of the condominium project, and the name, address, and telephone number of the developer and of the project manager or his agent;

(2) a general narrative description of the project stating the total number of units, a description of the types of units and price of each type of unit, the total number of units that may be included in the project by reason of future expansion or merger of the project, and a precise statement of the nature of the interest which is being offered;

(3) a general disclosure of the status of construction, zoning, site plan, or other approvals, and compliance or notice of failure to comply with any other Federal, State, or local statutes or regulations affecting the project, and the actual or scheduled dates of completion of buildings, recreation facilities, and other common elements;

(4) the significant terms of any financing offered by or through the developer to purchasers of the condominium units in the project, including the name of any

bank or other institution involved in the financing, the minimum downpayment, and the interest rate;

(5) a brief description of any warranties for structural elements and mechanical and other systems, stated separately for the individual units and the common elements;

(6) a two-year projection (revised and updated at least every six months) of annual expenditures necessary to operate and maintain the common elements of the condominium project, certified to have been based on generally accepted accounting principles, and a complete statement of estimated monthly cost per unit for such two-year period including—

(A) the formula for determining each unit's share of common element costs;

(B) the amount of principal, interest, taxes, and insurance, each listed separately;

(C) the dollar amount of operating and maintenance expenses;

(D) the monthly cost of utilities; and

(E) any other costs, fees, and assessments;

(7) in the case of a project the construction of which was completed more than twelve months prior to the date of the offer, a report by an independent certified engineer stating the condition and rate of de-

preciation and remaining useful life of structural elements and mechanical and supporting systems, together with an estimate of repair and replacement costs projected for five years;

(8) a statement of significant provisions for management of the condominium project including—

(A) conditions for the formation of an owners' association;

(B) the apportionment of voting rights among the members of the association;

(C) any provisions concerning meetings and required notice thereof;

(D) provisions for the activities of officers of the association and their election, duties, and functions;

(E) the contractual rights and responsibilities of the owners' association; and

(F) the binding nature of any provisions of documents establishing or controlling the condominium project and the method of amendment of any portions relating to the owners' association;

(9) a statement of purchaser's right to review the condominium instruments, to void the contract, any conditions for the return of deposit, a statement about any

present litigation concerning the condominium project, and the rights of purchasers under section 9;

(10) a statement of the extent of commercial or other nonresidential development in or near the condominium project and the potential effects of such development on the interests, rights, or obligations of the condominium unit owners;

(11) the existence (or requirement for the establishment) of a reserve fund to finance the cost of repair or replacement of common element components; and

(12) a clear, concise definition of all essential terms used in the abstract.

ESTABLISHMENT OF STATE CONDOMINIUM PLANS

SEC. 7. (a) Nothing in this Act may be construed to prevent or limit the authority of any State or local government to exercise authority or assert jurisdiction with respect to—

(1) any condominium project or condominium unit to which the provisions of this Act do not apply; or

(2) any matter which is not directly subject to the protections afforded by this Act.

(b) (1) It is the intent of Congress to encourage the assumption and exercise by States of the authority and

responsibility for the enforcement of the requirements of this Act.

(2) Any State may assume responsibility for the enforcement of the standards contained in this Act by obtaining from the Secretary approval of a State plan providing for the enforcement of such standards. A plan submitted by any State under this paragraph shall be approved by the Secretary if such plan—

(A) designates a State agency to administer the plan throughout the State;

(B) contains such assurances as the Secretary may prescribe with respect to the provision of adequate personnel and financial support for the designated agency;

(C) contains standards which meet or exceed the standards set forth in or under this Act;

(D) provides for the imposition of civil and criminal penalties at least as severe as the penalties which may be imposed under sections 9 and 10 of this Act;

(E) provides that the State agency will report to the Secretary at such times and in such manner as the Secretary may prescribe;

(F) complies with such other requirements as the Secretary may prescribe; and

(G) provides to the extent provided by State law

for the assumption by units of local government of the functions which may be assumed by a State under this section.

(3) If the Secretary determines that a State has, on the effective date of this Act, a condominium consumer protection law in effect, the provisions of such State law shall continue to apply in such State, and the provisions of this Act will not apply in such State, until the expiration of one year following such effective date or until such State plan is approved by the Secretary, whichever is earlier. Notwithstanding the preceding sentence, if, prior to the expiration of such one-year period, the Secretary determines that any provision of that law does not meet or exceed the requirements of or under this Act, he may disapprove such law and the provisions of this Act shall thereafter apply in such State.

(4) For the purpose of this subsection any provision contained in a State plan or law shall be deemed to meet or exceed a requirement of or under this Act if it provides the same or greater protection for prospective purchasers or if it provides for the same or greater disclosure to such purchasers, as the case may be.

(c) (1) The Secretary shall by order approve or disapprove a State plan submitted under subsection (b) not later than ninety days after the date of its submission. If the Secretary fails to take any action with respect to such a plan

within such ninety-day period, the State plan shall be deemed to be approved.

(2) Subsequent to any approval under paragraph (1), the Secretary shall review the administration of the plan at least annually to determine whether such plan is being carried out in a manner which complies with the provisions of this section. Upon any finding that the administration of the plan no longer meets the requirements of this section, the Secretary may issue an order disapproving such plan and the provisions of this Act shall apply in full in such State.

(d) (1) The Secretary may not issue an order disapproving any State plan under this section or determining any State law not to meet or exceed a requirement of or under this Act unless he has granted the State and interested persons notice and an opportunity for an agency hearing on the record with respect to the State plan or law.

(2) Any determination by the Secretary under this section shall be subject to judicial review in accordance with chapter 7 of title 5, United States Code, in the United States court of appeals for the circuit in which is located the State whose plan or law is the subject of such determination or in the United States Court of Appeals for the District of Columbia Circuit. Any such review shall be instituted within sixty days from the date on which the determination is made by the Secretary.

ASSISTANCE TO STATES

SEC. 8. (a) The Secretary is authorized to provide such technical assistance and information to the States to assist them in developing State plans as may be necessary or appropriate to carry out the provisions of section 7.

(b) (1) The Secretary may make grants where necessary to assist any State—

(A) in identifying its needs and responsibilities in the area of condominium sales disclosure and condominium consumer protection; or

(B) in developing a State condominium plan.

(2) The Governor of each State may designate an appropriate State agency for the receipt of any grant under this section prior to the designation of a State agency under section 7.

(3) The Federal share for a State grant under this subsection may not exceed 25 per centum of the total cost incurred by the State in carrying out the activities under paragraph (1). Payments under this subsection may be made in installments or in advance or by way of reimbursement with necessary adjustments on account of underpayments or overpayments.

CIVIL PENALTIES

SEC. 9. (a) Any developer or agent who sells any interest in a unit subject to this Act and who does not

comply with provisions of this Act is liable to the purchaser in an amount equal to the difference between the amount paid for the unit, and the lesser of (1) the value thereof as of the time such suit was brought, or (2) the price at which such a unit shall have been disposed of in a bona fide market transaction before suit, or (3) the price at which such a unit shall have been disposed of after suit in a bona fide market transaction but before judgment.

(b) In no case shall the amount recoverable under this section be less than the sum of $500 for each failure to comply and for each purchaser bringing an action under this section, together with court costs and a reasonable attorney's fee.

CRIMINAL PENALTIES

SEC. 10. Any developer or agent who willfully violates any provision of section 5 of this Act, or who willfully makes any untrue statement or omits to make any statement required to be made in violation of the provisions of section 6 of this Act shall upon conviction be fined not more than $10,000, or imprisoned for not more than one year, or both for each such violation, statement, or omission.

JURISDICTION

SEC. 11. The district courts of the United States, the United States courts of any territory, and the United States

District Court for the District of Columbia shall have jurisdiction of offenses and violations of this Act and under the rules and regulations prescribed by the Secretary pursuant thereto, and concurrent with State courts, of all suits in equity and actions at law brought to enforce any liability or duty created by this Act without regard to amount in controversy. Any such suit or action may be brought to enforce any liability or duty created by this Act. Any such suit or action may be brought in the district wherein the defendant is found or is an inhabitant or transacts business, or in the district where the offer or sale took place, if the defendant participated therein, and process in such cases may be served in any other district of which the defendant is an inhabitant or wherever the defendant may be found. Judgments and decrees so rendered shall be subject to review as provided in sections 1254 and 1291 of title 28. No case arising under this Act and brought in any State court of competent jurisdiction shall be removed to any court of the United States, except where the United States or any officer or employee of the United States in his official capacity is a party. No costs shall be assessed for or against the Secretary in any proceeding under this Act brought by or against him in the Supreme Court or other such courts.

INVESTIGATIONS, INJUNCTIONS, AND PROSECUTION OF OFFENSES

SEC. 12. (a) Whenever it shall appear to the Secretary that any person is engaged or about to engage in any acts or practices which constitute or will constitute a violation of the provisions of this Act, or of any rule or regulation prescribed pursuant thereto, he may, in his discretion ,bring an action in any district court of the United States, or the United States District Court for the District of Columbia to enjoin such acts or practices, and, upon a proper showing, a permanent or temporary injunction or restraining order shall be granted without bond. The Secretary may transmit such evidence as may be available concerning such acts or practices to the Attorney General who may, in his discretion, institute the appropriate criminal proceedings under this Act.

(b) The Secretary may, in his discretion, make such investigations as he deems necessary to determine whether any person has violated or is about to violate any provision of this Act or any rule or regulation prescribed pursuant thereto, and may require or permit any person to file with him a statement in writing, under oath or otherwise as the Secretary shall determine, as to all the facts and circumstances concerning the matter to be investigated. The Secretary is au-

thorized, in his discretion, to publish information concerning any such violations, and to investigate any facts, conditions, practices, or matters which he may deem necessary or proper to aid in the enforcement of the provisions of this Act, in the prescribing of rules and regulations thereunder, or in securing information to serve as a basis for recommending further legislation concerning the matters to which this Act relates.

(c) For the purpose of any such investigation, or any other proceeding under this Act, the Secretary, or any officer designated by him, is empowered to administer oaths and affirmations, subpena witnesses, compel their attendance, take evidence, and require the production of any books, papers, correspondence, memorandums, or other records which the Secretary deems relevant or material to the inquiry. Such attendance of witnesses and the production of any such records may be required from any place in the United States or any State at any designated place of hearing.

(d) In case of contumacy by, or refusal to obey a subpena issued to, any person, the Secretary may invoke the aid of any court of the United States within the jurisdiction of which such investigation or proceeding is carried on, or where such person resides or carries on business, in requiring the attendance and testimony of witnesses and the production of books, papers, correspondence, memorandums, and other records and documents. And such court

may issue an order requiring such person to appear before the Secretary or any officer designated by the Secretary, there to produce records, if so ordered, or to give testimony touching the matter under investigation or in question; and any failure to obey such order of the court may be punished by such court as a contempt thereof. All process in any such case may be served in the judicial district whereof such person is an inhabitant or wherever he may be found.

RULES, REGULATIONS, AND ORDERS

SEC. 13. (a) The Secretary shall have authority, from time to time to make, issue, amend, and rescind such rules and regulations and such orders as are necessary or appropriate to the exercise of the functions and powers conferred upon him elsewhere in this Act. For the purpose of his rules and regulations, the Secretary may classify persons and matters within his jurisdiction and prescribe different requirements for different classes of persons or matters.

(b) The Secretary is authorized to prescribe, in cooperation with appropriate Federal, State, and local officials, standard forms, instruments, and documents for use in connection with the sale of condominium units and for carrying out his functions under this Act.

(c) In addition to the standards contained in this Act, the Secretary may, after notice and opportunity for public

comment, prescribe additional standards for consumer protection or for disclosure which shall be applicable to condominium projects subject to this Act.

(d) The Secretary is authorized to prepare and distribute informational booklets describing the nature of a condominium unit and the protections afforded by this Act, and to require that any person considering the purchase of a condominium unit be provided with such a booklet by the developer or his agent.

CONTRARY STIPULATIONS VOID

SEC. 14. Any condition, stipulation, or provision binding any person acquiring any condominium unit in a condominium project subject to this Act to waive compliance with any provision of this Act or of the rules and regulations of the Secretary shall be void.

ADDITIONAL REMEDIES

SEC. 15. The rights and remedies provided by this Act shall be in addition to any and all other rights and remedies that may exist at law or in equity.

AUTHORIZATION OF APPROPRIATIONS

SEC. 16. There are authorized to be appropriated such sums not to exceed $10,000,000 as may be necessary to carry out the provisions of this Act.

EFFECTIVE DATE

SEC. 17. The provisions of sections 4, 5, and 6 of this Act shall become effective, and shall apply to any offer made or contract entered into, after the expiration of one year after the date of its enactment.

EXEMPTION FROM OTHER PROVISIONS OF LAW

SEC. 18. Compliance by a developer with the requirements imposed by or under this Act through a State plan approved under section 7 with respect to a condominium project located in that State shall be deemed to satisfy any requirement now or hereafter imposed under the Securities Act of 1933.

Secretary HILLS. I hope you have had the opportunity to review the principal findings of the detailed study of condominiums which HUD has conducted for the past year in accordance with section 821 of the Housing and Community Development Act of 1974.

In the course of that study we conducted extensive research on the industry and talked with dozens of consumers, Government housing officials, attorneys, lenders, industry officials, and others involved in the condominium market. We held public hearings in February and March of this year in Washington, D.C., and in Fort Lauderdale, Fla., to obtain firsthand data on the problems and abuses which have been occurring.

In our examination of the possible solutions to these problems we surveyed the present efforts of State and local governments in regulating condominiums. The study provides sound, factual data to use in determining the need and scope of any Federal intervention in the condominium market.

Next, I'd like to highlight a few of the chief conclusions of the study to provide a framework for my specific comments on S. 2273.

The number of condominiums increased 15-fold between 1970 and 1974, from 85,000 units to 1,250,000 units nationwide. Approximately 100,000 units were converted to condominiums from rental properties. Condominium development has been concentrated in certain parts of the country with Florida and California having by far the largest inventory of condominiums.

Condominiums compete successfully with conventional, single family homes on the basis of price, amenities, and location. The reduced maintenance responsibilities involved in condominium ownership attracts primarily young childless couples and couples of 45 to 65 years of age whose children are no longer living at home.

Some local officials have favored condominiums which generally require less land because of their higher density which may increase opportunities for home ownership and an expanded tax base. Converting projects to condominium status offers the potential for upgrading the housing stock. Ninety-five percent of the unit owners who responded to our survey replied that they were satisfied or very satisfied with their units. Nonetheless, our study did identify a number of significant problems for consumers which I will discuss in my comments on S. 2273.

We found that the problems affecting the condominium market have not had a severe impact at the national level but we found that some of them have had a serious impact on those directly affected.

Our study also included a comprehensive survey of State and local legislative activity. Since the condominium concept was first introduced in the United States in the early 1960s, every State has enacted basic enabling legislation to permit a condominium form of ownership. In response to the problems and abuses which accompany the recent surge in condominium construction, over half the States have amended their basic condominium statutes or have relied upon general subdivision statutes, land sales registration, or securities statutes to develop disclosure or regulatory controls to curb such abuses.

In general, our study found that the jurisdictions which have most actively regulated condominiums are those in which most condominium development has occurred and that the variety of statutory

approaches undertaken by the States appears to be an informed response to the diversity of real estate practices and property laws.

At this point I'd like to turn to the Administration's view on your legislative proposal based upon the results of our study and careful analysis of the proposal.

The bill has three major aspects: national standards for consumer protection and disclosure; assistance to the States to enforce those standards; and civil and criminal penalties for noncompliance.

We agree that there is a need to promulgate national minimum standards for disclosure and consumer protection and the sale of both new and conversion condominiums as long as these standards are kept to a minimum and do not involve Federal registration or direct regulation by HUD. Thus, we think that the basic approach proposed in S. 2273 is correct.

However, some provisions of the bill are, we feel, unworkable or unnecessary and there are certain modifications which we believe would strengthen the bill and provide an added measure of assistance to consumers.

With respect to the consumer protection standards, we believe that certain substantive standards should be left to the States in order that these requirements might be tailored to the diverse nature of the condominium market within those jurisdictions.

First, the condominium study found that the problem of long-term recreation leases is not an extensive one outside of Florida and that few new condominium projects are currently being sold with such leases. Further, recreational leases have significantly reduced the purchase price of some condominium units and have provided facilities that home owners could otherwise not afford. We estimate that recreation leases reduce the costs of a condominium unit from $2,000 to $8,000. Therefore, we feel that the bill unnecessarily contains a prohibition against any developer retention of interest in common elements such as recreation areas after control has been transferred to the owners association.

Secondly, the bill provides that the transfer of control from the developer to the owners association must be made within a year of initial occupancy or when 80 percent of the units are occupied. Our study has shown that there are many cases in which a requirement that control be transferred within 1 year would not be beneficial to consumers, developers, or lenders.

Thirdly, the bill would require a 2-year warranty on common elements and a 1-year warranty on individual units. We oppose the bill's onerous warranty requirements which would add substantially to the purchase price of the condominium unit. We have estimated that such a warranty on the average new condominium unit might cost as much as $1,600 and in older buildings could be twice this amount.

Fourthly, the bill would make service and management contracts voidable 6 months after control is transferred to the unit owners. The State of Virginia recently amended its law to eliminate a similar requirement because it caused all contracts, including such beneficial agreements as service contracts on elevators, to be voided. The provision added an element of risk to service contracts and thereby increased the cost to the home owners. We believe that the new Virginia

statute which eliminates any risk factors for commercially reasonable contracts is a preferable approach.

Finally, the bill would require that a developer assume all rights and obligations of a unit owner for unsold units prior to the transfer of control to the unit owners. We believe that the resulting additional cost to developers would be passed on to the consumer without sufficient benefit to justify the cost. We question whether a developer should be required to pay the full assessment for unsold units if the units are unoccupied and do not create expenses for utilities or maintenance.

We fully endorse the other consumer protection provisions contained in S. 2273, including the 15-day cooling off period, the 90-day minimum period in which tenants are offered the right of first refusal on purchasing a unit in the project, the minimum 120-day notice of requirement to vacate the premises, and the requirement for escrow of consumer deposits.

In summary, we support only those Federal consumer protection standards whose benefits outweigh their costs. A Federal condominium law should contain simple and explicit consumer protections that have as limited an economic impact as possible on the consumer, do not unnecessarily restrict the industry, and permit the States to act within their jurisdiction to the extent they deem appropriate to provide additional protection which might in their judgement be necessary.

With respect to national standards for disclosure, we are concerned that Federal disclosure requirements also be reasonable. Highly technical and voluminous disclosure statements are costly and we found during the study that they often are not read by the buyer.

Disclosure statements should be simple and limited to the provision of the information essential to a prudent purchase decision by consumers. Compliance with these requirements should not result in substantial additional costs nor discourage future condominium development. We are pleased to note that the draft bill does not contain requirements for registration or review of condominium documents by the Department.

We generally concur in the items required to be disclosed by S. 2273 and suggest in addition that developers be required to disclose all liens or encumbrances on the condominium. We would also recommend that the requirements for C.P.A. certification for a 2-year budget projection be dropped as unworkable and that instead the developer be required to disclose a 1- or 2-year budget estimate.

A Federal disclosure law could be a vehicle to solve one problem that became quite clear in our review of State condominium laws. There are a number of overlapping and contradictory requirements which make it difficult, and in some cases, impossible for developers to offer condominiums in certain States. At present, 18 States have laws that regulate to varying degrees the sale of out-of-State condominiums in their State.

The multiple filings that can be required under current laws are expensive and most of the expense is passed on to the consumer. For example, a Florida developer wishing to offer his units for sale across the Nation would be required to make 17 filings in addition to his

registration in Florida. A conservative estimate of the annual cost to the industry and in the end to the consumer is $13.5 million.

The use of a single uniform disclosure form for all condominium projects subject to the act would essentially eliminate the problem caused by multiple and conflicting disclosure requirements.

We recommend that HUD develop a simple model disclosure form covering eight basic items to be used by developers in preparing the disclosure abstract as required by S. 2273 and that the form be mandated for the sale of all condominiums subject to the provisions of the act. We recommend that States be precluded from requiring disclosure in addition to the Federal form and the disclosure statement required by the States in which the project was located.

The State could, however, place a warning on the Federal disclosure form indicating which disclosure requirements of that State's laws were not met by the out-of-State condominium.

Even more troublesome than differing State disclosure requirements are the direct conflicts in State laws. Such conflicts mean that a developer might be prevented from selling his project in another State because the out-of-State requirements differ from those of the State in which the project was located. For example, in California, the voting power of the unit owners is distributed on a one-vote-per-unit basis. In New York however, voting power is distributed on the basis of the ratio of the size of each unit to the total project square footage and one unit/one vote division is not permitted. As a result, a California unit cannot be marketed in New York and vice versa.

We therefore recommend that a State not be permitted to prohibit the sale of out-of-State condominiums if the developer has complied with the recommended Federal requirements and the laws of the State in which the condominium is located. However, the State of New York, for example, could indicate on the disclosure forms for the sale of a California unit in New York that if this condominium were to be located in the State of New York the voting rights of the unit owners could not be divided as indicated herein but would be divided on the following basis—and then set forth that basis.

We also oppose HUD's certification of State condominium programs, grants to certified States, investigation and enforcement by HUD, and the specification of penalties. We believe that these provisions would not add significantly to the degree of protection supplied by the act and that the cost in increased Federal involvement does not justify their inclusion.

Further, the administration supports an exemption from filing with the Securities and Exchange Commission as contained in S. 2273. We would recommend that an appropriate exemption from filing with the Office of Interstate Land Sales Registration also be included.

Finally, the bill does not include a provision for specific educational and technical assistance to the various sectors of the industry in addition to purchasers. We believe that this is a serious oversight and does not address an important need in an area in which we believe a Federal response is appropriate.

I want to assure you that we are most willing and anxious to work with the committee in improving S. 2273. We agree that condominiums are here to stay. We agree that the Federal role should be limited and that the State role should be encouraged in order that the

differences among the States in local property law and in condominium development will be accommodated.

I thank you very much for the opportunity to appear before you today. I would be happy to respond to your questions.

The CHAIRMAN. Well, thank you very much, Mrs. Hills, for your presentation.

We have been hearing a lot of complaints recently about the cost and burden of Federal laws designed to help the consumer. We have just been through a very difficult time with RESPA, Real Estate Settlement Procedures Act, a large part of which we expect to repeal. Senator Morgan and Senator Garn and some of the rest of us have been working hard on that and we expect to accomplish the repeal of titles IV, VI, and VII within a few weeks. At least we hope so.

Now your statement suggests the present situation involves a lot of cost and redtape that is absent in the Federal law. With differing conflicting State laws, complicated and confusing documents, and a lot of dissatisfied consumers whose complaints have helped to enfeeble the condominium market, do you think the Federal condominium legislation along the lines you have described could actually cut the cost and lighten the paperwork on the industry rather than the reverse?

Secretary HILLS. I do.

The CHAIRMAN. It seems to me this bill has a lot in it to benefit the condominium industry as well as the consumers, especially in the light of the bad names the condominiums have been getting because of the abuses, a bad name that may not be justified in view of your testimony that 95 percent of the people are either satisfied or very satisfied. What's been the reaction of the industry in the States that have recently adopted condominium laws?

Secretary HILLS. I think that in States such as California and Hawaii, which have had rather extensive regulatory schemes, the industry reaction after a period of time has been positive because the consumer feels confident and a confident consumer means a buyer. So I think that the reaction is generally positive from the developers point of view, and I'm certain that it is positive from the consumers' point of view.

On the other hand, I think undue regulation only adds to the complexity of the regulation. The point I made in my prepared remarks was that where a developer is frustrated by having to comply with 17 different kinds of regulations this puts a burden on him which increases his costs and ultimately translates into added expense for the consumer.

I think our approach therefore is to have a minimum kind of regulation that will encourage uniformity and simplicity. Our approach would allow each State to regulate the sale of condominiums located within its borders, but would provide uniform and moderate Federal regulation for sales of condominiums located outside the State's borders.

The CHAIRMAN. Now you suggest that HUD develop a model disclosure form that would be required in all condominium sales covered under the act. That goes farther than my bill which says States can adopt their own condominium plans and include additional standards as long as they meet all the Federal standards.

Would your approach still allow the States this flexibility which would be helpful to enable them to deal with particular problems that the Federal law won't reach?

Secretary HILLS. Yes. They would have the option to regulate the sale of condominiums located within their borders. Our interest in providing for the eight basic items of disclosure was to provide a minimum uniform document so that the Florida developer would not have to fill out different disclosure forms for each of the 17 States which have regulatory schemes in order to market units outside of Florida.

The CHAIRMAN. Well, then, I take it you mean that the States would use the HUD form as the basic document but would be free to impose additional disclosure or other requirements as long as they didn't contradict the Federal law. Is that right?

Secretary HILLS. That is basically true. In addition, a State could place upon the Federal uniform disclosure form an admonition that were this unit to have been built within that State, the State would have imposed additional or different restrictions.

The CHAIRMAN. If your recommendation were put into effect, would consumers lose any significant rights that they now have under State laws?

Secretary HILLS. There are some States which have more stringent regulations than our minimum proposed standards and disclosure requirements. However, we also provide assistance by our focus on consumer education. I think the honest answer is, yes, there are some consumers in some States who could be less protected by the Federal minimum approach, but I do believe that these are limited in number.

For example, I recall that with respect to New York there is heavy regulation and yet the filing in New York from out-of-State developers is not universal. I believe that minimum Federal disclosure and simple Federal regulatory standards would provide all consumers with a greater amount of protection. When the volume of materials supplied to the consumer becomes large, the inclination of most persons is to file it and not to read it. Our approach would encourage consumers to read the disclosure form, we think, and hence reduce abuses.

The CHAIRMAN. I wholeheartedly approve of what you're saying and I think all of us agree that we would like to get forms as simple and as clear as possible. The purpose of all this is to inform the consumer and with the least possible minimum requirements on the part of the seller so that the industry is not handicapped and the consumer is informed.

What realistic possibilities are there of getting this kind of simple form that would help consumers without excessive burden on the seller?

Secretary HILLS. Consumers would be greatly helped by the 15-day cooling off period, the 90-day notice and the right of first refusal when a unit is to be converted, a 120-day notice to vacate, and the requirement that deposits be escrowed. I think that we are of the same mind on those four basic standards.

In addition, the tight items of disclosure that we have alluded to—and I would be delighted to read them to you—will provide substantial protection to the consumer. In addition, an informational booklet, which would have a description of the most numerous problems and

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the things to look for, plus materials that address managerial problems will protect the consumer.

I think this combination is going to provide far more protection than uneven regulation which is heavy in some places and nonexistent in others.

The CHAIRMAN. In discussing this with the staff on Friday, I suggested that we take a kind of unique and unusual action with respect to the bill this time. We have learned a lot from RESPA and maybe we have overreacted to it, but would you oppose our holding up the enactment of the bill until we had a chance to find out how much time and effort and money the bill would add to buying, selling, or building a condominium. Recognizing in many cases it would reduce the time and how much disclosure protection would be worth to the condominium buyer, we'd like to look and see what the forms were. If we had done this with some of the previous acts we have enacted we would have saved the consumers puzzling and overwhelming data they don't need and we would have greatly eased the burden on the industry. Would you think that would be practical for the committee to proceed in that way?

Secretary HILLS. Certainly. I see no objection to trying to develop a form so that we are of the same mind when we discuss it. I have in mind eight basic disclosure provisions but how I articulate them may be different and certainly may benefit from editing.

The CHAIRMAN. Very good. One of the parts of RESPA that was so vigorously protested was the cooling off period, as you know. It was said in many cases it killed sales unfairly and it would inconvenience greatly consumers that would travel some place and not be able to move in because of the cooling off period. There were many difficulties involved in it. You say that you support the provision allowing a 15-day cooling off period for review of the documents after purchase contract was signed.

Do you find any problems with the length of that cooling off period?

Secretary HILLS. No. I would recommend the 15 days. I think that if the consumer buys rapidly there is a greater opportunity for that consumer not to be fully apprised of the step that he or she is taking. Two weeks does not seem to be an undue burden on the industry. We came to that conclusion based upon our hearings and a number of consultations with developers, consumer groups, and local officials who are engaged in condominium regulation.

The CHAIRMAN. Do we need a waiver provision or is it obvious from the language that settlement occurs before the end of 15 days if the buyer so chooses?

Secretary HILLS. I think that the provision in your bill which states that the contract shall be voidable is adequate. That means a happy purchaser won't void, but the unhappy purchaser who was swept into a purchase before the necessary information was provided to him or her will be able to get out of that contract. I think that's probably the best approach. To protect himself, the developer will be on the horns of a dilemma—he will either give the 15 days or be prepared to refund fully the remuneration that passed under the contract.

The CHAIRMAN. Well, let me think about that a little more. The problem, of course, is that in many cases you may have a sophisticated

businessman who may be in the real estate business himself buying a condominium and he doesn't want to wait around 15 days and look at this in a short time and be on top of it and be in a position to evaluate it. In other cases you do need that length of time.

What I'm wondering is whether or not this is discretionary with the consumer actually. If he wants to close the deal in less than 15 days and he wants to do it in a day or two, is he free to do so under the law as you read it?

Secretary HILLS. The way your language is drafted, it does not address waivers. Waiver provisions often are automatically offered to the consumer. The waiver becomes a part of the package and every consumer waives. I think it is an interesting balance and we could look into how many closings take place in fewer than 15 days. I suspect there are not a large number.

The CHAIRMAN. You suggest getting rid of the requirement of HUD review and approval of State condominium plans. That certainly would cut out some delay, but wouldn't there be some problem with State laws that conflicted with the Federal law?

Secretary HILLS. There would be State laws which would be more aggressive in their regulation and there would be State laws that would be less aggressive. I think that the approach in S. 2273 and the one that we would support is a moderate approach. It's a rather simple set of basic requirements for consumer protection.

The CHAIRMAN. What incentive would there be for a State to improve their laws?

Secretary HILLS. Well, if they felt that more could be done within their jurisdiction as to condominium projects located within their States, of course they would have a free hand. I think because the standards and the disclosure are limited in nature there are areas which the States could address that would be peculiar to local law.

The CHAIRMAN. My time is almost up but I will come back.

Senator Morgan?

Senator MORGAN. Mrs. Hills, in your study you found that more than half of the States have already enacted condominium consumer protection acts? Is that what I understood you to say?

Secretary HILLS. There's a chart as to the number of States that have enacted basic kinds of statutes. They vary into about five groups from the basic enabling legislation to a licensing approach to a disclosure approach, and then there are regulatory statutes and full regulatory statutes. I would say that about half have what we would call a regulatory scheme.

Senator MORGAN. Did your findings also disclose that most of the condominiums that have been developed and sold in this country lie within those States that have enacted consumer protection laws?

Secretary HILLS. Yes.

Senator MORGAN. What States are most active? Florida, California, New York, Virginia?

Secretary HILLS. And Hawaii.

Senator MORGAN. Do you find that the laws in those States where condominiums are most prevalent have been fairly adequate consumer protection laws?

Secretary HILLS. Yes. I would say that our quarrel is not with their inadequacy although developers in some States have had problems in trying to comply with the regulations of others.

Senator MORGAN. In that connection, Mrs. Hills, is it not true that a developer who's going to develop condominiums in one State—California is the example that you gave—and market those condominiums in the State of New York, is probably a pretty good sized developer and has an adequate staff to know and to understand the laws in the States in which he's going to market. So does that really present any real problem for a substantial number of developers?

Secretary HILLS. I think that it affects—and I asked that question when the report came up—something in excess of 20 percent of the sales. I think it isn't only the California developer seeking to comply with the New York regulations—and you happen to have picked a State which has extensive regulation—and so the cost appended to complying with that regulation is substantial and are passed on to the consumer. Some have given estimates of $50,000 per project—but also complying with Michigan, Hawaii, Florida, and the other States where the potential purchasers may be residing.

Senator MORGAN. But isn't it true that very, very few developers will market condominiums in more than two or three different States?

Secretary HILLS. We have not found that necessarily to be the case. There can be literature mailed into States, and it is not necessarily limited to one or two States. It may be a large number.

Senator MORGAN. Well, it may be, but what I'm trying to get at, Mrs. Hills, is that it seems to me that we are about to impose some rather stringent regulations from the Federal bureaucracy on builders all across the country in States where there are relatively few problems, solely for the protection maybe or convenience of a relatively small number of builders who are able to know and understand the laws of other States. For instance, I noticed in the testimony of the Minnesota official who's going to testify today—or it may have been in your statement—that there were about 160 condominiums in Minnesota if I read it right. It might be an unreasonable burden in those States where condominiums are relatively few in number and certainly an unreasonable burden on the local builders who are going to build and market condominiums in maybe one small market.

Secretary HILLS. Let me respond this way, Senator. First of all, I do not think that these proposed standards are stringent; and second of all, when we talk about protection of the few large developers, we are also talking about the protection of all their consumers.

Senator MORGAN. We are talking about the convenience of a few large developers. I didn't say anything about protection for them.

Secretary HILLS. Let me talk about convenience in terms of cost to the developer and ultimately to the consumer because that's how I look at this problem. It's really a balance of the regulation versus the cost of that regulation. The convenience of the developer in not having to register and in not having to prepare documents for a large number of States or even the convenience of a small developer in not having to register in one other State, translates in lower costs for the consumer.

Senator MORGAN. Sort of like the RESPA forms?

Secretary HILLS. I can't compare it to the RESPA forms because I regard this as far more modest and more uniform. This approach picks up from States which have regulation and utilizes their experience.

For example, one of the reasons why we oppose the requirement in S. 2273 with respect to prohibiting contracts that the developer had entered into is that we were informed from the Virginia experience that service contracts could indeed become much more expensive if such contracts were voidable. Based upon that experience we would back off of such a requirement and utilize the Virginia—and there are a number of other States—experience and permit commercially reasonable contracts.

Senator MORGAN. Well, let's go back to another subject. Mrs. Hills. Your findings were that 95 percent of the purchasers of condominiums were either satisfied or very satisfied?

Secretary HILLS. That's correct.

Senator MORGAN. So then we're talking about now in terms of protection of the 5 percent. But is it not true, Mrs. Hills, that the vast majority of all condominiums that have been sold have been sold in States that have consumer protection acts for condominium purchasers?

Secretary HILLS. That is correct.

Senator MORGAN. Well, aren't we really about to enlarge the bureaucracy that you head? And as I remember the testimony when you were confirmed, there was a great deal of discussion that it had become unmanageable already, and aren't we about to say to these States that: "You haven't adequately regulated consumer or enacted consumer protection acts, and therefore we all knowing and all powerful Federal Government is going to usurp"—and I really think that's what it is—"usurp this responsibility." Don't you think you could do better by working with the States and encouraging those that do not have adequate laws to enact them rather than trying to enlarge your bureaucracy and make it so difficult for the small builder and contractor to understand and comply with more regulations.

Secretary HILLS. It's precisely the last point which pushed me to the view that a very modest statement of minimum standards and very modest disclosure standards, just eight points, would be helpful because they are going to be easier for the developer to comply with than the full spectrum of State-regulatory schemes.

Senator MORGAN. Well, we'll go back again to what I was talking about. The developer who's going to market his condominiums in more than one State, in my estimation, is generally the developer who's large enough and has enough expertise and enough staff to easily meet the requirements of other States.

Secretary HILLS. At a cost.

Senator MORGAN. At a cost. He's usually large enough to do that. I believe we ought to keep the Federal Government out of areas where the States have demonstrated that they are acting responsibility. I take second place to no one in being a consumer advocate and when I was attorney general in my State I was bringing State consumer law actions second to no other State, but that's where it can best be done. I haven't seen any area in which I think the Federal Government can do a better job than State governments if the States are doing it, and apparently from your study it's pretty clear to me that they are doing it.

Secretary HILLS. Well, they are doing it now and we have taken many helpful examples from the States. The 5 percent of consumers who felt the burden of the abuses, of course, are heavily impacted and they are spread around. We believe that condominium development will continue to grow in the next 5 years as it has over the last 5 years, so those States which have developed some regulation will be joined by others.

I have considerable sympathy for your words because I came into this study with a view that we should engage in education and that the Federal role should be limited, but during the course of our study I also gained considerable sympathy for the frustrations arising from the lack of uniformity, and many of the people with whom we consulted—developers, consumers, and local officials alike—were quite concerned by the overlapping and conflicting requirements between States. It may be in this area that the Federal Government has a better vantage point to enforce minimum standards and to allow development to occur across State lines. That was persuasive to me, but I am sympathetic with your view.

Senator MORGAN. Well, uniformity, of course, is desirable, but it would also be desirable in motor vehicle traffic laws. It would be desirable in selling consumer products and so on. But how many additional personnel would have to be added to your department to carry out the provisions of this act?

Secretary HILLS. With the changes we have recommended, very few I think. We have removed HUD from reviewing State proposals. What HUD would do would be to have a role—and I think you would support this—in the educational and technical assistance material. We would need some people for that. I believe that with our present staff we could develop the minimum disclosure points. The sponsors have already begun developing the prohibitory standards, what I call the minimum consumer protection standards. We have pointed out where we have problems in those areas. So I don't see a large HUD role in the condominium area.

If you had the opportunity to look at our full statement you would see that we are opposed to taking on an enforcement role. We think we have enough Federal enforcement agencies with the Federal Trade Commission and the Department of Justice without putting HUD into that role. As we went through the bill we really tried to be constructive. Based upon our study we have recommended actions that would help the consumer on balance with respect to cost or could eliminate a lot of duplication or conflict. We would also provide education where we felt it would be useful, but our role is minimal.

Senator MORGAN. I'll have to study your statement in light of the chairman's bill, but as I understood your statement, in many ways you would be more stringent than this bill on States. As I understood the chairman's bill, if the States complied with certain minimum standards, they would not be affected.

Secretary HILLS. Let me be candid, because I think that is correct. As the bill was originally drafted, there would be minimum Federal requirements, a scheme of grants to encourage the States to participate by subsidizing 25 percent of their costs, and a scheme to give HUD a regulatory and enforcement role. We think that is excessive involvement.

We think we should decrease the complexity of regulation and burdens on the industry by having a minimum statement of standards and disclosure.

Senator MORGAN. Let's go back to the chairman's bill. As a lawyer, don't you think that the chairman's bill would be more acceptable in that the penalties in the bill itself, if I understand it right, would probably best be enforced in the State courts? We've got a bill pending now on the floor of the Senate that would provide for more than 50 new Federal judges at a—I have no idea how much it's going to cost—and considering the backlog in the Federal criminal courts and the Federal civil courts, and then we come along and make it a $10,000 penalty for violating section 5 and 6 and so on—wouldn't it be better if we could somehow find ways to persuade and encourage the States to do the job and for us to stay out of it except in the areas of education and technical assistance?

Secretary HILLS. Well, I have a lot of sympathy with what you say about the courts and the burdens that we place upon them. This provision would not abolish the State laws with respect to condominium development within their borders.

Senator MORGAN. But it would set up a new category of Federal criminal law.

Secretary HILLS. It would enable the Federal Trade Commission to proceed against a developer of condominiums in more than one State where there was evidence indicating violation of either the disclosure or the minimum standards of protection for the consumer.

Senator MORGAN. My time is up. May I ask one other question, Mr. Chairman?

The CHAIRMAN. By all means.

Senator MORGAN. Do you know what the Commission for Uniform State Laws has done or is doing with regard to preparing uniform legislation in the area of consumer protection for condominium purchases?

Secretary HILLS. Senator, I am advised that our staff has met with them. They are in the process of addressing the question, but they have not addressed it in a definitive fashion. Indeed, they have not made a proposal.

Senator MORGAN. Mr. Chairman, it seems to me we might want to consider this area in working with your bill because I think your bill could be made compatible with the Uniform State Laws Commission and maybe keep us out of it as much as possible.

Thank you, Mr. Chairman.

The CHAIRMAN. I appreciate that. I think the three of us are not very far apart. In fact, I think we are all working in the same direction. We certainly want to minimize the legislative impact as much as we possibly can and the Federal impact, and we want the States to have as much discretion as possible. We also believe—I think that Senator Morgan would share the view that you and I expressed, that we would like to keep the burden as light on everybody as possible—the industry and the consumer—and have the consumer informed with as clear and simple and brief a disclosure as would be effective. So I think that interrogation and response was most helpful.

I have a few more questions before I forget though.

Senator Tower couldn't be here this morning and he asked if you would reply for the record to some questions he would like to submit?

Secretary HILLS. Of course.

[The following was received for the record:]

QUESTIONS FOR SECRETARY CARLA HILLS FROM SENATOR JOHN TOWER

1. Your statement contains several changes you would like to see in S. 2273. If no changes were made, if the bill was passed in its present form, could you support S. 2273?

2. As everyone knows, housing starts for the past year are own. Multi-family starts, as compared to single-family starts, are dramatically down. While the number of condominium units have increased percentagewise over the past couple of years, vis-a-vis production of multi-family rental units, would not this bill be a deterrent to future condominium construction, at the precise time that all phases of construction need to be encouraged? Isn't this just another piece of red-tape the developer must endure?

3. Is this bill really necessary as it relates to new construction, especially in light of the following?

(*a*) In the survey you conducted, 95% of the condominium owners expressed satisfaction with their units.

(*b*) The vast majority of condominium construction has occurred in relatively few States, and those States have some form of statute on the books which regulate the construction of condominiums.

(*c*) Most of the problems that we are aware of with regard to newly constructed condominiums are confined to units constructed, predominately, in three States. (Florida, California, and New York).

4. Some people would argue that the Real Estate Settlement and Procedure Act (RESPA) was the result of Congressional "overkill" in response to problems that occurred in limited areas of the United States. Might these same people make the same claim with regard to this proposed legislation? Should a Federal law, such as this, govern condominium construction in North Dakota, or some other less populous state where there is little condominium construction, or where there is already in existence a state law which reflects that particular state's resolution to any problems associated with newly constructed condominiums?

RESPONSES TO SENATOR TOWER'S QUESTIONS

1. No. S. 2273 contains certain provisions that, in our view, are unworkable, add significantly to the cost to the consumer and involve the Federal bureaucracy to a degree unjustified by the findings of the HUD condominium study.

My comments before the Committee identified those provisions which would have to be changed or deleted before we could support the bill.

2. There can be no doubt that multi-family construction has been hard hit during the recent recession. The construction of condominiums and multi-family rental properties, especially, has dropped off. However, it is not appropriate to blame this downturn on government regulation. To the contrary, the current dramatic oversupply of condominiums is the result of many factors, including the adverse publicity surrounding abuses that have attended condominium development. Once buyer confidence in condominiums has been restored and the current inventory worked off, construction of additional condominium housing will resume at a substantial pace. We would not support adding additional layers of red tape to condominium development, and our proposed modification of S. 2273 would reduce the level of government involvement.

We believe that detailed, substantive regulation of condominiums and enforcement must remain the responsibility of the states. Each state would be free to impose the requirements it considers necessary for the protection of its own citizens.

However, multiple filings are currently required of many developers who choose to sell across state lines. The resulting duplicative and inconsistent state disclosure requirements impede inter-state sales and increase costs to consumers. A combination of the minimum protections offered by the proposed federal legislation and the protections already established in many states as to the comdominiums located in those states should prevent a recurrence of the abuses of the past and eliminate unnecessary burdens on inter-state sales. Easing the burden on inter-state sales may assist in reducing the serious oversupply of condominiuns which afflicts the industry and retards construction.

3. Although 95 percent of all condominium owners expressed satisfaction with their units, a significant proportion of that 95 percent did face problems and so indicated in the national surveys conducted for the HUD condominium study. For example, 20 percent of all unit owners surveyed complained of poor construction, and only 54 percent responded that developers' estimates of maintenance expenses were "reasonably accurate."

We agree that the occurrence of abusive practices is limited in terms of national aggregates, but the impact on those who are hurt by the abuses can be very serious. The modifications we propose in S. 2273 would focus the bill on the worst and most extensive abuses. Many states have acted to prohibit abusive practices, and we do not want to interfere in any way with their regulation of the sale of condominiums located within their borders.

The intent of a Federal law is simply to provide similar protections in states currently without condominium consumer protection laws but where condominium development is occurring or might occur in the immediate future. We are most willing to work with you and the other members of the Committee to ensure that this very limited objective is met in the final version of S. 2273.

4. Both the sponsors of S. 2273 and the Administration recognize that previous condominium legislative proposals were, in fact, "overkill."

The HUD study did, however, uncover significant and recurring problems in the condominium industry, some of which have had a severe impact on consumers. The states which already have had substantial condominium development have generally adopted some form of government control, although sometimes only after many consumers had been seriously harmed. Some of the states in which condominium activity is just beginning have established few such protections. The provisions of S. 2273 which we support only extend to other states the minimum protections which the active states have considered necessary to prevent major abuses. We oppose weakening existing state laws protecting consumers with respect to intra-state sales. However, North Dakota, cited in your question, is a state where current protections are extremely limited, and the proposed law would provide a minimal level of protection to condominium purchasers at little cost to consumers or developers.

The CHAIRMAN. Now both Senator Morgan and I commented and asked on this finding in your study that the overwhelming majority of people were either satisfied or very satisfied with their condominiums. As I understand it, a number of those who were satisfied and maybe even those who were very satisfied had some problems. This doesn't mean that only 5 percent said they had some kind of problems. I can understand it's consistent with somebody liking condominiums and liking the fact that they had a condominium, but they might have been unhappy about the arrangements about perhaps the lack of disclosure or the lack of protection. Is that correct?

Secretary HILLS. I think that's a fair statement. They were asked on the one hand whether they were satisfied or very satisfied and they answered that question and did not go on to enumerate any problems they may have had. It was in the course of the hearings that we were able to identify 10 difficult problems that affected the consumers in the condominium field.

The CHAIRMAN. If they did bring up a problem at the time, would they still be classified as satisfied or very satisfied?

Secretary HILLS. I believe they answered the question asked—are you dissatisfied, satisfied, or very satisfied—and that they responded to those categories without elaboration. This means that they may have felt satisfied and still have felt that there were problems in the transaction.

The CHAIRMAN. Now you oppose requirement of independent engineers' reports on the state of the structure in terms of older buildings saying it would be too costly. I'm concerned though that people don't know what they are getting when they buy an older building, buy a condominium in an older building—how much they're really paying for it, because they will face major repair bills after they move in.

Do you think some sort of engineer's report would be a good idea, perhaps a scaled-down version, for condominium buildings?

Secretary HILLS. I think so. Looking at pages 10 and 11 of your bill, there are really two parts to your engineering report disclosure requirement. One is that there be a report stating the condition, rate of depreciation, and remaining useful life of the structural elements and mechanical supporting systems, and I think that as to converted condominiums that such a report would be useful.

You go on to state that there must be an estimate of repair and replacement costs projected for 5 years. We are advised that that would be very difficult and when we're addressing new condominiums we question whether that requirement is necessary. Certainly is not balanced out by the attending cost, and there are other ways to protect consumers with respect to new condominiums.

The CHAIRMAN. There's a tendency for us here in Washington or if we come from big cities or think in those terms to design legislation that may be perfectly convenient and practical for a person living in a big city, but how about the availability of engineers to do this kind of thing in a smaller town, in a rural area, in a smaller State, in a Western State or a Southern State or a Midwestern State?

Secretary HILLS. The evidence that we have is that a traditional engineering report addressing the condition, rate of depreciation and remaining useful life of the property could be obtained in small towns as well as large ones, but that engineers would not want to and would not get into a 5-year estimate of repair and replacement costs. So that I think that the problems of procuring a 5-year estimate would be serious in large towns and even more aggravated in small towns, but that a traditional engineering report is obtainable.

The CHAIRMAN. You say you think the warranty provisions in the bill are too expensive, but what if some major defect appears after 6 months and each owner is assessed, say, $1,000 to repair it, which has happened? Might it not be better to have some warranty included in the basic cost of the unit and included in the mortgage so the buyer would know the full cost?

Secretary HILLS. I think you have to look, Mr. Chairman, on the interreaction between the warranty, the budget, and the engineering report. We would have the engineering report, as I mentioned, apply to the converted units; but we would trim the warranty down. With respect to new units, we would limit it to latent structural defects and to a term perhaps one year from substantial compliance, which is our practice with section 234 now.

As it is drafted, the warranty is very broad. It's a 2-year warranty covering a full cost of labor and materials for any repair or replacement of roof and structural components and mechanical, electrical, plumbing, and common service elements. That's a very broad warranty and we think that that would present great problems in terms of cost passed on.

Our study indicated that the cost with respect to new units would be from a half a percent to 5 percent and on a $35,000 condominium we're talking about $1,600, $1,700, or $1,800. With respect to converted or used units, we're talking about double the cost, 10 percent, and more like $3,000, and we just don't know that that cost is warranted here.

The CHAIRMAN. Then you would support a narrower warranty than that proposed in the bill?

Secretary HILLS. Yes.

The CHAIRMAN. There's been a lot of concern about condominium conversion and their impact. I think that's what gave it the most emphasis of all—displacement of tenants, particularly the elderly. We have seen that in this city and other places in my State.

What do you see as the problems of conversion and does this bill deal with them?

Secretary HILLS. Yes: I think that the 90-day provision giving the tenant notice and the right of first refusal and then a 120-day notice to permit the tenant to vacate, if that is his wish, prevent disruptive eviction. In terms of defining the scope of the problem, about 100,000 conversions occurred over the last half decade and that resulted in a displacement of about 80,000 families. About 80 percent of that 100,000 chose to move or were forced to move and I think your provisions are helpful to that category of people insofar as notice and the right of first refusal.

The CHAIRMAN. Now your excellent study indicates the tremendous expansion of condominiums. I think that's one of the most impressive aspects of it, the fact that this was really not very much—not very important in terms of the entire housing market a very few years ago and it's just exploded, particularly in New York and California and Florida and some other sections, and it might very well explode all over the country in time to come as the days and years go.

My question is: What are the permanent problems involved in condominiums after they have finished these growing pains that have been so serious? Are there problems that perhaps we have neglected in the bill that should be covered, or do you feel that we can study these problems and move ahead later?

Secretary HILLS. Let me discuss with you the 10 basic problems that our study has uncovered and let's talk about them just briefly.

Recreational leases were a problem in some parts of the country, essentially in Florida, particularly with respect to cost-of-living escalator clauses. There are many parts of the country, however, where consumers benefit from recreational leases and, in fact where the cost to the condominium purchaser is lower with a recreational lease than without it. People who have a part-time ownership enjoy that kind of benefit. So we would not say that was a permanent problem. We see Florida as properly handling the problem and as having enacted legislation which has really made the problem de minimus in scope.

Poor construction is the second problem alluded to by those who attended the hearings, but poor construction is a problem in basic housing construction, so I would not say that there is a need to address that for condominiums per se.

Complex documentation was a third problem identified, and it was our study of that problem that caused us to take the approach that we have taken in our testimony this morning.

Tenant displacement is a fourth problem, and that makes us gravitate toward the cures that you have set forth—the notice and the right that we just mentioned.

The association's operating problems are a fifth problem. The problems that we force upon notice homeowners when we tell them to really manage a complex costly establishment were found to be rather profound. We think that our educational material will assist greatly in this area.

Communal living or community living was described as a burden. That is something I daresay we cannot address.

The deposits, the escrowing of deposits, is a problem that was alluded to in terms of loss of deposits. You have addressed that in your bill and we think properly so.

Nonpayment of dues by the developer was a problem that is one of those interesting balances. I think that it is appropriate to ask the developer to pay a fair share of common cost but that is unfair to ask the developer to pay the using costs such as utilities or maintenance costs when his empty units of course, are not using their services. Whatever we do in this area, we know the developer will pass on the cost to the condominium owner.

We have already discussed warranties and the engineering reports. I think they should be minimal so as to provide the information without the burden of excessive cost.

And the tenth and last problem was underestimation of operating costs. I think that is a real problem where people enter a condominium and do not know what their costs are going to be. We think a budget should be supplied. On the other hand, we do not gravitate toward your cure of having it be a budget approved by a certified public accountant. We have discussed this with accountants. They would not be willing to make certifications as to future expenses. It's one thing to certify what the costs have been, looking back, but it's quite another thing to require a certified statement with respect to projections, and we feel that a budget, by its nature, is an estimate and that there are many intervening uncertainties. We would include a budget in the list of items that should be disclosed, perhaps with warnings that there have been problems with respect to estimates and that they almost always get larger, not smaller. That kind of protection would be far better than requiring a developer to have a certified statement which he could not obtain and thereby probably discouraging condominium development.

The CHAIRMAN. You oppose the requirement of CPA certified budget projections, although you require such projections for 1 or 2 years?

Secretary HILLS. That is correct.

The CHAIRMAN. Could you suggest any other way of pushing a developer to give a reasonably accurate good faith projection of cost to cut out the practice of low-balling?

Secretary HILLS. I think the problem would become less with the development of a standard form. However, a 1- or 2-year budget, as I described, just a simple disclosure statement of what it costs to live in the unit plus a warning that it is impossible to predict with great accuracy and that costs may increase would be useful. In other words, you could have a statement of the budget but not require it to be certified, and then the cost would be substantially less.

The CHAIRMAN. What can the Federal Government or should the Federal Government do to help people who have really been bilked in buying a condominium who have to deal with recreation leases and sweetheart contracts and all the bad things that S. 2273 would control in the future? I'm talking about the people who have been had.

Secretary HILLS. It's difficult to have this bill reach back and provide a remedy for those who have already been harmed. I think the purpose of this bill is not retroactive but rather it is to prevent the

same sort or sorts of grievances which have occurred in the past from having a repetition in the future. As to consumers who have already been injured—some of them have a remedy under the available State law, but I do not see that you have provided a remedy for them, nor do I see that as necessarily your focus or intent.

The CHAIRMAN. Do you think it would be desirable for us to try to do?

Secretary HILLS. I don't think so. I think any time you have retroactivity you have problems of what the various parties believed when they entered into the transactions.

The CHAIRMAN. Senator Morgan?

Senator MORGAN. I have no further questions.

The CHAIRMAN. Well, thank you very very much, Madam Secretary. You have been most helpful and we so much appreciate your excellent study and your fine presentation this morning.

Secretary HILLS. Thank you so much, Mr. Chairman. Thank you, Senator Morgan.

The CHAIRMAN. Our next witnesses will appear as a panel. We have John E. Hempel, chief deputy director, California State Department of Real Estate; Hugh H. Makens, director, corporation and securities bureau, Michigan Department of Commerce; John R. Larson, Commissioner of Securities, Minnesota Department of Commerce; Ross J. Lloyd, condominium administrator, Virginia Real Estate Commission; and Ms. Margaret A. Earner, Office of Policy Development, Planning and Evaluation, Department of Housing and Community Development, District of Columbia.

I understand the staff has suggested that you confine your remarks to 5 minutes in view of the fact that the hour is late, and we have statements which will be printed in full in the record. I have had a chance to go over these statements. They are excellent and very, very helpful.

Our first witness will be John Hempel, chief deputy director, California State Department of Real Estate.

STATEMENTS OF JOHN E. HEMPEL, CHIEF DEPUTY DIRECTOR, CALIFORNIA STATE DEPARTMENT OF REAL ESTATE; HUGH H. MAKENS, DIRECTOR, CORPORATION AND SECURITIES BUREAU, MICHIGAN DEPARTMENT OF COMMERCE; JOHN R. LARSON, COMMISSIONER OF SECURITIES, MINNESOTA DEPARTMENT OF COMMERCE; ROSS J. LLOYD, CONDOMINIUM ADMINISTRATOR, VIRGINIA REAL ESTATE COMMISSION; AND MARGARET A. EARNER, OFFICE OF POLICY DEVELOPMENT, PLANNING AND EVALUATION, DEPARTMENT OF HOUSING AND COMMUNITY DEVELOPMENT, DISTRICT OF COLUMBIA

Mr. HEMPEL. I am chief deputy director of the California State Department of Real Estate and on behalf of our department have filed a statement with the committee which we hope will be entered into the record.

The CHAIRMAN. It will indeed, in full.

[Complete statement follows:]

STATE OF CALIFORNIA EDMUND G. BROWN JR., Governor

DEPARTMENT OF REAL ESTATE
714 P Street, Suite 1550
Sacramento, CA 95814
(916) 445-3995

September 19, 1975

Hon. William Proxmire
Chairman, Senate Committee on
Banking, Housing and Urban Affairs
United States Senate
Washington, D.C. 20510

Dear Senator Proxmire:

Condominium Consumer Protection Act -- S2273

We understand that hearings are contemplated next week on S2273, and we would like to have this opportunity to comment on the bill and to explain something about California's regulatory posture toward condominium legislation.

Most of the regulatory mechanism within S2273 deals with disclosure to prospective purchasers, and appears to be consistent with the current requirements of California law and our own disclosure instrument -- which must be used in connection with all sales of subdivided land -- and which has been a part of California Subdivided Lands Act since the 1930's.

With the advent of the general utilization of the condominium concept and the other forms of community facility common ownership subdivisions during the 1960's, California adopted additional regulations providing for both the current affirmative standards approach (the developer must make a showing that he has made adequate financial arrangements for community and recreational facilities, off-site improvements, and the like) and the reasonableness test (which has given us considerable control to guard against abuses which have been troublesome in other areas).

There are three major points within S2273 that we feel deserve careful consideration:

1. The bill provides for a two-year warranty over common facilities and a one-year warranty over the balance of a condominium project. As desirable as a warranty may be, I am sure your committee would want to consider, carefully, the impact on the cost of construction if specific reserves must be provided for an economically feasible nationwide, required warranty program. Others, especially from the construction and homebuilding industry, I am sure, could provide helpful

input on this point. It occurs to us that Federal or State mandated warranty programs have not yet become a portion of the economic scene -- with the possible exception of financial responsibility laws in connection with the operation of motor vehicles where high risk of liability occurs.

If S2273 were to be adopted with the mandated warranty concept included, we think further consideration should be given as to spelling out the criteria for what would establish a warranty. For example, for a State plan to be acceptable, would the warranty of the developer include any sort of deductible clause? Would it extend to appliances, the manufacture of which has not to date seem fit to extend it to your warranty?

2. The second troublesome area would be that of the "15-day cooling off period." California is the leader in this field with respect to subdivision offerings in that this Department supported State legislation several years ago providing for a 14-day cooling off period in connection with the sale of lots in a "land project." This definition applies to large, rural vacant lot offerings, generally speaking, where high pressure sales to "captive" clients (often brought there by bus or plane) was the rule rather than the exception. In short, in that sort of situation the purchaser was effectively denied the opportunity for comparison shopping. We do not think the same situation exists in connection with the vast majority of condominium sales. These are substantial purchases, including loan applications and the like, and most such transactions occur within an urban setting in a free market environment. If, in the final analysis, a cooling off period remains in the bill, consideration might be given to having it mesh with those applying under the Interstate Land Sales Registration Act or Federal Truth-in-Lending legislation (i.e., three days).

3. Of primary concern to California would be the means by which a State plan would be approved by which a State may assume responsibility for the enforcement of the standards contained in the Act. A reading of S2273 suggests that this final administrative determination would lie with the Secretary of HUD. We would recommend that the Federal law could lay out the guidelines for State responsibility, that the State desiring to assume such responsibility could have a means for registering same, and that the assumption, thereafter, would be that the State is in compliance with Federal law unless a showing is made to the contrary. Such an approach would be dramatically less expensive for the Federal Government and more consistent with our belief as to the appropriate relationships.

Further, we cannot over-emphasize the importance (at least with respect to California) of the existence of the combination of requirements that affirmative standards be met by the developer and the application of the reasonableness test which affect the need for some of the disclosures which would otherwise unnecessarily lengthen and render less meaningful the disclosure instrument to be used by the State. In this regard we note that the language dealing with approval of a State plan or law is that it "shall be deemed to meet or exceed a requirement of or under this Act if it provides the same or greater protection for prospective purchasers or if it provides for the same or greater disclosure to such purchasers, as the case may be." The insertion of words such as "similar or greater," or "same, comparable or greater," would make it much more likely for States operating under different regulatory schemes designed to cover the same ground to be in a position to assume responsibility for the enforcement of the "standards contained in this Act."

A statement follows which was prepared for use in connection with proposals for 1976 legislation in California which might be of interest to the committee. Although prepared by this Department, none of the attached comments has been either adopted or rejected by the Executive Branch of State Government here, and are preliminary in nature. They do, however, show that (1) California has been a pioneer in effective condominium regulation, (2) We are well into serious consideration of second generation condominium statutes, (3) A substantial measure of our regulation is consistent with the aims of S2273, and that due to the existence of a well tested and highly effective set of substantive regulatory standards, California could best protect its citizens as prospective condominium purchasers by carrying out within its borders whatever Federal requirements are adopted with respect to such condominium sales transactions.

In addition to the statement which follows, we are attaching a complimentary copy of a recently completed research project by San Jose State University. This project was funded by this Department and may provide your committee with some useful information concerning condominium conversions as surveyed in the San Jose area. We cooperated with the Arthur D. Little research project authorized by HUD, and trust that when this report is published, it will further confirm some of the matters referred to herein.

Respectfully,

John E. Hempel
Chief Deputy Director

Attachments

STATEMENT ON BEHALF OF

CALIFORNIA DEPARTMENT OF REAL ESTATE
CONCERNING CALIFORNIA SUBDIVIDED LANDS ACT

The following information deals with the Department's role in the regulation of condominiums and similar common-interest subdivision projects. Now that we have had a dozen years experience in this field, we can tally some of the problems and contemplate such changes as are consistent with today's needs, including the growing activity in condominium conversions.

During the past year there has been a great deal of testimony and publicity concerning abuses by developers of condominium projects; mostly in states other than California.

In most of these states there was very little regulatory authority over the initial set-up of the project. That is one of the basic reasons for the gouging of purchasers, outright fraudulent transactions by developers and salesmen and unworkable, unmanageable homeowners associations.

We understand from testimony taken at U.S. Department of Housing and Urban Development hearings on condominiums and cooperatives held in Washington, D.C. on February 10-11-12, 1975, that about 600,000 condominium units are now in existence in Florida.

California did not keep statistics on the number of condominium units being offered for sale until 1969. Since 1969, we have issued public reports on 120,610 units. These units were in 2,113 projects throughout the state.

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In addition to condominium projects we have since also issued public reports on 157,758 planned development units in 1,933 subdivisions. We mention planned developments because planned developments take on many of the characteristics and problems of a condominium project and vice versa. Planned developments and condominiums alike have commonly-owned facilities operated and managed by homeowners associations.

We believe that California's laws and regulations have provided the necessary safeguards that cause condominium projects as well as planned developments, stock cooperatives and community apartments to be safe, economical, practical and highly enjoyable types of housing.

We can find such housing in California in all price classes from an $18,000 townhouse or community apartment to a $300,000 condominium or home located in a planned development. The residents in these various common-interest subdivisions are, on the whole, doing a creditable job of self-government with little or no previous experience.

The reasons California has been successful in regulating this type of development are:

(1) The Subdivision Map Act. The Map Act applies to all subdivisions in California and it is enforced by city and county authorities. The condominium must be approved first by local authorities before it is submitted to the state for state regulation. In most parts

of the country there is no such local regulation and in those states where there is some type of regulation of this sort, it is considerably less adequate than California's Subdivision Map Act which has been effective over the past 40 years.

(2) The Subdivided Lands Act covers all subdivisions in California, including condominium projects, stock cooperatives, community apartments and planned developments. It gives the Real Estate Commissioner the authority to assure that the purchaser of a lot or unit in one of these developments receives that for which he bargained.

In addition to the prevention of fraud, the Subdivided Lands Act provides for a disclosure instrument (the public report) and substantive controls before the public report is issued.

The California subdivision laws and regulations applying to condominium projects are as follows:

(1) Government Code Sections 66410 to 66499.37 (Subdivision Map Act.)

(2) California Business and Professions Code Sections 11000-11029.1 (Subdivided Lands Law) and

(3) Regulations of the Real Estate Commissioner, Title 10, California Administrative Code, Sections 2790-2823.1.

(4) Civil Code Section 783 and Sections 1350-1359, inclusive.

Some of the more basic requirements of California law enforced by the Department of Real Estate are as follows:

(1) Special provisions to provide adequate management of commonly owned areas by homeowners associations.

(2) A full disclosure in subdivision public reports of important features of the project, maintenance and operational expenses, management provisions concerning the commonly owned facilities and within the Commissioner's discretion, any item believed to be of considerable value for a prospective purchaser to read and understand.

(3) Adequate financial arrangements to assure completion of the entire project and lien free conveyance of individual units and common areas and facilities included in the offering.

(4) Adequate financial arrangements to guarantee payment of the subdivider's obligation to pay assessments attributable to unsold units during the early stages of ownership, operation and maintenance of common-areas and facilities by the homeowners association. This is accomplished through the posting of a bond or other surety device by the subdivider.

(5) All purchaser's deposit monies must be placed in an escrow and may not be withdrawn by the developer (unless he furnishes the Department of Real Estate with a bond) until title, free and clear of liens, is delivered to the purchaser or it has been determined that the purchaser has defaulted under his contract. This is one of the basic protections of the subdivision law and applies to all subdivisions in California.

(6) Laws that require the consent of the Commissioner to any change in the governing instruments for common-interest subdivisions that would materially change the rights of an owner in the subdivision. Until the developer is 3/4 sold out, an application must be made to the Commissioner for consent to hold a meeting of owners to vote upon such a change. Homeowners may not even be solicited to vote on such changes in advance of receiving consent from the Commissioner.

(7) Jurisdiction by the Commissioner over any other type of material change in the set-up of the subdivision. This requires the developer to apply for an amended public report prior to offering any additional units for sale in the condominium project after such change has occurred.

In some eastern states, the developers of some condominium projects retained ownership of recreational facilities within the subdivision development and leased these facilities to the homeowners association on terms that were extremely unfavorable to the association. Owners were forced to pay high monthly assessments to defray the lease payments on these recreation facilities. Moreover, in some instances the developer failed to maintain the facilities in a proper manner in spite of all the money collected through exorbitant rentals.

In California, such recreation leases are virtually unknown. Although not expressly prohibited, the existence of the "reasonableness" provision in our laws and regulations allows DRE to extract a commitment to maintain lease facilities and to freeze rentals for

them in such a manner that the potential for excess profits to developer at the expense of owners of units is simply not there. In California developers -- almost without exception from the beginning -- have provided for the homeowners association to own and control common facilities within the offering.

Another protection offered by California is a requirement that beneficiaries of mortgages and trust deeds subordinate to the conditions, covenants and restrictions in a condominium project or planned development. Thus if a lender forecloses on an individual unit or on 99% of the project, the development must continue as a condominium project as originally established.

A developer is restricted in his power to annex other properties to the original project. He may annex without the consent of other owners if it is so provided in the CC&R's and if the annexation plan is detailed in the application for a public report for the first phase of the development. If not so detailed in the initial filing, annexation must have the approval of 2/3 of the voting power of the owners association excluding the vote of the developer.

Another abuse in condominium development in some other states which has received a substantial amount of publicity is the long term "sweetheart" contract for management or services between the homeowners' association and the developer or his affiliate. These contracts are entered into by the developer on behalf of the owners' association at a time when the developer controls the governing body of the association. They frequently provide for exorbitant compensation to the developer or his affiliate for

extended terms. The homeowners' association is thus "locked in" to the contract when it is no longer controlled by the subdivider.

Under regulations of the Department of Real Estate management and service contracts in the name of the owners association for a term of more than one year must have the approval of a majority of the members of the association. Again, the "reasonable arrangements" test under California law provides the basis for the Department to impose such requirements.

To assure that the developer does not retain ownership and control of common facilities for too long a period after the first sale in the development, he must provide "reasonable arrangements" for delivery of control over the subdivision and for all off-site land and improvements to the unit purchasers.

The California Business and Professions Code provides that reasonable arrangements must be made as to the interest of each purchaser with respect to management, maintenance, preservation, operation, use, right of resale and control of units and other areas subject to the plan of control proposed by the subdivider which are included in the offering. This section is rather all encompassing and furnishes the Commissioner considerable discretion when determining the reasonableness of the total offering.

If the Commissioner determines that some aspect of the subdivision set-up is not a "reasonable arrangement" under the regulations, he may deny issuance of the public report. Without a subdivision public report, the developer cannot offer any unit for sale.

The Commissioner has "fair, just and equitable" authority over the offering in California of any subdivided land located outside of this state. The "fair, just and equitable" standard is an extension of the "reasonable arrangements" standard in that the Real Estate Commissioner also must decide that the unit prices are fair to California purchasers before the interest can be offered in California. To assure that the price elements of the "fair, just and equitable" standard is met, we send staff appraisers to the subdivision site to appraise the properties to be offered for sale in California. This is done at the subdivider's expense. If the subdivider's prices exceed the fair market value of the property, that is a ground to deny the issuance of a subdivision final public report and permit. Again, without a final subdivision public report and permit, an out-of-state developer cannot offer any subdivision interests for sale in California.

We believe that California's provisions included in the Business and Professions Code have enabled the DRE to do a highly effective job of public protection in the area of condominium sales to California.

Over-reaction to some of the abuses that have occurred out-of-state but do not exist here could be a serious mistake. This could result in severe limitations upon condominium construction in California at a time when need for this form of housing has never been greater. We believe that public protection has been afforded in California for more than a dozen years without any deleterious impeding of the growth of this important segment of the housing industry. Today, condominiums provide a less expensive, more environmentally sound ownership concept which should be encouraged through sound legislation and reasonable governmental controls.

California has no special laws concerning the conversion of apartments to condominium projects. The rules and regulations which pertain to new construction apply also to conversions. The Department of Real Estate appraisers, however, give particular emphasis to the amount of reserves needed for replacements and major repairs. If the owners' subdivision plan does not provide for the replacement of badly deteriorated fixtures before the units are to be offered for sale, the Department insists that the budget reflect the heavy assessments necessary to create the reserve to replace the fixtures during the short remaining useful life. Often this will be such an obvious deterrent to sales that the converter decides to replace or repair on his own.

We can see the need, however, for some additional protections for tenants and for prospective purchasers where condominium units are to be created from an apartment building. We support the idea of giving tenants reasonable notice of the plan to convert to permit them the opportunity to locate another place to live. We also believe that tenants presently occupying premises to be converted should be given the first opportunity to purchase the residential unit.

The "budget analysis" by Department of Real Estate appraisers is unique in the arena of governmental control of the offering of housing in the United States. Our regulations require the developer to submit a "pro-forma" budget for departmental analysis. Department appraisers have been reviewing budgets for planned developments

and condominium projects for several years and have developed a cost manual covering virtually every conceivable expense item in common-interest subdivisions. Our appraisers review the plans and specifications of the project as well as the developer's proposed budget and if we do not agree with the developer's budget, we then insist upon a satisfactory resolution of the differences before a public report is issued. In this time of rapidly fluctuating prices, we do not expect to be always precisely on target in our budget estimates. We do feel, however, that we are doing an effective job in assuring that prospective purchasers are given realistic estimates of assessments to be expected.

We believe that the use of staff appraisers to analyze these budgets and to appraise out-of-state subdivisions is of inestimable value to the California consumer. While the out-of-state subdivider is required to submit a report of an independent appraiser, we have observed that the market value determinations by the appraiser employed by the subdivider are frequently more favorable to the developer than the staff appriaiser's reports. This is also true of the budgets for common interest subdivisions. Estimates submitted by or on behalf of the developer are usually lower than those of the staff appraiser.

Returning, for the moment, to the question of condominium conversions, the Attorney General has ruled recently that under the housing element

of comprehensive local plans, local jurisdictions do have jurisdiction over conversions. The matter of rules relating to displacement of tenants and conformance to building codes might be best resolved at the local level under authority granted directly or indirectly (through ordinances) by the Subdivision Map Act. For example, the Subdivided Lands Act could include yet another basis for denial of the issuance of a condominium conversion report -- the failure to provide for separate meters for gas, electricity and water service (where indicated). Alternatively, should the homeowners association be allowed to find their own "reasonable" basis for dividing these costs? It cannot be overlooked that the added cost eventually passed on to the consumer for the mandatory installation of separate meters could be balanced against the equity to each individual homeowner under a homeowners association plan dealing with the consumption of these utility services.

The Department of Real Estate has recently established a homeowners association desk. Its function is to review condominium and community facility subdivisions at a point beginning six months after the first sale has been made. This review function will include a review of the operating statement for the homeowners association and direct contact with unit owner members of the homeowners association to assist them in "getting started" and in seeking appropriate relief if they are having any problems. This is the Department's first attempt at follow-up work in this field, and the initial results suggest it is being favorably received. It has already helped several homeowners associations to correct

delinquencies on the part of unit owners (often the developer, himself, to the extent the units are still unsold at the end of that period) and generally to help the homeowners associations to help themselves into a fully operating posture.

At this time we believe that insofar as new condominium projects are concerned they are well regulated by existing law. There have been a few problems in some common-interest projects in California, but they have been minimal based on the 300,000 such units built in California since 1969. No amount of legislation or governmental involvement can forestall every problem nor cure every problem after it develops. We do believe that California has the tools to handle significant problems in condominium marketing and living in California with the possible exception of the special problems that may arise out of condominium conversions.

9/19/75

STATE OF CALIFORNIA,
DEPARTMENT OF REAL ESTATE,
Sacramento, Calif., October 21, 1975.

COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS,
U.S. Senate, Washington, D.C.:

Thank you for your letter of October 14 and the attachment in the form of Secretary Hill's statement to the committee.

A review of the statement verifies what I thought I had heard in Secretary Hill's testimony. That is, "a state could not require disclosure in addition to the Federal form and the disclosure statement required by the State in which the project was located"; but the state could place a warning on the Federal or Federally-approved disclosure form "indicating which disclosure requirements of that State's law were not met by the out-of-state condominium." This, of course, being the HUD proposal in lieu of the type of jurisdiction contemplated by S. 2273. She concludes in her statement with respect to that proposal by stating that "we therefore recommend that a State not be permitted to prohibit the sale of out-of-state condominiums if the developer has complied with the recommended Federal requirements and the laws of the State in which the condominium is located."

As stated during our meeting there, we would be opposed to such a proposal, because it would lessen public protection to the citizens of California by nullifying the many substantive provisions of California subdivision laws.

We would also like to point out that the information provided Secretary Hill concerning the sample difficulty of a New York subdivision qualifying in California is incorrect. We have run into no situation involving any other state where its requirements were prohibited by this state, therefore, "boxing-in" a subdivider so that he could not meet our qualifications. I do not know whether this would apply to a California subdivision being marketed in New York, but the statement on page 41 that "as a result, a California unit cannot be marketed in New York and vice versa," is incorrect. Our one vote per unit basis is established as meeting the California reasonableness test. Any other arrangement which is found to be reasonable would also be acceptable. For example, we approve a two-class voting structure in certain circumstances, etc.

All of this, of course, is outside the consideration of S. 2273, but I would like this information to be in your file.

Many thanks for your extended courtesy and that of Jerry Buckley and the others.

We expect to be attending a state interim legislative hearing on condominiums here in mid-November. In addition to discussing the applicability of existing California statutes, we will be discussing with them the potential for adding the 90-day right of first refusal and 120-day extension of tenancy provision to California law (in connection with condominium conversions) at the 1976 legislative session. If there are any further steps taken concerning S. 2273 in the form of policy determinations on amendments by early November, we would appreciate being advised so that we could make reference to the current status of Federal legislation at that interim hearing.

Sincerely,

JOHN E. HEMPEL,
Chief Deputy Director.

Mr. HEMPEL. Thank you. As you have heard stated here earlier this morning, California has a rather substantial regulatory scheme in the subdivision field. In fact, there are three or four different regulatory schemes.

Just to very briefly summarize them, for something like 40 years, subdivisions in California have been subject to the disclosure concept where the department—and I point out that's the department, not the developer—prepares a disclosure instrument which must be given to every prospective purchaser and that disclosure instrument also doubles as a permit without which he cannot offer any subdivided lands for sale.

In 1963, in addition to the disclosure requirements, California enacted what we refer to as the affirmative standards concept and this added to the law that in addition to the disclosure instrument the

department prepares that prior to the preparation of that disclosure instrument the developer is going to have to make a showing that the people are going to get that for which they bargain: that is, he has to make adequate financial arrangements for everything included in the offering.

Now some of those factors are in a sense a direct answer to some of the abuses that have come up in the condominium field in general.

Two years later, condominium legislation was enacted which superimposed in addition to the disclosure and affirmative standards tests that are applied to the application for subdivision public report, as we refer to the disclosure instrument, the developer had to meet the reasonableness test. This allows a substantial amount of discretion to the department as to what is considered reasonable in connection with the documentation and rights and privileges, the by-laws, management agreements, budgets and all the rest that are involved in condominiums and planned unit developments.

This has helped us to have a minimum record of abuse in California, although that's not to say there have been no abuses, that we have had no problems; but we think that the condominium field has been well regulated in California and so naturally when Federal legislation was proposed we took a look at it to see to what extent it might be disadvantageous rather than advantageous to California purchasers and to the California home building community.

Most condominiums, of course, are not built in resort areas. They are not sold across State lines. They are built in the urban setting and sold in a free market and that is why one of the concerns that we have with the bill has to do with the 15-day cooling off period. We do have a cooling off period in California but there again that's another regulatory scheme that I wasn't going to address my attention to except as it relates to the cooling off period.

We have a definition of what really is a rural highly promotional subdivision and there we have a 14-day cooling off period. This was departmental legislation passed by the legislature of California a few years ago, but we did that because we didn't have a free market situation. This was typical of the interstate land sales type of abuses that you have heard about in the past where boondock subdivision was being offered to a captive set of purchasers who were either bussed out or flown out to the property and that certainly seemed like an ideal situation to apply a cooling off period because they had no opportunity for comparative sales and were usually subjected to a high pressure sales presentation.

We don't think that fits in the condominium field and we'd like to bring your attention to the consideration of the fact that if you have a cooling off period of 15 days it doesn't mean that the typical transaction will take 15 days to close in any event, and therefore there might not be much time lag. On the contrary, I think the real world would show that due to the heavy cost involved in leading up to what are settlement costs eventually the tendency would be for the agent to place the money into his trust account or into a sales escrow solely for the purpose of holding the money until the cooling off period had passed, because otherwise there would be substantial costs multiplied by the tens of thousands of condominium unit owners who would have the right to such a cooling off period.

So I think consideration should be given as to whether or not it's really necessary in that field, and if so, perhaps it would be more typical if it were restricted to a time limit more consistent with HUD's office of interstate land sales registration which is a 3-day time period, and I believe the Truth-in-Lending is 3 days, and in any event, we question the 15 days.

Also, comments have been made about the warranty setup. Under our affirmative standards approach we require the developer—and this is a statutory requirement—to make adequate financial arrangements for any guarantees included in the offering.

I am advised my time is up. Thank you, Senator.

The CHAIRMAN. Thank you, Mr. Hempel.

Mr. MAKENS. Senator Proxmire and Senator Morgan, I was going to follow a predetermined pattern, but in line of the testimony of Mrs. Hills I feel I should address myself to some of the specific questions she raised.

The CHAIRMAN. Your statement will be printed in full, also.

Mr. MAKENS. I appreciate that.

[Complete statement follows:]

Hugh H. Makens
PRESENTATION BEFORE SENATE COMMITTEE
ON BANKING, HOUSING AND URBAN AFFAIRS
OCTOBER 6, 1975

Senator Proxmire, Committee Members, Interested Participants:

I speak to you today as the administrator of the Condominium Law for the State of Michigan, a position I have occupied for the past 3 1/2 years. Michigan is a national leader in condominium development. We presently have 1014 condominiums in the state involving 62,604 units. The approximate value of those units is 1.6 billion dollars. In 1973 we processed over 3 times the number of condominiums developed in New York as an example.

We have been fortunate that our problems with condominiums have been few in number and isolated in example. During the period of my administration we have received only 199 complaints. These have resulted in barring one developer from the business, refusing a permit to another, and withholding approvals of permits pending corrective action for a few others.

Michigan has no long term management contracts between the developer or its affiliates and the condominium association. Advertising is strictly controlled.

Long term leases from the developer are barred except leases of shared facilities with PUDs or apartments, and such leases are on a cost basis only.

Failure of completion of amenities has been a significant problem in only four cases to date.

Our principal problem has been the transition from a financially troubled developer to the financial institution stepping into the developer's shoes in lieu of foreclosure.

We affirmatively require the appointment of an advisory committee of unaffiliated co-owners within the first year and turnover by a specific date.

These steps, plus a careful review of each document affecting the rights of co-owners prior to turnover to determine that it contains no terms which would "work an imposition" on co-owners, account for the success of condominium regulation in Michigan. We regulate without retarding legitimate development.

FEDERAL BILL

The Committee should be aware that at least 95% of condominiums offered in Michigan are offered by Michigan developers selling condominiums located in Michigan to Michigan residents. There is little need for federal regulation of this activity.

However, I wholeheartedly endorse the concept of this bill for several reasons:

1. The disgraceful conditions found in a few other states, most notably Florida, have tainted the entire national market. The national press and television rightly identified those problems, but in the process did not delineate the states experiencing difficulty from those that maintained proper regulation. Hence, the bad reputation rubbed off on all condominiums. When I was contacted by the "60 Minutes" program, all they wanted were horror stories and the names of complainants -- they had no interest in what we were doing right or why. In my opinion, condominium living is a desireable living form for many groups of people which should not be discouraged by unscrupulous developers, promoters, or biased reporting. Elimination of the potential for abuses is the only solution to this problem. To the extent that states fail in their responsibilities, federal legislation is necessary.

2. National developers, operating in multiple states, create more difficulties than local developers with a tendency to ignore co-owner complaints or be excessively slow in response, to fail to adhere to local advertising standards, and to maintain poorer control over sales representations. Uniform national standards and apprehension over national sanctions should assist co-owners in dealing with condominium problems, thus providing more rapid identification of potential dangers and an avenue for resolving them.

CONDOMINIUM SECURITIES

I oppose the preemption of securities laws as they relate to condominiums sold as investments, and I believe that time sharing arrangement and vacation licenses must be tightly controlled under separate regulations from residential and business condominiums.

When a condominium is sold as an investment with promoter management and control, the securities laws are designed to elicit the vital information which condominium disclosure forms will not provide. Securities enforcement powers provide a far more meaningful check on abuses than could a small understaffed federal agency and state securities administrators are currently equipped to deal with illegal sales.

DISCLOSURE

We are now in the process of drafting a second generation condominium bill in Michigan with the help of a cross-section of those involved in condominium living, development, design, management and financing. We have developed a two-stage disclosure process. The first is a brochure which is attached,to this submission, telling generally about condominiums, which must be distributed at the time of initial serious interest in the condominium. The second is a full-blown disclosure statement, more comprehensive than that contemplated by this federal act, which must be delivered ten days prior to closing. In our opinion ten days is adequate advance review time.

We will specifically design our statute to encompass the federal disclosure statement. I would urge that no attempt be made to limit additional state disclosure requirements and that the administrative agency work with regulatory states to design an acceptable uniform form.

CONCLUSION

I have attached to this submission a list of suggested changes to the proposed legislation. These are largely technical comments, which we hope the committee and its staff will find helpful. If the State of Michigan can offer further assistance to this Committee or to the administering body in this matter we stand prepared to do so.

Securities Division
Corporation & Securities Bureau
5511 Enterprise Drive
Lansing, Michigan 48913

HUGH H. MAKENS, DIRECTOR

STATE OF MICHIGAN

WILLIAM G. MILLIKEN, Governor

Securities Division
(517) 373-0485
Corporation Division
(517) 373-0496
Condominium Section
(517) 373-8026

DEPARTMENT OF COMMERCE

RICHARD K. HELMBRECHT, Director

PROPOSED TECHNICAL CHANGES TO CONDOMINIUM

CONSUMER PROTECTION ACT OF 1975

The following changes, suggestions and comments are made with a view to improving the draft of the Act so that it will become compatible with state regulation.

1. Definitions:

   a. Section 2(5) - Common elements should be amended to read as follows:

      A. "Common Elements" means all portions of the condominium other than the condominium units.

      B. "General Common Elements" means all common elements other than the limited common elements.

      C. "Limited Common Elements" means a portion of the common elements reserved in the Master Deed for the exclusive use of one or more persons entitled to use one or more, but less than all, of the units.

   b. Section 2(12) includes a definition of developer that is overly broad. It would include a co-owner unaffiliated with the developer who buys two or more units for personal use or for investment. Also the definition loses the developer when he has only one unit left to sell.

2. Prohibitions - We would recommend that the 15 day period be reduced to 10 days, an ample time to review the documents.

3. National Standards for Consumer Protection -

   a. Section 5(2) prohibits the developer from retaining an interest in the common elements except as a co-owner after turnover. This would prevent the developer from using part of the common elements, such as the community building, as a sales office, a widely used practice in Michigan and one which does not appear to harm the co-owner.

   b. Section 5(3) requires a 1 year trunover to co-owners. This is impractical since very few units may be sold at that time. We recommend a turnover within 3 years and require a definite date of turnover, subject to change if all co-owners consent.

MICHIGAN
THE GREAT LAKE STATE

c. Section 5(5) should not be so broad as to include all landscaping since landscaping warranties are difficult especially after turnover.

d. Section 5(6) requires the developer to assume the obligation of co-owners as to units not yet sold prior to the turnover of the association to the co-owners. This would require that a developer pay the monthly assessment on all units owned by him prior to the turnover by the association to the co-owners. On large projects the developer may not be able to financially meet this obligation. In Michigan we usually require that prior to turnover the developer is responsible for only actual operating expenses on units he owns and has not sold or leased prior to the turnover and after turnover he is treated as a co-owner.

4. National Standards for Disclosure - To the extent practical specific requirements should be left to rule making to provide amply opportunity to the states to cooperate with the new agency and develop uniform standards. I would term the "abstract" a disclosure statement to prevent confusion.

a. Section 6(3) appears to be too specific and should be left to the rule making process. Our disclosures in this area will be extensive and the number of variations of construction plans cannot be adequately covered by a brief summary. I would recommend leaving construction data and schedules to rules.

b. Section 6(6) is too specific and is not broad enough in its coverage. I would recommend including only the following:

A. "A projection of annual expenditures necessary to operate and maintain the condominium project".

B. There are no generally accepted accounting principles for condominium accounting so I would recommend striking that term. I hope we can move to a budget sheet similar to the attached, but this should be done by rule.

c. The final subsection in Section 6 should be:

A. "Other material information necessary to fully explain the sale, development or operation of the condominium project as the secretary may prescribe".

5. Establishment of State Condominium Plans -

a. Section 7(b)(2)(B) is so broadly written that it causes some concern. The needs of the states for staff will vary with size, popularity of the condominium as a residential form, and strength of enforcement of general real estate laws.

6. Civil Penalties - Rather than the complicated formula of Section 9(a) I would recommend an outright recision right for a period of one year with a 7% interest attached.

We are pleased with the endeavor to provide for a cooperative state federal program and will pledge our continued cooperation toward the development of an effective state-federal regulatory plan.

The following items should be included in the budget where appropriate:

1. Total Payroll: Including amounts paid to janitors, telephone switchboard operators, maintenance personnel, etc., and payroll taxes and welfare benefits.

2. Supplies: Show all janitorial supplies, uniforms for employees and other supplies which do not belong under painting, decorating, maintenance or repairs.

3. Painting and Decorating (Interior): Include the cost of all contracted labor, decorators on building payroll, and all materials and supplies to be used in decorating or maintaining the interior of the building.

4. Maintenance and Repairs: All items of general maintenance and repairs, both interior and exterior. This includes landscaping costs, exterior painting or cleaning, boiler inspection and repair contracts, air-conditioning service contracts and parts, small hand tools, fire extinguishers, plumbing, electrical, plastering, masonry, carpentry, heating, roofing, etc.

5. Services: This includes such contracted independent services as window washing, exterminating, rubbish removal, TV antenna service and snow removal.

6. Miscellaneous Operating Expenses: This category is designed to include operating costs which do not fit under any other caption. Among such items might be damage to property of others not covered by insurance, directional signs, door lettering, etc. DO NOT use this category if any other caption clearly applies.

7. Water: Show all water costs including, if applicable in your community, sewage charges. If other utility charges are billed to the water bill, give an estimate of each charge in its appropriate category.

8. Gas: Show here the cost of gas for utilities, i.e., air-conditioning, hot water, swimming pools, etc.

9. Heating Fuel: This figure should represent the cost of heating your building whether you use coal, gas, oil, electricity or any other fuel.

10. Management Fees: This figure includes the agency fee and the salaries of personnel in the management office.

11. Other Administrative Costs: This category includes the cost of all legal and auditing fees, architectural or professional engineer's fees, telephone and office expenses.

12. Insurance: Include all one-year charges for fire, liability, compensation theft, boiler explosion, rent fidelity bonds and all insurance premiums.

13. Real Estate Taxes: This includes all local or state real estate taxes.

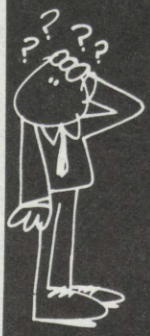
14. Other Taxes, Fees and Permits: Any personal property taxes applicable to the building, sign permit fees or any other tax necessary to the operation of the building.

15. Community Facilities: Cost of the operating of the facilities if not covered elsewhere.

16. General Operating Reserve: State basis for determination of amount.

17. Reserves for Replacement of Common Elements: The amount of these reserves should be included and the basis for determination of this amount.





The Condominium Buyer's Handbook

down-to-earth answers to your questions
about the condominium concept in michigan

Corporation and Securities Bureau
Michigan Department of Commerce

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do you know

- Your rights and responsibilities as a co-owner?
- The developer's background and financial references?
- What's planned for future development in the project?
- What rights the developer retains in the project?
- The developer's rental policy?
- When the recreation facilities will be completed?
- Who will control the recreation facilities?
- What's included as standard equipment in your unit?
- What's under warranty?
- What costs are included in the monthly assessment?
- When the co-owners will be permitted to vote for directors of the condominium's Association?

what is a condominium?



You've heard about condominiums, perhaps read newspaper ads, or have a friend or relative who's living in one. Now you are considering this kind of housing for yourself. What, actually, is a condominium?

The word is Latin, meaning common ownership or control. It has been defined as an "internal cube of air," that is, it generally means all the space inside the inner walls of an apartment or house. You own this space, and it is yours to decorate, to maintain, to live in. Everything else in the condominium development — the exterior walls, the grounds, the common hallways, the recreation facilities, and so on — is the common property of everyone who owns a unit there and is termed "common elements."

Some of this commonly-owned property is called limited common elements. It is limited to *use* by your family, such as your patio or balcony or carport space, or by the families who live in your building, in the case of stairways or laundry facilities, but it remains the common property of all the co-owners in the development. The rest of the common elements — roads, green areas, recreation facilities — are termed general common elements and are available for use by everyone in the development.



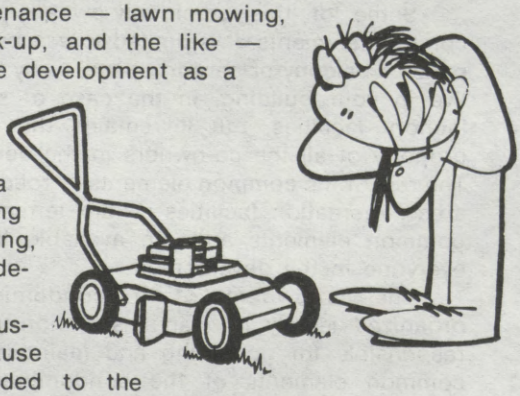
The co-owners of a condominium are organized legally into an association, which is responsible for governing and maintaining the common elements of the condominium. Each co-owner pays a monthly fee or assessment for these services.

This division of exclusive and common ownership is true whether the condominium is a high-rise apartment building, attached townhouses, single-family or cluster homes, an office building, shopping center, or industrial development established as a condominium. The condominium may be newly-built or an existing apartment building or development that is converted from rental housing to this type of ownership control.



Condominiums are an increasing part of the housing market, and there are several reasons for this. This idea appeals to buyers because in a condominium unit, you hold a deed to your property and can build an equity in it, unlike an apartment where you pay rent to a landlord. A condominium is treated like other real estate for tax purposes, too. This means that you are allowed to deduct from your federal income tax your property taxes and the interest you pay on your condominium mortgage.

Another feature that appeals to people who buy condominiums is that the outside maintenance — lawn mowing, snow removal, trash pick-up, and the like — usually is handled for the development as a whole.



Still another attraction for buyers are recreation facilities such as a community house, swimming pool, tennis courts, boating, etc. included in some developments.

The condominium housing development, because many facilities are provided to the development as a whole rather than duplicated for each home, uses less land per unit than conventional housing, an important environmental and cost consideration.

history and legal status

Condominiums are not a new concept in the housing field. The Romans used them and they were popular in the walled cities of the Middle Ages in what is now Western Europe. In the first half of the Twentieth Century other European countries enacted statutes permitting condominiums.

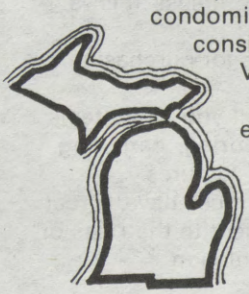
A few condominiums existed in the United States as early as 1947, but they were not legally established in this country until 1961.

The concept of condominium housing was incorporated into Michigan law with the passage of the Horizontal Real Property Act, P.A. 229 of 1963. This Act is important to buyers and developers of condominiums in Michigan, because it provides safeguards for both and outlines the rights and responsibilities of each. It is administered by the Corporation and Securities Bureau of the Michigan Department of Commerce.

In legal language, it:

Provides for the establishment of condominiums and condominium projects; defines apartments and common elements in such projects; prescribes the contents of and provides for the recording of master deeds establishing such projects; defines and provides for the identification and description of condominium apartments for purposes of ownership, mortgaging, taxation, possession, sale and other juridic acts; provides for review and approval of proposed condominium projects and the sale of apartments therein.

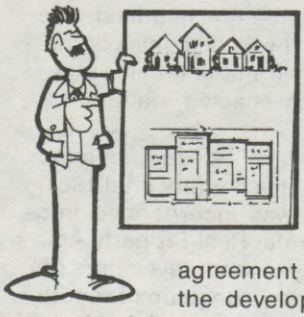
Not all states provide this degree of regulation and protection for condominium buyers and developers. Michigan is considered a leader, along with New York, California, Virginia and Hawaii.



This Act is important to you because it establishes the legal basis for two relationships: (1) Between you as the buyer, and the developer of the condominium, and (2) between you as the owner of a housing unit, and the association of co-owners.

Let's consider the first relationship in detail:

the buyer and the developer



When a developer plans to establish a condominium, he applies to the Corporation and Securities Bureau of the Michigan Department of Commerce in Lansing for a *Permit To Take Reservations*. Ordinarily he files a Reservation and Subscription Agreement and an escrow agreement for the Bureau's approval. This Permit gives the developer the right to advertise his units as a condominium and to take reservations for future sale.

advertising and sales

There are some prohibitions on the content of the developer's advertising, covering newspaper ads, radio and television announcements, brochures, material in the sales office, sales presentations, and the housing models themselves.

The developer or salesman cannot advertise or tell you orally

- that your unit will automatically increase in value if you wish to sell in the future;
- that you must act quickly to purchase a unit because of limited availability or because the price will increase, unless this is actually the case;
- that you will receive a discount or savings unless this is actually the case;
- that you will receive "free" goods or services for purchasing a unit.

In a model of the unit, the developer must tell you what items are not standard equipment, such as special flooring, carpeting, ceiling beams, moldings, light fixtures, or other features.

Persons selling condominiums in Michigan must have a real estate broker's or salesman's license and are subject to the rules of the Michigan Department of Licensing and Regulation.

reservation and subscription agreement

The Permit To Take Reservations generally does two things; First, it enables the developer to get an idea of the market for his units, and second, it reserves a particular type of unit in a specified location at an agreed-on price for you. The Reservation and Subscription Agreement provides that a percentage of the purchase price be paid by you as a deposit and held in escrow, that is, held by an approved escrow depository such as a bank, savings and loan association, or title insurance company.

At the point the developer feels he has enough reservations to make the project economically feasible and is ready to proceed with the project, he applies for a *Permit To Sell*. This application also goes to the Corporation and Securities Bureau, along with the proposed Master Deed and Condominium Bylaws.

Keep in mind that at this point, before a Master Deed has been recorded and a Permit To Sell issued, *either* the developer or you as the buyer can withdraw from the transaction. The developer can decide not to establish the condominium at all. You can decide not to buy the unit. You will get all of your money back.

how the agreement becomes binding



The Reservation and Subscription Agreement will become a binding agreement between you and the developer in one of two ways:

(1) *The 10-Day Notice:*

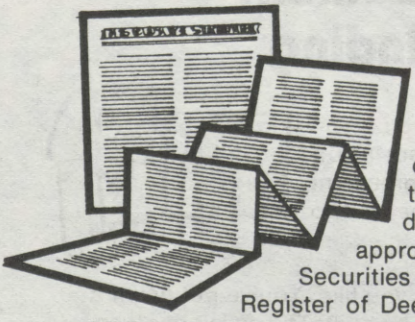
Let's assume you've found an unit you like. You've put down a deposit and are waiting for your unit to be built. The developer then receives his Permit To Sell. At this point, he is required to send you written notice that the Permit To Sell has been approved and to convey to you the Master Deed, Condominium Bylaws, and other documents. You now have 10 days to make your final decision about purchasing the condominium. If you decide not to buy, you may still

apply for the return of your deposit in full. At the end of 10 days, the Reservation and Subscription Agreement is binding on you and the developer. If you decide to withdraw after this 10-day period, your deposit will be forfeited up to 10 per cent of the purchase price, which includes any extras, or special features, you have ordered. *Note:* In the case of unusual or expensive extras, a higher percentage of their cost may be forfeited. This must be spelled out in the Reservation and Subscription Agreement or purchase agreement.

(2) *Immediate Effect:*

If the developer already has his Permit To Sell at the time you are considering purchasing a condominium, the Reservation and Subscription Agreement becomes binding as soon as you sign it. The 10-day notice is not required. Examine the Master Deed, Condominium Bylaws, and other documents carefully *before* you sign *any* agreement. After you sign, you cannot withdraw without forfeiting your deposit up to 10 per cent of the purchase price, including extras ordered. As noted, a higher percentage of the cost of unusual or expensive extras may be forfeited if this is spelled out in the Reservation and Subscription Agreement or purchase agreement.

the master deed and condominium bylaws



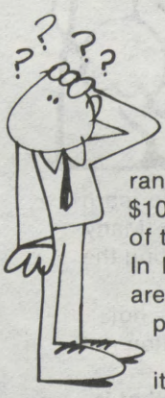
The Master Deed and Condominium Bylaws are the basic documents establishing and describing your condominium and the future operation of the development. They must be approved by the Corporation and Securities Bureau and recorded with the Register of Deeds in the county where the condominium is located.

Read all these legal documents carefully. You should be aware of restrictions or covenants which govern the use of your condominium and surrounding land. Check the Master Deed and your Reservation and Subscription Agreement or purchase

agreement to learn what the developer reserves the right to change or modify in the future. The most common reservation is the right to expand the development. Make sure you understand just how the developer plans to do this. Other usual reservations might be the right to rent units that are not sold, the right to amend to enable purchasers to obtain individual mortgage loans, the right to make changes in the documents that do not materially diminish the rights of any co-owners or mortgagees, the right to correct survey errors, or the right to assign specific garage or parking space locations.

Except for actions specifically reserved in the Master Deed, the developer is not allowed to amend, vacate, or revoke the Master Deed without the consent of all the co-owners and mortgagees.

what to ask before you buy



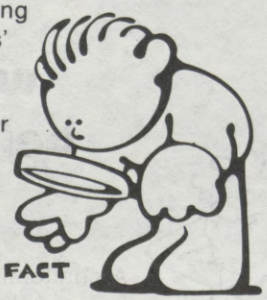
A condominium is a large investment of your money, ranging anywhere from about $15,000 to more than $100,000. It is important, both from your standpoint and that of the developer, that you be fully informed before you buy. In Michigan, a number of protections for your investment are written into the law. A Disclosure Statement will be provided to you by the developer along with the Master Deed and other documents. This statement, the first of its kind in the United States, will give you information in simple language about specific aspects of the condominium.

The development must meet the zoning laws, building codes and ordinances of the local community or governmental unit in which it is located. Sewer and water systems often must be

approved by the local public health department, and in some cases the county drain commissioner must be satisfied that the project meets local standards. A certificate of occupancy, indicating that the unit meets local housing standards, is required for each unit. If the project is a conversion, it must comply with current building codes and zoning and be checked by a local building inspector. Local laws vary regarding the extent of the inspection required.



The most important safeguard for you as a buyer, however, is to know your developer. A reputable developer is just as interested as you are in dealing with you fairly, in establishing harmonious relationships with the owners' association and in general creating satisfied owners. Request financial and professional references for the developer from your bank or your prospective lender; ask about the developer's background and previous experience in housing, particularly condominiums. Talk to co-owners in his previous developments or in the one you are considering.



Study the Master Deed and other documents carefully to learn what his rights and responsibilities are and what yours are. Many condominium buyers consult with an attorney before completing the purchase agreements.

The following list of questions to ask the developer is not intended to be comprehensive, but it includes those areas often not clear to buyers.

1. What size is the project? Will it be built in sections? What is the construction schedule?

It is important to know what will be built in the vicinity of your condominium. Many developers build a small number of units at a

time, holding sections of nearby land for other phases or future parts of the condominium. The right to do this must be reserved in the Master Deed. The developer can expand your condominium by adding units or by building independent sections and merging them all together at the end of construction. In either case, he must file a consolidating Master Deed showing the condominium as it exists in its final state. The reservation to expand should give the expected time period for expansion and the scope of the completed project.

The developer also may be holding nearby land for other homes, apartments, or commercial projects, and you should inquire about this.

2. What does the monthly assessment include?

The monthly assessment varies from one development to another, but in general it will include repairs and maintenance costs, taxes, insurance, reserve funds, management costs, and upkeep for recreation facilities, for example. You should receive a Disclosure Statement itemizing the budget at the time you are given the Master Deed. Study it carefully so that you understand exactly what is included in the budget for your development. While economic trends seem to indicate that costs of all types will rise eventually, deliberate underestimation of the budget by the developer can constitute fraud.

If the project is a conversion — that is, converted from rental housing to condominium ownership — the developer should tell you actual past costs of maintenance and repairs and taxes from previous years and how they compare with the proposed budget. When the project is converted, it likely will be reassessed by local authorities.

3. Do I pay the same monthly assessment as everyone else? What if I don't use the recreational facilities, do I still have to pay for maintaining them?

As a co-owner, the monthly fee is a lien on the apartment, and you cannot exempt yourself from paying it by not using the facilities.

Your monthly assessment is calculated on the percentage of value of your unit in comparison with other units. The developer determines this figure and must include it in the Master Deed. If your unit has a higher percentage of value, you will pay a higher monthly assessment.

If the developer has reserved the right to expand the project, he is allowed, with the approval of the Bureau, to amend the Master

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Deed to change the percentages of values assigned to the units so that the entire project reflects a total of 100. For example, an original group of 10 units might each have an assigned value of 10. If a second group of 10 units is added, each of the 20 units might have a value of 5. If the developer reassigns percentages, the relationship between percentages, based on size and amenities of each unit, must be reasonable.

A change in assigned values is unlikely to affect your monthly assessment.

Monthly costs for units that are completed but not yet sold are paid by the developer. This cost is not the same as the monthly assessment. The formula used to arrive at these costs varies from project to project. Check the condominium documents to learn what the developer's obligations are in this regard.

4. What if the monthly fee is not enough to cover costs before the Association's first meeting?

This varies by development. Some developers will make up the difference if costs are not covered by the monthly maintenance fee in the first year of operation. Others retain the right in the Master Deed to reassess the co-owners if this occurs. Again, check your condominium documents. Find out if the developer will advise you of his payments so you can anticipate any increase in your monthly assessment.

5. Can the Association decide to add on other assessments not covered in the budget?

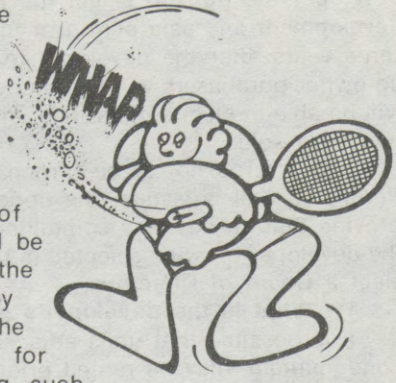
Yes, See Rights and Responsibilities of the Association, Pg. 17.

6. If I deposited money for extras or options, and then change my mind about buying the unit, will my money be refunded?

Until there is a binding Reservation and Subscription Agreement or a purchase agreement you will receive a refund of any money deposited, including that deposited for extras or options. After there is a binding agreement, the developer may collect up to a 10 per cent penalty if you withdraw. For example, if your unit costs $20,000 and you have ordered $5,000 worth of extras, you may forfeit $2,500 of your deposit if you withdraw from the agreement. You should ask about the conditions under which you might forfeit more of your payment for extras.

7. How are the recreation facilities operated and controlled?

You should find out if, and when, recreation facilities are to be built. As a co-owner, you should be informed of ownership of the



facilities, management and control the co-owners have over the rules and regulations governing the facilities. Find out when they will be turned over to the association and whether third parties will be sharing the facilities. If they are to be shared, discuss how the expenses of administration and maintenance will be prorated among all users. If the recreation facilities are to be owned by other than the co-owners, find out the co-owners' financial obligations for supporting the facilities, how long such support is required, and under what circumstances, if any, it can be terminated.

Ask the developer about his financial obligations for the recreation facilities, how long he will support them and the amount of his support. Find out what happens if the developer fails to promptly pay his share of expenses after he turns over the facilities.

8. Does the developer's mortgage contain any clause that the mortgagee (bank, etc.) will not release any units from the mortgage until a certain percentage of units has been reserved?

If so, it may increase the time until you can take title to your own unit. If pre-sale requirements exist and they have not been met at the time the Corporation and Securities Bureau is ready to issue a Permit To Sell, the Bureau may delay releasing your escrowed deposit funds to the developer until the required percentage of units has been reserved. You should know if the developer has an exclusive mortgage arrangement; that is, you must obtain any mortgage for your unit from a specified financial institution.

9. Who will be managing the development? What is the relationship between the developer and the manager or management firm?

10. When will the developer turn over control of the development to the co-owner purchasers?

A buyer becomes a member of the condominium Association as soon as he or she takes title to a unit. Each condominium Association is governed by a Board of Directors elected by the co-owners. Generally, the condominium documents give the

developer the right to select the Board of Directors during the development and sale period of the project. Usually within one to three years after the developer receives his Permit To Sell, the co-owner purchasers will become entitled to vote for directors and will be able to elect a majority of directors once a majority of units has been sold.

If control is not to be turned over within one year after the Permit To Sell is issued, the condominium documents usually provide that an advisory committee of co-owners unaffiliated with the developer must be selected in the interim before the co-owners elect a Board of Directors.

11. What is the developer's policy on renting units?

It is possible that units adjacent to yours, or elsewhere in the condominium, may be rented prior to their sale. You may wish to inquire whether the developer has rented any units in the condominium or whether he plans to do so. The Corporation and Securities Bureau requires that the developer disclose his policy on rentals.

12. What is under warranty in the condominium and what is the developer responsible for repairing or replacing? How long are the warranties?

Usually the Reservation and Subscription Agreement or purchase agreement will contain a one-year warranty from the developer as to building defects in workmanship and materials. Find out when the warranty begins. Each co-owner generally deals directly with the developer regarding warranty repair work unless the problem involves a number of co-owners' units or the common elements. Learn whether the warranties cover building structures, recreational facilities, roads, sidewalks, special equipment, and shrubbery. Warranties ordinarily are restricted to new construction projects.



13. If the project is a conversion, what renovation does the developer plan?

Many conversion projects are offered "as is" to the buyer. Although heating, plumbing, electrical systems, roofing and

structure ordinarily must be inspected and approved by local authorities, the developer will not warranty the project if it is offered "as is."

14. What kind of insurance will the developer carry on the common elements before they are turned over to the Association? What should be covered by the Association's policy? What kind of insurance do I have to carry on my own unit?

While the development is being built, the mortgagee requires adequate coverage on the property. As the individual units are purchased, the bank or savings and loan association holding each unit's mortgage also requires insurance. To cover the contents of your unit, you will likely purchase a tenant's policy similar to that used by renters. The Association also will carry insurance. Check to be sure that interior surfaces of walls in your unit — paneling, for example — are covered either by your own policy or the Association's policy.

A loss assessment clause covering replacement costs that exceed the amount of coverage of common elements is recommended for your individual policy by some insurance companies. Under such a clause, you can be covered for additional assessment if it costs the Association more to replace a clubhouse destroyed by fire, for example, than the amount of insurance carried on the building. Liability coverage of personal injury may be included in this clause, too.

Before the common elements are turned over to the co-owner purchasers, you should ascertain that there is adequate coverage on this property and check to determine the extent of the coverage. From the moment of the first conveyance of a condominium unit to a purchaser, the fire and extended coverage insurance for the project is carried by the Association and not by the developer. You should check on whether the Association policy is adequate and is in conformity with the Condominium Bylaws requirements.

The Urban Land Institute has advised a minimum of $1 million liability for an Association and suggests up to $5 million for a larger development. Other circumstances that may be covered include: Bonding for Association officers, coverage for mistakes made by officers that result in financial loss; workmen's compensation for Association employees; personal property owned by the Association; and demolition costs for damaged buildings. The replacement value of all buildings should be updated each year.

15. Are there easements other than public utility easements which might affect the condominium project or my unit?

16. Are there any unusual conditions that I should know about, such as unusual water or sewage systems?

17. If the roads in the project are private, what costs are involved in their upkeep?

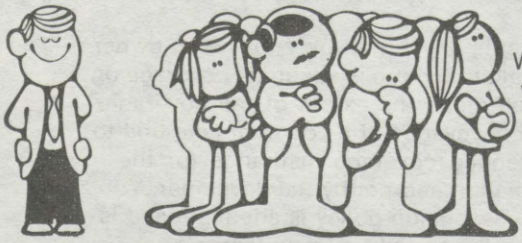
18. What happens when I want to sell my unit? Are there any restrictions? May I rent it to someone else? May it be willed without restrictions?

19. What restrictions are there about children or pets?

20. Does each unit have a carport, parking space or garage assigned to it?

If spaces are not yet assigned, the developer may reserve the right to assign them with an amendment to the Master Deed. Make sure your unit has adequate parking space.

the buyer and the association



When you take title to your unit, you automatically become a member of the co-owners' Association, which is generally a non-profit corporation formed to administer the affairs of the condominium.

Each co-owner may vote on the actions taken by the Association after control of the development has been turned over by the developer. The value of each vote is determined by the value given to each living unit and set forth in the Master Deed.

The Association must meet at least once a year and is governed by a Board of Directors elected by the co-owners at their first meeting. The first meeting of the co-owner purchasers may be called

at any time after 50 per cent of the units are sold, in the discretion of the developer. In no event may it be called later than the time when 80 per cent of the units are sold or within three years after the Master Deed is recorded. In the case of conversions, the time limit is generally one year.

Provisions for holding the annual meeting and designating the voting procedures are included in the Condominium Bylaws, along with other information about the operation of the Association. You are given a copy of the Condominium Bylaws along with the Master Deed when you buy a condominium.

The Association may also operate under its own Bylaws, in addition to the Condominium Bylaws. Association Bylaws provide for the operation of the Association as a non-profit corporation including details of officers, directors, meetings, order of business, and so on.

Before the first annual meeting of the Association, the developer can amend the Condominium Bylaws with the consent of the Corporation and Securities Bureau, so long as the amendment does not materially affect the rights of the co-owners. If the co-owners do not have the right to veto any rules and regulations before the first meeting, the Corporation and Securities Bureau must approve the rules. If the developer is still selling units after the first meeting of the Association takes place, he functions as any other co-owner, in relationship to the Association.

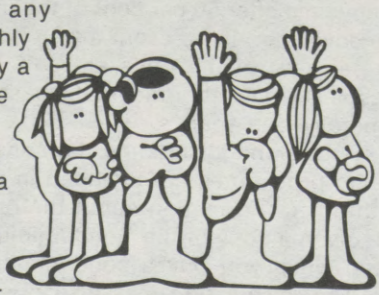
responsibilities and rights of the association

The Association usually is responsible for outside maintenance of the units; for lawn care, snow removal, trash pick-up, street maintenance if the roads are private, and operation of the common elements, including the recreation facilities. These jobs are usually done through a management firm or manager hired by the Association, by employees hired directly by the Association, or, in some cases, by co-owners themselves.

You have the opportunity to decorate the interior walls of your unit and are responsible for their maintenance.

The Association sets fees for the maintenance that falls under its responsibility and may increase the charges. Special assessments may be made by the Board of Directors to cover capital

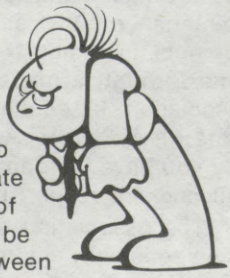
improvements, but generally any substantial increase in the monthly assessment must first be approved by a vote of the co-owners. The Condominium Bylaws set out the dollar limit on what may be approved by the Board of Directors without a vote of the co-owners.



The Condominium Bylaws also will provide for settling disputes arising from interpretation or application of the Master Deed, bylaws, management agreement or between co-owners, between co-owners and the Association, or between the Association and the management firm.

There may be restrictions on your use of your unit that can be applied by the Association. Check the Condominium Bylaws for these. The Association sets rules for use of the recreation facilities and other common elements. It may require approval of repairs or structural modifications you wish to make in your unit. The Association may retain "first refusal" rights if you wish to sell your unit; that is, you may be required to give the Association the opportunity to approve the sale. If you mortgage your unit, you must notify the Association who is holding the mortgage, and the Association may inform the mortgagee of unpaid assessments due from you for your unit.

what to do if you have a complaint



A reputable developer is interested in dealing with you fairly if you have problems with your condominium, as persons living in other types of housing also experience from time to time. It is in the developer's best interests to create satisfied owners, and, therefore, the majority of your questions and complaints usually can be handled by communication and negotiation between the two of you.

Ask your developer for the name, address and telephone number of the persons within his organization to contact when you have a complaint.

There are procedures to follow if you are not satisfied with the construction of the development, or you think you have been misinformed by a condominium sales representative, or you are in disagreement with the practices of the co-owners' Association, or some other problem does arise.

First, if your complaint is with the Association, check the Condominium Bylaws to find out what recourse you have.

If your difficulty is with the developer, first contact him by letter. If no response is received within 15 days after the developer receives a certified, return receipt requested letter, contact:

1. *For Construction Defects:*
   - A. Your local building inspector
   - B. Department of Licensing and Regulation, Residential Builders and Maintenance and Alteration Contractors Board, 1033 South Washington, Lansing, Michigan 48926. Telephone: (517) 373-0678
2. *For Sales Misrepresentations:*
   - A. Corporation and Securities Bureau, Michigan Department of Commerce, 5511 Enterprise Drive, Lansing, Michigan 48913. Telephone (517) 373-8026
   - B. Department of Licensing and Regulation, Real Estate Division, 1033 South Washington, Lansing, Michigan 48926. Telephone: (517) 373-0490
3. *Actions Regarding Permit To Take Reservations, Master Deed, or Permit To Sell:*
   - A. Corporation and Securities Bureau, Michigan Department of Commerce, 5511 Enterprise Drive, Lansing, Michigan 48913. Telephone: (517) 373-8026

The Corporation and Securities Bureau requests that complaints from co-owners of condominium projects be in writing with supporting documents and include details about the complaint involved, what response the co-owners have had from the developer regarding the complaint, and the possible remedies and solutions.

When the Bureau receives a complaint, it contacts the writer to obtain any other necessary information and then determines whether the Bureau has jurisdiction or whether the complaint

should be forwarded to the Department of Licensing and Regulation for its review.

If it is within the Bureau's jurisdiction, the Bureau contacts the developer and tries to work out a solution satisfactory to all parties involved.

If persuasion and negotiation fail to settle the dispute, the Bureau can consider other administrative remedies.

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Mr. MAKENS. I would like to reiterate the initial part of our testimony; that is, in Michigan we have over 1,000 condominiums involving 62,000 condominium units, approximately the value of which is $1.6 billion in terms of their initial sales price. I believe we are the third largest State in the United States in terms of the development of condominiums.

We have been fortunate. We have had minuscule amount of problems in the State. I think we are what Mrs. Hills would classify as a "high degree of regulation" type State. In 1973, with the last statistics we have for New York, we processed three times the number of condominiums developed in New York. So in fact, we do believe that we encourage legitimate condominium development within our State.

Under the concept proposed by Mrs. Hills, we would not have, in my mind, uniform disclosure. We would have lowest common denominator type of disclosure. I'm afraid the disclosure from what I have heard, has the potential of being HUD-dictated disclosure rather than the disclosure which I think would be more in spirit of this bill, that is, the disclosure which would derive from a concept of the States or at least concurrence and joint action by the States that are involved in condominium regulation.

Therefore, Senator, I would highly recommend that an effort be made to coordinate with the States and have the States operate together with our staff or with HUD or whoever else in the development of such a disclosure statement.

The question was asked what's been the developer reaction to the regulation. It's been really positive. We have kept them advised of what we are doing. We brought them in when rules or regulations are proposed or when we are engaged as we are now in the update of our statute, we bring them in along with condominium associations, lenders, and with consumer organizations, to participate in the actual drafting sessions. We believe the reaction is positive. We believe these sessions have been very helpful.

I feel that you cannot, in light of the complexity and variation of condominiums, come up with a simple uniform disclosure statement that's going to be used in every single instance. We have had condominiums that involve a funicular railway and I dare say they will not be able to write that kind of extreme into a condominium disclosure provision.

Therefore, the States must have the authority and the power to include within the condominium disclosure document that information that is unique to a particular condominium and provide a danger or a prospective risk to a purchaser investing in that condominium.

I do not believe that the problem of out-of-State condominiums, as described by Mrs. Hills, is an accurate one. In fact, less than 5 percent of our condominiums that come into Michigan involve out-of-State participation and the burden that is placed on them is minuscule. In Michigan I think our burden may be lighter than in other States but in examining the laws of other States that burden does not seem to me to be unreasonable or to represent a large cost in relation to the cost of housing that's existing in the industry today.

I would recommend the inclusion of a waiver provision such as you described for the 15-day cooling off period. My personal recommendation and the recommendation we will make to our State legis-

lature is for a 10-day cooling off period rather than 15 days, but with the ability to make a waiver but the waiver should not be something that is just done as a matter of quick form but rather should be something that is definitely pointed out. We will have a specific form and certain caveats that must be presented separately so the waiver is presented knowingly and we will have the right to review those in the developers' files if the question is raised.

We would recommend a two-stage disclosure process when the first contact is made with the prospective buyer. We use what is known as the condominium buyer's handbook. I believe copies have been provided. This handbook explains the concept of the condominium, the obligations co-owners are undertaking and the obligations that the developer takes to the prospective purchaser.

This is followed or will be followed by a specific disclosure document of the type that is found in your proposed bill and found in our legislation as well.

The committee asked the question of the Commission on Uniform State Laws. It's my understanding now that a professor at the University of Michigan is in the process, with the help of one of his law school classes, of drafting such a bill for that Commission and doing it on his behest. I do not believe there's been substantial progress done at this time toward any kind of a working draft.

Thank you.

The CHAIRMAN. Thank you very much, Mr. Makens.

Mr. LARSON. Thank you, Mr. Chairman. Members of the committee, I assume my statement will also be entered into the record.

The CHAIRMAN. Yes, indeed.

[Complete statement follows:]

STATE OF MINNESOTA
DEPARTMENT OF COMMERCE
ST. PAUL, MINNESOTA 55101

STATEMENT OF JOHN R. LARSON

COMMISSIONER OF SECURITIES

DEPARTMENT OF COMMERCE

STATE OF MINNESOTA

HEARINGS ON THE CONDOMINIUM

CONSUMER PROTECTION ACT OF 1975

U.S. SENATE COMMITTEE ON BANKING

HOUSING AND URBAN AFFAIRS

5302 DIRKSEN OFFICE BUILDING

WASHINGTON, D.C.

OCTOBER 6, 1975

Mr. Chairman and members of the Committee:

Thank you for the opportunity to be here today and discuss with you the legislation introduced by the Chairman and members of this Committee to protect purchasers of residential condominium units and residents of multi-family structures being converted to condominiums. Specifically, I refer to S 2273 which is known as the "Condominium Consumer Protection Act of 1975".

Residential condominium construction and conversion is occurring on an extensive scale in certain parts of the country. In some states, this phenomenon is being accompanied by a substantial number of consumer complaints, as witnessed by the condominium hearings before the sub-committee on Housing and Urban Affairs of this Committee on October 9 and 10 of 1974 and the Department of Housing and Urban Development's Condominium and Cooperative Study recently completed by that agency. The failure of existing measures to provice redress to consumers has stimulated the legislation under discussion today as well as consumer protection measures adopted or under consideration in various states. There appears to be countless examples of abuses by the developer through self-dealing during the construction period as well as during the time when such developer controls the condominium association. An unscrupulous developer may engage in "flip sales", award subcontracts to firms he owns or controls, enter into exhorbitant leases for common areas which he owns, enter into exhorbitant management contracts with firms he owns, avoid assessments for common areas, change project plans or misuse deposits. In addition, some developers employ a wide variety of legal loopholes and deceptive selling practices when dealing with

condominium purchasers. Problems such as misleading sales representations, cost underestimations or "low balling", and "hidden" contract clauses have been cited throughout the country.

The problems inherent, or at least possible, in a condominium conversion situation add to the problems noted above. Since all of the problems noted herein are well documented and without question establish the need for regulation, there is an additional area which I feel deserves some attention. This is the area of understanding condominium living.

The purchase of a unit in a condominium project is not just the purchase of a home. In addition, there is the membership in the condominium unit owner's association which governs the project. This association governs the day-to-day operation of the condominium project and determines what amenities, improvements or modifications may be made to the project. It is this local form of government that controls, for the most part, the life style of the condominium project. If a swimming pool, tennis court or children's play area is to be added to the project, it must first be approved by the association. If a unit owner desires to plant a garden or paint an exterior door or redesign the interior of the condominium unit, it would require the approval of the association in many cases. The freedom previously enjoyed in a single-family home where a fence may be built on the owner's property or a children's swing set constructed in the backyard is not present in a condominium project. Unfortunately for many condominium purchasers, such fact is not fully appreciated until after the purchase is made.

This is a most common occurrence in Minnesota. It is simple to

write off this problem by saying the purchaser looked at the property, was presented with all of the documents, and should have known what was being purchased prior to signing the contract. The question that comes to my mind is what effort did the developer undertake to adequately explain condominium living.

In the past two years I, and members of my staff, have shopped a number of condominium projects in and around the Minneapolis - St. Paul area. We have found many instances where purchasers did not fully appreciate the impact of condominium living. We have additionally encountered a number of situations where the developer or his selling agent did not understand condominium living. With the absence of such an understanding on the part of the seller it is not difficult to see how many purchasers may not appreciate such consequences.

We in Minnesota, and I am sure in other midwestern states, are the product of single-family homes. I and many others in my generation need only go back to our fathers or grandfathers to see a life on the farm or at least in a rural community. Life centered around the family and the family lived in a single-family home. Apartment or condominium living was viewed as a form of living secondary to the single-family home. The ability to own a piece of real property has been for hundreds of years and is today a fundamental goal of most young people in our part of the country.

While this continues to be by far the most popular form of living of residents in our state, the economic realities of such living have made it prohibitive to a large segment of our society. A recent survey of all major metropolitan areas in the country indicated the

cost for building a new single-family home in the Minneapolis - St. Paul area was the highest in the country. The survey indicated the cost of the average new home in our area was in excess of $57,000. With current mortgage interest rates in excess of 9%, I ask what level of income is necessary to afford this average house? Obviously other forms of housing must be and are being sought, with the most popular form being condominiums.

Condominium development in Minnesota at the present time has been somewhat limited. There are approximately 150 condominiums on file in the various counties of our state. Approximately two-thirds of these are located in the Minneapolis - St. Paul area and approximately one-half of that number are conversion condominiums. The Minnesota statute regulating condominiums is basically the FHA Model Act which was adopted in 1963. As you may be aware, this is a self-administering act. There is no agency enforcing or administering such a statute and there are no disclosure requirements other than what may be contained in the Declaration or By-Laws. We have encountered some problems in condominium development in our state, but they have not reached epidemic proportions as they have in other parts of the country. Our most serious problem is the lack of complete understanding not only on the part of consumers and the general public, but also on the part of the developers concerning condominium living. In observing these problems and in anticipation of increased condominium development in our state, we have proposed an amendment to the Minnesota Condominium Act which will provide for the disclosures and safeguards necessary for condominium purchaser protection. Such legislation is the product of approximately eighteen (18) months of work

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by my office. We have reviewed condominium legislation in other states, the Minnesota Uniform Land Sales Practices Act and the proposed federal legislation. We have spent countless hours of deliberation with the construction industry and practicing bar in Minnesota. It is believed that this state legislation, which is currently pending in the Minnesota Legislature, is substantially in conformity with the provisions of the Condominium Consumer Protection Act of 1975. In testifying at the hearings on condominiums and cooperatives conducted by the Department of Housing and Urban Development in February of this year, I indicated that I believed such legislation would pass during the 1975 Minnesota legislative session. Regrettably this passage did not occur and I would represent to you now that I am optimistic this bill will pass during the 1976 legislative session. At the present time this bill has passed the House of Representatives and is awaiting a committee hearing in the Senate.

The failure of this legislation to pass is not the result of any opposition but rather a result of the time problems that exist in most state legislatures. I am aware of no opposition to this condominium legislation. In fact, many developers viewed the disclosure requirements as a method of enhancing condominium development. They feel that equal disclosure by all developers will assist the sales of their projects and will improve the industry.

In light of this I would like to offer my support for the legislation under consideration today. It is my opinion that condominium purchasers will benefit in three (3) ways as a result of this legislation:

1. All purchasers will be provided with a public offering state-

ment setting forth all material information concerning the condominium, thus allowing them to intelligently compare various condominium projects;

2. The minimum protections set forth in the legislation will eliminate the abuses and frauds perpetrated on innocent condominium purchasers; and
3. The cost of such protection will not substantially increase the cost of the condominium unit.

In summary, the purchaser obtains the needed protection without incurring unnecessary expense.

In my support for the "Condominium Consumer Protection Act of 1975", I cite the need for material disclosure and minimum safeguards to protect the general public. I strongly support the position of the authors, which is reflected by Section 7 of the bill, which authorizes and encourages states to take charge and administer their own condominium plans. As Senator Proxmire indicated in his comments in introducing this bill:

> "... We recognize that states do have interest and expertise in real estate matters, including condominiums. Indeed, a few states have led the way in enacting strict condominium consumer protection laws and setting up offices to administer these laws.
>
> We have no desire to blunt the initiative states have taken in this area. Rather we want to give a firm federal commitment to to their efforts and provide the same protections to consumers in all states."

While I support the intent of this section, I have some reserva-

tion concerning the amount of discretion provided the Secretary of HUD. A review of Section 7 (b) (2) indicate the Secretary in approving a state plan needs assurances that adequate personnel and financial support for a designated agency, will require the imposition of civil and criminal penalties at least as severe as the federal legislation, will require reporting requirements and such other requirements as may be prescribed. Many of these requirements will have to be further defined by rule and regulation. It is specifically requested that state administrators be allowed to participate in such rule making procedures.

A point of concern for myself as a securities commissioner is Section 18 of the proposed legislation which exempts condominium projects from the Securities Act of 1933 provided the developer has complied with the requirements of this act through a state plan. Is it the intent of this Section to exempt the sale of a condominium project where the units are being sold in the form of an investment contract consequently a security? If such is the case, I would recommend that the opposite form of exemption be placed in this act. I would recommend that a condominium project being sold in the form of an investment contract and subject to the registration requirements of the Securities Act of 1933 be exempt from this Act altogether. Condominiums being sold as a security are being sold for a purpose other than a primary residence. Typically, this is a recreational development where the owner will occupy the premises for a very short period of time during the year. The condominium unit will be available for rental during the remainder of the year with the income going to the owner on a shared basis with other owners.

It seems to me that the Securities and Exchange Commission is one of the most effective agencies in the federal government. If a developer chooses to sell condominium units in a project as an investment rather than a primary home the securities law should govern. The SEC has over forty (40) years of experience in dealing with full and accurate disclosure. I would certainly feel that HUD and the SEC could coordinate their efforts in the proper disclosure and sale of a condominium project, but the SEC should be responsible in all cases where a security is being offered or sold.

Mr. LARSON. With that in mind, I will go to some specific points in S. 2273 that I feel are important from a State regulatory point of view.

The first is Section 7 which authorizes the Secretary of HUD to approve a State plan. The requirements for approving a plan are set forth in the statute and my only question in that area is some guidance to the States in knowing that their state plan will in fact be approved if that provision remains in the bill.

One of the requirements is that the State plan is equal to or stronger than the Federal legislation in the area of substantive standards and disclosure. If that is to be interpreted by a point by point technical analysis of the State legislation, I do not think that that is in the best interest. I believe State plans should be looked at overall and I would cite a couple examples for you.

The Federal act, your proposed bill, cites criminal penalties of $10,000 or 1 year in prison, while the State proposal in Minnesota says $5,000 or 5 years in prison. My question is: Is that the same as or equal to and would that comply with the Federal standard?

The second provision is the area of turning control of the unit owners association over to the owners. The Federal proposal provides 1 year or 80 percent. The Minnesota proposal basically provides 2 years or 60 percent. Again, my point is, if the Secretary of HUD is going to view the state plan overall to make sure that the intent of the legislation—the intent of protection for the condominium purchasers is there, then the plan should be approved and not each point technically complied with.

The second part of the act which I feel is very important is Section 18 which exempts out or provides the power of the Secretary of HUD to exempt condominium projects from the Securities Act of 1933 provided the developer has complied with the requirements of the state plan.

My recommendation would be just the opposite be included. If a condominium project is subject to the Securities Act of 1933, then it should be exempt from the condominium legislation, the reason being that condominiums which are sold as securities are sold with a different emphasis than simply residential living. They are sold with an investment intent. They are purchased with an investment intent and the disclosure and the criminal sanctions that are directed toward such investment requirements should be applicable to those situation.

I think that the Securities and Exchange Commission with its extensive experience in the area of disclosure should not be invalidated, and in fact, should prevail.

Thank you, Mr. Chairman.

The CHAIRMAN. Thank you, Mr. Larson.

Mr. LLOYD. Mr. Chairman, Senator Morgan, I too wish to focus on disclosure. I had made some prepared remarks summarizing the written statement submitted last week, however I think remarks of a more general nature are called for at this moment.

The CHAIRMAN. All the statements will be printed in the record, including Ms. Earner's.

Mr. LLOYD. Thank you.

[Complete statement follows:]

S T A T E M E N T T O

The United States Senate Committee on

BANKING, HOUSING, AND URBAN DEVELOPMENT

Relating to S.2273,

The Condominium Consumer Protection Act of 1975

This statement is prepared and presented by Ross J. Lloyd, a Special Assistant Attorney General of the Commonwealth of Virginia, assigned as Condominium Administrator of the Virginia Real Estate Commission. The statement is prepared on behalf of the Virginia Real Estate Commission at the behest of its chairman but represents only the thinking of the draftsman. Because of the rush of events, this statement will not have been reviewed or adopted by the Commission as of the date of its presentation.

The statement focuses on two separate issues. They are, one, technical defects in the proposed Act and, two, the probable effect in Virginia of enactment of the Act. Technical defects are treated in Items 1 through 8 of the statement. Probable effect is treated in the remaining portion of the statement.

1. I find that the Act does not adequately address the question of who must make the disclosure to prospective purchasers required by §6. Clearly, the disclosure requirements of §6 must be imposed on the party which is responsible for the creation of the condominium project and which first offers for sale the units therein, provided that the project contains ten or more units. (The party referred to cannot be labeled a "developer" within the meaning of §2(12) since that term includes all parties who own two or more units in a project and undertake to sell same. I suggest that "developer" be redefined to reflect the common understanding of the term.)

Two other aspects of the disclosure question pose greater difficulties. First, should the owner of a single condominium unit who wishes to sell his unit be required to make any special disclosures to a prospective purchaser? Second, should an investor who has acquired a substantial number of condominium units and who offers them for sale be required to make any special disclosures to prospective purchasers?

When considered from the standpoint of the prospective purchaser's need for protection, the answers to both questions must be identical since the need for protection, if it exists, exists independently of the number of units being offered and irrespective of whether the unit to be purchased is on the market for the first time or as a resale. Stated in another fashion, the ideal of consumer protection contemplates that every offering of a condominium unit be subject to full scale disclosure requirements.

Practically, however, comprehensive disclosure can be required of only those sellers who are offering a substantial number of condominium units. The owner of a single unit who resells can be required to make only a limited form of disclosure. In Virginia, the Condominium Act provides that a reselling unit owner shall obtain from the unit owners' association and furnish to a prospective purchaser a statement disclosing such matters as the financial condition of the association, the existence of liens against the unit, pending litigation involving the association and available insurance coverage (Virginia Code §55-79 97)

Perhaps an investor who offers several units for sale should be required to make disclosure to an extent greater than that required of the single unit owner and approaching or equalling that required by §6. To point out a statutory parallel, it is observed that an underwriter ("any person who has purchased from an issuer with a view to, or offers or sells for an issuer in connection with, the distribution of any security...," §2(11) of the Securities Act of 1933) will be held to the same disclosure requirements imposed on an issuer by §§4(1) and 5 of the Securities Act of 1933, subject to the provisions of SEC Rule 144 promulgated thereunder.

2. Because of the breadth of the definition of "offer", §4 could reasonably be construed as prohibiting all marketing activities including advertising of a condominium project prior to furnishing to prospective purchasers an abstract making the disclosures required by §6. In my opinion, a construction of "offer" which results in so sweeping a prohibition is unnecessarily broad. An "offer" should be limited in its definition to those contacts between a developer or his agents and an individual prospective purchaser in which the prospective purchaser is encouraged to execute a contract of sale or do some other act which creates or purports to create a legal or equitable interest in a condominium unit other than a security interest in the condominium unit.

To prohibit advertising and other marketing activities before disclosure information is furnished to prospective purchasers is to prohibit what ought to be considered a normal practice. Indeed, the decision to develop a condominium might not be made if the developer were forbidden to arouse public interest in the condominium prior to the time that it becomes practicable to furnish disclosure information. The economics of condominium development are such that it would not be feasible in most cases to go forward with development unless the developer could assure itself at an early stage that there exists a substantial number of persons desirous of purchasing units when they become available. Pre-disclosure advertising and other marketing activities are vital to obtaining that assurance.

Having stated the developer's need to advertise before making the statutory disclosures, it is necessary also to consider the effect of such advertising upon the public. It is in the nature of advertising that its subject will be described in glowing terms. In order to "whet the appetite" of prospective purchasers for acquisition of condominium units, the advertising thereof will typically mention subjectively determined attributes of the units and contain representations which are mere opinions of the advertiser.

It must be recognized that unregulated advertising could impart to a prospective purchaser a distorted picture of a condominium unit. However, §6 affords ample protection against the possibility that a purchaser will be harmed by non-objective advertising by its provision for a disclosure abstract making full and accurate disclosure of all material circumstances and features affecting the project. No prospective purchaser will be legally bound by a commitment to purchase until at least 15 days after he has received a disclosure abstract. (This is the presumed intent of §4(b). See Item 3 of my statement.) Thus, any harm which may have been done by inaccurate or incomplete advertising will either be remedied by the disclosure abstract or the purchaser will not be bound.

In light of the foregoing considerations, it is urged that "offer" be redefined.

3. Section 4(b) makes reference to condominium units subject to §4(a). It is not clear whether the effect of that reference is to make voidable only those transactions which are unlaw-

ful under §4(a) or whether all transactions involving use of the mailes or interstate commerce or federal financing are voidable. I'm certain that the intent is to make the broader category of transactions voidable, but this intent should be explicit.

4. Section 4(b) should provide that some form of notice to the developer is necessary to avoid the contract or agreement.

5. The period provided in §5(3) during which the developer may retain control of the condominium owners' association is inadequate with regard to condominiums which are developed in stages, as is frequently the case with larger projects. In Virginia and in jurisdictions with laws similar to Virginia, a developer may develop and market a condominium and reserve to itself the option to expand the condominium if experience with the initial stage so warrants. The development process typically extends over a period exceeding one year and may require several years.

It is deemed appropriate in Virginia that a developer retain control of such a project while the development process continues. Conversely, it does not seem appropriate that a developer should be required to turn over control of the condominium owners' association to the unit owners while the condominium is only fractionally completed or, indeed, that the unit owners should be required to assume control under such circumstances. A provision which ties the length of developer's control to the length of the development process is in order. I would recommend that the standards provided in Virginia Code §55-79.74(a) be adopted.

If such a longer period of developer's control is provided for, protection for unit owners against abuse by the developer of its right to control the owners' association will inhere in the fact that the developer's performance in governing the condominium will inevitably affect its ability to dispose of remaining unsold units. The developer will operate under a constraint to prevent dissatisfaction among existing unit owners.

6. Section 5(4) is a vital protection against the so-called "sweetheart contract", but the rigidity of its restriction on contracts entered into by the developer may have adverse consequences. There are and will be projects in which the scheme of development calls for the leasing of a portion of the common elements to a business enterprise which will provide a desired service to the unit owners, e.g., a dry cleaning establishment or a convenience store. A business enterprise will be reluctant to enter such a lease when §5(4) raises the possibility that the lease will be terminated at an unspecified time in the near future. In any event, the statutory restriction will place the developer acting on behalf of the owners' association in a disadvantageous position when attempting to negotiate such a lease.

Virginia law permits the developer, while in control of the condominium owner's association, to enter into a contract, lease or agreement on behalf of the association which is not terminable by the association prior to its natural expiration "if such contract, lease or agreement is bona fide and commercially reasonable to the unit owners' association at the time entered into under the circumstances" (Virginia Code §55-79-74(b)(2)). Thus, the "sweetheart contract" is regulated while the agreement beneficial to the unit owners may be entered into free from unnecessary and prejudicial restrictions on its duration. It is recommended that such a provision be incorporated in §5(4).

7. The two-year warranty provided by §5(5) on the roof, structural components and mechanical, electrical, plumbing and common service elements serving the condominium project as a whole is inadequate in two respects.

On the one hand, a mechanical, electrical, plumbing or common service element may serve more than one unit but less than the whole project, as would normally be the case where the project consists of two or more buildings. The warranty would not apply in such cases. In order to provide full coverage, the phrase "the condominium project as a whole" should be deleted and for it should be substituted the phrase "more than one unit."

On the other hand, the provision that the warranty begins running at the time of initial occupancy of the project gives no protection as to warranted elements built or furnished more than two years from the time of initial occupancy of the project. A refinement of the provisions is necessary to cover the various circumstances in which the project may be initially occupied prior to the time at which the warranty period should logically commence. An example of such a refinement is found in Virginia Code §55-79.79(b).

8. Section 5(7) also requires refinement to govern properly certain situations which arise in practice. The developer which is required to give a tenant 120 days notice to vacate may not know four months in advance the actual date on which the premises in question will have to be vacated to facilitate conversion. However, in order to ensure that notice is properly given, the developer is obligated to tender notice 120 days prior to the earliest date on which the premises may have to be vacated.

It will frequently occur that the premises are not needed for conversion at the date stated in the notice and the tenant will be permitted to hold over past said date. In that instance the question arises: May the tenant be summarily ordered to vacate when the premises are subsequently needed for conversion or must some additional grace period be provided? It would seem equitable that the tenant be afforded notice and a reasonable time in which to vacate. A suggested solution is to treat the tenant who is permitted to hold over past the date originally provided for in the 120-day notice as having a tenancy from month to month. State law would then govern the additional notice to be given.

Section 5(7) should also provide that, if the tenancy is from month to month in the first instance, the 120-day notice may also constitute a notice to terminate the tenancy provided for in applicable state law, except that, notwithstanding any contrary provisions of such state law, a tenancy from month to month may only be terminated upon 120 days notice when such termination is in regard to the creation of a conversion condominium.

9. Turning to the subject of national standards for disclosure, it should be observed that the statutory standards of §6 will have to be greatly elaborated by administrative rules. I make this observation on the basis of our experience in Virginia with disclosure standards which are similar in substance to those of §6. We have found that the disclosure standards of our Act (Virginia Code §§55-79.90(a) and 94(a)) leave a great deal to the imagination.

Following are a number of illustrations of the need to fill the statutory interstices via the administrative process. Many others could be cited.

Section 6(a)(2) requires disclosure of the price of each type of unit. Does this requirement mean that the developer must state an exact dollar figure or may a price range be stated? Does the requirement mean that developer is not free to sell the unit for a different price on the basis of subsequent negotiations?

Section 6(a)(6)(B) calls for a two-year projection of the taxes to be paid on a unit. In most instances the property involved will not have been assessed or reassessed as a condominium. Should the developer in such a case state the assessed value/fair market value ratio and the tax rate prevailing in the taxing jurisdiction? Should taxes be calculated on the basis of an estimated assessed value?

Numerous questions arise concerning the provisions of §6(a)(7). Must the special disclosure required by the subsection be made in the case of a condominium unit initially sold in the thirteenth month following completion of a newly constructed project? Must the engineer's report cover each structural element and mechanical and supporting system specifically or may the report deal with categories of structural elements and mechanical and supporting systems? If the engineer bases his report on a random inspection of selected elements or systems, must he state the percentage of all elements or systems inspected? Since a statement of useful life is, by its nature, speculative, may the engineer take into account uncertanties in his determination by qualifying his statement of useful life or by stating useful life within a range of years? Should a statement of replacement cost of a given element or system indicate whether the element or system is part of a unit or part of the common elements, i.e., whether the cost of replacement will be borne by a unit owner individually or as a common expense to be apportioned among all unit owners? In the case of an element or system which cannot readily be replaced without disturbing the structure in which it is found, e.g., electrical wiring, should the statement of replacement cost be based on replacement of the element or system alone or on replacement of the element or system in connection with a general reconstruction of the structure in which it is found?

In addition to specific problems of administrative implementation created by §6, there are considerations of a general nature which must be addressed. Is the information required to be disclosed exclusive or should the developer be required to disclose other information which might reasonably affect the decision of the prospective purchaser to accept or reject the offer of a condominium unit? May disclosure be made by reference to extrinsic sources? May the disclosure abstract contain expressions of opinion?

All of the questions posed in the foregoing paragraphs are intended to exemplify the kinds of issues which §6 leaves unresolved. I do not suggest that §6 is deficient because of its silence on the issues. On the contrary, I believe that an attempt to make comprehensive provisions for disclosure by statute would prove to have fallen short of the work. The draftsman would be sure to find that they have failed to anticipate everything; the day will come when a special circumstance arises for which the statute makes no provision. I believe it is preferable to leave matters of detail to the administrative process which, because of its greater flexibility, is better adapted for the task.

My entire purpose in dwelling at such length on the need for administrative elaboration of §6 is to make plain the considerable extent to which the Secretary of Housing and Urban Development will have to exercise her rulemaking authority under §13(c) in order to make disclosure work. There is no doubt in my mind that, if the Condominium Consumer Protection Act of 1975 is enacted as proposed, national condominium regulation will be accomplished at least as much by HUD as by Congress.

10. I wish to focus further on the issue of implementing disclosure standards by administrative regulation. (I am suggesting in the next Item that Virginia be exempted from compliance with S.2273, but I will assume for the moment that no such exemption will be made.)

Leaving aside any questions of the capabilities of the Secretary and her subordinates, I would offer the observation that a system in which state regulatory agencies are compelled to apply federal rules in performing their regulatory tasks is bound to prove unsatisfactory. My observation is based on the following rationale.

The quality and effectiveness of regulations governing any particular subject would seem to have a direct relationship to the experience of the author of the regulations with the particular subject. Presently, many states are actively engaged in condominium regulation. The typical scheme of regulation is one in which the developer is required to obtain some form of acceptance of its condominium project from a state agency before he can offer any units to the public. The Department of Housing and Urban Development has never engaged in any such condominium regulatory activity and will not do so if S.2273 is enacted. Granting that HUD has experience in the financing of condominium projects and has gained valuable insights through the recent condominium study conducted at Congress' direction, it cannot be said that this type of experience matches the experience acquired by many state agencies in the day-to-day administration of condominium regulatory systems over a period of years. With this in mind, it must be said that, insofar as many of the states are concerned, the appropriate source of rules implementing the statutory standards is not HUD but a state agency. It would be presumptuous in the extreme to insist that all states be subject to rules promulgated by HUD.

There is, of course, the question of how to determine whether HUD rules or local rules be applied in a given state. I suggest that if (1) a state's statutory standards are equivalent to those of S.2273 and (2) a state agency is interposed between developer and purchaser at least to the extent of ensuring that required disclosure is actually being made, the state should be allowed to augment the statutory standards with its own rules. In such a situation, I find no need for the state to have imposed upon it rules handed down from above, especially where there is no indication that said rules would be more effective than state rules in regulating condominiums.

11. In Virginia we are administering a statute which has been acclaimed a model condominium law and the first of a new generation of condominium laws. The beauty of our Act consists in its being, simultaneously, comprehensive in its provision for the creation and operation of a condominium and flexible in the varying approaches to condominium development which it permits. Having provided for the creation and operation of a condominium, our Act then requires that it be registered with the Virginia Real Estate Commission before any condominium units may be offered to the public (assuming that the project is residential).

As I mentioned earlier, our Act contains disclosure standards substantially akin to those of §6. If S.2273 is enacted, we will have one year in which to continue our present operation (assuming that the Secretary of HUD recognizes our Act as a condominium consumer protection law pursuant to §7(b)(3)). At the end of that year any of our statutory standards which are inconsistent with the federal standards would be preempted. Moreover, we would be unable to obtain state plan approval from the Secretary pursuant to §7(b)(2). To avoid those eventualities, our General Assembly would be asked to amend the Condominium Act to conform to the federal law.

It becomes appropriate at this juncture to raise a fundamental question: Does it make sense to tamper with effective state legislation solely because Congress finds that certain legislation

in other states is ineffective? We in Virginia have worked long and hard to provide the kind of regulation of condominiums which is best for the Commonwealth. We believe that we have achieved a modicum of success. I wish to state emphatically that I personally do not believe that Congress can do better. On the contrary, I believe that our thinking in the condominium area is more advanced than that of the draftsmen of S.2273. I point to the earlier discussion of technical defects in S.2273 as evidence tending to support my assertion.

I submit that, if S.2273 is to be given serious consideration, it must first be revised to provide that states such as Virginia whose methods of condominium regulation are more sophisticated than those proposed at the federal level be exempted from federal regulation. I suggest such an exemption not simply on the basis of some generalized states' rights thory or as a blind reaction to federal intervention. I suggest exemption for the positive reason that evolution of the methods by which consumers are protected in condominium transactions would be greatly enhanced if those states which are active in the area were free to continue their efforts unhampered by unnecessary federal restrictions.

The need for further evolution is apparent to us in Virginia for, if there is one thing which we have established as a certainty, it is that we have not passed beyond the experimental stage in providing protection to purchasers of condominium units. I believe that officials in our sister states charged with providing protection to condominium purchasers would agree that a wholly satisfactory system has yet to be implemented. I would label fatuous anyone's claim to have devised a totally effective procedure.

If my analysis of the present situation is correct, then it would seem that Congress would desire to encourage the several states to carry on their work. To repeat an oft-used phrase, the states acting independently can serve as "laboratories" in which various solutions to the condominium consumer protection problem may be attempted. At some future date, a system may emerge as the single best means of protecting condominium purchasers. Then Congress could justifiably impose the system on all the states.

Until such time, Congress should regulate condominiums only in those states in which (1) abuses in condominium development and marketing are occurring and (2) the state itself has not acted to protect consumers. The standard by which it is determined whether federal regulation is needed in a particular state should not be a rigid one but should be adopted in recognition of the possibility that a state's actions may not conform to a pre-conceived, uniform federal standard and may yet serve to protect condominium purchasers.

CODE OF VIRGINIA
1950

CONDOMINIUM ACT
with 1975 Amendments

Title 55—Chapter 4.2

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ARTICLE 1.

General Provisions.

§ 55-79.39. How chapter cited.—This chapter shall be known and may be cited as the "Condominium Act." (1974, c. 416.)

§ 55-79.40. Application and construction of chapter.—This chapter shall apply to all condominiums and to all horizontal property regimes or condominium projects. For the purposes of this chapter, the terms "horizontal property regime" and "condominium project" shall be deemed to correspond to the term "condominium"; the term "apartment" shall be deemed to correspond to the term "unit"; the term "co-owner" shall be deemed to correspond to the term "unit owner"; the term "council of co-owners" shall be deemed to correspond to the term "unit owners' association"; the term "developer" shall be deemed to correspond to the term "declarant"; the term "general common elements" shall be deemed to correspond to the term "common elements"; and the terms "master deed" and "master lease" shall be deemed to correspond to the term "declaration" and shall be deemed included in the term "condominium instruments." This chapter shall be deemed to supersede the Horizontal Property Act, §§ 55-79.1 through 55-79.38, and no condominium shall be established under the latter on or after July one, nineteen hundred seventy-four. But this chapter shall not be construed to affect the validity of any provision of any condominium instrument recorded prior to July one, nineteen hundred seventy-four. Nor shall article 4 of this chapter be deemed to supersede §§ 55-79.16 through 55-79.31 of the Horizontal Property Act as to any condominiums established prior to the effective date hereof. (1974, c. 416.)

§ 55-79.41. Definitions.—(a) *"Common elements"* shall mean all portions of the condominium other than the units.

(b) *"Common expenses"* shall mean all expenditures lawfully made or incurred by or on behalf of the unit owners' association, together with all funds lawfully assessed for the creation and/or maintenance of reserves pursuant to the provisions of the condominium instruments; "future

common expenses" shall mean common expenses for which assessments are not yet due and payable.

(c) *"Common profits"* shall mean all income collected or accrued by or on behalf of the unit owners' association, other than income derived from assessments pursuant to § 55-79.83.

(d) *"Condominium"* shall mean real property, and any incidents thereto or interests therein, lawfully submitted to this chapter by the recordation of condominium instruments pursuant to the provisions of this chapter. No project shall be deemed a condominium within the meaning of this chapter unless the undivided interests in the common elements are vested in the unit owners.

(e) *"Condominium instruments"* shall be a collective term referring to the declaration, bylaws, and plats and plans, recorded pursuant to the provisions of this chapter. Any exhibit, schedule, or certification accompanying a condominium instrument and recorded simultaneously therewith shall be deemed an integral part of that condominium instrument. Any amendment or certification of any condominium instrument shall, from the time of the recordation of such amendment or certification, be deemed an integral part of the affected condominium instrument, so long as such amendment or certification was made in accordance with the provisions of this chapter.

(f) *"Condominium unit"* shall mean a unit together with the undivided interest in the common elements appertaining to that unit. (Cf. the definition of "unit," infra.)

(g) *"Contractable condominium"* shall mean a condominium from which one or more portions of the submitted land may be withdrawn in accordance with the provisions of the declaration and of this chapter. If such withdrawal can occur only by the expiration or termination of one or more leases, then the condominium shall not be deemed a contractable condominium within the meaning of this chapter.

(h) *"Conversion condominium"* shall mean a condominium containing structures which before the recording of the declaration, were wholly or partially occupied by persons other than those who have contracted for the purchase of condominium units and those who occupy with the consent of such purchasers.

(i) *"Convertible land"* shall mean a building site; that is to say, a portion of the common elements, within which additional units and/or limited common elements may be created in accordance with the provisions of this chapter.

(j) *"Convertible space"* shall mean a portion of a structure within the condominium, which portion may be converted into one or more units and/or common elements, including but not limited to limited common elements in accordance with the provisions of this chapter. (Cf. the definition of "unit," infra.)

(k) *"Declarant"* shall mean all persons who execute or propose to execute the declaration or on whose behalf the declaration is executed or proposed to be executed. From the time of the recordation of any amendment to the declaration expanding an expandable condominium, all persons who execute that amendment or on whose behalf that amendment is executed shall also come within this definition. Any successor of the persons referred to in this subsection who come to stand in the same relation

to the condominium as their predecessors did shall also come within this definition.

(l) *"Dispose"* or *"disposition"* shall refer to any voluntary transfer of a legal or equitable interest in a condominium unit, except as security for a debt.

(m) *"Executive organ"* shall mean an executive and administrative entity, by whatever name denominated, designated in the condominium instruments as the governing body of the unit owners' association.

(n) *"Expandable condominium"* shall mean a condominium to which additional land may be added in accordance with the provisions of the declaration and of this chapter.

(o) *"Identifying number"* shall mean one or more letters and/or numbers that identify only one unit in the condominium.

(o1) *"Institutional lender"* means one or more commercial or savings banks, savings and loan associations, trust companies, credit unions, industrial loan associations, insurance companies, pension funds, or business trusts including but not limited to real estate investment trusts, any other lender regularly engaged in financing the purchase, construction, or improvement of real estate, or any assignee of loans made by such a lender, or any combination of any of the foregoing entities.

(o2) *"Land"* is a three-dimensional concept and includes parcels with upper or lower boundaries, or both upper and lower boundaries, as well as parcels extending ab solo usque ad coelum. Parcels of airspace constitute land within the meaning of this chapter. Any requirement in this chapter of a legally sufficient description shall be deemed to include a requirement that the upper or lower boundaries, if any, of the parcel in question be identified with reference to established datum.

(p) *"Leasehold condominium"* shall mean a condominium in all or any portion of which each unit owner owns an estate for years in his unit, or in the land within which that unit is situated, or both, with all such leasehold interests due to expire naturally at the same time. A condominium including leased land, or an interest therein, within which no units are situated or to be situated shall not be deemed a leasehold condominium within the meaning of this chapter.

(q) *"Limited common element"* shall mean a portion of the common elements reserved for the exclusive use of those entitled to the use of one or more, but less than all, of the units.

(r) *"Nonbinding reservation agreement"* shall mean an agreement between the declarant and a prospective purchaser which is in no way binding on the prospective purchaser and which may be cancelled without penalty at the sole discretion of the prospective purchaser by written notice, hand-delivered or sent by United States mail, return receipt requested, to the declarant or to any sales agent of the declarant at any time prior to the formation of a contract for the sale or lease of a condominium unit or an interest therein. Such agreement shall not contain any provision for waiver or any other provision in derogation of the rights of the prospective purchaser as contemplated by this subsection, nor shall any such provision be a part of any ancillary agreement.

(s) *"Offer"* shall mean any inducement, solicitation, or attempt to encourage any person or persons to acquire any legal or equitable interest in a condominium unit, except as security for a debt.

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(t) *"Officer"* shall mean any member of the executive organ or official of the unit owners' association.

(u) *"Par value"* shall mean a number of dollars or points assigned to each unit by the declaration. Substantially identical units shall be assigned the same par value, but units located at substantially different heights above the ground, or having substantially different views, or having substantially different amenities or other characteristics that might result in differences in market value, may, but need not, be considered substantially identical within the meaning of this subsection. If par value is stated in terms of dollars, that statement shall not be deemed to reflect or control the sales price or fair market value of any unit, and no opinion, appraisal, or fair market transaction at a different figure shall affect the par value of any unit, or any undivided interest in the common elements, voting rights in the unit owners' association, liability for common expenses, or rights to common profits, assigned on the basis thereof.

(v) *"Person"* shall mean a natural person, corporation, partnership, association, trust, or other entity capable of holding title to real property, or any combination thereof.

(w) *"Purchaser"* shall mean any person or persons who acquire by means of a voluntary transfer a legal or equitable interest in a condominium unit, except as security for a debt.

(x) *"Size"* shall mean the number of cubic feet, or the number of square feet of ground and/or floor space, within each unit as computed by reference to the plat and plans and rounded off to a whole number. Certain spaces within the units including, without limitation, attic, basement, and/or garage space may but need not be omitted from such calculation or partially discounted by the use of a ratio, so long as the same basis of calculation is employed for all units in the condominium, and so long as that basis is described in the declaration.

(y) *"Unit"* shall mean a portion of the condominium designed and intended for individual ownership and use. (Cf. the definition of "condominium unit", supra.) For the purposes of this chapter, a convertible space shall be treated as a unit in accordance with § 55-79.62 (d).

(z) *"Unit owner"* shall mean one or more persons who own a condominium unit, or, in the case of a leasehold condominium, whose leasehold interest or interests in the condominium extend for the entire balance of the unexpired term or terms. (1974, c. 416; 1975, c. 415.)

§ 55-79.42. Separate titles and taxation.—Each condominium unit shall constitute for all purposes a separate parcel of real property, distinct from all other condominium units. If there is any unit owner other than the declarant, then no tax or assessment shall be levied on the condominium as a whole, but only on the individual condominium units. (1974, c. 416.)

§ 55-79.43. County and municipal ordinances; nonconforming conversion condominiums; applicability of Uniform Statewide Building Code.—No zoning or other land use ordinance shall prohibit condominiums as such by reason of the form of ownership inherent therein. Neither shall any condominium be treated differently by any zoning or other land use ordinance which would permit a physically identical project or development under a different form of ownership. No subdivision ordinance in any county, city or town in the Commonwealth shall apply to any condominium or to any

subdivision of any convertible land, convertible space, or unit unless such ordinance is by its express terms made applicable thereto. Nevertheless, counties, cities and towns may provide by ordinance that proposed conversion condominiums and the use thereof, which do not conform to the zoning, land use and site plan regulations of the respective county or city in which the property is located, shall secure a special use permit, a special exception, or variance, as the case may be, prior to such property becoming a conversion condominium. In the event of an approved conversion to condominium, counties, cities, towns, sanitary districts, or other political subdivisions may impose such charges and fees as are lawfully imposed by such political subdivisions as a result of construction of new structures to the extent that such charges and fees, or portions of such charges and fees, imposed upon property subject to such conversions may be reasonably related to greater or additional services provided by the political subdivision as a result of the conversion. Nothing in this section shall be construed to permit application of any provision of the Uniform Statewide Building Code which is not expressly applicable to condominiums by reason of the form of ownership inherent therein to a condominium in a manner different from the manner in which such provision is applied to other buildings of similar physical form and nature of occupancy. (1974, c. 416; 1975, c. 415.)

§ 55-79.44. **Eminent domain.**—(a) If any portion of the common elements is taken by eminent domain, the award therefor shall be allocated to the unit owners in proportion to their respective undivided interests in the common elements. Provided, however, that the portion of the award attributable to the taking of any permanently assigned limited common element shall be allocated by the decree to the unit owner of the unit to which that limited common element was so assigned at the time of the taking. If that limited common element was permanently assigned to more than one unit at the time of the taking, then the portion of the award attributable to the taking thereof shall be allocated in equal shares to the unit owners of the units to which it was so assigned or in such other shares as the condominium instruments may specify for this express purpose. A permanently assigned limited common element is a limited common element which cannot be reassigned or which can be reassigned only with the consent of the unit owner or owners of the unit or units to which it is assigned.

(b) If one or more units is taken by eminent domain, the undivided interest in the common elements appertaining to any such unit shall thenceforth appertain to the remaining units, being allocated to them in proportion to their respective undivided interests in the common elements. The court shall enter a decree reflecting the reallocation of undivided interests produced thereby, and the award shall include, without limitation, just compensation to the unit owner of any unit taken for his undivided interest in the common elements as well as for his unit.

(c) If portions of any unit are taken by eminent domain, the court shall determine the fair market value of the portions of such unit not taken, and the undivided interest in the common elements appertaining to any such units shall be reduced, in the case of each such unit, in proportion to the diminution in the fair market value of such unit resulting from the taking. The portions of undivided interest in the common elements thereby divested from the unit owners of any such units shall be reallocated among those units and the other units in the condominium in proportion to their respec-

tive undivided interests in the common elements, with any units partially taken participating in such reallocation on the basis of their undivided interests as reduced in accordance with the preceding sentence. The court shall enter a decree reflecting the reallocation of undivided interests produced thereby, and the award shall include, without limitation, just compensation to the unit owner of any unit partially taken for that portion of his undivided interest in the common elements divested from him by operation of the first sentence of this subsection and not revested in him by operation of the following sentence, as well as for that portion of his unit taken by eminent domain.

(d) If, however, the taking of a portion of any unit makes it impractical to use the remaining portion of that unit for any lawful purpose permitted by the condominium instruments, then the entire undivided interest in the common elements appertaining to that unit shall thenceforth appertain to the remaining units, being allocated to them in proportion to their respective undivided interests in the common elements, and the remaining portion of that unit shall thenceforth be a common element. The court shall enter a decree reflecting the reallocation of undivided interests produced thereby, and the award shall include, without limitation, just compensation to the unit owner of such unit for his entire undivided interest in the common elements and for his entire unit.

(e) Votes in the unit owners' association, rights to future common profits, and liabilities for future common expenses not specially assessed, appertaining to any unit or units taken or partially taken by eminent domain, shall thenceforth appertain to the remaining units, being allocated to them in proportion to their relative voting strength in the unit owners' association, with any units partially taken participating in such reallocation as though their voting strength in the unit owners' association had been reduced in proportion to the reduction in their undivided interests in the common elements, and the decree of the court shall provide accordingly.

(f) The decree of the court shall require the recordation thereof among the land records of the city or county in which the condominium is located. (1974, c. 416; 1975, c. 415.)

ARTICLE 2.

Creation, Alteration and Termination of Condominiums.

§ 55-79.45. How condominium may be created.—No condominium shall come into existence except by the recordation of condominium instruments pursuant to the provisions of this chapter. No condominium instruments shall be recorded unless all units located or to be located on any portion of the submitted land, other than within the boundaries of any convertible lands, are depicted on plats and plans that comply with the provisions of § 55-79.58 (a) and (b). The foreclosure of any mortgage, deed of trust, or other lien shall not be deemed, ex proprio vigore, to terminate the condominium. (1974, c. 416.)

§ 55-79.46. Release of liens.—(a) At the time of the conveyance to the first purchaser of each condominium unit following the recordation of the declaration, every mortgage, deed of trust, any other perfected lien, or any mechanics' or materialmen's liens, affecting all of the condominium or a

greater portion thereof than the condominium unit conveyed, shall be paid and satisfied of record, or the declarant shall forthwith have the said condominium unit released of record from all such liens not so paid and satisfied. The provisions of this subsection shall not apply, however, to any withdrawable land in a contractable condominium, nor shall any provision of this subsection be construed to prohibit the unit owners' association from mortgaging or causing a deed of trust to be placed on any portion of the condominium within which no units are located, so long as any time limit specified pursuant to § 55-79.74 has expired, and so long as the bylaws authorize the same.

(b) In the event that any lien, other than a deed of trust or mortgage, becomes effective against two or more condominium units subsequent to the creation of the condominium, any unit owner may remove his condominium unit from that lien by payment of the amount attributable to his condominium unit. Such amount shall be computed by reference to the liability for common expenses appertaining to that condominium unit pursuant to § 55-79.83 (c). Subsequent to such payment, discharge or other satisfaction, the unit owner of that condominium unit shall be entitled to have that lien released as to his condominium unit in accordance with the provisions of § 55-66.4, and the unit owners' association shall not assess, or have a valid lien against, that condominium unit for any portion of the common expenses incurred in connection with that lien, notwithstandng anything to the contrary in §§ 55-79.83 and 55-79.84. (1974, c. 416.)

§ 55-79.47. **Description of condominium units.**—After the creation of the condominium, no description of a condominium unit shall be deemed vague, uncertain, or otherwise insufficient or infirm which sets forth the identifying number of that unit, the name of the condominium, the name of the city or county wherein the condominium is situated, and either the deed book and page number where the first page of the declaration is recorded or else the document number assigned to the declaration by the clerk. Any such description shall be deemed to include the undivided interest in the common elements appertaining to such unit even if such interest is not defined or referred to therein. (1974, c. 416; 1975, c. 415.)

§ 55-79.48. **Execution of condominium instruments.**—The declaration and bylaws, and any amendments to either made pursuant to § 55-79.71 shall be duly executed by or on behalf of all of the owners and lessees of the submitted land. But the phrase "owners and lessees" in the preceding sentence and in § 55-79.63 does not include, in their capacity as such, any mortgagee, any trustee or beneficiary under a deed of trust, any other lien holder, any person having an inchoate dower or curtesy interest, any person having an equitable interest under any contract for the sale and/or lease of a condominium unit, or any lessee whose leasehold interest does not extend to any portion of the common elements. (1974, c. 416.)

§ 55-79.49. **Recordation of condominium instruments.**—All amendments and certifications of condominium instruments shall set forth the name of the city or county in which the condominium is located, and the deed book and page number where the first page of the declaration is recorded. All condominium instruments, and all amendments and certifications thereof, shall be recorded in every city and county wherein any portion of the con-

dominium is located, and shall set forth the name and address of the condominium. Wherever the phrase "city or county" appears in this chapter, the disjunctive shall be deemed to include the conjunctive and the singular shall be deemed to include the plural. (1974, c. 416; 1975, c. 415.)

§ 55-79.50. **Construction of condominium instruments.**—Except to the extent otherwise provided by the condominium instruments:

(a) The terms defined in § 55-79.41 shall be deemed to have the meanings therein specified wherever they appear in the condominium instruments unless the context otherwise requires.

(b) To the extent that walls, floors, and/or ceilings are designated as the boundaries of the units or of any specified units, all doors and windows therein, and all lath, wallboard, plasterboard, plaster, paneling, tiles, wallpaper, paint, finished flooring, and any other materials constituting any part of the finished surfaces thereof, shall be deemed a part of such units, while all other portions of such walls, floors, and/or ceilings shall be deemed a part of the common elements.

(c) If the chutes, flues, ducts, conduits, wires, bearing walls, bearing columns, or any other apparatus lies partially within and partially outside of the designated boundaries of a unit, any portions thereof serving only that unit shall be deemed a part of that unit, while any portions thereof serving more than one unit or any portion of the common elements shall be deemed a part of the common elements.

(d) Subject to the provisions of subsection (c) hereof, all space, interior partitions, and other fixtures and improvements within the boundaries of a unit shall be deemed a part of that unit.

(e) Any shutters, awnings, window boxes, doorsteps, porches, balconies, patios, and any other apparatus designed to serve a single unit but located outside the boundaries thereof, shall be deemed a limited common element appertaining to that unit exclusively. (1974, c. 416.)

§ 55-79.51. **Complementarity of condominium instruments; controlling construction.**—The condominium instruments shall be construed together and shall be deemed to incorporate one another to the extent that any requirement of this chapter as to the content of one shall be deemed satisfied if the deficiency can be cured by reference to any of the others. In the event of any conflict between the condominium instruments, the declaration shall control; but particular provisions shall control more general provisions, except that a construction conformable with the statute shall in all cases control over any construction inconsistent therewith. (1974, c. 416; 1975, c. 415.)

§ 55-79.52. **Validity of condominium instruments; discrimination prohibited.**—(a) All provisions of the condominium instruments shall be deemed severable, and any unlawful provision thereof shall be void.

(b) No provision of the condominium instruments shall be deemed void by reason of the rule against perpetuities.

(c) No restraint on alienation shall discriminate or be used to discriminate on the basis of religious conviction, race, color, sex, or national origin.

(d) Subject to the provisions of subsection (c) hereof, the rule of property law known as the rule restricting unreasonable restraints on alienation shall not be applied to defeat any provision of the condominium instruments

restraining the alienation of condominium units other than such units as may be restricted to residential use only. (1974, c. 416; 1975, c. 415).

§ 55-79.53. **Compliance with condominium instruments.**—The declarant, every unit owner, and all those entitled to occupy a unit shall comply with all lawful provisions of this chapter and all provisions of the condominium instruments. Any lack of such compliance shall be grounds for an action or suit to recover sums due, for damages or injunctive relief, or for any other remedy available at law or in equity, maintainable by the unit owners' association, or by its executive organ or any managing agent on behalf of such association, or, in any proper case, by one or more aggrieved unit owners on their own behalf or as a class action. (1974, c. 416; 1975, c. 415.)

§ 55-79.54. **Contents of declaration.**—(a) The declaration for every condominium shall contain the following:

(1) The name of the condominium, which name shall include the word "condominium" or be followed by the words "a condominium".

(2) The name of the city or county in which the condominium is located.

(3) A legal description by metes and bounds of the land submitted to this chapter.

(4) A description or delineation of the boundaries of the units, including the horizontal (upper and lower) boundaries, if any, as well as the vertical (lateral or perimetric) boundaries.

(5) A description or delineation of the limited common elements, if any, showing or designating the unit or units to which each is assigned.

(6) A description or delineation of all common elements not within the boundaries of any convertible lands which may subsequently be assigned as limited common elements, together with a statement that they may be so assigned and a description of the method whereby any such assignments shall be made in accordance with the provisions of § 55-79.57.

(7) The allocation to each unit of an undivided interest in the common elements in accordance with the provisions of § 55-79.55.

(8) Such other matters as the declarant deems appropriate.

(b) If the condominium contains any convertible land the declaration shall also contain the following:

(1) A legal description by metes and bounds of each convertible land within the condominium.

(2) A statement of the maximum number of units that may be created within each such convertible land.

(3) A statement, with respect to each such convertible land, of the maximum percentage of the aggregate land and floor area of all units that may be created therein that may be occupied by units not restricted exclusively to residential use.

(4) A statement of the extent to which any structure erected on any convertible land will be compatible with structures on other portions of the submitted land in terms of quality of construction, the principal materials to be used and architectural style.

(5) A description of all other improvements that may be made on each convertible land within the condominium.

(6) A statement that any units created within each convertible land will be substantially identical to the units on other portions of the submitted

land, or a statement describing in detail what other types of units may be created therein.

(7) A description of the declarant's reserved right, if any, to create limited common elements within any convertible land, and/or to designate common elements therein which may subsequently be assigned as limited common elements, in terms of the types, sizes, and maximum number of such elements within each such convertible land.

Provided, that plats and plans may be recorded with the declaration and identified therein to supplement information furnished pursuant to items (1), (4), (5), (6) and (7) of this subsection, and that item (3) of this subsection need not be complied with if none of the units on other portions of the submitted land are restricted exclusively to residential use.

(c) If the condominium is an expandable condominium the declaration shall also contain the following:

(1) The explicit reservation of an option to expand the condominium.

(2) A statement of any limitations on that option, including, without limitation, a statement as to whether the consent of any unit owners shall be required, and if so, a statement as to the method whereby such consent shall be ascertained; or a statement that there are no such limitations.

(3) A time limit, not exceeding seven years from the recording of the declaration, upon which the option to expand the condominium shall expire, together with a statement of the circumstances, if any, which will terminate that option prior to the expiration of the time limit so specified.

(4) A legal descripion by metes and bounds of all land that may be added to the condominium, henceforth referred to as "additional land."

(5) A statement as to whether, if any of the additional land is added to the condominium, all of it or any particular portion of it must be added, and if not, a statement of any limitations as to what portions may be added or a statement that there are no such limitations.

(6) A satement as to whether portions of the additional land may be added to the condominium at different times, together with any limitations fixing the boundaries of those portions by legal descriptions setting forth the metes and bounds thereof and/or regulating the order in which they may be added to the condominium.

(7) A statement of any limitations as to the locations of any improvements that may be made on any portions of the additional land added to the condominium, or a statement that no assurances are made in that regard.

(8) A statement of the maximum number of units that may be created on the additional land. If portions of the additional land may be added to the condominium and the boundaries of those portions are fixed in accordance with item (6) of this subsection, the declaration shall also state the maximum number of units that may be created on each such portion added to the condominium. If portions of the additional land may be added to the condominium and the boundaries of those portions are not fixed in accordance with item (6) of this subsection, then the declaration shall also state the maximum number of units per acre that may be created on any such portion added to the condominium.

(9) A statement, with respect to the additional land and to any portion or portions thereof that may be added to the condominium, of the maximum percentage of the aggregate land and floor area of all units that may be

created thereon that may be occupied by units not restricted exclusively to residential use.

(10) A statement of the extent to which any structures erected on any portion of the additional land added to the condominium will be compatible with structures on the submitted land in terms of quality of construction, the principal materials to be used, and architectural style, or a statement that no assurances are made in those regards.

(11) A description of all other improvements that will be made on any portion of the additional land added to the condominium, or a statement of any limitations as to what other improvements may be made thereon, or a statement that no assurances are made in that regard.

(12) A statement that any units created on any portion of the additional land added to the condominium will be substantially identical to the units on the submitted land, or a statement of any limitations as to what types of units may be created thereon, or a statement that no assurances are made in that regard.

(13) A description of the declarant's reserved right, if any, to create limited common elements within any portion of the additional land added to the condominium, and/or to designate common elements therein which may subsequently be assigned as limited common elements, in terms of the types, sizes, and maximum number of such elements within each such portion, or a statement that no assurances are made in those regards.

Provided, that plats and plans may be recorded with the declaration and identified therein to supplement information furnished pursuant to items (4), (5), (6), (7), (10), (11), (12) and (13) of this subsection, and that item (9) of this subsection need not be complied with if none of the units on the submitted land is restricted exclusively to residential use.

(d) If the condominium is a contractable condominium the declaration shall also contain the following:

(1) The explicit reservation of an option to contract the condominium.

(2) A statement of any limitations on that option, including, without limitation, a statement as to whether the consent of any unit owners shall be required, and if so, a statement as to the method whereby such consent shall be ascertained; or a statement that there are no such limitations.

(3) A time limit, not exceeding seven years from the recording of the declaration, upon which the option to contract the condominium shall expire, together with a statement of the circumstances, if any, which will terminate that option prior to the expiration of the time limit so specified.

(4) A legal description by metes and bounds of all land that may be withdrawn from the condominium, henceforth referred to as "withdrawable land."

(5) A statement as to whether portions of the withdrawable land may be withdrawn from the condominium at different times, together with any limitations fixing the boundaries of those portions by legal descriptions setting forth the metes and bounds thereof and/or regulating the order in which they may be withdrawn from the condominium.

(6) A legal description by metes and bounds of all of the submitted land to which the option to contract the condominium does not extend.

Provided, that plats may be recorded with the declaration and identified therein to supplement information furnished pursuant to items (4), (5) and (6) of this subsection, and that item (6) of this subsection shall not

be construed in derogation of any right the declarant may have to terminate the condominium in accordance with the provisions of § 55-79.71.

(e) If the condominium is a leasehold condominium, then with respect to any ground lease or other leases the expiration or termination of which will or may terminate or contract the condominium, the declaration shall set forth the city or county wherein the same are recorded and the deed book and page number where the first page of each such lease is recorded; and the declaration shall also contain the following:

(1) The date upon which each such lease is due to expire.

(2) A statement as to whether any land and/or improvements will be owned by the unit owners in fee simple, and if so, either (a) a description of the same, including without limitation a legal description by metes and bounds of any such land, or (b) a statement of any rights the unit owners shall have to remove such improvements within a reasonable time after the expiration or termination of the lease or leases involved, a statement that they shall have no such rights.

(3) A statement of the rights the unit owners shall have to redeem the reversion or any of the reversions, or a statement that they shall have no such rights.

Provided, that after the recording of the declaration, no lessor who executed the same, and no successor in interest to such lessor, shall have any right or power to terminate any part of the leasehold interest of any unit owner who makes timely payment of his share of the rent to the person or persons designated in the declaration for the receipt of such rent and who otherwise complies with all covenants which, if violated, would entitle the lessor to terminate the lease. Acquisition or reacquisition of such a leasehold interest by the owner of the revision or remainder shall not cause a merger of the leasehold and fee simple interests unless all leasehold interests in the condominium are thus acquired or reacquired.

(f) Wherever this section requires a legal description by metes and bounds of land that is submitted to this chapter or that may be added to or withdrawn from the condominium, such requirement shall be deemed satisfied by any legally sufficient description and shall be deemed to require a legally sufficient description of any easements that are submitted to this chapter or that may be added to or withdrawn from the condominium, as the case may be. In the case of each such easement, the declaration shall contain the following:

(1) A description of the permitted use or uses.

(2) If less than all of those entitled to the use of all of the units may utilize such easement, a statement of the relevant restrictions and limitations on utilization.

(3) If any persons other than those entitled to the use of the units may utilize such easement, a statement of the rights of others to utilization of the same.

(g) Wherever this section requires a legal description by metes and bounds of land that is submitted to this chapter or that may be added to or withdrawn from the condominium, an added requirement shall be a separate legally sufficient description of all lands in which the unit owners shall or may be tenants in common or joint tenants with any other persons, and a separate legally sufficient description of all lands in which the unit owners shall or may be life tenants. No units shall be situated on any such

lands, however, and the declaration shall describe the nature of the unit owners' estate therein. No such lands shall be shown on the same plat or plats showing other portions of the condominium, but shall be shown instead on separate plats. (1974, c. 416; 1975, c. 415.)

§ 55-79.55. Allocation of interests in the common elements.—(a) The declaration may allocate to each unit depicted on plats and plans that comply with § 55-79.58 (a) and (b) an undivided interest in the common elements proportionate to either the size or par value of each unit.

(b) Otherwise, the declaration shall allocate to each such unit an equal undivided interest in the common elements, subject to the following exception: each convertible space so depicted shall be allocated an undivided interest in the common elements proportionate to the size of each such space, vis-a-vis the aggregate size of all units so depicted, while the remaining undivided interest in the common elements shall be allocated equally to the other units so depicted.

(c) The undivided interests in the common elements allocated in accordance with subsection (a) or (b) hereof shall add up to one if stated as fractions or one hundred per centum if stated as percentages.

(d) If, in accordance with subsection (a) or (b) hereof, an equal undivided interest in the common elements is allocated to each unit, the declaration may simply state that fact and need not express the fraction or percentage so allocated.

(e) Otherwise, the undivided interest allocated to each unit in accordance with subsection (a) or (b) hereof shall be reflected by a table in the declaration, or by an exhibit or schedule accompanying the declaration and recorded simultaneously therewith, containing three columns. The first column shall identify the units, listing them serially or grouping them together in the case of units to which identical undivided interests are allocated. Corresponding figures in the second and third columns shall set forth the respective areas of par values of those units and the fraction or percentage of undivided interest in the common elements allocated thereto.

(f) Except to the extent otherwise expressly provided by this chapter, the undivided interest in the common elements allocated to any unit shall not be altered, and any purported transfer, encumbrance, or other disposition of that interest without the unit to which it appertains shall be void.

(g) The common elements shall not be subject to any suit for partition until and unless the condominium is terminated. (1974, c. 416.)

§ 55-79.56. Reallocation of interests in common elements.—(a) If a condominium contains any convertible land or is an expandable condominium, then the declaration shall not allocate undivided interests in the common elements on the basis of par value unless the declaration:

(1) Prohibits the creation of any units not substantially identical to the units depicted on the plats and plans recorded pursuant to § 55-79.58 (a) and (b), or

(2) Prohibits the creation of any units not described pursuant to § 55-79.54 (b) (6) (in the case of convertible lands) and § 55-79.54 (c) (12) (in the case of additional land), and contains from the outset a statement of the par value that shall be assigned to every such unit that may be created.

(b) Interests in the common elements shall not be allocated to any units

to be created within any convertible land or within any additional land until plats and plans depicting the same are recorded pursuant to § 55-79.58 (c). But simultaneously with the recording of such plats and plans the declarant shall execute and record an amendment to the declaration reallocating undivided interests in the common elements so that the units depicted on such plats and plans shall be allocated undivided interests in the common elements on the same basis as the units depicted on the plats and plans recorded simultaneously with the declaration pursuant to § 55-79.58 (a) and (b).

(c) If all of a convertible space is converted into common elements, including without limitation limited common elements, then the undivided interest in the common elements appertaining to such space shall thenceforth appertain to the remaining units, being allocated among them in proportion to their undivided interests in the common elements. The principal officer of the unit owners' association, or such other officer or officers as the condominium instruments may specify, shall forthwith prepare, execute, and record an amendment to the declaration reflecting the reallocation of undivided interests produced thereby.

(d) In the case of a leasehold condominium, if the expiration or termination of any lease causes a contraction of the condominium which reduces the number of units, then the undivided interest in the common elements appertaining to any units thereby withdrawn from the condominium shall thenceforth appertain to the remaining units, being allocated among them in proportion to their undivided interests in the common elements. The principal officer of the unit owners' association, or such other officer or officers as the condominium instruments may specify, shall forthwith prepare, execute, and record an amendment to the declaration reflecting the reallocation of undivided interests produced thereby. (1974, c. 416.)

§ 55-79.57. Assignments of limited common elements.—(a) All assignments and reassignments of limited common elements shall be reffected by the condominium instruments. No limited common element shall be assigned or reassigned except in accordance with the provisions of this chapter. No amendment to any condominium instrument shall alter any rights or obligations with respect to any limited common elements without the consent of all unit owners adversely affected thereby as evidenced by their execution of such amendment, except to the extent that the condominium instruments expressly provided otherwise prior to the first assignment of that limited common element.

(b) Unless expressly prohibited by the condominium instruments, a limited common element may be reassigned upon written application of the unit owners concerned to the principal officer of the unit owners' association, or to such other officer or officers as the condominium instruments may specify. The officer or officers to whom such application is duly made shall forthwith prepare and execute an amendment to the declaration reassigning all rights and obligations with respect to the limited common element involved. Such amendment shall be delivered forthwith to the unit owners of the units concerned upon payment by them of all reasonable costs for the preparation and acknowledgment thereof. Said amendment shall become effective when the unit owners of the units concerned have executed and recorded it.

(c) A common element not previously assigned as a limited common element shall be so assigned only in pursuance of § 55-79.54 (a) (6). The amendment to the declaration making such an assignment shall be prepared and executed by the principal officer of the unit owners' association, or by such other officer or officers as the condominium instruments may specify. Such amendment shall be delivered to the unit owner or owners of the unit or units concerned upon payment by them of all reasonable costs for the preparation and acknowledgment thereof. Said amendment shall become effective when the aforesaid unit owner or owners have executed and recorded it, and the recordation thereof shall be conclusive evidence that the method prescribed pursuant to § 55-79.54 (a) (6) was adhered to. (1974, c. 416.)

§ 55-79.58. **Contents of plats and plans.**—(a) There shall be recorded simultaneously with the declaration one or more plats of survey showing the location and dimensions of the submitted land, the location and dimensions of any convertible lands within the submitted land, the location and dimensions of any existing improvements, the intended location and dimensions of any contemplated improvements which are to be located on any portion of the submitted land other than within the boundaries of any convertible lands, and, to the extent feasible, the location and dimensions of all easements appurtenant to the submitted land or otherwise submitted to this chapter as a part of the common elements. If the submitted land is not contiguous, then the plats shall indicate the distances between the parcels constituting the submitted land. The plats shall label every convertible land as a convertible land, and if there be more than one such land the plats shall label each such land with one or more letters and/or numbers different from those designating any other convertible land and different also from the identifying number of any unit. The plats shall show the location and dimensions of any withdrawable lands, and shall label each such land as a withdrawable land. If, with respect to any portion or portions, but less than all, of the submitted land, the unit owners are to own only an estate for years, the plats shall show the location and dimensions of any such portions, and shall label each such portion as a leased land. If there is more than one withdrawable land, or more than one leased land, the plats shall label each such land with one or more letters and/or numbers different from those designating any convertible land or other withdrawable or leased land, and different also from the identifying number of any unit. The plats shall show all easements to which the submitted land or any portion thereof is subject, and shall show the location and dimensions of all such easements to the extent feasible. The plats shall also show all encroachments by or on any portion of the condominium. In the case of any improvements located or to be located on any portion of the submitted land other than within the boundaries of any convertible lands, the plats shall indicate which, if any, have not been begun by the using of the phrase "(NOT YET BEGUN)," and which, if any, have been begun but have not been substantially completed by the use of the phrase "(NOT YET COMPLETED)." In the case of any units the verticle boundaries of which lie wholly or partially outside of structures for which plans pursuant to subsection (b) hereof are simultaneously recorded the plats shall show the location and dimensions of such vertical boundaries to the extent that

they are not shown on such plans, and the units or portions thereof thus depicted shall bear their identifying numbers. Each plat shall be certified as to its accuracy and compliance with the provisions of this subsection by a registered land surveyor, and the said surveyor shall certify that all units or portions thereof depicted thereon pursuant to the preceding sentence of this subsection have been substantially completed. The specification within this subsection of items that shall be shown on the plats shall not be construed to mean that the plats shall not also show all other items customarily shown or hereafter required for land title surveys.

(b) There shall also be recorded, simultaneously with the declaration, plans of every structure which contains or constitutes all or part of any unit or units, and which is located on any portion of the submitted land other than within the boundaries of any convertible lands. The plans shall show the location and dimensions of the vertical boundaries of each unit to the extent that such boundaries lie within or coincide with the boundaries of such structures, and the units or portions thereof thus depicted shall bear their identifying numbers. In addition, each convertible space thus depicted shall be labelled a convertible space. The horizontal boundaries of each unit having horizontal boundaries shall be identified on the plans with reference to establish datum. Unless the condominium instruments expressly provide otherwise, it shall be presumed that in the case of any unit not wholly contained within or constituting one or more such structures, the horizontal boundaries thus identified extend, in the case of each such unit, at the same elevation with regard to any part of such unit, lying outside of such structures, subject to the following exception: In the case of any such unit which does not lie over any other unit other than basement units, it shall be presumed that the lower horizontal boundary, if any, of that unit lies at the level of the ground with regard to any part of the unit lying outside of such structures. The plans shall be certified as to their accuracy and compliance with the provisions of this subsection by a registered architect or registered engineer, and the said architect or engineer shall certify that all units or portions thereof depicted thereon have been substantially completed.

(c) When converting all or any portion of any convertible land, or adding additional land to an expandable condominium, the declarant shall record new plats of survey conforming to the requirements of subsection (a) hereof. (In any case where less than all of a convertible land is being converted, such plats shall show the location and dimensions of the remaining portion or portions of such land in addition to otherwise conforming with the requirements of subsection (a) hereof.) At the same time, the declarant shall record, with regard to any structures on the land being converted, or added, either plans conforming to the requirements of subsection (b) hereof, or certifications, conforming to the certification requirements of said subsection, of plans previously recorded pursuant to § 55-79.59.

(d) When converting all or any portion of any convertible space into one or more units and/or limited common elements, the declarant shall record, with regard to the structure or portion thereof constituting that convertible space, plans showing the location and dimensions of the vertical boundaries of each unit and/or limited common elements formed out of such space. Such plans shall be certified as to their accuracy and compliance with the

provisions of this subsection by a registered architect or registered engineer.

(e) For the purposes of subsections (a), (b), and (c) hereof, all provisions and requirements relating to units shall be deemed equally applicable to limited common elements. The limited common elements shall be labeled as such, and each limited common element depicted on the plats and plans shall bear the identifying number or numbers of the unit or units to which it is assigned, if it has been assigned, unless the provisions of § 55-79.50 (e) make such designations unnecessary. (1974, c. 416; 1975, c. 415.)

§ 55-79.59. Preliminary recordation of plans.—Plans previously recorded pursuant to the provisos set forth in § 55-79.54 (b) and (c) may be used in lieu of new plans to satisfy in whole or in part the requirements of § 55-79.56 (b), § 55-79.61 (b) and/or § 55-79.63 if certifications thereof are recorded by the declarant in accordance with § 55-79.58 (b); and if such certifications are recorded, the plans which they certify shall be deemed recorded pursuant to § 55-79.58 (c) within the meaning of the three sections aforesaid. (1974, c. 416.)

§ 55-79.60. Easement for encroachments.—To the extent that any unit or common element encroaches on any other unit or common element, whether by reason of any deviation from the plats and plans in the construction, repair, renovation, restoration, or replacement of any improvement, or by reason of the settling or shifting of any land or improvement, a valid easement for such encroachment shall exist. The purpose of this section is to protect the unit owners, except in cases of willful and intentional misconduct by them or their agents or employees, and not to relieve the declarant or any contractor, subcontractor, or materialman of any liability which any of them may have by reason of any failure to adhere strictly to the plats and plans. (1974, c. 416.)

§ 55-79.61. Conversion of convertible lands.—(a) The declarant may convert all or any portion of any convertible land into one or more units and/or limited common elements subject to any restrictions and limitations which the condominium instruments may specify. Any such conversion shall be deemed to have occurred at the time of the recordation of appropriate instruments pursuant to subsection (b) hereof and § 55-79.58 (c).

(b) Simultaneously with the recording of plats and plans pursuant to § 55-79.58 (c), the declarant shall prepare, execute, and record an amendment to the declaration describing the conversion. Such amendment shall assign an identifying number to each unit formed out of a convertible land and shall reallocate undivided interests in the common elements in accordance with § 55-79.56 (b). Such amendment shall describe or delineate the limited common elements formed out of the convertible land, showing or designating the unit or units to which each is assigned.

(c) All convertible lands shall be deemed a part of the common elements except for such portions thereof as are converted in accordance with the provisions of this section. Until the expiration of the period during which conversion may occur or until actual conversion, whichever occurs first, real estate taxes shall be assessed against the declarant rather than the unit owners as to both the convertible land and any improvements thereon. No such conversion shall occur after five years from the recordation of the

declaration, or such shorter period of time period as the declaration may specify. (1974, c. 416; 1975, c. 415.)

§ 55-79.62. **Conversion of convertible spaces.**—(a) The declarant may convert all of any portion of any convertible space into one or more units and/or common elements, including, without limitation, limited common elements, subject to any restrictions and limitations which the condominium instruments may specify. Any such conversion shall be deemed to have occurred at the time of the recordation of appropriate instruments pursuant to subsection (b) hereof and § 55-79.58 (d).

(b) Simultaneously with the recording of plats and plans pursuant to § 55-79.58 (d), the declarant shall prepare, execute, and record an amendment to the declaration describing the conversion. Such amendment shall assign an identifying number to each unit formed out of a convertible space and shall allocate to each unit a portion of the undivided interest in the common elements appertaining to that space. Such amendment shall describe or delineate the limited common elements formed out of the convertible space, showing or designating the unit or units to which each is assigned.

(c) If all or any portion of any convertible space is converted into one or more units in accordance with this section, the declarant shall prepare and execute, and record simultaneously with the amendment to the declaration, an amendment to the bylaws. The amendment to the bylaws shall reallocate votes in the unit owners' association, rights to future common profits, and liabilities for future common expenses not specially assessed, all as in the case of the subdivision of a unit in accordance with § 55-79.70 (d).

(d) Any convertible space not converted in accordance with the provisions of this section, or any portion or portions thereof not so converted, shall be treated for all purposes as a single unit until and unless it is so converted, and the provisions of this chapter shall be deemed applicable to any such space, or portion or portions thereof, as though the same were a unit. (1974, c. 416.)

§ 55-79.63. **Expansion of condominium.**—No condominium shall be expanded except in accordance with the provisions of the declaration and of this chapter. Any such expansion shall be deemed to have occurred at the time of the recordation of plats and plans pursuant to § 55-79.58 (c), together with an amendment to the declaration, duly executed by the declarant, including, without limitation, all of the owners and lessees of the additional land added to the condominium. Such amendment shall contain a legal description by metes and bounds of the land added to the condominium, and shall reallocate undivided interests in the common elements in accordance with the provisions of § 55-79.56 (b). Such amendment may create convertible or withdrawable lands or both within the land added to the condominium, but this provision shall not be construed in derogation of the time limits imposed by or pursuant to §§ 55-79.54 (d) (3) and 55-79.61 (c). (1974, c. 416; 1975, c. 415.)

§ 55-79.64. **Contraction of condominium.**—No condominium shall be contracted except in accordance with the provisions of the declaration and of this chapter. Any such contraction shall be deemed to have occurred at the time of the recordation of an amendment to the declaration, executed

by the declarant, containing a legal description by metes and bounds of the land withdrawn from the condominium. If portions of the withdrawable land were described pursuant to § 55-79.54 (d) (5), then no such portion shall be so withdrawn after the conveyance of any unit on such portion. If no such portions were described, then none of the withdrawable land shall be withdrawn after the first conveyance of any unit thereon. (1974, c. 416.)

§ 55-79.65. **Easement to facilitate conversion and expansion.**—Subject to any restrictions and limitations the condominium instruments may specify, the declarant shall have a transferable easement over and on the common elements for the purpose of making improvements on the submitted land and any additional land pursuant to the provisions of those instruments and of this chapter, and for the purpose of doing all things reasonably necessary and proper in connection therewith. (1974, c. 416.)

§ 55-79.66. **Easement to facilitate sales.**—The declarant and his duly authorized agents, representatives, and employees may maintain sales offices and/or model units on the submitted land if and only if the condominium instruments provide for the same and specify the rights of the declarant with regard to the number, size, location, and relocation thereof. Any such sales office or model unit which is not designated a unit by the condominium instruments shall become a common element as soon as the declarant ceases to be a unit owner, and the declarant shall cease to have any rights with regard thereto unless such sales office or model unit is removed forthwith from the submitted land in accordance with a right reserved in the condominium instruments to make such removal. (1974, c. 416.)

§ 55-79.67. **Declarant's obligation to complete and restore.**—(a) No covenants, restrictions, limitations, or other representations or commitments in the condominium instruments with regard to anything that is or is not to be done on the additional land, the withdrawable land, or any portion of either, shall be binding as to any portion of either lawfully withdrawn from the condominium or never added thereto except to the extent that the condominium instruments so provide. But in the case of any covenant, restriction, limitation, or other representation or commitment in the condominium instruments or in any other agreement requiring the declarant to add all or any portion of the additional land or to withdraw any portion of the withdrawable land, or imposing any obligations with regard to anything that is or is not to be done thereon or with regard thereto, or imposing any obligations with regard to anything that is or is not to be done on or with regard to the condominium or any portion thereof, this subsection shall not be construed to nullify, limit or otherwise affect any such obligation.

(a1) The declarant shall complete all improvements labeled "(NOT YET COMPLETED)" on plats recorded pursuant to the requirements of this chapter unless the condominium instruments expressly exempt the declarant from such obligation, and shall, in the case of every improvement labeled "(NOT YET BEGUN)" on such plats, state in the declaration either the extent of the obligation to complete the same or that there is no such obligation.

(b) To the extent that damage is inflicted on any part of the condomin-

ium by any person or persons utilizing the easements reserved by the condominium instruments or created by §§ 55-79.65 and 55-79.66, the declararant together with the person or persons causing the same shall be jointly and severally liable for the prompt repair thereof and for the restoration of the same to a condition compatible with the remainder of the condominium. (1974, c. 416; 1975, c. 415.)

§ 55-79.68. Alterations within units.—(a) Except to the extent prohibited by the condominium instruments, and subject to any restrictions and limitations specified therein, any unit owner may make any improvements or alterations within his unit that do not impair the structural integrity of any structure or otherwise lessen the support of any portion of the condominium. But no unit owner shall do anything which would change the exterior appearance of his unit or of any other portion of the condominium except to such extent and subject to such conditions as the condominium instruments may specify.

(b) If a unit owner acquires an adjoining unit, or an adjoining part of an adjoining unit, then such unit owner shall have the right to remove all or any part of any intervening partition or to create doorways or other apertures therein, notwithstanding the fact that such partition may in whole or in part be a common element, so long as no portion of any bearing wall or bearing column is weakened or removed and no portion of any common element other than that partition is damaged, destroyed, or endangered. Such creation of doorways or other apertures shall not be deemed an alteration of boundaries within the meaning of § 55-79.69. (1974, c. 416.)

§ 55-79.69. Relocation of boundaries between units.—(a) If the condominium instruments expressly permit the relocation of boundaries between adjoining units, then the boundaries between such units may be relocated in accordance with (1) the provisions of this section and (2) any restrictions and limitations not otherwise unlawful which the condominium instruments may specify. The boundaries between adjoining units shall not be relocated unless the condominium instruments expressly permit it.

(b) If the unit owners of adjoining units whose mutual boundaries may be relocated desire to relocate such boundaries, then the principal officer of the unit owners' association, or such other officer or officers as the condominium instruments may specify, shall, upon written application of such unit owners, forthwith prepare and execute appropriate instruments pursuant to subsections (c), (d) and (e) hereof.

(c) An amendment to the declaration shall identify the units involved and shall state that the boundaries between those units are being relocated by agreement of the unit owners thereof, which amendment shall contain conveyancing between those unit owners. If the unit owners of the units involved have specified in their written application a reasonable reallocation as between the units involved of the aggregate undivided interest in the common elements appertaining to those units, the amendment to the declaration shall reflect that reallocation.

(d) If the unit owners of the units involved have specified in their written application a reasonable reallocation as between the units involved of the aggregate number of votes in the unit owners' association allocated to

those units, an amendment to the bylaws shall reflect that reallocation and a proportionate reallocation of liability for common expenses and rights to common profits as between those units.

(e) Such plats and plans as may be necessary to show the altered boundaries between the units involved together with their other boundaries shall be prepared, and the units depicted thereon shall bear their identifying numbers. Such plats and plans shall indicate the new dimensions of the units involved, and any change in the horizontal boundaries of either as a result of the relocation of their boundaries shall be identified with reference to established datum. Such plats and plans shall be certified as to their accuracy and compliance with the provisions of this subsection (1) by a registered land surveyor in the case of any plat and (2) by a registered architect or registered engineer in the case of any plan.

(f) When appropriate instruments in accordance with the preceding subsections hereof have been prepared, executed, and acknowledged, they shall be delivered forthwith to the unit owners of the units involved upon payment by them of all reasonable costs for the preparation and acknowledgment thereof. Said instruments shall become effective when the unit owners of the units involved have executed and recorded them, and the recordation thereof shall be conclusive evidence that the relocation of boundaries thus effectuated did not violate any restrictions or limitations specified by the condominium instruments and that any reallocations made pursuant to subsections (c) and (d) hereof were reasonable.

(g) Any relocation of boundaries between adjoining units shall be governed by this section and not by § 55-79.70. Section 55-79.70 shall apply only to such subdivisions of units as are intended to result in the creation of two or more new units in place of the subdivided unit. (1974, c. 416.)

§ 55-79.70. Subdivision of units.—(a) If the condominium instruments expressly permit the subdivision of any units, then such units may be subdivided in accordance with (1) the provisions of this section and (2) any restrictions and limitations not otherwise unlawful which the condominium instruments may specify. No unit shall be subdivided unless the condominium instruments expressly permit it.

(b) If the unit owner of any unit which may be subdivided desires to subdivide such unit, then the principal officer of the unit owners' association, or such other officer or officers as the condominium instruments may specify, shall, upon written application of the subdivider, as such unit owner shall henceforth be referred to in this section, forthwith prepare and execute appropriate instruments pursuant to subsections (c), (d) and (e) hereof.

(c) An amendment to the declaration shall assign new identifying numbers to the new units created by the subdivision of a unit and shall allocate to those units, on a reasonable basis acceptable to the subdivider, all of the undivided interest in the common elements appertaining to the subdivided unit. The new units shall jointly share all rights, and shall be equally liable jointly and severally for all obligations, with regard to any limited common elements assigned to the subdivided unit except to the extent that the subdivider may have specified in his written application that all or any portions of any limited common element assigned to the subdivided unit exclusively should be assigned to one or more, but less than all of the new

units, in which case the amendment to the declaration shall reflect the desires of the subdivider as expressed in such written application.

(d) An amendment to the bylaws shall allocate to the new units, on a reasonable basis acceptable to the subdivider, the votes in the unit owners' association allocated to the subdivided unit, and shall reflect a proportionate allocation to the new units of the liability for common expenses and rights to common profits formerly appertaining to the subdivided unit.

(e) Such plats and plans as may be necessary to show the boundaries separating the new units together with their other boundaries shall be prepared, and the new units depicted thereon shall bear their new identifying numbers. Such plats and plans shall indicate the dimensions of the new units, and the horizontal boundaries thereof, if any, shall be identified thereon with reference to establish datum. Such plats and plans shall be certified as to their accuracy and compliance with the provisions of this subsection (1) by a registered land surveyor in the case of any plat and (2) by a registered architect or registered engineer in the case of any plan.

(f) When appropriate instruments in accordance with the preceding subsections hereof have been prepared, executed, and acknowledged, they shall be delivered forthwith to the subdivider upon payment by the subdivider of all reasonable costs for the preparation and acknowledgment thereof. Said instruments shall become effective when the subdivider has executed and recorded them, and the recordation thereof shall be conclusive evidence that the subdivision thus effectuated did not violate any restrictions or limitations specified by the condominium instruments and that any reallocations made pursuant to subsections (c) and (d) hereof were reasonable.

(g) Notwithstanding the provisions of §§ 55-79.41 (y) and 55-79.62 (d), this section shall have no application to convertible spaces, and no such space shall be deemed a unit for the purposes of this section. However, this section shall apply to any units formed by the conversion of all or any portion of any such space, and any such unit shall be deemed a unit for the purposes of this section. (1974, c. 416.)

§ 55-79.71. Termination of condominium or amendment of instruments before conveyance of any unit.—If there is no unit owner other than the declarant, the declarant may unilaterally terminate the condominium or amend the condominium instruments, and any such termination or amendment shall become effective upon the recordation thereof if the same has been executed by the declarant. But this section shall not be construed to nullify, limit, or otherwise affect the validity of enforceability of any agreement renouncing or to renounce, in whole or in part, the right hereby conferred. (1974, c. 416.)

§ 55-79.72. Termination of condominium or amendment of instruments after conveyance of any unit.—(a) If there is any unit owner other than the declarant, then the condominium shall be terminated only by the agreement of unit owners of units to which four fifths of the votes in the unit owners' association appertain, or such larger majority as the condominium instruments may specify.

(b) If there is any unit owner other than the declarant, then the condominium instruments shall be amended only by agreement of unit owners of units to which two thirds of the votes in the unit owners' association

appertain, or such larger majority as the condominium instruments may specify, execept in cases for which this chapter provides different methods of amendment.

(c) If none of the units in the condominium are restricted exclusively to residential use, then the condominium instruments may specify majorities smaller than the minimums specified by subsections (a) and (b) hereof.

(d) Agreement of the required majority of unit owners to termination of the condominium or to any amendment of the condominium instruments shall be evidenced by their execution of the termination agreement or amentment, or of ratifications thereof, and the same shall become effective only when such agreement is so evidenced of record. For the purposes of this section and § 55-79.71, an instrument terminating a condominium shall be deemed a condominium instrument subject to the provisions of § 55-79.49, and for the purposes of this section, any ratification of such an amendment shall also be deemed such an instrument.

(e) Except to the extent expressly permitted or expressly required by other provisions of this chapter, no amendment to the condominium instruments shall change the boundaries of any unit, the undivided interest in the common elements appertaining thereto, the liability for common expenses or rights to common profits appertaining thereto, or the number of votes in the unit owners' association appertaining thereto.

(f) Upon recordation of an instrument terminating a condominium, all of the property constituting the same shall be owned by the unit owners as tenants in common in proportion to their respective undivided interests in the common elements immediately prior to such recordation. But as long as such tenancy in common lasts, each unit owner or the heirs, successors, or assigns thereof shall have an exclusive right of occupancy of that portion of said property which formerly constituted his unit.

(g) Upon recordation of an instrument terminating a condominium, any rights the unit owners may have to the assets of the unit owners' association shall be in proportion to their respective undivided interests in the common elements immediately prior to such recordation, except that common profits shall be distributed in accordance with the provisions of § 55-79.82.

(h) No provision of this chapter shall be construed in derogation of any requirement of the condominium instruments that all or a specified number of the beneficiaries of mortgages or deeds of trust encumbering the condominium units approve specified actions contemplated by the unit owners' association. (1974, c. 416; 1975, c. 415.)

ARTICLE 3.

Management of Condominium.

§ 55-79.73. Bylaws to be recorded with declarations; contents; unit owners' association; executive organ; amendment of bylaws.—(a) There shall be recorded simultaneously with the declaration a set of bylaws providing for the self-government of the condominium by an association of all the unit owners. The unit owners' association may be incorporated.

(b) The bylaws shall provide whether or not the unit owners' association shall elect an executive organ. If there is to be such an organ, the by-

laws shall specify the powers and responsibilities of the same and the number and terms of its members. The bylaws may delegate to such organ, inter alia, any of the powers and responsibilities assigned by this chapter to the unit owners' association. The bylaws shall also specify which, if any, of its powers and responsibilities the unit owners' association or its executive organ may delegate to a managing agent.

(c) In any case where an amendment to the declaration is required by § 55-79.56 (b), (c) or (d), the person or persons required to execute the same shall also prepare and execute, and record simultaneously with such amendment, an amendment to the bylaws. The amendment to the bylaws shall allocate votes in the unit owners' association to new units on the same basis as was used for the allocation of such votes to the units depicted on plats and plans recorded pursuant to § 55-79.58 (a) and (b), or shall abolish the votes appertaining to former units, as the case may be. The amendment to the bylaws shall also reallocate rights to future common profits, and liabilities for future common expenses not specially assessed, in proportion to relative voting strengths as reflected by the said amendment. (1974, c. 416.)

§ 55-79.74. Control of condominium by declarant.—(a) The condominium instruments may authorize the declarant, or a managing agent or some other person or persons selected or to be selected by the declarant, to appoint and remove some or all of the officers of the unit owners' association and/or its executive organ, or to exercise powers and responsibilities otherwise assigned by the condominium instruments and by this chapter to the unit owners' association, the officers, or the executive organ. But no amendment to the condominium instruments shall increase the scope of such authorization if there is any unit owner other than the declarant, and no such authorization shall be valid after the time limit set by the condominium instruments or after units to which three fourths of the undivided interests in the common elements appertain have been conveyed, whichever occurs first. For the purposes of the preceding sentence only, the calculation of the fraction of undivided interest shall be based upon the total undivided interests assigned or to be assigned to all units registered with the Virginia Real Estate Commission pursuant to § 55-79.92 (b) hereof. The time limit initially set by the condominium instruments shall not exceed five years in the case of an expandable condominium, three years in the case of a condominium (other than an expandable condominium) containing any convertible land, or two years in the case of any other condominium. Such time period shall commence upon settlement of the first unit to be sold in any portion of the condominium.

(b) (1) If entered into any time prior to the expiration of the period of declarant control contemplated by subsection (a) hereof, no contract or lease entered into with the declarant or any entity controlled by the declarant, management contract, employment contract or lease of recreational or parking areas or facilities, which is directly or indirectly made by or on behalf of the unit owners' association, its executive organ, or the unit owners as a group, shall be entered into for a period in excess of two years. Any such contract or agreement may be renewed for periods not in excess of two years; however, at the end of any two-year period the unit owners' association or its executive organ may terminate any further renewals or

extensions thereof. The provisions of this subsection shall not apply to any lease or leases which are subject to § 55-79.54 (e).

(2) If entered into at any time prior to the expiration of the period of declarant control contemplated by subsection (a) hereof, any contract, lease or agreement, other than those subject to the provisions of subsection (b) (1) hereof, may be entered into by or on behalf of the unit owners' association, its executive organ, or the unit owners as a group, if such contract, lease or agreement is bona fide and is commercially reasonable to the unit owners' association at the time entered into under the circumstances.

(c) If the unit owners' association is not in existence or does not have officers at the time of the creation of the condominium, the declarant shall, until there is such an association with such officers, have the power and the responsibility to act in all instances where this chapter requires action by the unit owners' association, its executive organ, or any officer or officers.

(d) This section shall be strictly construed to protect the rights of the unit owners. (1974, c. 416; 1975, c. 415.)

§ 55-79.75. Meetings of unit owners' association; when held; notice.—Meetings of the unit owners' association shall be held in accordance with the provisions of the condominium instruments at least once each year after the formation of said association. The bylaws shall specify an officer who shall, at least twenty-one days in advance of any annual or regularly scheduled meeting, and at least seven days in advance of any other meeting, send to each unit owner notice of the time, place, and purpose or purposes of such meeting. Such notice shall be sent by United States mail, return receipt requested, to all unit owners of record at the address of their respective units and to such other addresses as any of them may have designated to such officer; or such notice may be hand delivered by the said officer, provided he obtains a receipt of acceptance of such notice from the unit owner. (1974, c. 416.)

§ 55-79.76. Same; quorums.—(a) Unless the condominium instruments otherwise provide, a quorum shall be deemed to be present throughout any meeting of the unit owners' association until adjourned if persons entitled to cast more than thirty-three and one third percent of the votes are present at the beginning of such meeting. The bylaws may provide for a larger percentage, or for a smaller percentage not less than twenty-five percent.

(b) Unless the condominium instruments specify a larger majority, a quorum shall be deemed to be present throughout any meeting of the executive organ if persons entitled to cast one half of the votes in that body are present at the beginning of such meeting. (1974, c. 416.)

§ 55-79.77. Same; voting.—(a) The bylaws may allocate to each unit depicted on plats and plans that comply with § 55-79.58 (a) and (b) a number of votes in the unit owners' association proportionate to the undivided interest in the common elements appertaining to each such unit.

(b) Otherwise, the bylaws shall allocate to each such unit an equal number of votes in the unit owners' association, subject to the following exception: Each convertible space so depicted shall be allocated a number of votes in the unit owners' association proportionate to the size of each such space, vis-a-vis the aggregate size of all units so depicted, while the re-

maining votes in the unit owners' association shall be allocated equally to the other units so depicted.

(c) Since a unit owner may be more than one person, if only one of such persons is present at a meeting of the unit owners' association, that person shall be entitled to cast the votes appertaining to that unit. But if more than one of such persons is present, the vote appertaining to that unit shall be cast only in accordance with their unanimous agreement unless the condominium instruments expressly provide otherwise, and such consent shall be conclusively presumed if any one of them purports to cast the votes appertaining to that unit without protest being made forthwith by any of the others to the person presiding over the meeting. Since a person need not be a natural person, the word "person" shall be deemed for the purposes of this subsection to include, without limitation, any natural person having authority to execute deeds on behalf of any person, excluding natural persons, which is, either alone or in conjunction with another person or persons, a unit owner.

(d) The votes appertaining to any unit may be cast pursuant to a proxy or proxies duly executed by or on behalf of the unit owner, or, in cases where the unit owner is more than one person, by or on behalf of all such persons. No such proxy shall be revocable except by actual notice to the person presiding over the meeting, by the unit owner or by any of such persons, that it be revoked. Any proxy shall be void if it is not dated, if it purports to be revocable without notice as aforesaid, or if the signatures of any of those executing the same has not been duly acknowledged. The proxy of any person shall be void if not signed by a person having authority, at the time of the execution thereof, to execute deeds on behalf of that person. Any proxy shall terminate automatically upon the adjournment of the first meeting held on or after the date of that proxy.

(e) If fifty percent or more of the votes in the unit owners' association appertain to twenty-five percent or less of the units, then in any case where a majority vote is required by the condominium instruments or by this chapter, the requirement for such a majority shall be deemed to include, in addition to the specified majority of the votes, assent by the unit owners of a like majority of the units.

(f) Anything in this section to the contrary notwithstanding, no votes in the unit owners' association shall be deemed to appertain to any condominium unit during such time as the unit owner thereof is the unit owners' association. (1974, c. 416.)

§ 55-79.78. **Officers.**—(a) If the condominium instruments provide that any officer or officers must be unit owners, then any such officer who disdisposes of all his units in fee and/or for a term or terms of six months or more shall be deemed to have disqualified himself from continuing in office unless the condominium instruments otherwise provide, or unless he acquires or contracts to acquire another unit in the condominium under terms giving him a right of occupancy thereto effective on or before the termination of his right of occupancy under such disposition or dispositions.

(b) If the condomininum instruments provide that any officer or officers must be unit owners, then notwithstanding the provisions of § 55-79.50 (a), the term "unit owner" in such context shall, unless the condominium instruments otherwise provide, be deemed to include, without limitation,

any director, officer, partner in, or trustee of any person which is, either alone or in conjunction with another person or persons, a unit owner. Any officer who would not be eligible to serve as such were he not a director, officer, partner in, or trustee of such a person, shall be deemed to have disqualified himself from continuing in office if he ceases to have any such affiliation with that person, or if that person would itself have been deemed to have disqualified itself from continuing in such office under subsection (a) hereof were it a natural person holding such office. (1974, c. 416.)

§ 55-79.79. Upkeep of condominiums; warranty against structural defects.—(a) Except to the extent otherwise provided by the condominium instruments, all powers and responsibilities with regard to maintenance, repair, renovation, restoration, and replacement of the condominium shall belong (1) to the unit owners' association in the case of the common elements, and (2) to the individual unit owner in the case of any unit or any part thereof. Each unit owner shall afford to the other unit owners and to the unit owners' association and to any agents or employees of either such access through his unit as may be reasonably necessary to enable them to exercise and discharge their respective powers and responsibilities. But to the extent that damage is inflicted on the common elements or any unit through which access is taken, the unit owner causing the same, or the unit owners' association if it caused the same, shall be liable for the prompt repair thereof.

(b) Notwithstanding anything in this section to the contrary, the declarant shall warrant or guarantee, against structural defects, each of the units for two years from the date each is conveyed, and all of the common elements for two years. The two years referred to in the preceding sentence shall begin as to each of the common elements whenever the same has been completed or, if later, (1) as to any common element within any additional land or portion thereof, at the time the first unit therein is conveyed, (2) as to any common element within any convertible land or portion thereof, at the time the first unit therein is conveyed, and (3) as to any common element within any other portion of the condominium at the time the first unit therein is conveyed. For the purposes of this subsection, no unit shall be deemed conveyed unless conveyed to a bona fide purchaser. For the purposes of this subsection, structural defects shall be those defects in components constituting any unit or common element which reduce the stability or safety of the structure below accepted standards or restrict the normal intended use of all or part of the structure and which require repair, renovation, restoration, or replacement. Nothing in this subsection shall be construed to make the declarant responsible for any items of maintenance relating to the units or common elements. (1974, c. 416; 1975, c. 415.)

§ 55-79.80. Control of common elements.—(a) Except to the extent prohibited by the condominium instruments, and subject to any restrictions and limitations specified therein, the unit owners' association shall have the power to:

(1) Employ, dismiss, and replace agents and employees to exercise and discharge the powers and responsibilities of the said association arising under § 55-79.79.

(2) Make or cause to be made additional improvements on and as a part of the common elements.

(3) Grant or withhold approval of any action by one or more unit owners or other persons entitled to the occupancy of any unit which would change the exterior appearance of any unit or of any other portion of the condominium, or elect or provide for the appointment of an architectural control committee, the members of which must have the same qualifications as officers, to grant or withhold such approval.

(4) Acquire, hold, convey, and encumber title to real property, including but not limited to condominium units, whether or not the association is incorporated.

(b) Except to the extent prohibited by the condominium instruments, and subject to any restrictions and limitations specified therein, the executive organ of the unit owners' association, if any, and if not, then the unit owners' association itself, shall have the irrevocable power as attorney-in-fact on behalf of all the unit owners and their successors in title to grant easements through the common elements and accept easements benefiting the condominium or any portion thereof.

(c) This section shall not be construed to prohibit the grant, by the condominium instruments, of other powers and responsibilities to the unit owners' association or its executive organ. (1974, c. 416; 1975, c. 415.)

§ 55-79.80:1. Tort and contract liability; judgment lien.—(a) An action for tort alleging a wrong done (1) by an agent or employee of the declarant or of the unit owners' association, or (2) in connection with the condition of any portion of the condominium which the declarant or the association has the responsibility to maintain, shall be brought against the declarant or the association, as the case may be. No unit owner shall be precluded from bringing such an action by virtue of his ownership of an undivided interest in the common elements or by reason of his membership in the association or his status as an officer.

(b) Unit owners other than the declarant shall not be liable for torts caused by agents or employees of the declarant within any convertible land or using any easement reserved in the declaration or created by § 55-79.65 or 55-79.66.

(c) An action arising from a contract made by or on behalf of the unit owners' association, its executive organ, or the unit owners as a group, shall be brought against the association, or against the declarant if the cause of action arose during the exercise by the declarant of control reserved pursuant to § 55-79.74 (a). No unit owner shall be precluded from bringing such an action by reason of his membership in the association or his status as an officer.

(d) A judgment for money against the unit owners' association shall be a lien against any property owned by the association, and against each of the condominium units in proportion to the liability of each unit owner for common expenses as established pursuant to § 55-79.83 (c), but not against any other property of any unit owner. Such judgment shall be otherwise subject to the provisions of § 8-386. (1975, c. 415.)

§ 55-79.81. Insurance.—(a) The condominium instruments may require the unit owners' association, or the executive organ or managing agent on behalf of such association, to obtain:

(1) A master casualty policy affording fire and extended coverage in an amount consonant with the full replacement value of the structures within

the condominium, or of such structures that in whole or in part comprise portions of the common elements.

(2) A master liability policy, in an amount specified by the condominium instruments, covering the unit owners' association, the executive organ, if any, the managing agent, if any, all persons acting or who may come to act as agents or employees of any of the foregoing with respect to the condominium, and all unit owners and other persons entitled to occupy any unit or other portion of the condominium.

(3) Such other policies as may be required by the condominium instruments, including, without limitation, workmen's compensation insurance, liability insurance on motor vehicles owned by the association, and specialized policies covering lands or improvements in which the unit owners' association has or shares ownership or other rights.

(b) When any policy of insurance has been obtained by or on behalf of the unit owners' association, written notice of the obtainment thereof and of any subsequent changes therein or termination thereof shall be promptly furnished to each unit owner by the officer required to send notices of meetings of the unit owners' association. Such notices shall be sent in accordance with the provisions of the last sentence of § 55-79.75. (1974, c. 416.)

§ 55-79.82. **Rights to common profits.**—The common profits shall be applied to the payment of common expenses, and rights in any surplus remaining shall accrue to the condominium units in proportion to the number of votes in the unit owners' association appertaining to each such unit. Any such surplus shall be distributed accordingly to the unit owners, except to such extent as the condominium instruments may require the same to be added to reserves maintained pursuant to those instruments. (1974, c. 416.)

§ 55-79.83. **Liability for common expenses.**—(a) Except to the extent that the condominium instruments provide otherwise, any common expenses associated with the maintenance, repair, renovation, restoration, or replacement of any limited common element shall be specially assessed against the condominium unit to which that limited common element was assigned at the time such expenses were made or incurred. If the limited common element involved was assigned at that time to more than one condominium unit, however, such expense shall be specially assessed against each such condominium unit equally so that the total of such special assessments equals the total of such expenses, except to the extent that the condominium instruments provide otherwise.

(b) To the extent that the condominium instruments expressly so provide, any other common expenses benefiting less than all of the condominium units or caused by the conduct of less than all those entitled to occupy the same or by their licensees or invitees, shall be specially assessed against the condominium unit or units involved, in accordance with such reasonable provisions as the condominium instruments may make for such cases.

(c) The amount of all common expenses not specially assessed pursuant to subsections (a) or (b) hereof, less the amount of all common profits, shall be assessed against the condominium units in proportion to the number of votes in the unit owners' association appertaining to each such units. Such assessments shall be made by the unit owners' association annually, or more often if the condominium instruments so provide. No change in the

number of votes in the unit owners' association appertaining to any condominium unit shall enlarge, diminish, or otherwise affect any liabilities arising from assessments made prior to such change. (1974, c. 416.)

§ 55-79.84. **Lien for assessments.**—(a) The unit owners' association shall have a lien on every condominium unit for unpaid assessments levied against that condominium unit in accordance with the provisions of this chapter and all lawful provisions of the condominium instruments. The said lien, once perfected, shall be prior to all other liens and encumbrances except (1) real estate tax liens on that condominium unit, (2) liens and encumbrances recorded prior to the recordation of the declaration, and (3) sums unpaid on any first mortgages or first deeds of trust recorded prior to the perfection of said lien for assessments and securing institutional lenders. The provisions of this subsection shall not affect the priority of mechanics' and materialmen's liens.

(b) Notwithstanding any other provision of this section, or any other provision of law requiring documents to be recorded in the miscellaneous lien books or the deed books in the clerk's office of any court, on or after July one, nineteen hundred seventy-four, all memoranda of liens arising under this section shall, in the discretion of the clerk, be recorded in the miscellaneous lien books or the deed books in such clerk's office. Any such memorandum shall be indexed in the general index to deeds, and such general index shall identify the lien as a lien for condominium assessments.

(c) The unit owners' association, in order to perfect the lien given by this section, shall file before the expiration of ninety days from the time such assessment became due and payable in the clerk's office in the county or city in which such condominium is situated, a memorandum, verified by the oath of the principal officer of the unit owners' association, or such other officer or officers as the condominium instruments may specify, which contains the following:

(1) A description of the condominium unit in accordance with the provisions of § 55-79.47.

(2) The name or names of the persons constituting the unit owners of that condominium unit.

(3) The amount of unpaid assessments currently due or past due together with the date when each fell due.

(4) The date of issuance of the memorandum.

It shall be the duty of the clerk in whose office such memorandum shall be filed as hereinabove provided to record and index the same as provided in subsection (b) hereof, in the names of the persons identified therein as well as in the name of the unit owners' association. The cost of recording such memorandum shall be taxed against the person found liable in any judgment or decree enforcing such lien.

(d) No suit to enforce any lien perfected under subsection (c) hereof shall be brought after six months from the time when the memorandum of lien was recorded; provided, however, that the filing of a petition to enforce any such lien in any suit wherein such petition may be properly filed shall be regarded as the institution of a suit under this section; and provided further that nothing herein shall extend the time within which any such lien may be perfected.

(e) The judgement or decree in an action brought pursuant to this sec-

tion shall include, without limitation, reimbursement for costs and attorneys' fees, together with interest at the maximum lawful rate for the sums secured by the lien from the time each such sum became due and payable.

(f) When payment or satisfaction is made of a debt secured by the lien perfected by subsection (c) hereof, said lien shall be released in accordance with the provisions of § 55-66.3. For the purposes of that section the principal officer of the unit owners' association, or such other officer or officers as the condominium instruments may specify, shall be deemed the duly authorized agent of the lien creditor.

(g) Nothing in this section shall be construed to prohibit actions at law to recover sums for which subsection (a) hereof creates a lien, maintainable pursuant to § 55-79.53.

(h) Any unit owner or purchaser of a condominium unit, having executed a contract for the disposition of the same, shall be entitled upon request to a recordable statement setting forth the amount of unpaid assessments currently levied against that unit. Such request shall be in writing, directed to the principal officer of the unit owners' association or to such other officer as the condominium instruments may specify. Failure to furnish or make available such a statement within five business days from the receipt of such request shall extinguish the lien created by subsection (a) hereof as to the condominium unit involved. Such statement shall be binding on the unit owners' association, the executive organ, and every unit owner. Payment of a fee not exceeding ten dollars may be required as a prerequisite to the issuance of such a statement if the condominium instruments so provide. (1974, c. 416; 1975, c. 415.)

§ 55-79.85. **Restraints on alienation.**—If the condominium instruments create any rights of first refusal or other restraints on free alienability of the condominium units, such rights and restraints shall be void unless the condominium instruments make provision for promptly furnishing to any unit owner or purchaser requesting the same a recordable statement certifying to any waiver of, or failure or refusal to exercise, such rights and restraints, in all cases where such waiver, failure, or refusal does in fact occur. Failure or refusal to furnish promptly such a statement in such circumstances in accordance with the provisions of the condominium instruments shall make all such rights and restraints inapplicable to any disposition of a condominium unit in contemplation of which such statement was requested. Any such statement shall be binding on the association of unit owners, the executive organ, and every unit owner. Payment of a fee not exceeding twenty-five dollars may be required as a prerequisite to the issuance of such a statement if the condominium instruments so provide. (1974, c. 416.)

ARTICLE 4.

Administration of Chapter; Sale, etc., of Condominium Units.

§ 55-79.86. **Administrative agency.**—This act shall be administered by the Virginia Real Estate Commission which hereinafter is called the agency. (1974, c. 416.)

§ 55-79.87. **Exemptions from certain provisions of article.**—Unless the method of offer or disposition is adopted for the purpose of evasion of this chapter, the provisions of §§ 55-79.88, 55-79.89, 55-79.90, 55-79.91, 55-79.92, 55-79.93, 55-79.94 (a) and (c), and 55-79.97 of this chapter do not apply to:

(a) Dispositions in a condominium in which all units are restricted to commercial, industrial, or other nonresidential use;

(b) Dispositions pursuant to court order;

(c) Dispositions by any government or government agency; or

(d) Offers by the declarant on nonbinding reservation agreements. (1974, c. 416; 1975, c. 415.)

§ 55-79.88. **Limitations on dispositions of units.**—Unless exempt by § 55-79.87:

(a) No declarant may offer or dispose of any interest in a condominium unit located in this Commonwealth, nor offer or dispose in this Commonwealth of any interest in a condominium unit located without this Commonwealth prior to the time the condominium including such unit is registered in accordance with this chapter.

(b) [Repealed.]

(c) No declarant may dispose of any interest in a condominium unit unless he delivers to the purchaser a current public offering statement by the time of such disposition and such disposition is expressly and without qualification or condition subject to cancellation by the purchaser within ten days from the contract date of the disposition, or delivery of the current public offering statement, whichever is later. If the purchaser elects to cancel, he may do so by notice thereof hand-delivered or sent by United States mail, return receipt requested to the declarant. Such cancellation shall be without penalty, and any deposit made by the purchaser shall be promptly refunded in its entirety. (1974, c. 416; 1975, c. 415.)

§ 55-79.89. **Application for registration; fee.**—(a) The application for registration of the condominium shall be filed as prescribed by the agency's rules and shall contain the following documents and information:

(1) An irrevocable appointment of the agency to receive service of any lawful process in any noncriminal proceeding arising under this chapter against the applicant or his personal representative;

(2) The states or jurisdictions in which an application for registration or similar document has been filed, and any adverse order, judgment, or decree entered in connection with the condominium by the regulatory authorities in each jurisdiction or by any court;

(3) The applicant's name, address, and the form, date, and jurisdiction or organization; and the address of each of its offices in this State;

(4) The name, address, and principal occupation for the past five years of every officer of the applicant or person occupying a similar status or performing similar functions; the extent and nature of his interest in the applicant or the condominium as of a specified date within thirty days of the filing of the application;

(5) A statement, in a form acceptable to the agency, of the condition of the title to the condominium project including encumbrances as of a specified date within thirty days of the date of application by a title opinion of a

licensed attorney, not a salaried employee, officer or director of the applicant or owner, or by other evidence of title acceptable to the agency;

(6) Copies of the instruments which will be delivered to a purchaser to evidence his interest in the unit and of the contracts and other agreements which a purchaser will be required to agree to or sign;

(7) Copies of any management agreements, employment contracts or other contracts or agreement affecting the use, maintenance or access of all or a part of the condominium;

(8) A statement of the zoning and other governmental regulations affecting the use of the condominium, including the site plans and building permits and their status, and also of any existing tax and existing or proposed special taxes or assessments which affect the condominium;

(9) A narrative description of the promotional plan for the disposition of the units in the condominium;

(10) Plats and plans of the condominium that comply with the provisions of § 55-79.58 other than the certification requirements thereof, and which show all units and buildings containing units to be built anywhere within the submitted land other than within the boundaries of any convertible lands; except that the agency may establish by rule or order requirements in lieu of the provisions of § 55-79.58 for plats and plans of a condominium located outside this Commonwealth;

(11) The proposed public offering statement;

(12) Any other information, including any current financial statement, which the agency by its rules requires for the protection of purchasers.

(b) If the declarant registers additional units to be offered for disposition in the same condominium he may consolidate the subsequent registration with any earlier registration offering units in the condominium for disposition under the same promotional plan.

(c) The declarant shall immediately report any material changes in the information contained in an application for registration.

(d) Each application shall be accompanied by a fee in an amount equal to ten dollars per unit, except that the initial application fee shall be not less than five hundred dollars nor more than one thousand dollars, and the fee for any application for registration of additional units shall be not less than two hundred and fifty dollars nor more than one thousand dollars. All fees shall be remitted by the agency to the Treasurer of the Commonwealth, and shall be placed to the credit of the special fund of the Virginia Real Estate Commission, which is hereby established and shall be expended solely for compliance with the provisions of this chapter; provided, however, that if any surplus remains at the end of a fiscal year, such surplus shall be placed in the general fund. (1974, c. 416; 1975, c. 415.)

§ 55-79.90. Public offering statement.—(a) A public offering statement shall disclose fully and accurately the characteristics of the condominium and the units therein offered and shall make known to prospective purchasers all unusual and material circumstances or features affecting the condominium. The proposed public offering statement submitted to the agency shall be in a form prescribed by its rules and shall include the following:

(1) The name and principal address of the declarant and the condominium;

(2) A general narrative description of the condominium stating the total number of units in the offering; the total number of units planned to be sold and rented; the total number of units that may be included in the condominium by reason of future expansion or merger of the project by the declarant;

(3) Copies of the declaration and bylaws, with a brief narrative statement describing each and including information on declarant control, a projected budget for at least the first year of the condominium's operation (including projected common expense assessments for each unit), and provisions for reserves for capital expenditures and restraints on alienation;

(4) Copies of any management contract, lease of recreational areas, or similar contract or agreement affecting the use, maintenance or access of all or any part of the condominium with a brief narrative statement of the effect of each such agreement upon a purchaser, and a statement of the relationship, if any, between the declarant and the managing agent or firm;

(5) A general description of the status of construction, zoning, site plan approval, issuance of building permits, or compliance with any other State or local statute or regulation affecting the condominium;

(6) The significant terms of any encumbrances, easements, liens and matters of title affecting the condominium;

(7) The significant terms of any financing offered by the declarant to purchaser of units in the condominium;

(8) Provisions of any warranties provided by the declarant on the units and the common elements, other than the warranty prescribed by § 55-79.79 (b);

(9) A statement that the purchaser may cancel the disposition within ten days of delivery of the current public offering statement, or within ten days of the contract date of the disposition, whichever is later;

(10) Additional information required by the agency to assure full and fair disclosure to prospective purchasers.

(b) The public offering statement shall not be used for any promotional purposes before registration of the condominium project and afterwards only if it is used in its entirety. No person may advertise or represent that the agency approves or recommends the condominium or disposition thereof. No portion of the public offering statment may be underscored, italicized, or printed in larger or heavier or different color type than the remainder of the statement unless the agency requires it.

(c) The agency may require the declarant to alter or amend the proposed public offering statement in order to assure full and fair disclosure to prospective purchasers, and no change in the substance of the promotional plan or plan of disposition or development of the condominium may be made after registration without notifying the agency and without making appropriate amendment of the public offering statement. A public offering statement is not current unless all amendments are incorporated.

(d) The provisions of this section shall be deemed to be complied with if the public offering statement filed pursuant to the provisions of § 55-79.89 (a) (11) is for offers of units currently registered with the Securities Division of the State Corporation Commission or the Securities and Exchange Commission. (1974, c. 416.)

§ 55-79.91. **Inquiry and investigation.**—Upon receipt of an application for registration in proper form, the agency shall forthwith initiate an investigation to determine that:

(a) The declarant can convey or cause to be conveyed the units offered for disposition if the purchaser complies with the terms of the offer;

(b) There is reasonable assurance that all proposed improvements will be completed as represented;

(c) The advertising material and the general promotional plan are not false or misleading and comply with the standards prescribed by the agency in its rules and afford full and fair disclosure;

(d) The declarant has not, or if a corporation, its officers, and principals have not, been convicted of a crime involving condominium unit dispositions or any aspect of the land sales business in this State, United States, or any other state or foreign country within the past ten years and has not been subject to any injunction or administrative order restraining a false or misleading promotional plan involving land dispositions; and

(e) The public offering statement requirements of this chapter have been satisfied. (1974, c. 416.)

§ 55-79.92. **Notice of filing and registration.**—(a) Upon receipt of the application for registration in proper form, the agency shall, within five business days, issue a notice of filing to the applicant. Within sixty days from the date of the notice of filing, the agency shall enter an order registering the condominium or rejecting the registration. If no order of rejection is entered within sixty days from the date of notice of filing, the condominium shall be deemed registered unless the applicant has consented in writing to a delay.

(b) If the agency affirmatively determines, upon inquiry and examination, that the requirements of § 55-79.91 have been met, it shall enter an order registering the condominium and shall designate the form of the public offering statement.

(c) If the agency determines upon inquiry and examination that any of the requirements of § 55-79.91 have not been met, the agency shall notify the applicant that the application for registration must be corrected in the particulars specified within ten days. If the requirements are not met within the time allowed the agency shall enter an order rejecting the registration which shall include the findings of fact upon which the order is based. The order rejecting the registration shall not become effective for twenty days after the lapse of the aforesaid ten-day period during which twenty-day period the applicant may petition for reconsideration and shall be entitled to a hearing or correct the particulars specified in the agency's notice. Such order of rejection shall not take effect, in any event, until such time as the hearing, once requested, is given to the applicant. (1974, c. 416.)

§ 55-79.93. **Annual report by declarant; termination of registration.**—The declarant shall, during any period of control of the condominium by the declarant pursuant to § 55-79.74, file a report in the form prescribed by the rules of the agency within thirty days of each anniversary date of the order registering the condominium. The report shall reflect any material changes in information contained in the original application for registration.

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In the event that the annual report reveals that all of the units in the condominium have been disposed of, and that all periods for conversion or expansion have expired, the agency shall issue an order terminating the registration of the condominium. (1974, c. 416; 1975, c. 415.)

§ 55-79.94. Conversion condominiums; special provisions.—(a) Any declarant of a conversion condominium shall include in his public offering statement in addition to the requirements of § 55-79.90 the following:

(1) A specific statement of the amount of any initial or special condominium fee due from the purchaser on or before settlement of the purchase contract and the basis of such fee;

(2) Information on the actual expenditures made on all repairs, maintenance, operation or upkeep of the subject building or buildings within the last three years, set forth tabularly with the proposed budget of the condominium, and cumulatively broken down on a per unit basis in proportion to the relative voting strengths allocated to the units by the bylaws. If such building or buildings have not been occupied for a period of three years then the information shall be set forth for the maximum period such building or buildings have been occupied;

(3) A description of any provisions made in the budget for reserves for capital expenditures and an explanation of the basis for such reserves, or, if no provision is made for such reserves, a statement to that effect;

(4) A statement of the declarant as to the present condition of all structural components and major utility installations in the condominium, which statement shall include the approximate dates of construction, installation, and major repairs, and the expected useful life of each such item, together with the estimated cost (in current dollars) of replacing each of the same.

(b) In the case of a conversion condominium, the declarant shall give at least ninety days' notice to each of the tenants of the building or buildings which the declarant intends to submit to the provisions of this chapter. During the first sixty days of such ninety-day period, each of the said tenants shall have the exclusive right to contract for the purchase of the unit he occupies, but only if such unit is to be retained in the conversion condominium without substantial alteration in its physical layout. Such notice shall be hand delivered or sent by first class mail, return receipt requested, and shall inform the tenants of the declarant's intent to create a conversion condominium. Such notice may also constitute the notice to terminate the tenancy as provided for in § 55-222 of this Code, except that, despite the provisions of § 55-222, a tenancy from month to month may only be terminated upon ninety days notice as set forth herein when such termination is in regard to the creation of a conversion condominium. If, however, a tenant so notified remains in possession of the unit he occupies after the expiration of the ninety-day period with the permission of the declarant, in order to then terminate the tenancy, such declarant shall give the tenant a further notice as provided in § 55-222 of this Code.

(c) The declarant of a conversion condominium, shall, in addition to the requirements of § 55-79.89, include with the application for registration a copy of the notice set forth in paragraph (b) and a certified statement that such notice, fully complying with the provisions of paragraph (b), shall be, at the time of the registration of such condominium, mailed or delivered to each of the tenants in the building or buildings for which registration is sought.

(d) Notwithstanding the provisions of § 55-79.40 of this chapter, in the case of any conversion condominium created under the provisions of the Horizontal Property Act (§ 55-79.1 et seq.) for which a final report has not been issued by the agency pursuant to § 55.79.21 prior to June one, nineteen hundred seventy-five, the provisions of subsections (a) and (b) of this section shall apply and the declarant shall be required to furnish evidence of full compliance with subsections (a) and (b) prior to the issuance by the agency of a final report for such conversion condominium. (1974, c. 416; 1975, c. 415.)

§ 55-79.95. Escrow of deposits.—Any deposit made in regard to any disposition of a unit, including a nonbinding reservation agreement, shall be held in escrow until delivered at settlement. Such escrow funds shall be deposited in a separate account designated for this purpose; except where such deposits are being held by a real estate broker or attorney licensed under the laws of this Commonwealth such funds may be placed in that broker's or attorney's regular escrow account and need not be placed in a separate designated account. Such escrow funds shall not be subject to attachment by the creditors of either the purchaser or the declarant. (1974, c. 416.)

§ 55-79.96. Declarant to deliver declaration, etc., to purchaser.—The declarant shall within ten days of recordation of the condominium instruments as provided for in §§ 55-79.45 and 55-79.49 hereof, forward to each purchaser at his last known address by first class mail, return receipt requested, an exact copy of the recorded declaration and bylaws. (1974, c. 416.)

§ 55-79.97. Resale by purchaser.—(a) In the event of any resale of a condominium unit by a unit owner other than the declarant, such owner shall obtain from the unit owners' association and furnish to the purchaser, prior to the contract date of the disposition, the following:

(1) Appropriate statements pursuant to § 55-79.84(h) and, if applicable, § 55-79.85;

(2) A statement of any capital expenditures anticipated by the unit owners' association within the current or succeeding two fiscal years;

(3) A statement of the status and amount of any reserve for replacement fund and any portion of such fund earmarked for any specified project by the board of directors;

(4) A copy of the statement of financial condition of the unit owners' association for the last fiscal year for which such statement is available;

(5) A statement of the status of any pending suits or judgments in which the unit owners' association is a party;

(6) A statement setting forth what insurance coverage is provided for all unit owners by the unit owners' association and what additional insurance coverage would normally be secured by each individual unit owner; and

(7) A statement that any improvements or alterations made to the unit, or the limited common elements assigned thereto, by the prior unit owner are not in violation of the condominium instruments.

(b) The principal officer of the unit owners' association, or such other officer or officers as the condominium instruments may specify, shall furn-

ish the statements prescribed by subsection (a) hereof upon the written request of any unit owner within ten days of the receipt of such request.

(c) Subject to the provisions of § 55-79.87, but notwithstanding any other provisions of this chapter, the provisions and requirements of this section shall apply to any such resale of a condominium unit created under the provisions of the Horizontal Property Act (§ 55-79.1 et seq.). (1974, c. 416; 1975, c. 415.)

§ 55-79.98. General powers and duties of the Virginia Real Estate Commission.—(a) The agency shall prescribe reasonable rules which shall be adopted, amended or repealed in compliance with law applicable to the administrative procedure of agencies of government. The rules shall include but not be limited to provisions for advertising standards to assure full and fair disclosure; provisions for operating procedures; and other rules as are necessary and proper to accomplish the purpose of this chapter.

(b) The agency by rule or by an order, after reasonable notice and hearing, may require the filing of advertising material relating to condominiums prior to its distribution.

(c) If it appears that a person has engaged or is about to engage in an act or practice constituting a violation of a provision of this chapter, or a rule or order hereunder, the agency, with or without prior administrative proceedings may bring an action in the circuit court of the city or county in which any portion of the condominium is located to enjoin the acts or practices and to enforce compliance with this chapter or any rule or order hereunder. Upon proper showing, injunctive relief of temporary restraining orders shall be granted. The agency is not required to post a bond in any court proceedings or prove that any other adequate remedy at law exists.

(d) The agency may intervene in any suit involving the declarant. In any suit by or against a declarant involving a condominium, the declarant shall promptly furnish the agency notice of the suit and copies of all pleadings.

(e) The agency may:

(1) Accept registrations filed in other states or with the federal government;

(2) Contract with similar agencies in this State or other jurisdictions to perform investigative functions;

(3) Accept grants in aid from any governmental source.

(f) The agency shall cooperate with similar agencies in other jurisdictions to establish uniform filing procedures and forms, uniform public offering statements, advertising standards, rules and common administrative practices. (1974, c. 416.)

§ 55-79.99. Investigations and proceedings.—(a) The agency may make necessary public or private investigations in accordance with law within or outside of this State to determine whether any person has violated or is about to violate this chapter or any rule or order hereunder, or to aid in the enforcement of this chapter or in the prescribing of rules and forms hereunder.

(b) For the purpose of any investigation or proceeding under this chapter, the agency or any officer designated by rule may administer oaths or affirmations, and upon its own motion or upon request of any party shall

subpoena witnesses, compel their attendance, take evidence, and require the production of any matter which is relevant to the investigation, including the existence, description, nature, custody, condition and location of any books, documents, or other tangible things and the identity and location of persons having knowledge of relevant facts or any other matter reasonably calculated to lead to the discovery of material evidence.

(c) Upon failure to obey a subpoena or to answer questions propounded by the investigating officer and upon reasonable notice to all persons affected thereby, the agency may apply to the Circuit Court of the city of Richmond for an order compelling compliance. (1974, c. 416.)

§ 55-79.100. Cease and desist orders.—(a) If the agency determines after notice and hearing that a person has:

(1) Violated any provision of this chapter;

(2) Directly or through an agent or employee knowingly engaged in any false, deceptive, or misleading advertising, promotional, or sales methods to offer or dispose of a unit;

(3) Made any substantial change in the plan of disposition and development of the condominium subsequent to the order of registration without notifying the agency;

(4) Disposed of any units which have not been registered with the agency; or

(5) Violated any lawful order or rule of the agency;

it may issue an order requiring the person to cease and desist from the unlawful practice and to take such affirmative action as in the judgment of the agency will carry out the purposes of this chapter.

(b) If the agency makes a finding of fact in writing that the public interest will be irreparably harmed by delay in issuing an order, it may issue a temporary cease and desist order. Prior to issuing the temporary cease and desist order, the agency shall give notice of the proposal to issue a temporary cease and desist order to the person. Every temporary cease and desist order shall include in its terms a provision that upon request a hearing will be held promptly to determine whether or not it becomes permanent. (1974, c. 416; 1975, c. 415.)

§ 55-79.101. Revocation of registration.—(a) A registration may be revoked after notice and hearing upon a written finding of fact that the declarant has:

(1) Failed to comply with the terms of a cease and desist order;

(2) Been convicted in any court subsequent to the filing of the application for registration for a crime involving fraud, deception, false pretenses, misrepresentation, false advertising, or dishonest dealing in real estate transactions;

(3) Disposed of, concealed, or diverted any funds or assets of any person so as to defeat the rights of unit purchasers;

(4) Failed faithfully to perform any stipulation or agreement made with the agency as an inducement to grant any registration, to reinstate any registration, or to approve any promotional plan or public offering statement; or

(5) Made intentional misrepresentations or concealed material facts in an application for registration.

Findings of fact, if set forth in statutory language, shall be accompanied

by a concise and explicit statement of the underlying facts supporting the findings.

(b) If the agency finds after notice and hearing that the developer has been guilty of a violation for which revocation could be ordered, it may issue a cease and desist order instead. (1974, c. 416.)

§ 55-79.102. **Judicial review.**—Proceedings for judicial review shall be in accordance with law governing appeals from actions of governmental agencies. (1974, c. 416.)

§ 55-79.103. **Penalties.**—Any person who willfully violates any provision of §§ 55-79.87, 55-79.88, 55-79.89, 55-79.90, 55-79.93, 55-79.94, 55-79.95, or any rule adopted under or order issued pursuant to § 55-79.98, or any person who willfully in an application for registration makes any untrue statement of a material fact or omits to state a material fact shall be guilty of a misdemeanor and may be fined not less than one thousand dollars or double the amount of gain from the transaction, whichever is the larger but not more than fifty thousand dollars; or he may be imprisoned for not more than six months; or both, for each offense. (1974, c. 416.)

Mr. LLOYD. I believe anybody familiar with the subject of condominiums is aware of the fact that the Commonwealth of Virginia is among the leaders in condominium legislation at the State level. We have been at it since the early days of 1962 and recently we enacted our Condominium Act which is considered by many experts as a model for legislation at the State level governing condominiums.

Focusing on disclosure, we in Virginia have found that if there's one thing that's certain it's disclosure is a difficult matter. To require full and accurate disclosure is very fine, but our experience has been that the developers are only too willing to do that. What happens is that the counsel for the developer will prepare a statement which covers everything, including the kitchen sink, and he comes up with a document that can only be read and understood by another lawyer. But this is given to the purchaser to explain to him what he's getting into.

Well, the purchaser has, in Virginia, 10 or 15 days, if this law is enacted, in which to try to understand that and what he must do is take it to his attorney and say, "What have I got here?" The attorney, if he has time within those 15 days, will have to sit down and study it himself, running up some legal fees.

In recognition of all this, the complexity that the disclosure statements tend to have, we have undertaken a simplification program. We are in the early stages of that right now, but I would submit to you that there are many different approaches that are possible. Several States are actively involved, as you have heard this morning, in regulating condominiums, and I don't think any one of them can be said to have the ideal approach; and if that's so, then I don't think that HUD is going to be able to come up with the ideal disclosure approach either.

At this stage of regulation of condominiums, I believe that there ought to be experimentation permitted. The States function as laboratories, to use the well-worn phrase. At some time you might determine which is the best way, but until then I would hate to see HUD deciding within the very near future what is the best way to make disclosure of a condominium, especially in view of the unique characteristics that many of them have and in view of the fact that it's really in a very experimental stage at this point.

In the interest of saving time, I will conclude my remarks with that.

The CHAIRMAN. Thank you, Mr. Lloyd.

Finally, we have Ms. Earner.

Ms. EARNER. Thank you. I'd like to just take a moment to tell you a little about where the District of Columbia is in terms of condominiums. We have only been in the disclosure regulation business for about 11 months, so we are probably junior at this table in terms of history.

So far we have registered 17 projects with 1,804 units and of those, 12 projects were condominium conversions for a little over 1,300 units. So most of our experience has been in the conversion area.

I'd like to comment specifically on two points which have received a good deal of discussion this morning. First is transfer of control. Under the proposed bill before us this morning transfer of control would occur at 80 percent occupancy or 1 year. I have some concern for the 1 year date in that transfer of control may occur too soon and may be actually injurious to the purchasers in the project. The District

is about to propose a new condominium statute. We have submitted it to council and council is going to hold hearings on that bill next month and we have introduced a new type of transfer of control I believe, something that we would call a phased transfer of control, where instead of just giving the owners control of the board immediately at some given date in time we provided a method whereby they will be gradually introduced to the board. Twenty-five percent of the members of the executive board would be resident owners when one-fourth of the interest in the common elements had been conveyed. When one-half of the common elements had been conveyed, no less than 33⅓ percent of the board would be resident members. Final transfer of control would occur when 75 percent of the units had been conveyed or no later than 2 years.

We feel in this way the residents would be introduced to the process of governing their own project and would not be subject to the situation of seeing the balance sheet for the first time the night they are elected at that 1 year date.

Another issue that has received a lot of discussion this morning is that of engineers' reports. The District of Columbia regulations does require an engineering report be submitted for a conversion project and we feel it's one of the strongest provisions for consumer protection in a conversion condominium. When we passed our law we got the usual amount of complaints from both developers and engineers that the requirement was impossible: that it would be absolutely totally beyond the capability of the developer to carry expensewise.

However, we have registered 12 conversion projects and we have an engineering report for each of those projects. I believe one thing that has helped the District in this area is that the liability for the property report rests with the developer. It's the developer who signs a sworn statement that the contents of that report are true and the engineers have agreed to submit engineering reports because they feel the responsibility does rest with the developer.

Finally, I'd like to make a comment about remarks this morning about the burden of disclosure regulations upon the developer or the seller of the units. I'm sure it is a burden on them. It's also a burden on consumers to be stuck with a bad project. I think that the burden is not without benefit however. Those developers who complained the hardest to us about the District disclosure regulation came back to us weeks or months after they had been registered and said, "Gee, we really are glad we registered with you. The property report has become the best selling tool we have had in condominium sales. The engineer's report lets people think we're honest. We're able to put up front what the building is like. The budget report is there. They know we're doing our best."

So I think there's benefit along with the burden and I think any disclosure legislation should be looked at in that light.

The CHAIRMAN. Thank you, Ms. Earner.

[Complete statement follows:]

GOVERNMENT OF THE DISTRICT OF COLUMBIA
DEPARTMENT OF HOUSING AND COMMUNITY DEVELOPMENT
WASHINGTON, D.C.

Reply To

TESTIMONY

OF

MARGARET A. EARNER
STAFF PLANNER

OFFICE OF POLICY DEVELOPMENT, PLANNING AND EVALUATION

BEFORE THE

SENATE COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS

ON

OCTOBER 6, 1975

My name is Margaret A. Earner. I am a staff planner with the Office of Policy Development, Planning and Evaluation in the Department of Housing and Community Development of Washington, D.C. In my capacity as staff planner, I carry major responsibility for the administration of the District's condominium law and regulations.

The District of Columbia, like most states, passed a condominium enabling act in 1963. Until 1972, we had only 469 condominium units in the city. In 1973, however, an additional 1,305 condominiums were created and the demand for more protective condominium legislation became more evident.

Approximately 11 months ago, the District responded with passage of Regulation 74-26 which we commonly refer to as our condominium disclosure regulations. Many of the provisions contained in S. 2273 are already incorporated in our regulations. We have to date registered 17 projects containing 1,604 units. Of this number, 12 were conversion condominiums with a total of 1,380 units.

I would like to take my time this morning to share with you our experiences in implementing a disclosure law from both the consumer and tenant perspective.

1. Transfer of Control [Sec. 5 (3)] S. 2273 proposes that transfer of control of the owner's association should occur when 80% of the units are occupied or not later than one year after initial occupancy, whichever occurs first. Our present regulations require control to be transferred within 180 days after 80% of the units are conveyed. We felt the 180 day "grace" period was important since many by-laws require certain notification periods for meetings at which board members are elected. However, I would like to bring to the Committee's attention new language regarding transfer of control which we have developed in rewriting our enabling statute. [Mayor Washington has forwarded a new condominium enabling statute to

City Council which will hold hearings on the subject later this month].

In the short period of time in which we have administered our disclosure regulations, it has become clear how critically important is the issue of transfer of control. One problem we have experienced is a developer who simply drops control upon a resident board, who have had no previous experience with managing the project. Often, residents have not seen operating statements or balance sheets until the day they elect their own board.

Therefore, in our new law we are recommending a staged transfer of control whereby 25% of the members of the executive board will be resident owners, when one-fourth of the undivided interests in the common elements is conveyed. When one-half of the undivided interest in the

common elements is conveyed, no less than 33-1/3% of the board shall be resident owners. Final transfer of control will occur when 75% of the units have been conveyed or no later than 2 years after settlement of the first. We chose 2 years since most projects selling time ranges from 14-24 months. There is some danger in transferring control too early.

2. Warranty [Sec. 5 (5)]

The bill before you today proposes a warranty period of two years (from date of initial occupancy) on all common elements, and one year on individual units. Our experience has shown that the requirement of such a warranty is not unreasonable. Presently, the District requires a warranty for 1 year from the date of conveyancy of 80% of the units to bona fide purchasers. In some

cases, our required warranty period would extend beyond the period recommended in the bill before you. We feel that it is very important that the warranty extend at least through the period of developer control. In our new legislation, we recommend the warranty run from completion of the common elements through one year after transfer of control.

3. Tenant Option to Buy [Sec. 5 (7)]
S. 2273 would, in the case of a conversion condominium, give tenants a 90 day option to purchase any unit in the project. The District's existing and proposed legislation offers an option to buy only on the unit the tenant occupies at the time of the conversion. Extending the option to buy to any unit in the project gives the tenant more flexibility and

opportunity, and appears more favorable than any limited option approach.

4. Estimating Budget Projections [Sec. 6 (a)(6)]

The District has required the submission of an estimated operating budget for a period of one year from the expected first occupancy. While all developers were able to provide such figures, many felt that the preparation of that budget was almost tantamount to crystal ball gazing, in light of rising utility and material costs. Provisions for a 2 year projection of expenses, as required under S. 2273, could be extremely difficult.

One of the principle reasons for requiring some kind of budget projection is to prevent the developer from engaging in "low-balling," the practice of setting unreasonably low condominium fees to encourage sales. I think that

the requirement of a one-year budget helps toward eliminating this practice. Once a developer is required to commit a budget to paper, the setting of fees, almost by force, becomes a more realistic practice.

5. Engineer's Report for Conversion Condominiums [Sec. 6 (a)(7)]

The requirement of an engineer's report may be one of the most controversial provisions of the bill before you. It certainly was in the writing of our regulation. The District requires a report from an engineer registered in the District of Columbia as to the condition, expected useful life and replacement cost, in dollars of the time prepared, of all major common elements. While there was a great deal of discussion about the impossibility of developer's

securing such statements in the District they have been written and incorporated in the registered property report. In addition, several developer's have returned after registration to tell us that the engineer's statement in particular, and the property report in general, are the best selling tools they could have. An up front statement of condition has helped them show consumers, who are becoming more and more sophisticated in the condominium market, exactly what they are buying.

The major problem seems to be one of liability. The District has attempted to place full responsibility where it belongs, on the shoulders of the developer, by requiring him to sign a sworn statement attesting to the contents of the property report, including the engineer's statement. This may have helped us to secure the necessary statements. In any case securing an engineer's statement is not impossible and we have 12 of them to prove it.

In conclusion I would like to make one comment on the general intent of S. 2273 to place major responsibility for enforcement of condominium legislation on the states. Previous bills have professed a more complete federal role with H.U.D. as the principle enforcement body. I feel the state approach embraced in S. 2273 is far superior.

Our short time of administering a condominium disclosure law has convinced me that the enforcement agency must be close to the problem. This aids in responsive and effective enforcement as well as increased insight into refinements which may be necessary as a law matures. The District is in a unique situation of being both city and state which allows us to really address the problem first hand.

The CHAIRMAN. Thank you, all of you. I want to thank you for your very concise summaries and hitting the high points here so well.

I'd like each of you to comment on whether or not you think that this bill should be passed, whether if you do or even if you don't if any part of it should be passed or any part of it should be modified. You might particularly tell us about the coverage, the consumer protection, the national standards for consumer protection, the national standards for disclosure, civil penalties and enforcement. We'll start off with Mr. Hempel.

Mr. HEMPEL. Thank you, Senator. Our concern about the bill was registered in my earlier remarks but our concern for the State is we think we have a regulatory standard which is much higher than most and goes far beyond in total concept of what this Federal bill would do and we are concerned somewhat about the potential for preemption for the protection of California purchasers.

The CHAIRMAN. Do you see the same problem Mr. Larson indicated he felt that it's very hard to interpret which law—Federal or State—is the stronger or the more protective and the notion that we had that we might easily know the circumstances in which the Federal law would give way and the States would prevail if they wanted to go any farther?

Mr. HEMPEL. Yes, but the problem Mr. Larson mentioned—we happen to have the same penalty provision in our law as they have and it varies from that contained in the Federal law, but not necessarily less than. If the Federal proposal were to include something substantive such as the warranty provision, let's assume for the moment that that's entirely desirable but that California law didn't have a warranty provision and if some of the other regulatory standards in California were therefore preempted by the Federal law the net result to the purchaser might be negative. The same thing for the engineering report.

The CHAIRMAN. Supposing we can meet your objection. I presume we could. I take it you think we could on preemption. You wouldn't have any difficulty in advising us how we could draft the legislation so that your law would not be preempted, would you?

Mr. HEMPEL. Probably not.

The CHAIRMAN. If that were so, would you support the legislation?

Mr. HEMPEL. I can't speak for the State of California to that extent. I was sent here as a resource witness.

The CHAIRMAN. As a resource witness, will you tell us what you think about it? That's why we're having these hearings, for you experts to tell us what we ought to do. Even though I have introduced the legislation, my mind is open on it. I'm perfectly willing, if the testimony warrants that we shouldn't have the legislation, that we shouldn't propose it.

Mr. HEMPEL. Obviously, Senator, since we have a lot of these things in our California law and a lot of things not addressed in this bill, we feel that regulation in the condominium field is desirable. If there are some States that don't have it and this would help them get it, then we feel such a bill would be desirable.

The CHAIRMAN. All right. Mr. Makens?

Mr. MAKENS. Senator, I have included a series of what we classify as technical comments which I think would address the various sections of the bill.

Let me say, in essence, as long as the disclosure is properly drafted and the State preemption provisions are not too tightly drawn so they are in fact going to hurt the potential purchasers rather than help them, the State of Michigan would wholeheartedly endorse the bill.

The CHAIRMAN. Wholeheartedly endorse it provided we make the corrections you suggest?

Mr. MAKENS. Yes, sir, and I believe we could by working together with the staff.

The CHAIRMAN. Mr. Larson?

Mr. LARSON. Thank you, Senator. I would like to say, first of all, that the Minnesota proposed legislation is probably 85 to 90 percent in conformity with the proposals are that you have in your bill, Senator, and I would support those proposals wholeheartedly.

I think that Federal legislation providing minimum standards, minimum safeguards, will be a benefit to all condominium purchasers throughout the country, not just in Minnesota, but Wisconsin and all over the country. This bill will encourage States to get into the area of condominiums, to look at condominiums.

As I noted in my prepared statement, we have not had the abuses in Minnesota that have existed around the country, however, I feel that condominium development in Minnesota is going to expand greatly in the next few years. I noted that the average cost of building a new home in Minneapolis-St. Paul right now is $57,000. Many people can't afford that, so they are going to turn to other forms of housing, one of which will be condominiums.

Dealing specifically with warranties, I think there's a question of whether condominiums should be segregated from other types of housing. In the Minnesota legislature right now, there is a bill dealing with house warranties across the board. I'm wondering if warranties should be looked at in all forms of housing and not just for condominiums. Therefore, we do not have such a warranty proposal.

My personal feeling on warranties in housing is there should be some minimum level of protection, at least some disclosures, to make sure people appreciate what they're buying.

In the area of the cooling off period, Minnesota's proposal is 5 days versus your proposed 15 days. We can all sit and talk about whether it's 5 days, 6 days, 10 days, 20 days. The point is, I think that there should be some form of cooling off period. I think I would disagree with Mr. Makens to the extent that a waiver should be provided. It seems to me a decision should be made up front whether or not there should be a cooling off period or should not be a cooling off period and then we should decide how long it's going to be. If we decide there should not be a cooling off period, then let's take it out altogether. If there should be one, let's apply it across the board. We feel 5 days is a reasonable time. I can't honestly imagine where a person is going to walk in and close a transaction in less than a 5-day period. This will allow a person to get technical advice and consequently the proper protection needed.

The CHAIRMAN. Mr. Lloyd?

Mr. LLOYD. As I indicated earlier, I believe that Virginia has a model statute and I think I spot several Virginia provisions in the proposed bill today, however they are not entirely uniform. So the question becomes, will Virginia be able to administer a State plan

under the terms of S. 2273? If we deviate in one detail are we out, or is it going to take a somewhat broader view of things and determine if our performance and the effect of our legislation is substantially akin to that in the Federal legislation? Are we going to then be permitted to administer a State plan? Hopefully, we would be able to. I think there's a fundamental question here: Should effective State legislation of the kind that many States presently have be preempted because certain State legislation is deemed ineffective?

Again, as I indicated earlier, I think that those States that are active in the area ought to be permitted to remain active because of the early stages in which we all find ourselves.

The CHAIRMAN. That's certainly our intent, at least my intention, Mr. Lloyd, and I think that would be the intention of Congress, that certainly if the State is doing the job, can do the job and has demonstrated that as well as you have, heaven knows, we don't want to have the Federal Government imposing changes: and I think we have had a lot of experience with statutes that have been not preemptive in the sense that they have permitted States to develop further restrictions without much difficulty. We have done that in Truth-in-Lending and other areas.

My question would be, if we could solve that problem. You have been very helpful in addressing yourself as forcefully to it. It's been a most useful contribution. If we solve that problem, do you think this legislation would be desirable or do you think it would be an asset?

Mr. LLOYD. I think it's certainly a valuable piece of legislation, assuming that the State plan provisions were clarified to allow States like Virginia to continue their ongoing role.

The CHAIRMAN. Thank you. Ms. Earner?

Ms. EARNER. I think if a bill is meant to establish some minimum standards whereby areas of the country that do not have any condominium provisions at all would be forced to either devise their own or adopt the Federal standards, to that extent the bill is useful.

I share Mr. Lloyd's concerns about infringing on States that have already been extremely active in the area of regulating. I'm sure that will be addressed by the committee. There's one problem particular to the District I might highlight here and that is our existing regulations as well as our proposed statute provide the Mayor the ability to waive certain provisions of our law if the facts of the case justify that waiver and do not injure the consumer in so doing. I do not see a provision like that in this bill and I would be concerned if the national standards would invalidate that waiver.

The CHAIRMAN. What you're suggesting is the local official be allowed to waive rather than the Secretary of HUD?

Ms. EARNER. Yes, sir. I am suggesting that. There are certain cases in which the waiver has already been used in the District of Columbia which may be very peculiar to one project over 10 years, but it's extremely useful in that one project to be able to waive that provision given that you have adequately assured yourself that the consumer is not being harmed by that waiver.

The CHAIRMAN. My time is up. Senator Morgan?

Senator MORGAN. Mr. Hempel, would this bill afford the consumers in California any protection that you're not now affording to them?

Mr. HEMPEL. Only with respect to the two provisions that we raised some questions about. If indeed the warranty provision were desirable and the cooling off period were desirable, then that would be consumer protection that doesn't currently exist for the typical urban condominium sale.

Senator MORGAN. As interested as California has been, do you not think this is an area where people of California should decide for themselves?

Mr. HEMPEL. Well, yes. That's been our general approach toward this legislation.

Senator MORGAN. In other words, you think that California can protect the consumers as well as we can here in Washington?

Mr. HEMPEL. Yes, sir.

Senator MORGAN. Mr. Makens, I noticed your endorsement of the bill. Would it afford any protection for the consumers in Michigan that you do not now afford the consumers in Michigan?

Mr. MAKENS. Yes, sir. It seems to me it would do two things in that area. First, I believe Florida basically managed to somehow paste condominiums throughout the United States with a black eye. It's put a fear of purchasing a condominium in Michigan residents that's taken almost a year to dissipate. I was asked to provide some information of an adverse nature on the condominium in Michigan in the "60-Minute" program. They weren't interested in what was going right. That kind of thing I think this legislation would help.

Senator MORGAN. Do you not think we should put the entire program in HUD so we would have a uniform system across the Nation so the consumers and the contractors and builders alike would look to HUD rather than having to look to the various State governments and to the Federal Government?

Mr. MAKENS. No: simply because I said at least 95 percent of our buildings are for Michigan residents.

Senator MORGAN. Do you think that the other 5 percent warrants the bureaucracy of a $10 billion appropriation this bill carries plus the additional cost each State would have to bear in order to coordinate their regulations?

Mr. MAKENS. I would hope as the bill is finally drafted, in fact, the amount of cost to the Federal Government would be practically de minimis. I would like to see the establishment of minimum Federal standards because I think that's beneficial to the condominium industry and the people who live in the condominiums as a whole. Whether or not we need subsidies and that kind of thing—obviously, the State of Michigan does not need subsidies.

Senator MORGAN. Well, I must say I disagree with you. You apparently feel that the Federal Government can do things that the State of Michigan doesn't do. I just happen to think that you people are doing and can do a better job than we can do here in Washington.

Mr. Larson, you said about 85 percent of the protection that is now afforded under this bill or would be afforded under this bill is afforded in Minnesota?

Mr. LARSON. It is not afforded at the present time, Senator. We have a condominium bill that is in our legislature at the present time. It has passed the House of Representatives and it's pending in a committee in the Senate.

Senator MORGAN. And you think the legislature at least recognizes the problem in this area?

Mr. LARSON. Yes, sir.

Senator MORGAN. And you'd be willing to trust your own faith in the legislature of Minnesota?

Mr. LARSON. Yes. I would say that I believe they will pass such legislation. I believe that such legislation will operate sufficiently to protect the needs of the Minnesota purchasers and operate in such a manner that it does not materially increase the cost of condominium units. If such legislation does not pass, of course, assuming that this Federal legislation passed, we would be subject to this legislation. I see a need for some legislation. I think it can be done at the State level, but absent that, I would support this.

Senator MORGAN. I'd just simply say this to all of you, I'm sure that we can make some arguments for this bill, but I'm also sure that the Federal Government can't do all things for all people and I'm sure that in trying to do all things for all people we're going to do less for les people, and I just happen to believe that you people are closer to the problem than we are. Circumstances vary in different sections of the Nation and I think our legislatures are responsible and responsive and I think our city governments are becoming more and more so, and for that reason I'm not really passing judgment on this bill. There may be some provisions in it that we may want to consider once we look to see what States are not active, whether or not those are States in which there are problems; but basically, I think you have demonstrated here this morning that States can and are doing a good job.

Mr. LARSON. Senator, if I may comment, one of the remarks that Secretary Hills made was in the area of uniformity in disclosure. She proposed that the Federal legislation should preempt all the other States from looking at disclosure. I would just like to say that our experience has been that you cannot dictate, HUD or any other Federal agency, cannot dictate what the uniform disclosure should be. We are very concerned about uniformity in all the areas we become involved with. Mr. Makens and myself are involved in a number of overlapping jurisdictions and in securities and franchises and we work very hard seeking uniform requirements in his State and my State and all the other States.

If HUD is willing to sit down and work with all the States to come up with some uniform disclosure that can be used in all the other States, I would support that, but if HUD is going to dictate and preempt us from commenting on it, I do not think that's an advantageous way to go.

Senator MORGAN. I really think the way to go about bringing about the desired uniformity is just the way you and Mr. Makens are doing, working together, working together with the Commission on Uniform State Laws. If we want uniformity, then the Congress can bring it about by almost abolishing or preempting the rights of State governments altogether and we have gone a long way toward doing that.

Thank you, Mr. Chairman.

The CHAIRMAN. I think this panel has added greatly to the determination, at least on my part, to make sure that we don't preempt the States in providing the protections which they think they ought to

provide. You're experts in this area and I think you have made a very, very convincing presentation.

I just have one other question I'd like to ask each of you to respond to. I think it can be done briefly.

The problem is, aside from the condominiums sold internally, the problem is that the condominium sale, for example, by Florida developers to people who live in your States and other States, Secretary Hills addressed herself to that problem to some extent. Do you see any major problem arising if we prohibit States from proposing provisions of sales to out-of-State residents of their condominiums?

Mr. HEMPEL. Yes, I do, Senator. As the comment was made on that subject previously, for example, in California where we apply the fair and just and equitable standard to out-of-State sales because of the fact that many of them are made either sight unseen or again as more or less captive prospects of the developer, that if we were geared to whatever the minimum standards at the Federal level were, it would be highly undesirable for California citizens. They would have a good deal less protection when buying a condominium located somewhere else than they would in California.

The CHAIRMAN. How about what Mrs. Hills suggested, that you put a kind of disclaimer on each sale so that if people wouldn't have to comply with the California requirements for instance or the Minnesota or Michigan requirements, but a disclaimer saying this sale does not comply with our State law?

Mr. HEMPEL. We think that would be almost as undesirable because the fact is that the sales could be made in California without qualifying with the typical California statutes and I think it would open up the same kind of sales abuses that existed a dozen years ago when the Interstate Land Sales Act was first being talked about and some of those still continue, but it was very widespread and we feel our primary duty is to protect our California citizens. We think they would get less protection under such a regulatory scheme.

The CHAIRMAN. Mr. Makens?

Mr. MAKENS. Senator, under the aegis of the HUD land sale there have been millions and millions of dollars of consumer fraud perpetrated across the United States, including on many residents in the State of Michigan. Where we don't have disclosure documents it just seems to me to create a great regulatory void. I cannot express more deeply my wholehearted opposition to the Secretary's two proposals, first on elimination of all but minimum requirements and secondly, some little note on the front that says "You may be getting ripped off, but here are the things you're not going to know about."

I would also indicate that a good many of the offerings that you're talking about are offerings that will fit within the definition of State and Federal securities laws and I would second Mr. Larson's suggestion that the Securities Act ought to be permitted to remain as they relate to the sale of vacation license type situations or investment condominiums where people may be in them for a week out of the year and the front end risks are just astronomical, particularly in a condominium that has not been built. I'm putting my money up front with the risk that maybe something is going to happen in the future.

The CHAIRMAN. Like we have a situation where one family will provide the regulation of this, both in the SEC and HUD.

Mr. MAKENS. That would be meritorious to the extent the statute can define a line. I think that would make a great deal of sense, but there shouldn't be a line drawn "condominium—automatically HUD." That's the wrong place for the line.

The CHAIRMAN. Mr. Larson?

Mr. LARSON. Mr. Chairman, I oppose very strongly the suggestion by Secretary Hills that the State with the lowest common denominator for regulation should be allowed to prevail in Minnesota. I think if you're faced with the situation where the Minnesota legislature and Governor decided that Minnesota residents deserve this type of protection, then that protection should be afforded irrespective of where the land is. The problem which you're asking about is should you allow—and I'm not citing any specific State—but if you're allowing Arizona condominiums to be sold in Minnesota subject to the Arizona scheme of regulation, while you're requiring Minnesota condominiums to be sold in Minnesota subject to a Minnesota form of regulation, which may be stronger, it is discriminatory. If the Minnesota regulation is going to be meaningful it should be intended to protect all the people of Minnesota and not just those who happen to purchase property in that State. I think that simply indicating that the condominium does not meet with Minnesota law is insufficient. I believe there is a definite need and regulatory scheme that should prevail and it should prevail for the protection of everyone.

The CHAIRMAN. Mr. Lloyd?

Mr. LLOYD. Mr. Chairman, I think the concern that Secretary Hills was expressing was that, for example, a condominium developer in Florida who begins by selling in Florida and preparing a Florida offering circular, then decides that he will market up the east coast and must prepare a Virginia public offering statement and a New York offering plan and so on. This is burdensome to the developer and the burden will ultimately be passed to the buyer.

In Virginia we have provided that the Florida developer can use a modified version of the Florida offering circular and I believe they have a different name for it now—it was called the Florida offering circular—provided it's modified so as to meet Virginia standards of disclosure. So that I don't see the great problem that the Secretary has envisioned. For that reason I would oppose her proposal.

The CHAIRMAN. Ms. Earner?

Ms. EARNER. We have had almost no experience in this area. I can offer a couple personal comments. Our bill that is just before City Council now would permit developers in Virginia and Maryland to continue to advertise their projects in the Washington Post in the classified ads and we wouldn't have to register those projects. They're just advertised in the Post. I think our concern is for the developer who would personally solicit sales and conduct a sales campaign by means of a sales office or a door to door sales force. Those individuals should be subject to our regulation and I feel they should be. In terms of the advertisement, it's up to the resident of the District to respond to that. If he wants to go out and look, that's fine. If he's going to be solicited for a sale in the District, that's something of a different ball game. He's subjected to a little more pressure and they would be under our regulations.

I assume our right to waive our regulations might allow us to modify a statement so it doesn't have to be so comprehensive.

The CHAIRMAN. You don't see any problems so strongly expressed by the previous witnesses of the panel that you should have the right to protect the citizens of the District from being defrauded by out-of-State developers?

Ms. EARNER. I believe I would like the District to have that right. I'm not sure the District or any other large metropolitan area could do the job. I have some personal reservations about whether the District could register every project that might come to advertise in the Washington Post or the Washingtonian Magazine or something of that nature. We could have a monolithic organization as HUD would have.

The CHAIRMAN. We have that situation now. That's what Mrs. Hills was complaining about. She said it's costing a great deal of money, millions of dollars. On the other hand, the States, including the representatives who are here today, the other members of the panel, seem to feel that this is a proper protection which the legislature and Governor have every right to provide their own citizens.

Ms. EARNER. And I suppose I would find myself somewhere in between and speaking from a lack of experience on it that's probably where we're going to remain.

The CHAIRMAN. Are you part of HUD?

Ms. EARNER. No. I'm not. I am with the District of Columbia.

The CHAIRMAN. Because your job description says Department of Housing and Community Development. But that's the District's department?

Ms. EARNER. Yes, sir. That's a newly created housing department of the District Government.

The CHAIRMAN. I was confused. As a matter of fact, we have had complaints when we have some people from HUD on a panel with outside witnesses. No wonder there was no complaint in your case.

Well, thank you very, very much for your most helpful testimony. We appreciate it.

We've received a statement from the American Bankers Association relative to S. 2273 which we will include in the record at this point.

[The statement follows:]

STATEMENT OF
THE AMERICAN BANKERS ASSOCIATION
ON S. 2273
THE CONDOMINIUM CONSUMER
PROTECTION ACT OF 1975

October 23, 1975

The American Bankers Association appreciates this opportunity to comment on the Condominium Consumer Protection Act of 1975 (S. 2273) as proposed legislation before the Senate Committee on Banking, Housing and Urban Affairs. The ABA agrees with the sponsor of S. 2273 that the condominium purchaser deserves and expects fair treatment. The ABA does, however, have reservations which center on the need for Federal legislation to achieve this objective. The enormous amount of attention being given disclosure/consumer-oriented legislation over recent years and the unforeseen results of enacted law and regulation cause us to consider cautiously the action contemplated by S. 2273.

Banks, as the principal lenders of construction funds to the builder/developer and as one principal source of mortgage funds to the individual home purchaser, have significant interest in this legislation.

Real estate finance bankers, who have reviewed this bill, are troubled by the prospect of increased Federal involvement in matters primarily of local or state concern. This reaction is from the standpoint of the lender as well as that of the builder/developer and, ultimately, the purchaser. The Secretary of HUD also questions the need for Federal legislation. As reported in a recent HUD study of the condominium industry, there are states in which more active condominium construction

has been and continues to be underway-namely, Arizona, California, Florida Hawaii, Michigan, Montana, New York, Oregon, Virginia and the District of Columbia. These states account for over 50 percent of all condominium units in the U.S.. Secretary Hills pointed out that in these states law now exists fully regulating the condominium, its construction and sale. Bankers in those states tell us this is fact. Expressed another way, those states having the most involvement in condominium construction and sale are now regulating themselves in an exemplary fashion, considering the youthfulness of the industry. We believe the degree of interest shown by the states generally in regulating the condominium interests within their borders will continue and, therefore, we question the need for Federal legislation in this area at the time.

The cost of compliance with this proposed legislation could create such hardships on the small builder/developer, the heart of the condominium industry, that it might be economically unfeasible to create projects of less than 50 units in size. In support of this thought, consider the provisions of Section 6(a) Subsection 6, which requires "a two-year projection (revised and updated at least every six months) of annual expenditures necessary to operate and maintain the common elements of the condominium project, certified to have been based on generally accepted accounting priciples, and a complete statement of estimated monthly cost per unit for such a two-year period... ", etc. As with the Real Estate Procedures Act (RESPA), the cost of compliance for the "little guy" mounts rapidly. Considering the recent sales history of the condominium, the small builder/developer needs no new discouragement from continuing to support our national housing goals.

Mentioning RESPA stirs the emotions of builders, developers, lenders, attorneys, and the consumer. The American Bankers Association has and can again attest to the costs in time, money and effort created by RESPA and its misapplied Federal control over extremely localized circumstances. The confusion and excessive paperwork brought on by compliance with RESPA causes us to consider very carefully the application of this proposed disclosure-oriented legislation concerning the condominium industry.

Banking's current involvement in condominium construction and sale is very significant. The bank, as a construction lender, through its routine inspection and disbursement procedures continually attempts to insure the quality of the condominium product being constructed prior to the disbursement of loan funds in payment for that stage of development achieved. Banks, as construction lenders, develop a construction clientele known to the bank for quality, reputation, ethics, and a continued interest in the consumer, the bank's mortgage customer, and the community. The bank's interest continues in a project well beyond completion and liquidation of the construction loan. The mortgage customer then enters the bank for financing of the new home. Our interest in timely development, quality construction, and project success is essential in our real estate financing business. We believe the vast majority of builder/developers share this interest. Continued support of that majority is the banking industry's goal. Becoming a part of that supported majority must become the goal of the minority number of builder/developers guilty of abuse lest they find no funds available to them for future projects. The availability of bank funds combined with state and local regulation of condominium construction and sale should help to manage the condominium industry for the future

and limit further problems and abuse. S. 2273 targets the entire condominium industry for Federal regulation while the real target appears to be an extremely small segment of that industry. The problems should fall away as we allow the free enterprise system and local government to function.

In commenting on specific problem areas of this proposed legislation, please consider these points:

1) Section 2(12)

Definition of Developer--The definition is very ambiguous. Where foreclosure of a project becomes necessary we would be concerned as to the possibility of derivative liability as the bank then becomes the seller of properties, and in fact, the owner of the project. The bank would be held liable for warranties, repair, management, etc. none of which is the institution's design at the time of granting a construction loan. We would question the value of national bank venue protection in many cases, which would work a hardship and expense on the lender potentially causing, in the long run, a drop in availability of construction funds.

2) Section 4(b)

Fifteen day "cooling off period"--We feel the 15 days "cooling off period" does not necessarily create additional protection for the consumer but creates difficulty for the developer. It ties up a unit for that 15 day period and creates the legal expense of drawing contracts of sale only to find at the

end of a two-week period of time there is no sale. This ability of the consumer to cancel a sales contract after 15 days would have the effect of causing the consumer to enter into a housing purchase with less thought given the seriousness of their action. Additionally, this section raises a problem regarding ownership of the property securing the mortgage loan should a purchaser void a contract of sale due to inadequate disclosure under Section 6.

3) Section 5(1)

Escrow Account--We agree that the purchaser's desposit should be held in escrow. We would recommend that a third party act as the escrow agent in lieu of the developer holding the escrow funds.

4) Section 5(3)

Control of Common Elements--Setting a specific time period (1 year) at the end of which the developer must relinquish control of the common elements regardless of the number of units he has sold, is too restrictive. Control of the project should be passed to the homeowners association only after a certain percentage, 75-85%, of the units have been sold. As a matter of course, many projects are conceived as 3 to 5 year efforts. If a project is less than 85% sold after 1 year, the developer may have to relinquish control of his project at a time when he has too few units to control the homeowners association yet too many to allow any group to control common element maintenance during the remainder of his sales effort. We believe that the developer

having remaining units to sell will maintain the common elements of his project and that of his unsold units in an effort ot complete the sale of those units.

5) Section 5(5)

Warranty Provision--This provision appears to hold the developer liable for any type of repair with no consideration given to the fact that the maintenance of common areas and unit elements will vary from project to project depending on the income level of the owners, the quality of management, and numerous other variables and deteminants of the quality of the project upkeep. It would be our recommendation that the warranty period be held at 1 year for both the project and the individual units.

6) Section 6(2)

Description of Project--Should allow for a definition of "merger of project".

7) Section 6(3)

Status Disclosure--Should add following "site plan", "school district".

8) Section 6(6)

Projection of Costs--We have commented earlier with respect to the effects of this section on the small builder/developer. In addition, there is no provision for these projections being made by acceptable accountants rather than "acceptable accounting principles". Any approach to these projections, however, would be costly and an unfair burden on the developer.

9) Section 6(8)(d)

Projection of Costs--Which reads: ". . .the monthly cost of utilities. . ." should add, ". . .remuneration, if any. . .".

10) Section 6(10)

Projection of Effects-- This provision should be deleted as it is unfair to expect a developer to judge the effects of area development outside or adjacent to his project for the present or future time.

11) Section 6(11)

Maintenance Features--In general, it is recommended that reserves for the replacement of certain common elements such as heating and air conditioning systems, swimming pools, parking lots, private streets, roofs etc., should be made mandatory and the mandate should be set forth in the by-laws of the homerowners' association. This would serve to protect lenders as well as homeowners insuring proper long-term maintenance of the project.

12) Section 10

Criminal Penalities--It is recommended that a statute of limitations be set for the purposes of this section.

Again, the ABA appreciates this opportunity to comment on S. 2273. Our primary interests are the consumer/customer and our continued ability to support a growing industry.

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The CHAIRMAN. The committee will stand in recess until tomorrow morning when we will hear from further witnesses.

[Whereupon, at 12:20 p.m., the hearing was recessed, to be reconvened at 10 a.m., Tuesday, October 7, 1975.]

CONDOMINIUM CONSUMER PROTECTION ACT OF 1975

TUESDAY, OCTOBER 7, 1975

U.S. SENATE,
COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS,
Washington, D.C.

The committee met at 10:05 a.m., pursuant to adjournment, in room 5302, Dirksen Senate Office Building, Senator William Proxmire, chairman of the committee, presiding.

The CHAIRMAN. The meeting will come to order.

We resume the hearings on the Condominium Consumer Protection Act of 1975.

Our first witness is not here yet, I understand, unless Congressman Lehman has come.

Absent Congressman Lehman, we will start with Mr. James DeLong, Assistant Director for Special Projects, Bureau of Consumer Protection, Federal Trade Commission.

If you could give us your remarks in 5 or 10 minutes, we would appreciate it.

STATEMENT OF JAMES V. DE LONG, ASSISTANT DIRECTOR FOR SPECIAL PROJECTS, BUREAU OF CONSUMER PROTECTION, FEDERAL TRADE COMMISSION

Mr. DELONG. We have filed a statement for the record which provides some detail on technical issues raised by the proposed legislation.

At this point, I will briefly summarize what the FTC is doing, and then answer any questions you may have. I should make it clear that I am giving you my own views, not those of the Commission.

As you know, the Commission has had an industrywide investigation going on for some time. Such investigations can lead the FTC staff toward a recommendation for a trade regulation rule directed at future practices in an industry.

In this case, however, the staff is not tending in this direction. Many people are interested in condominium issues, including this committee, the Congress, HUD, and the States. Given the possibilities of legislation, we do not think FTC staff should devote resources to the development of a proposed trade regulation rule. Rather, at the present time the staff is thinking in terms of redress for past transactions.

As I am sure you know, the Commission has some authority to seek consumer redress for fraudulent activities in the past. The staff investigation is focusing on whether such fraudulent or dishonest things have occurred and whether the Commission should seek consumer redress under the Magnuson-Moss Act. We are pushing the investigation and hope to make recommendations to the Commission in the near future.

Beyond this, I will make myself available for questions.

[Statement follows:]

TESTIMONY OF

JAMES V. DELONG

ASSISTANT DIRECTOR FOR SPECIAL PROJECTS

BUREAU OF CONSUMER PROTECTION

FEDERAL TRADE COMMISSION

BEFORE THE

COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS

UNITED STATES SENATE

OCTOBER 7, 1975

THE REMARKS IN THIS STATEMENT REPRESENT ONLY THE VIEWS OF A MEMBER OF THE FEDERAL TRADE COMMISSION STAFF. THEY ARE NOT INTENDED TO BE, AND SHOULD NOT BE CONSTRUED AS, REPRESENTATING THE VIEWS OF THE COMMISSION OR ANY COMMISSIONER.

Mr. Chairman, I am pleased to have the opportunity to present to the Committee this statement on S.2273, the Condominium Consumer Protection Act. My role will be to comment on particular sections of the proposed bill, then to discuss briefly the activities of the Federal Trade Commission in this area.

At the outset, I would like to make my status clear. I am appearing as a representative of the staff of the FTC's Bureau of Consumer Protection. My remarks do not constitute an official statement of the Federal Trade Commission or any Commissioner.

The Commission staff would like to acknowledge its debt to the Department of Housing and Urban Development for the work done on the study of condominium and cooperative housing. The report itself admits there are gaps, imposed by limitations of data and time. Nonetheless, it provides an excellent picture of the growth of condominiums during the past five years and of the problems that have arisen. Equally important, the report lays out the bounds of those problem areas by discussing their frequency, severity, and geographical extent. It is, of course, important that regulation be cost effective. No one wants to impose costs on an

industry, and thus on consumers, greater than the damage caused by the particular problem. The HUD report analyzes the problems in these terms, and provides a good basis for discussion of condominium regulation and S.2273.

FTC staff is most interested in HUD's examination of problems and abuses. Our investigation and the Department's identified the same problem areas. Since these are also the focus of S.2273, there is no need to reiterate them again here. My staff and I have reviewed this legislation and offer the following comments.

Specific Provisions of S.2273

Section 3(1) exempts projects of fewer than 10 units from the protections of the bill. The HUD study does not contain estimates of the number of units in this category. Two to four unit structures constituted 15% of all condominium starts between 1970 and 1974, however, and it is possible that the exemption of projects with fewer than 10 units will leave a substantial segment of the condominium market unprotected.

The exemption also creates a loophole for large developments. It is perfectly possible for a unified development to consist of a number of small, separate condominium projects. A row of 50 four-unit garden apartments might be a good example. Each might be a separate condominium, even though all were planned and built as a single development. While such an organization might be adopted solely "for the purpose of evasion" of the Act, and excluded from the exemption by the terms of the bill, a developer might argue that there were sound business reasons for the form of the development and that the saving clause did not apply. At the least, there is an ambiguity here which could cause problems.

The Committee may wish to consider exempting projects of less than 10 units except when these are part of a common development scheme.

Section 4(b) provides a 15 day "cooling off" period after the contact of sale is signed and the condominium documents are provided. This would allow the purchaser the time to examine the documents required by Section 6 and to seek legal advice prior to making a binding commitment. This provision requires that all deposits be promptly refunded if the consumer decides during that period not to purchase. This provision would help to eliminate hasty and uninformed decision making.

The FTC has often required cooling off periods, and they are an excellent remedy for unfair or deceptive high pressure sales practices. In particular, the Commission staff believes the unusually long, 15 day period is necessary. Condominium arrangements are technical and complex, and this is a reasonable time to allow for adequate review.

The bill does not require the seller to give the actual legal documents to the purchaser for review, however. It applies only to the special disclosures of Section 6 of S.2273. I believe that at the same time the special disclosure statement is presented the formal documents should either be given the purchaser or made fully available for detailed examination.

Section 5(1) requires that deposits be held in escrow prior to settlement. This would eliminate consumer losses when a builder comingles consumer deposits with construction funds, then goes bankrupt before completing the development. The buyer in that case does not get the unit for which he contracted. He loses his deposit as well, through no fault of his own and contrary to his reasonable expectation that his deposit is tied to the builder's performance. This has not occurred often, but it can be catastrophic for the families involved. This unfortunate situation should be corrected.

In Section 5(2) the proposed legislation deals with a problem that has created much bitterness. Some developers have retained ownership of communal facilities and leased them to the condominium owners. (These are generically called "recreation leases" because they often involve recreational facilities, but they can encompass other installations as well.) As the HUD study notes, and our own investigation confirms, these leases are often for long terms and bear rates with little relation to the underlying value of the facilities. They are sometimes subject to periodic increases tied to indices (such as the consumer price index) that have no relationship to actual cost increases. Recreation leases are often secured by a lien on the consumer's condominium unit. If charges increase beyond his ability to pay, foreclosure may occur.

As a theoretical proposition, recreation leases should have a place in the condominium industry. Such devices should offer a method of financing that might bring condominium ownership and communal amenities within reach of people who could not otherwise afford them.

However, in practice this device has been the instrument of much abuse. Experience so far indicates that the benefits of this device are minimal in comparison to the costs to unwary purchasers. Total abolition of recreation leases may be the only answer. In most cases recreational facilities will still be built, but they will be owned in fee simple by the condominium unit owners.

I do have some reservations about the proposed legislation. First, it seems that it would be possible for a developer to put recreational facilities located on land adjacent to a condominium apartment complex into a separate parcel. He could then contend that he was not retaining any interest in any "common element" because the recreational parcel was now separate from the condominium apartment parcel. Would S.2273 cover this device?

My second problem concerns the case where a development consists of a number of separate condominium projects which share common recreational facilities. Would each apartment owner have a share of his immediate building plus another share of a separate recreational parcel? What if the developments were to be built in sequence over a period of years - S.2273 would make this impossible.

Third, what if condominium ownership carries with it a right to use recreational facilities that are also open to non-resident members or to residents of other condominiums? One can readily imagine recreational facilities with a capacity exceeding the demand generated by a particular project. In such a case it might be advantageous to condominium owners to have the expenses of the facilities spread over a broader basis. This in turn would require ownership and management devices. A condominium owners' association might not be interested in managing a recreational complex, or in making the required capital investment.

The principal problem with recreation leases has been that they lead logically, and perhaps inexorably, to specific abuses. The escalator clause contract has been a leading example. In many instances the nature or capacity of the facilities seems to have been grossly misrepresented. There are the problem created by the tying of the condominium unit and the recreational facility. While abolition may be the only answer, neither the HUD report nor our own investigation has developed adequate information on possible legitimate uses of recreation leases. As

the Committee obtains information in the course of these hearings, it may wish to consider legislation targeted more closely on these specific abuses than on recreation leases per se.

Section 5(3) grants control of the common elements and the owners' association to the unit owners after the first year of occupancy or after 80% of the units are occupied. This provision would avoid the anomalous circumstance of property owners having no control over their property until such time as the seller determines that he will relinquish that control. Commission staff has examined condominium documents having such provisions in the course of its investigation, and believes that they frustrate the buyers' legitimate expectations and tend to produce abuses. The developer's interests are protected by 5(6), which provides that he has the rights of a unit owner for the unsold units.

One minor point is that the term "control" in this section could be defined more clearly. It should specifically include all the functions normally performed by the unit owners association, including the right to elect and remove officers, to amend the association's bylaws, to make contracts on behalf of the unit owners, and to collect and disburse the association's funds.

This does not mean, however, that the bill should force on active management rule on those whose interest in participating in management is small or non-existent. As long as full disclosure is made, it should be possible to establish a condominium in which major management functions are delegated to professionals. The intent of this section is that the developer should not be able to retain control indefinitely. Once this limited intent is fulfilled, it is important not to force condominium government into any rigid mold.

In the same vein, Section 5(4) gives the unit owners the right to choose their own management six months after taking control. Any outstanding management contract entered into by the developer would have to be ratified by the owners as of that time. This is a good solution to a difficult problem. There is an argument that a developer should remain heavily involved in a new project for a time because some unit owners may want professional management, and, as the HUD report points out, the period of transition can be difficult. The bill allows for these interests, and at the same time protects condominium owners from unfair management contracts.

Neither 5(3) nor 5(4) precludes a group of unit owners from retaining the developer as a manager of the condominium association's interests or in any other

capacity the association sees fit. The provision merely permits this decision to be made by the unit owners themselves, not by the developer.

Section 5(5) addresses another set of significant problems identified by the HUD report: low quality construction and the buyers' lack of ability to judge the quality and adequacy of the structure, especially as compared to that of the buyer of a traditional single family home. This provision would require the developer to warrant certain major components of the building for up to two years.

While I cannot claim to be a construction engineer, I see no reason this should pose a problem for new construction. If the builder cannot make this warranty at only slight increase in cost the construction techniques used must be very questionable. Furthermore, the costs of repairing major components are likely to exceed the costs of doing a good job during construction. If the builder is forced to pay the price of his decisions on quality the unit owners should gain.

For conversions, the economics are trickier because the remaining useful life of major components is more uncertain and their original quality is not within the seller's control. To protect himself the developer might have to charge a high premium. The result could be an

undue rise in the cost of converted units and an undue discouragement of conversions. FTC staff has no real basis on which to judge the feasibility of the bill's proposals. A rigorous requirement of disclosure that there is no warranty might be preferable. In a competitive market, this would provide a substantial incentive for a converter to provide guarantees if at all possible.

There is another technical difficulty with Section 5(5). It says nothing about the terms, conditions and limitations of the required warranty. As the Magnuson-Moss Warranties Act (P.L. 93-637, 93rd Cong., 2d Sess., Jan. 4, 1975) shows, these questions can get very complicated.

Section 5(6) would eliminate what has been called the "funding fee" rip off, which requires consumers buying into a condominium development in its early stages to pay the maintenance charges for the developer's unsold units. Commission staff does not understand why persons who have already purchased the developer's product should be obliged to pay the maintenance costs on his unsold inventory. We also believe that provisions such as this are usually buried in the fine print of the condominium documents. The practice should be limited.

The only objection to this is that part of the assessment on unit owners may be based on expenses incurred only if a unit is actually occupied (e.g., utilities, trash collection). It would be fairer to exclude such variable charges.

Section 5(7) sets a standard for treating displaced tenants in conversions. This provision would require that tenants receive an option to purchase for 90 days and 120 days written notice prior to being required to vacate. Obviously, tenants deserve adequate notice, and these periods seem fair.

Section 6 of S.2273 prescribes national standards for disclosure by the developer of all major features of the condominium project and the terms under which any unit is offered for sale. Since so many of the consumer problems with condominiums are related to the complexity and novelty of the transaction, and since there have been so many misunderstandings and misrepresentations, FTC staff strongly endorses the disclosure principle.

The only major issue is whether the disclosures would require costly procedures for collecting information. With the possible exception of Section 6(7), I do not think they would. All the information required should be known to a reasonably prudent developer, and the only added expense should

be the cost of writing it up and printing it. Given the magnitude of the condominium purchase, this added expense should be de minimis.

Staff does have some comments on specific provisions.

The section 6 disclosures must be made to "each prospective purchaser." Since the bill would be enforced by civil and criminal penalties, a bright line standard on when a potential buyer achieves this status would be useful. For example, is a reader of a newspaper ad included, or the recipient of a mailed flier?

Sections 6(a)(2) and (10) require a prospect to be informed about the number and nature of present and possible units in the project itself, and about non-residential development in or near the project. It should also include nearby prospective residential development known to the developer, even if not part of the project itself. This also influences the desirability of a condominium.

Section 6(a)(3) addresses the problem of delayed completion by requiring disclosure of the status of construction and the actual or scheduled dates of completion of the building, recreational facilities and other common elements. The FTC staff investigation of the condominium industry has developed information

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that substantial delays in completion of projects are frequent and cause significant injury to purchasers. However, disclosure of actual or scheduled completion dates will not eliminate the injury because there is no remedy for non-completion. Section 9's provision for civil penalties is ambiguous. As staff reads Section 9, it creates a remedy for failure to disclose the actual or scheduled completion date, but not for failing to meet the stated date. The Committee may wish to consider a private remedy for undue delays and a statement of any circumstances excusing the developer from liability for such delays.

Section 6(a)(6) requires a two-year projection of annual expenditures for the operation and maintenance of common elements as well as a detailed estimate of monthly costs. It speaks to another major deception which can be perpetrated by a developer, "lowballing" or understating common expenses.

I think that any competent developer will have prepared such estimates in the course of his own planning and that it is reasonable to require this revelation. To bolster the protections afforded by the projection, I recommend adding an incentive to assure reasonably accurate projections. Large unexplained discrepancies between actual and projected costs should raise a presumption of intentional misrepresentation.

Sections 7 and 8 are designed to encourage assumption by the states of primary enforcement responsibility, providing the state has a plan approved by HUD. The administrative issues raised are intricate, and we must defer to HUD.

Sections 9 and 10 provide for civil and criminal penalties, respectively. FTC staff has grave reservations about both sections.

First, we are far from convinced that this is an appropriate area for criminal penalties. The objective of the bill is to protect condominium purchasers, and compensate them for injury, at the lowest possible cost. The use of criminal sanctions will force developers to take elaborate and expensive precautions to avoid any risk. The costs of these will be passed on to buyers. To compound the problem, most of the cost of compliance will ultimately be paid by those buyers who least need the protection. Scrupulous developers will be the most careful and will spend the most on double-checking.

A good system of compensating buyers for harm caused by violations would be more effective and efficient. To this end I recommend three changes in section 9:

(1) A right to rescind should be included as a remedy as well as the proposed right to damages;

(2) The bill should make clear that the remedies are available for material non-disclosures. As drafted, it is not clear whether inadequate or false disclosures count as compliance;

(3) State or HUD officials should have authority to sue a developer for violations and a determination that all contracts are voidable. This would complement the injunctive authority of section 12.

The remaining sections concern issues of jurisdiction, venue and regulation, on which FTC staff defers to other agencies.

FTC Involvement in Condominium Problems

After a preliminary investigation by staff attorneys, on June 25, 1974, the Commission authorized a formal industry wide investigation of condominium practices. Commencement of the investigation was publicly announced on July 4, 1974.

The work of the staff in conducting this investigation has included research on the condominium industry, evaluation of consumer complaints, and interviews with consumers, developers, state officials and others with knowledge of condominium practices. The staff has also obtained and is reviewing legal documents, promotional materials and other information pertaining to condominium developments all over the country.

In making its recommendations to the Commission the staff has two major options. First, it could suggest that the FTC promulgate a Trade Regulation Rule prohibiting specific unfair and deceptive practices in the condominium industry. At the present time, I doubt that the staff will recommend this. Both HUD and the Congress are intensely interested in the issues, and there appears to be a good prospect of legislation. For FTC staff to pursue this possibility now would duplicate work being done more effectively elsewhere.

Prospective legislation does not cure past harm, however. Unlike the other governmental bodies involved, the FTC has a mandate to seek relief for consumers who were subjected to unfair and deceptive practices in the past. The second alternative is to investigate the possibility of recommending litigation to provide such relief in specific cases. Redress for fraudulent or dishonest conduct can be sought under the recent Magnuson-Moss Act. In addition, the Commission may have general authority under Section 5 of the Federal Trade Commission Act to prevent a developer who has engaged in past unfair acts or practices from continuing to gather the fruits of this conduct in the future. This alternative seems to be the best use of staff resources.

One of the FTC staff's major concerns is for those purchasers who have condominiums with such appurtenances as escalator-clause recreation leases or management contracts. Given the present state of consumer distaste for these devices, such units may be almost completely unmarketable. Ironically, the greater the protection offered condominium buyers in the future the more disadvantaged these unfortunate past purchasers will be. This is no reason not to protect future buyers, of course, but it is a good reason to be specially concerned with existing owners.

As a staff member, I cannot, of course, predict the response of the Commission to any proposals which the staff may make. I must also emphasize the legal complexity and novelty of this area. However, the investigation is proceeding and we expect to make specific recommendations to the Commission in the next few months.

The CHAIRMAN. I am concerned about the fact that the Commission seems not to have given us much detail in the statement. Yesterday, I asked the Secretary of HUD whether we could do anything about the abuses that occurred to date.

She said we could, but shouldn't make this legislation retroactive. We are considering prospective legislation.

But I think it is important for the committee to know what the Commission intends to do to clear up existing abuses.

Since this affects what we do on the bill, that is important.

As you know, I was one of a number of Members of Congress who criticized the Commission for cutting off its condominium investigation last March.

FTC appropriations bill contains language approved by the House and Senate requiring the Commission to resume this investigation, including $75,000 additional for that purpose.

In view of that language and in view of the fact the Chairman of the FTC received an invitation to appear before this committee, I don't understand why you can't give us any definite information on what you intend to do about the investigation.

Mr. DELONG. The investigation has been resumed and is going on now. I cannot give you definite information about what the Commission itself will do, of course, but the staff will make recommendations to the Commission as to the actions we think it should take. The Commission will have to decide whether we have met the burden of proof on this.

It will come up before the Commission as an adjudicated matter.

The CHAIRMAN. Why couldn't the Commission send us a statement giving us a more comprehensive understanding of their investigation, what they are doing, and where they are going and so forth?

Mr. DELONG. Mr. Chairman, I cannot be specific in the sense of saying that we are investigating developer X at the present time or that we intend to send a complaint forward to the Commission concerning a particular developer. I can say that the staff has found a number of situations in which we believe there is a legitimate argument that unfair, deceptive, fraudulent, or dishonest practices have occurred or are occurring.

We all agree on the types of practices that have been causing the most harm. We all agree particularly——

The CHAIRMAN. As I understood it, you would have test cases. Are you pursuing that line?

Mr. DELONG. Yes. We are particularly concerned about those instances in which past transactions have imposed a particular continuing burden on the unit owners, such as management contracts, recreation leases, escalator clauses, and which can make a unit virtually unmarketable.

The CHAIRMAN. When can we expect cases to be filed?

Mr. DELONG. I expect we will make recommendations to the Commission within a very few months. I should make clear that the Commission may reject our recommendations. I am speaking only for the staff.

The CHAIRMAN. Do you think successful challenges as to recreation leases and sweetheart contracts and court would obviate the need for the legislation?

Mr. DeLong. No. There is no private right of action under the FTC statute. It seems to me that general legislation laying down particular standards is clearly preferable to a case-by-case approach.

The Chairman. This bill would prohibit leases of the recreational facilities or any other common element of a condominium.

HUD opposes this provision, saying that the recreation leases can be a good thing in that they can reduce the purchase price. Your statement, as I read it here, suggests that the potential for abuses in this area outweigh the potential gain.

Do you think we should retain the ban on recreation leases as it is in the bill?

Mr. DeLong. In the abstract, one would think that there ought to be a good use for these, in terms of making facilities available and increasing flexibility in the whole condominium industry. As these devices have been used in practice, however, it seems they lead almost inexorably to abuses. Nor did the HUD report on condominiums give us much specific information on possible legitimate uses, or much in the way of specific example.

My own view is that abolition may be the only answer. I have some reservations about this because there may be additional information which could change my mind.

The Chairman. Your statement indicated the ways that the developer may be able to get around the lease ban contained in the bill.

Do you think we should go further to prohibit tie-in arrangements in condominium sales?

Mr. DeLong. If you eliminate the tie-in aspect, you eliminate much of the harm caused by these leases. The unit owner would have the option, and would be less susceptible to pressure selling.

There would still be real disclosure problems. There is an interaction between these leases and the complexity of the documents. Even if tie-ins were legally eliminated, much would depend on the nature of the disclosures.

The Chairman. You comment on the requirement that actual or potential completion dates be exposed. You are correct that delays in dates affect and are harmful to the interest of the condominium buyers.

Can we strengthen that provision to give a private remedy for undue delays?

Mr. DeLong. I think you have stated the answer. There should be a private remedy for the undue delays, possible right of rescission if the delay is over a given period.

The Chairman. How do we define undue delay?

Mr. DeLong. My understanding is that delays in the construction business tend to be endemic, anyway. I have no expertise on what would constitute a fair standard of undue in these circumstances. However, I would think that it would be possible for you to find out from people in HUD, who have a lot of experience with construction, where a reasonable line may be drawn.

Obviously, no line is perfect, but I think one could find a reasonable place to draw it.

The Chairman. You question whether it is appropriate to include criminal penalties in the act. Since the committee is sensitive to the problem and cost of white-collar crime, there is some feeling that criminal penalties could be a deterrent.

Could you elaborate on your conclusion about the criminal penalties?

Mr. DeLong. The basic concerns of the statute is to find some way to prevent abuses and to compensate consumers when abuses do occur. This should be done at the least possible cost.

The difficulty with criminal penalties is that they can force scrupulous developers to spend a great deal of money to make sure they are running no risk of noncompliance. Those costs will be passed on to the buyers.

It seems to me that civil remedies enabling a buyer to get his money back or rescind the transaction might actually achieve your purpose at somewhat less cost. Furthermore, the costs involved would be borne by the dishonest developer, and not by everyone.

The Chairman. You support the 15-day cooling-off period, something that gives some members of the committee some concern in view of our situation with Reston.

Some have said that 15 days is too long or that a waiver may be needed. Can you comment on that?

Mr. DeLong. Yes. In connection with cooling-off periods, the FTC staff has been cynical about waivers because they tend to become part of the boilerplate in a contract.

In the condominium situation, one can assume that one is dealing with buyers of some sophistication, and a waiver may be acceptable if the disclosure is adequate and very strong. I hesitate to say this because I share the skepticism. But compulsory cooling off periods have caused problems in some contexts, and it is probably worth the risk here.

In this situation, one can assume that one is dealing with buyers of some sophistication.

A waiver may be acceptable if the disclosure was adequate and very strong. I hesitate to say that because I share the skepticism.

The Chairman. Thank you very much. You have been helpful and responsive.

Has Congressman Lehman arrived?

STATEMENT OF WILLIAM LEHMAN, REPRESENTATIVE IN CONGRESS FROM THE STATE OF FLORIDA, ACCOMPANIED BY ALAN S. BECKER, REPRESENTATIVE, 103D DISTRICT, MIAMI BEACH, FLA.

The Chairman. We are delighted to have you this morning. You have a handsome, tan, Congressman Lehman, which is a good ad for your district.

Mr. Lehman. Thank you very much.

I want to compliment the Senator and this committee for undertaking this legislation. Certainly the experience I have had in the south Florida area indicates the need for the kind of relief for the condominium owner that you have been addressing in the work of this committee.

In the 13th Congressional District, perhaps it is not only one of the most condominiumized districts in the country, but the first condominium development.

The Chairman. Does your district encompass Miami Beach?

Mr. LEHMAN. Suburban Miami Beach. Some of the very first new condominium experiments at that time was in the 13th Congressional District in suburban Miami and suburban Miami Beach.

This area experienced some of the original abuses. You are aware of those abuses. I heard you mention a few minutes ago, the sweetheart contracts between developer and management.

We have the problem now that is coming on which is the conversion of apartments, rental units, into condominiums and the abuses in these kinds of conversion and also the problem of dealing with the kind of warranties in the purchase of these condominiums that seem to be, at this time, not fully protective of the condominium owner.

As we—as is apparent, this committee is involved in this area because of the rapid growth in the use of condominiums as a substitute for old single-family dwellings.

In south Florida, the value of land has skyrocketed to the point where the conventional use of 75 by 125 plots are no longer justified in relation to the cost of the single-family dwelling.

I believe that the condominium concept, if properly used, will be the home of the future in most of our metropolitan and suburban areas.

But I didn't come here to tell you about my experience with condominiums, although I will say one-half of the time I spend in the district is involved with various condominium groups.

We have with us today someone that is far more an expert than I am in this whole situation. He is Representative Alan Becker of the Florida Legislature, who I would, without fear, categorize as the number one condominium expert in the whole country, even with the possible staffing membership of this committee.

He was one of the first involved in this. He has been involved in writing legislation. He has been involved in litigation in regards to condominiums.

At this time I would like to yield back whatever time I have to my friend Alan Becker from the 13th Congressional District in Florida Legislature.

The CHAIRMAN. We are delighted to have you, Mr. Becker. You have a prepared statement that is concise. If you would like to abbreviate it in any way, we would appreciate it, and the statement will be printed in full in the record, including the biographical sketch that is appended.

Mr. BECKER. Thank you, Senator. I want to thank Congressman Lehman for suggesting to the committee I be invited.

Rather than go through my statement—I tried to get it to 5 minutes, but my standard 40-minute speech reduces to 8 rather than 5.

I would like to discuss the statement briefly and perhaps relate to the extent possible to the proposed Federal legislation our experience in Florida.

Many of the provisions of your proposed bill do relate or are against some of the provisions we have in Florida. The abuses we uncovered in Florida are described in the HUD report. They were there long before HUD noticed them. Misrepresentations abound. My favorite example was the tennis club condominium that had no tennis courts. Other sorts of misrepresentations are the inaccurate underestimates of operating expenses, which is very common. Completion dates is a serious problem. Warrantees is a very serious problem because of the

developers lack of interest in the future of the project. Your engineer says you can save $35,000 by getting this air conditioner, which will not work 5 years hence. Too often these people don't follow their own plans and specs or building codes.

The consequences of expensive developer control are many: the developer's failure to pay his expenses for unsold units is one. Misappropriations—I call it stealing—of association funds for developer purposes such as personnel and payroll doing warrantee work.

The entry of the developer into the management contract with his alter ego usurping management functions from the association and benefiting the manager for an extended period of time is a problem.

The recreation leases—I don't know why when the FTC talks they are afraid to say they violate section 1 and 2 of the Sherman Act. There is private litigation pending already in the Southern District of Florida. The attorney general of our State has taken that position as well. The rec leases, which again is the developer, while in control of the association, entering a contract with himself or his alter ego, his lessor for 99 years.

The average lease returns 50,000 percent profit if it is any good at all. The lien on the unit is persuasive.

I don't want to give the impression that all problems are developer related. They are not. HUD accurately predicts that as developer problems are resolved by legislation, litigation, agency action, one of the big problems we will see is the problem of the people interrelating among themselves in order to operate a democratic housing community in that area. I don't think Federal legislation would be appropriate.

Florida legislation dealing with the internal operation of a condominium has helped us make some progress in that regard. Our condominium act is not entirely successful. It is a vast improvement over what we had before, the 1963 act, which is merely enabling.

The author of that act, who is a developer's attorney, wrote an article which the staff may have discovered in the University of Florida Law Review of 1965. He warned that if the industry didn't clean its own house, the Government would. The Government is getting there: our Florida act dealing in the area of openness and participation by condominium members. All members have access to books and reports, insurance policies, meetings of the board of directors being open, approvals of budgets that exceed 15 percent over the prior year.

Associations are strengthened to represent the members. For the first time, there is an implied warranty of merchantability and fitness which applies against the developer, contractor, subcontractor, and suppliers for a period of 5 years that can be reduced to 3 years by early relinquishment of developer control or the statement of an engineer certifying the condition of the building.

Florida law mandates turnover of control to unit owners other than the developer within 3 years of 50 percent of the units being sold or 90 days or 90 percent sold.

Deposits are a big problem. We say you must escrow the first 5 percent of the selling price. The rest may be used in construction. We should escrow it all or bond it all. This has been a real problem this year. Millions of dollars have been lost by consumers.

I think, too, the committee may profit from looking at the role lenders have played in the losses. Negligence of lenders has contributed to it.

We should have eliminated the recreation leases. We have restricted them, requiring greater disclosure in that regard. This year we did pass a law declaring the escalation clauses in the leases to be against public policy and void. They do apply retroactively. We deal somewhat inadequately with the question of conversions. It is similar to the provision in the proposed Federal law. As I said, the emphasis is on disclosure, although there is more to it.

In order to make the act more meaningful, as of October 1, there is a division of land sales and condominium authorized to enforce the Condominium Act by cease and desist orders, arbitration.

This law is better than what most States have and may provide a good model for Federal legislation.

I have reviewed the bill before the committee. I am prepared to relate it to our experience if you so desire.

[Complete document follows:]

FLORIDA HOUSE OF REPRESENTATIVES
Tallahassee

Alan S. Becker
Representative, 103rd District
Reply to:
☐ 4014 Chase Avenue, Suite 212
Miami Beach, Florida 33140
(305) 538-3606
☐ 414 House Office Building
Tallahassee, Florida 32304
(904) 488-5102

OCT 2 1975

Committees:

Regulated Industries & Licensing,
Vice Chairman
Finance & Taxation
Judiciary

STATEMENT PRESENTED TO THE COMMITTEE ON BANKING AND CURRENCY, UNITED STATES SENATE, ON OCTOBER 7, 1975, BY STATE REPRESENTATIVE ALAN S. BECKER

In 1963, Florida passed its original Condominium Act. That law was merely enabling legislation which provided no protection at all for the consumer. The industry mushroomed and so did the abuses which include the now infamous long term management contracts and recreation leases. As early as 1965, the author of the '63 Act wrote an article in which he described those contracts as "perverting" the act and he called upon the industry to police itself or face government regulation. The anguish of hundreds of thousands of Florida condominium buyers finally led our Legislature to take belated action by passing a complete revision of the Condominium Act in 1974 and some additional modifications in 1975.The new law sought to remedy certain abuses that appear with consistency, to some degree in every condominium. Those problem areas are:

a) Misrepresentations. Almost invariably the developer promises, through advertising or other promotional activities, more than he delivers. My favorite example is the "Tennis Club" Condominium which had no tennis courts, but other examples include understated estimates of operating costs, unrealistic completion dates and models which bear little relation to the finished product;

b) Warranties. The developer's object is to build, sell and get out. He has no financial stake in the future operation of the project. Cost cutting is the rule. As a result, many if not most projects are not constructed in a good and workmanlike manner, are not constructed according to developer's own plans and specifications, and are not even built in accordance with local building code requirements;

c) Extended developer control. By setting himself or his designee up as initial officers and directors of the condominium association, usurping the unit owners' right to self government often for several years, the developer creates certain additional problems:

(i) Misappropriated funds. Too often many thousands of dollars are spent on developer purposes such as construction or warranty work. Instead, the Association funds should only be spent on legitimate Association (maintenance) purposes.

(ii) Management contracts. Described by one Florida Supreme Court Justice as "long term contracts of adhesion" these are sweetheart deals between the developer controlled

association and the developer controlled management company for X number of years on terms completely favorable to the manager, exluding the association and its members from the running of the association.

(iii) Recreation Leases. These, like many of the management contracts, probably violate §1 of the Sherman Act which prohibits tie-sales as restraints of trade. The Federal Trade Commission should have taken action on this long ago. In this scheme the developer retains title to the recreation facilities (sometimes vast facilities, sometimes just a small pool), requiring the unit owners to pay a monthly rent for the use of the facilities whether they use them or not. The leases are usually net-net with the owners paying all taxes, insurance and maintenance costs. The rent is secured by a lien on the condominium. Usually the rent increases periodically with increases in the cost of living index (it does not decrease, however). A typical lease will return 50,000 per cent on the original investment.

Another problem unrelated to the developer is that of people living together in a democratic housing community. Lack of understanding of the condominium concept, democratic operation of multi-million dollar complexes and equitable enforcement of rules and regulations all play a part in the interaction of condominium owners.

The Florida Legislature has attempted to address itself (with varying degrees of success) to all these areas and more.

Our present law, in most basic terms, provides for "condominium in the sunshine": meetings of the board of directors are open to all members; all members have access to association insurance policies, minutes, and books and records. Increases in budgets are restricted to 15 per cent over the prior year without unit owner approval (if the board is developer controlled), or acquiescence. Almost every aspect of the creation and operation of the condominium is now spelled out in detail with the emphasis on openness and participation. The Association's powers are broadened, including the right to represent its members in legal matters of common interest. The developer's practice of not paying his share of maintenance for unsold units is severely restricted.

For the first time there is a statutory implied warranty of merchantability and fitness which applies against the developer, contractor, subcontractors and suppliers for a period of five years that can be reduced to three years by early relinquishment of developer control or the statement of an engineer certifying the condition of the buildings. The remaining problem here is the question of developer's solvency to stand behind the warranty three or five years down the road. Most were shell corporations in the first place. To be effective the warranty law needs a bonding requirement.

The Florida law mandates turn over of control to unit owners other than the developer within three years of 50

per cent of the units being sold or 90 days of 90 per cent sold. This is a step in the right direction but is not fast enough. Once owners have control they can, by 75 per cent vote, cancel any contract made for them by the developer controlled board.

Deposits is a big problem area. The statutes require that the first five per cent of the purchase price be held in escrow, but the rest of a deposit can be used in construction if that fact is disclosed. Events of this year prove the inadequacy of this provision. Thousands of Florida purchasers have lost millions of dollars as a result of insolvencies. Here too, perhaps bonding of deposits is the answer. Some consideration should be given to the liability of lenders as well, since many of the failures were brought about by their negligence.

The Florida law now requires developers to file their commitment for phase developments prior to construction and be bound by it.

The leases should have been eliminated, but instead have been restricted. The law requires disclosure of what property is covered by the lease and how many people will be using the facility. Rent need not be paid until facilities are ready for use. There is an option for purchase of the leased facilities at the end of ten years, at fair market value. Unfortunately, existing leases were grandfathered. In 1975, escalation clauses in condominium leases were declared void as against

public policy.

The law deals -- though inadequately -- with conversions from rental to condo, providing for extensions of expiring leases for 120 days and restricting lease clauses that cut short the term of the lease in order to effect a conversion.

Much of the Act is devoted to disclosure. A developer is required to file a prospectus as well as other disclosure materials and the disclosure requirements are extensive. Remedies for misleading statements were strengthened and purchasers can now rescind a purchase agreement up to 15 days after receiving all disclosure materials or the signing of the contract whichever is later.

As of October 1, 1975, there is a Division of Land Sales and Condominiums authorized to enforce our condominium chapter by use of cease and desist orders, injunction and arbitration.

Florida's Condominium law is certainly imperfect. However, it does provide a suitable model if Federal legislation is enacted to set minimum standards for other state laws.

The CHAIRMAN. Thank you. I appreciate your testimony; particularly the fact, Mr. Becker, as Mr. Lehman generously said, you have had more ability demonstrated in this area, more expertise and understanding than almost any legislative official in the country.

Mr. LEHMAN. Senator, would you yield for a moment?

The CHAIRMAN. Certainly.

Mr. LEHMAN. We were talking the other day and Mr. Becker addressed a group in Palm Beach County recently, of condominium owners from one condominium development. In the auditorium there were 5,000 people to hear him speak on condominiums. You don't find these kind of single-issue groups getting together very often.

From a political standpoint and standpoint of concern, probably the No. 1 issue that forms a unity for a single purpose, is the condominium issue in south Florida.

These are the kinds of groups that are seeking relief. They are seeking it individually. They are seeking it in their organizations. I want to again commend this committee for being responsive to the needs of these mainly retired, fixed-income people that have nowhere to turn except for this situation where you can help in the redress of grievances.

The CHAIRMAN. This legislation is far from home free. It may not be enacted. There is strong opposition in Congress and in the committee. Part of the opposition is based on the notion that this ought to be left to the States. Florida has done quite a bit. California has comprehensive legislation. The opinion has been strongly expressed that the States ought to be able to handle it themselves.

First, Mr. Becker, as a State representative and one who has taken the leadership in Florida—which has had more experience than any of the other States—why can't the States do this?

Mr. BECKER. They can but they haven't. Florida has done an admirable job if the bill was passed in 1965. The bill we now have was too late. I think Federal legislation is necessary to protect consumers, particularly in those areas of the country where they haven't experienced the boom in condominiums that is coming.

Experience should not always be the teacher. Our experience in Florida should be sufficient to provide a lesson for those areas of the country that haven't yet experienced this.

Yet we know that this is not going to be the case. We know that States will not react—States will react. They will not act. They will not provide protective legislation that is needed.

I think the approach taken by your bill is a good one, to establish minimum standards and to permit the States flexibility within those parameters.

The CHAIRMAN. Of course, the people who are opposed to this legislation argue that it ought to be up to the State to decide whether they need it or not. Condominiums are concentrated heavily in relatively few States. They have enormously expanded, however, in the last 5 years. They are arguing that after all they believe in State initiative. States are closer to the people. The States know what peculiar problems their particular State may have. The State can work something out that would be preferable.

I think you have answered that. Let me go on to ask you: Why should not the State be free to specify tougher standards than

national consumer protection standards with respect to out-of-State people who are selling in the State?

What I am getting at is the position taken by the Secretary of Housing and Urban Development yesterday. She indicated that one of the advantages of the Federal legislation would be to have a uniformity and not have the people who are selling condominiums—and they sell more in Florida out-of-State than any other State in the Union—she argued it would be greatly useful to both the consumer and developer because you reduce the cost enormously if you didn't have to comply with all kinds of State laws that sell condominiums, in New York, Michigan, Wisconsin, and Illinois. You would not have to comply with a great variety of consumer requirements, some of which may or may not be necessary, but are different.

Mr. BECKER. I think there is merit in what the Secretary says. The Federal Government can preempt the field. I don't know that it would be wise to do so. The only area that has become a problem for developers, an inordinate burden on them, is under Louis Levkowitz in New York. That is probably the only place that Florida developers, as a whole, have been kept honest, or relatively so. Perhaps there is merit on the other side, too.

The CHAIRMAN. I don't understand the principle of why a State shouldn't be free to protect its own consumers, that is, require that people from out-of-State who want to sell condominiums would have to comply with the consumer laws of that State.

Mr. BECKER. I think a State ought to be able to.

The CHAIRMAN. The solution suggested was ingenious. It may not go far enough. It is an ingenious attempt at compromise. Secretary Hills said they simply specify in the out-of-State sales that they do not comply with the States' requirement but they comply with national requirement, so the buyer would be alerted to the fact that he is not getting full protection.

Mr. BECKER. The disclosure materials are so extensive as it is. You come to a question of merit regulations versus something less than that. We are presently engaged in this debate in Florida over a question of securities' regulations. I do not subscribe to the theory that the red stamp solution is the correct one; warning that this issue may be dangerous to your health doesn't do it. We know that from other products.

It becomes your philosophy of government, whether you think government has an obligation to protect the consumer from adverse market influences or merely warn him of them.

The CHAIRMAN. There is another problem. I mentioned this to the previous witness. You may be aware of the problems we have had with the Real Estate Settlement Procedures Act. It has been a nightmare. It is complicating and increasing the cost of sellers and lenders and many consumers have been dissatisfied with aspects of it. We want to avoid that as much as we can in this legislation and make it as simple as possible. One of the suggestions I made yesterday was before we enact this legislation, we should have HUD provide the forms they expect to use and the procedures, so we can work that out with the people in the industry to find out whether or not they can do it with a reasonable cost and in a reasonable time.

What do you think of that?

Mr. BECKER. One of the things we have done in the Florida Act which has been successful in avoiding the complexities which are predicted, is set out the form we are going to require and set out the language in the Act.

The CHAIRMAN. You did that in Florida?

Mr. BECKER. Yes. I think it is probably better. One of the major criticisms I had in reading the proposed Federal legislation is that it claims not to be a red-tape producing bill. To the contrary. Where you give that kind of vast authority to the Secretary of HUD, it is going to be, it has to be. I think more legislative direction in the inception would probably avoid those problems later on.

Mr. LEHMAN. Would the Senator yield?

I think that any move we can make toward uniform forms as the one you are talking about or standardized forms, would be most helpful. When I speak to condominium groups the big problem they tell me is that as nonlawyers, they sign 75- and 100-page documents during the purchase of their condominium. It is impossible for them to understand what they were signing for and what they were obligating themselves for.

The very complexity of the condominium agreement between the purchaser and developer is one of the pitfalls of that agreement, which I hope we can address ourselves to at the State and National level.

The CHAIRMAN. That is a good point, Congressman Lehman. I am glad you made it. We want to avoid that for the consumer as well as the burden on the industry.

Finally, since the problems of recreation leases have occurred in Florida and since the Florida law includes provisions to remedy these problems, is there any need for Federal law to prohibit recreation leases?

Mr. BECKER. Florida law does not prohibit recreation leases. It should. It was passed in the House and not adopted by the Senate.

The CHAIRMAN. Why didn't they adopt it in the Senate?

Mr. BECKER. Disagreement over the basic philosophy.

The CHAIRMAN. That would trouble very able and concerned members of this committee who feel after all, if the sovereign body of the legislature in the State doesn't want it, why should the Federal Government impose it on them?

Mr. BECKER. You have to start with the concept first of all——

The CHAIRMAN. The Senate didn't pass it. If the legislature doesn't act——

Mr. BECKER. Legislative action is no indication of legislative intent.

The CHAIRMAN. What infuriates people is to say that the bureaucrats in Washington know more of what the people in Florida need than their own legislature.

Mr. BECKER. I can understand congressional concern with that. There are overriding Federal policies. One is the Federal antitrust laws and Congress' right to expand upon that. I think recreation leases can be approached from that viewpoint of legislative intent.

I think, too, we have at any level the inherent obligation once we recognize the concept—in this case if we decide we will legislate in that area, we have an obligation to legislate wholly.

It is a question of how far you wish to extend the power of Congress.

The only reason I am for it here is because our State hasn't done a good job. If you were talking about something else, I may say, "Hell, no. Don't do it in my State."

Mr. LEHMAN. In regard to recreation leases, it is true that Florida today, over half the condominiums are being sold with the recreation leases involved. In southeast Florida, the people why buy condominiums have gotten smart and any condominium agreement that involved recreation leases almost condemns the sale of the condominium because it is a dirty word in the condominium purchase.

The recreational lease was not a bad idea. It was abuse of the recreational lease, the fact it was tied to the cost of living in degrees of cost of food, whichever was higher, and squeezed people on fixed incomes with escalating recreational leases where they didn't own their own home. They had only bought a right to pay an escalating rent for the recreational facilities.

This is the abuse of the recreation lease that has been such a hardship. What is happening in Florida—and I think Representative Becker can bear me out—is that many of the condominium units are now buying back their recreation leases, getting them financed through various major institutions.

Perhaps we need some kind of legislation to structure a good method for the people who are locked into the recreational leases to buy them back, to get off this escalation process they are on and to acquire and to live with a self-owned and self-contained 25-year, instead of 99-year, recreation lease.

Perhaps Representative Becker can expand on this, because he is more involved than I am.

Mr. BECKER. Senator, there is a comment I would like to make, if I might, with respect to the prior question about congressional involvement in a State—what may be perceived as a State concern on leases.

First of all, I think Congress can say, if you are going to sell condominiums, you must sell condominiums. It is regulating a business as much as regulating the use of land.

More important, the recreation leases would not have occurred had it not been for the instigation in many cases, acquiescence always of the federally insured lending institutions which made loans on that portion of the developer's project at the inflated value. They sought to get every last bit out themselves; the Federal Government, through the federally insured institutions involved.

If there is an abuse that arises as a result of that, they have an obligation to do something about it.

The CHAIRMAN. Thank you, gentlemen. That is most helpful testimony. We are grateful to you.

Our next witnesses are Mr. Wayne S. Hyatt, Georgia Association of Condominium Owners; Mr. Richard Arkin, National Capital Condominium Federation.

I would like to ask Mr. Cruickshank, if he is here, the National Council of Senior Citizens, to come up here. If he is not here, I understand there is someone with his statement who will fill in.

STATEMENTS OF WAYNE S. HYATT, GEORGIA ASSOCIATION OF CONDOMINIUM OWNERS; RICHARD ARKIN, NATIONAL CAPITAL CONDOMINIUM FEDERATION; AND DAVID MARLIN AND ERICA WOOD, NATIONAL COUNCIL OF SENIOR CITIZENS

Mr. HYATT. I am Wayne Hyatt, president of the Georgia Association of Condominium Owners. I have submitted a prepared statement. I will not dwell on the statement or any of the points I have raised. If the Senator would allow me, I would like to touch on a few potential objections that those opposed to this worthwhile legislation might raise.

I pick these potential objections out, based on our experience in the Georgia legislation enacted last February, a second generation statute that goes quite far in the form of consumer protection. The first objection was touched on by you, which is: Why is there a need for Federal legislation which some States have already enacted?

Without some impetus from the Federal Government, too many States will fail to act. As we have seen in the last 3 or 4 years, most of the abuses in condominium sales and living have come from a very few States. Yet, all States' markets have been damaged by these abuses. It doesn't serve the industry if Georgia passes a strong second generation condominium act if other States that attract the industry do not do so.

The second objection raised in Georgia was that such legislation would chill sales and the disclosure would result in people not buying. The clearest repudiation of that was that I had a client come and ask me to review a complex set of documents. I did. I gave him the analysis. He said, "What should I do?"

I said, "I can't tell you."

He said, "Please tell me."

I said, "Don't buy."

He said, "I have to because my wife loves the place."

People will buy, but they will be informed and knowledgeable about what they are buying.

The third objection that is raised is that such protections as contained in this bill do not apply to other forms of real property sales. That is correct. They don't. We are not talking about the common sale of a piece of property. We are not talking about the ownership of a quarter-acre of land with a house. We are talking about a purchase into a complex form of housing. We are talking about an association with mutual responsibility and mutual benefits. We shouldn't compare apples and oranges when we say there is no need for condominium legislation, because there is none for the single-family dwelling.

It would increase expenses; that is the fourth objection. But I think that the increased expense would be a small price to pay for protecting a significant segment of the consuming public in the housing industry.

Not only are older people buying condominiums, but a significant percentage of those who are buying their first home buy condominiums.

I frankly became involved in condominiums when I returned from the service to Atlanta, Ga., and found a condominium was the only

thing I could afford that I wanted to live in. They serve a real purpose for all sections of our society.

The escrow requirement is unfair because the small builders need the escrow to build their projects. That is the fifth objection. We have had too many people see developers going under, unable to complete their projects. When they try to recover their escrow, they find it is gone.

There must be some protection.

The sixth objection raised is that the developer should not be required to pay assessments. He should not be required to support his share of the cost of running the association. That is shortsighted from several points of view.

As was made clear in the remarks of the three Senators who offered this bill, the developer is an owner. He is an owner as much as any other individual involved with that project, and has the same responsibilities.

More than that, a well run association, clean pool, nicely cut grass, all of those things that are made up in the expenditures of those common funds might as well be budgeted in the advertising account of that construction project. You don't sell projects that are poorly run, poorly maintained, and don't look nice.

They use the fine association as a selling point. From a business point of view, the developer should pay his or her share of the expenses of that association.

The last objection that I have heard is that section 5, and possibly section 6 should be made permissive and that the Federal Government should offer them only as a suggestion.

Senator, I think that the carrot won't work without the stick. If you make it permissive and suggest to the States that some action be taken, too often no action will be taken. We will continue to have the same problems that will destroy the condominium concept.

This is a good bill. It correctly appraises the best method of solving the problem. We do not need another Federal regulatory agency. We do not need a condominium SEC that requires filings. I frankly think we don't need State agencies. I think the consumer and the State of Georgia can solve the problems if given legislative support.

My prepared remarks touch on minor changes that I envision to be proper in the bill. I would be delighted to answer any questions the committee may have.

The CHAIRMAN. Thank you very much. We also have a statement from the assistant attorney general of the State of New York which we'll insert in the record at this point.

[The statements follow:]

REMARKS OF WAYNE S. HYATT, PRESIDENT

GEORGIA ASSOCIATION OF CONDOMINIUM OWNERS

Mr. Chairman:

It is a pleasure to appear before the Committee on behalf of the Georgia Association of Condominium Owners (GACO), a non-profit membership organization representing individual condominium owners and their associations as its president. GACO's membership consists primarily of associations, but it also includes developer-builders, managers, lenders, and others interested and involved in condominiums and their successful development and operation. Additionally, I have been the president of a 163 unit condominium in Atlanta and, as an attorney, represent approximately 75 associations in the problems and opportunities inherent in the turnover and development stages. While clearly accepting the responsibility of speaking for the consumer in condominium matters, the Georgia Association of Condominium Owners has as its goal and role of assisting all parties in the successful development and operation of homeowners associations and most particularly, aiding the individual unit owners in the ongoing task of association management. It is in this capacity of representing all owners and seeking a legis-

lative position most supportive of the condominium concept that we appear, for owners' and purchasers' interests must be protected in order to restore and to assure the economic viability of all who would deal with or develop condominiums.

Secretary Hill's testimony and the report from the Department of Housing and Urban Development have discussed the explosive growth of the condominium form of ownership in the past five years, a growth which in conjunction with other forms of compulsory membership association developments is predicted to continue. The basic theories underlying this popularity are obvious. With greater land utilization made possible by multifamily development and with the tax and other economic advantages of ownership, the purchaser is supposed to receive more for his or her dollar. Normally this is the case, for not only does the purchaser receive a housing unit for less money per square foot than could be purchased in a single family detached house, but also he usually acquires recreational and other facilities as part of the condominium not available or affordable otherwise. The surrounding community benefits from an enlarged base of property owners and taxpayers and from an improvement in both the number and nature of housing units. That is how it should work.

The experience in metropolitan Atlanta is instructive of how the process has worked in an area of medium heavy condominium development. Georgia, particularly Atlanta, had an active condominium market, but the percentage share of housing starts and the total number of units constructed has not been as great as in several other areas. It is this factor of balance that makes the Georgia experience perhaps more representative than other states or cities with a very light or extremely heavy development experience.

At year end 1974, there were 202 condominium projects either fully developed, under construction, or undergoing conversion in Atlanta. These projects consisted of 11,157 units, and according to housing surveys in Atlanta, an additional 1,207 units are to be constructed in the second half of 1975. Twenty-eight projects are totally sold out and under homeowner control. Unit prices have ranged from the high teens to well over $100,000. However, the greatest popularity has been with the buyer seeking a home for less than $40,000, and many have found houses otherwise unaffordable, available as condominium units in the $19,000 - $30,000 range. According to the Federal Home Loan Bank Board, the average selling price for a new home in Atlanta during the first six months of 1975 was in excess of $50,000. Without the price savings resulting from the greater possible land use and lower building costs

available in the condominium format, thousands of people, particularly young marrieds and older people, could not afford to be homeowners.

The availability of condominium housing is threatened, however. The threat comes not only from sharp sales and development practice but also, and more seriously, from the deterioration in consumer and lender confidence. This deterioration results in part from certain practices, widely publicized but not widely followed, which constitute the Florida "horror stories." Georgia developers have avoided many of these oppresive actions, but the deterioration in consumer confidence continues. This is true beçause there has been such a serious failure on behalf of lender, developer, seller, and consumer to understand the concepts involved and as a result there has been conscious and unconscious misrepresentations. What is needed is a restoration of this confidence through a procedure that insures full and thorough disclosure of sufficient information about the condominium and its association and that establishes standards for construction and operation. Georgia on the state level has enacted legislation to secure these ends, and the Condominium Consumer Protection Act on the national level is also an excellent beginning.

The experience in Georgia where consumer abuses have not been as acute as in other states yet where meaningful consumer protection legislation has been enacted illustrates that the federal-state cooperative approach can work and that the authors of S.2273 are correct in refraining from establishing a mandatory federal registration procedure. Georgia has, however, adopted an enforcement procedure relying not upon a state agency but upon strong civil and, if necessary, criminal actions. Frankly, the Georgia Association of Condominium Owners felt and continues to feel that such individual enforcement is preferable to the addition of an agency. S.2273 follows this general approach but with an agency to oversee the state's plan. GACO strongly urges that this step be eliminated and that all enforcement be through civil damage actions, either by individuals or the Secretary of H.U.D. or by criminal actions as needed. All state laws meeting basic federal standards would be approved; those not meeting such standards would be preempted.

The Georgia Association of Condominium Owners applauds and approves the motives and purposes of the authors of S.2273. However, principles of federalism and the basic state's role in governing real property

transactions militate against direct imposition of federal guidelines. The guidelines or standards should be established by the states in order more precisely to meet local needs and conditions; Georgia, Maryland, Virginia, and a few other states have shown that this local initiative is sufficient to produce sound regulatory legislation. Regrettably, however, not all states have or will act, and as the Florida experience has shown, questionable practices in one state too often have national implications. The reputation of the condominium form and consumer-lender confidence therein have both been substantially damaged on that basis. Accordingly uniform, national minimum standards are necessary and proper. The approach in the bill affording the states one year to enact a local plan is, however, perhaps too short. Based on the experience in Georgia where drafting and enactment proceeded with dispatch, a two year period would be more appropriate. States failing to act during that period should be subject to the provisions of the Condominium Consumer Protection Act.

Section 5 containing the National Standards for Consumer Protection represents a fair compromise of the various interests permitting developer flexibility while at the same time affording consumer protection.

Escrowing of deposits is required by the Georgia Condominium Act and is only fair. Some argue that the deposits are necessary for the small developer's use. If so, the developer should be required to post bond to assure the innocent prospective purchaser does not suffer loss. Such losses have happened and should not be permitted in the future.

Georgia has not experienced to any great degree, the oppresive practice of developer retention of recreational leases. Such practices elsewhere have, however, scarred condominiums generally and should be restricted. Whether such leases may constitutionally be prohibited by statute is a troublesome question. GACO feels that substantial controls such as a prohibition of cost of living increases, mandatory disclosure, and permissive termination is the preferred approach.

Based on our experience there is a serious need to limit the period of time that the developer controls the association. An indefinite control period often instills a sense of hopelessness in association members and is frought with potential abuse and self-dealing. More often, however, the period of developer control is one of neglect, indecision, and drift. Administrative procedures are

not established; the initial owner enthusiasm is lost; and financial and maintenance planning is neglected. Too often the developer simply does not understand the nature and extent of these responsibilities or even that he has them. The ideal approach to this problem would be to require a graduated involvement of homeowners in the association's affairs. In our practice and experience, we have had excellent results when approximately one third of the board is composed of owners by the time one thirds of the units are sold. The percentages gradually shift as units are sold with the unit owners assuming full control when 70 or 80 percent of the units are occupied. The one year mandatory turnover required by Section 5(3) of S.2273 is too short under present sales conditions unless a significant number of units have been sold. There must be a percentage factor employed to protect the small minority of owners who might otherwise be unduely burdened after one year of very slow sales. Such a percentage control coupled with a clear imposition upon the developer to operate the association in accordance with general principles of fiduciary law would accomplish the desired end.

The provision of subsection (4) concerning the right to cancel contracts is most necessary. It should, however, be extended to all contracts rather than just

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to "any management contract or other agreement...." In order to remove doubt, the word "management" should be removed.

The reach of the warranty provision of subsection (5) is also unnecessarily limited. If the warranty be from "the time of the initial occupancy of the project" as provided in S.2273, the common area warranty will in all probability have expired before many units have been sold. Warrany questions are difficult, particularly in light of the vagaries of state law. There is a need for a warranty provision, but the common area warranty should not be tied to initial occupancy. A better approach would be for a warranty running from the completion of construction or the sale of a specified percentage of units, whichever is later.

Warranties, of course, are only as good as those standing behind them. Reliance upon a contractor or subcontractor that incorporates a new business for each job does not constitute a warranty. A bond requirement or a warranty program sponsored by an organization such as the National Association of Home Builders is a better approach.

It is most necessary that the developer assume the rights and obligations of unit ownership, particularly the financial obligations. Although the H.U.D. study

finds this problem not to be widespread, it is most serious. Developers have followed a cavalier attitude of refusing to pay assessments with the result that associations often have inadequate finances to maintain quality operations and little or no reserves at turnover. There is no reason for this. Developers benefit from well cut lawns, clean pools, paved roads and smoothly operating associations. Costs which are purely functions of occupancy, e.g., sewer and garbage, can easily be apportioned as Georgia has done. All other ownership responsibilities, including financial must be borne by all owners.

No one could seriously object to the disclosure requirements of S.2273 or to the 15 day right to rescind the sales contract. Without full and fair disclosure there is such misunderstanding and harm as to destroy the value of all other promotional efforts. I would suggest only one change. In subsection (6) there should be an operating budget for full occupancy; this obviates the problem of "low balling" and provides to the prospective purchaser an idea of what assessments will be like at turnover. Ideally, the budget for any period of less than full occupancy should bear a reasonable and direct relationship to the budget for full occupancy.

Mr. Chairman, I am concerned about Section 18 of the bill which appears to be a blanket exemption from the reach of the Securities Act of 1933. Our experience has concerned residential condominiums, not resort projects. In the latter areas, of course, there has been considerable discussion of the reach of the securities laws, and rightly so, where the thrust of the sale is the profit return from the rental or other third party use of the unit. The disclosure required in a residential sale does not afford protection in the sale of a unit designed to be the vehicle for the production of income by virtue of the efforts of others. There is a need for this investment aspect to be separately addressed, and section 18 should be deleted.

In establishing civil penalties, Mr. Chairman, this Committee is adopting the preferred approach. Response to violations will be more immediate and will be of a nature which assures the owner or purchaser that there is "something he can do." The difficulty in proving damage is substantial, particularly for violations of those provisions relating to the association's operation. Perhaps this should be so in order to protect innocent developers. However, as in other substantive areas there should be some

provision for the recovery of a multiple of the actual damage suffered. A recovery of $500.00 is scant deterrent and even less compensation for the distress which can be caused by violations.

Lastly, Mr. Chairman, I submit that the problems we are discussing may ultimately be cured only through greater education, awareness, and appreciation for what the condominium concept is and what its potentials are. This form of ownership has great potential as a partial cure to problems of available shelter, for lower and middle income groups, for revitalization and restructuring of shelter forms in inner cities. It is a means of restoring a much needed sense of the community to those isolated in a suburban crowd. The innovative possibilities and variations in the compulsory membership association derived from the condominium are seemingly unlimited - except by greed, carelessness, and misunderstanding.

The H.U.D. study is accurate in its analysis of the problem areas. However, to cure all problem areas save two would be of no avail if problems 5 and 6, association operating problems and problems of community living, remain. If the association cannot successfully operate, there will not be a condominium. There must

be a uniform, accurate process of education to train the professionals as well as the laymen. There must be an appreciation of the dual roles of an association and of the necessity for owner, developer, and lender support and participation in order to fulfill these roles. Education can accomplish much more than legislation and the national program of technical assistance is a giant step forward. Such a program operating through H.U.D. or other appropriate federal agencies would insure uniformity and thoroughness both so vital in this regard.

The standards for consumer protection and the disclosure requirements will cure the "horror stories." At that point, the real work of making the development and the condominium concept last begins. This work can, however, be brought to a successful conclusion so long as everyone appreciates what is involved.

Mr. Chairman, I appreciate this opportunity, and I appreciate the Committee's efforts. My normal inclination is that the states should deal with these matters, and I am confident of sharing that feeling with members of the Committee. As a consumer and as a consumer representative, moreover, I know that this

bill could be much more strenuous and restrictive. It is, however, a fair compromise making possible state action and federal assistance and education. It provides an impetus to those who would not otherwise act and in so doing it protects not only the consumer of condominiums but also all those who would build, sell, or invest in them.

STATEMENT

BY

Arthur S. Levine

Assistant Attorney General
State of New York

My name is ARTHUR S. LEVINE.

I am Assistant Attorney General of the State of New York in charge of the Real Estate Financing Bureau in the office of Attorney General Louis J. Lefkowitz. The protective legislation developed by him and enacted at his urging in New York State is now in its fourteenth year of existence.

For the past twelve years, I have been involved on a day to day basis in the enforcement of New York State laws relative to the registration of cooperative and condominium offering literature and the policing of that segment of the real estate industry for adherence to applicable law and regulation. Since our statute provides for jurisdiction over selling practices in New York of cooperatives and condominiums constructed beyond its boundaries, I have some familiarity with the condominium laws and practices in such jurisdictions as Arizona, Connecticut, Florida, Massachusetts, New Jersey, Puerto Rico, Spain, and to a lesser degree with the laws of most of the other states.

It is with this background in mind that Attorney General Lefkowitz has directed that I accept your invitation to try to be of assistance to your committee.

Senate 2273 includes many of the recommendations made on Mr. Lefkowitz's behalf by my predecessor, David Clurman, on October 9, 1974 the details of which can be found on page 112 of the Hearings on Condominiums before the Subcommittee on Housing and Urban Affairs. Consistent with the suggestions then made, the bill provides under Section 7, "any State may assume responsibility for the enforcement of the standards contained in this Act". Further, that under Section 5, National Standards for Consumer Protection, purchaser's deposits must be held in escrow pending settlement; sponsor retained or leased recreational and other facilities is prohibited; provisions for surrender of sponsor's minority control are provided; specific warranties for construction are set forth; sweetheart management contracts are barred and that in case of conversions there is a 90 day option to tenants and 120 day delay in eviction. Because of the foresight of Mr. Lefkowitz all of these standards as well as the basic provisions of the National Standards of Disclosure (Section 6 of the bill) have been a part of New York law, regulation and practice for about 10 years. As to provisions which may exceed New York requirements, the Attorney General of New York is confident that appropriate State legislation will be forthcoming to conform to Federal law, if and when enacted.

It is regrettable, however, that those States which have been pioneers in condominium consumer protection and, as in the case of New York, spent millions of dollars to establish and support adequate laws and facilities for its enforcement, are excluded

from the benefits of Section 8, which would authorize grants to States to assist in carrying out the provisions of Section 7 (Establishment of State Condominium Plans). We urge that the language of Section 8b(1)B be broadened to permit the Secretary of HUD to make grants to assist any State to improve an existing State condominium plan as well as developing one that had not been previously established.

Substantial expense will be incurred by the State of New York as well as other states in adapting their own protective laws to Federal legislation. Of necessity, there will be a flow of reports, letters, documents and personnel to and from Washington seeking to meld our current State and the new Federal program. New State laws and regulations will have to be created and a period of retraining required for our staff. These are items of expenses which would not exist but for a new Federal law.

The draftsmen of S.2273 have done a monumental job in bringing together some of the best thinking yet encompassed in a single condominium bill. Nevertheless there remains doubt as to the scope of this bill as a result of the language used in defining relevent words and phrases.

The definition of condominium project set forth in Section 2(2) is equally descriptive of planned unit development or some forms of homeowners associations, tenancies in common and partnerships. In Section 7(7), the definition of leasehold condominium project is equally descriptive of the traditional membership

in or ownership of interests in corporations and accompanying proprietary lease, time sharing and vacation leases and licenses and a host of other similar schemes. If this is your intent we heartly applaud the foresight of the draftsmen in addressing themselves to this growing problem.

It has been our experience that the very same shoddy practices, fraudulent misrepresentations and abuses now current in the market place for condominiums also exists in the case of cooperatives, planned unit developments, homeowners associations and other schemes. Even if your committee believes that at the moment the problems relating to these alternate forms of home ownership has not yet reached epidemic proportions our experience indicates that it soon will be as a result of this legislation.

In New York where the condominium registration and disclosure requirements have proven uncomfortable to the condominium industry, there has been a shift toward planned unit development and homeowners associations. Fortunately, our disclosure and registration requirements apply equally to such offerings.

We urge this committee to take an aggressive stand against shoddy and fraudulent practices in the offering and sale of all forms of home ownership which relies upon the sharing of title and responsibility for the maintenance of commonly owned and used facilities and amenities by following New York's example. Our

enabling statute uses a generic term "cooperative interests in realty" which includes all the forms described herein. All these ownership devices, including condominiums have a common thread - shared ownership and maintenance of real estate to provide housing for the purchasers.

This bill may have been prepared with only the statutory condominium in mind and many of the provisions may not be applicable to such other forms. However, authorization to the Secretary of HUD to promulgate appropriate rules and regulations specifically applicable to the non-condominium forms of cooperative interest in realty taking into consideration the legal and business aspect of the offering and the public policy as set forth in the bill should suffice to create a workable program.

Federal jurisdiction is sought to be acquired over condominium offerings on the basis of being financed by lenders whose deposits are insured under a Federal program; which is directly or indirectly subsidized by an agency of the Federal government; is made by a creditor who makes or invests in residential real estate loans aggregating more than $1,000,000 per year or who solicits by mail. Thus under S.2273 the sponsor of a $50,000,000 condominium conversion would be exempt from the strictures imposed by this bill simply because there was no institutional financing; may not be subsidized by an agency

of the Federal government and the sponsor was not in the business of lending more than $1,000,000 per year. The sponsor need merely offer for all cash or take back purchase money mortages, hand deliver his offering literature and rejected all communications received by any other means than hand delivery to his office on the project site. To forestall any such attempt at avoidance of nationwide standards of protection and disclosure the definition of Federally related should be expanded to include any sponsor who maintains accounts or transacts business through banks or lending institutions which are Federally insured.

Sometimes, we in government attempt the impossible and in doing so frustrate public policy and perform a disservice to the very persons sought to be protected. Such is the case of the provisions Section 6(a) requiring a two year projection (revised and updated at least every six months) of annual expenditures necessary to operate and maintain the common elements of the condominium project certified to have been based on generally accepted accounting principals etc. New Yorks experience indicates a reasonably valid budget projection for more than the first year assuming full occupancy is impossible to achieve and even one year is sometimes a pipe dream. We have had extraordinary increases in real estate taxes, fuel, labor and snow removal at different times over a period of six months which knocked every conceivable projection into a cocked hat. Does this mean that every promoter is going to jail for such inaccurate estimates. In New York we prefer to alert the prospective buyer to the dangers of

unpredictability by compelling the sponsor to state that no one can accurately project future cost of operation which is effected by so many variables. If a customer still wants to buy he is under no illusion that there is any agency of government which will or can protect him against the unexpected and the extraordinary. The crossed fingers of a condominium purchaser is more useful to him than a blind faith in the power of government to protect against every shift in the economy, weather or politics.

And what about the phrase "generally accepted accounting principles" found in Section 6(a)6. Does anyone have any idea what this means. The least qualified person to make a projection is an accountant. We believe that the only qualified person is an independent property manager or managing agent who can demonstrate a reasonable amount of experience with operating properties of a like kind and size on a day to day basis. We want to know the background of the so called expert - is he a person who has leased apartments, negotiated sales or leases, collected rents, kept records of his daily activities, hired porters, dealt with unions, ordered labor and material for repairs, attempted to reduce real estate tax assessment, dealt with contractors, and ordered insurance policies. Does he know the price structure for labor, materials and services in his community; has he participated in board of directors or board of managers meetings. Is he qualified to project maintenance schedules for clearing rain gutters, gardening, servicing heating

and cooling systems, and painting iron work. Accountants in my opinion are useless for this purpose. I urge you to modify the language of this section to require that estimates be made by independent qualified experts and leave the description of such qualifications to the Secretary of HUD.

Somewhat the same criticism can be made of Section 6(a)7 calling for an estimate of repair and replacement costs projected for five (5) years in connection with condominium conversions. We have had unhappy experiences with projections for even one year and we have completely eliminated that requirement for capital repairs and replacement estimates. In Schumann v. 250 Tenants Corp. 317 N.Y.S. 2d 500 (1970) Edward J. Greenfield, Justice of the New York Supreme Court stated in speaking of estimates for repairs and renovations in a conversion prospectus:

> "These are estimates, and they are clearly labeled as such, since no firm factual figure as to the future could be set forth unless contracted for. Without the limiting language explaining what the figure set forth actually stands for, the Prospectus would fail to distinguish between fact and opinion, and in setting forth as certain that which must be uncertain would be guilty of serious misstatement."

We have found that just as sponsors tend to obtain understated estimates, tenant groups obtain overstated estimates, to counter the under estimations. Court rooms become the battleground for experts. We in New York prefer the scare them technique of nobody really knows rather than the lull them to sleep technique of this bill, which is to say, - stop worrying and if after five years you find we were wrong sue our architect, engineer or estimator who certified to the estimate and upon whose figures the sponsor also relied.

With respect to the conversion features of S.2273 Attorney General Lefkowitz has asked to say the following on his behalf: "The conversion feature of the bill fails to evidence an understanding of the best protection captive tenants can have against excessive pricing and unfair terms. We in New York find that the requirement of sales to at least 35% of the existing tenants within one year to make the plan effective enables the tenants to organize into a strong bargaining unit. A well organized group of tenants can engage architects, engineers, lawyers, accountants and real estate experts to review the plan, develop their own estimates make counter offers and to either negotiate acceptable terms or defeat the sponsors plan. This or a higher percentage coupled with a prohibition against excessive rent increases, statutory extension of the term of the unexpired leases for a period of two years after the plan is presented and, in the event

of failure to obtain required percentage, a prohibition against a reoffering until two years after the first presentation would be a more effective consumer protection than the provisions of this bill.

I urge that S.2273 be strengthened in accordance with the recommendations herein. But in no event should this Committee reject this bill because it is not perfect. The need for consumer condominium protection is so great that its failure of passage would be a national tragedy."

There are some additional matters which should be given consideration by your committee. The matter of State processing fees for registration should be left to the States and fees to make complaints to the State agencies (as in the case of the $25 fee to a Florida agency) should be prohibited. Conflicting statutes and regulations of other Federal agencies, such as the Office of Inter-State Land Sales should be taken up and resolved in this bill.

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Mr. ARKIN. My name is Richard Arkin. I am president of the National Capital Condominium Federation. Accompanying me are James McIntyre, C. E. Bodwell, and Michael Friedman. Thank you for inviting us to testify.

Mr. McIntyre, chairman of the federation's legislative committee and an NCCF director, is a certified public accountant with expertise in condominium financial management. He is former president, and currently a director, of the Marlow Towers Condominium in Silver Hill, Md.

Mr. Bodwell, the federation's vice president and former legislative committee chairman, is a director and president of the Park Terrace Condominium in Rockville, Md.

Mr. Friedman, who is also an NCCF director, is an attorney in private practice in Maryland, and is a member of the Maryland Bar Association's condominium law committee. Mr. Friedman is a director of the Inverness Forest Homeowners Association, a planned-unit development in Potomac, Md.

I am currently in my second term as president of the National Capital Condominium Federation, and I am a director and former president of the Autumn Walk Condominium in Layhill, Md., a suburb near Silver Spring. I am also a condominium specialist for the Montgomery County, Md., Office of Consumer Affairs, the office charged with the enforcement and administration of Montgomery County's Condominium Disclosure Act, which is similar in many respect to the legislation currently before this committee.

We support this bill wholeheartedly, with a few suggestions we would like to discuss later.

We would state that it is our experience that some of the most flagrant abuses being discussed here are abuses not limited to the Florida market alone. We have, for example, seen abuses in the Washington market that are similar to recreation leases, but are more inclusive than simple recreation leases.

For example, we have seen situations where parking lots or laundry rooms, or other common facilities in a mixed-use building are held by the developer in perpetuity, and leased back to the association.

Abuses are not just limited to recreation leases in Florida.

Many of the other problems—the sweetheart management contracts, for instance—are the kind of problems we have all experienced. They, too, are not problems limited just to the Florida market, as the HUD study would suggest.

We feel that passage of the bill that you have introduced, S. 2273, is an absolute necessity of condominium development is to succeed in the long run. We would like to suggest a few modifications, however.

In section 5, subsection 3, the word "occupied" should be replaced by the word "settled," as units occupied through a rental or presettlement agreement could end up being counted as part of the 80 percent required for owner control. During the selloff period, the developer has a legitimate interest in retaining a measure of control over the project, to insure its marketability.

Similarly, it is in the interest of the consumer that the project be marketed effectively, since the consumer's investment is tied up in a successful sellout, as well as in the long-range success of the project.

NCCF would actually prefer to see a formula devised to assure that consumers are represented on a builder-controlled board long before the turnover of control takes place, so an orderly transition can be combined with a period of guidance and training for the owner-leaders.

In a five-member board, for example, for each 20 percent of the units sold, a unit-owner could be given a seat on the board, with the developer retaining his veto power until settlement on, say, 75 percent of the units has taken place.

In this respect, we feel that the 1-year maximum for developer control proposed in the bill may actually be too restrictive and inflexible, since a project consisting of several hundred units could take considerably more than a year to build and sell. We would prefer a more flexible approach.

In section 5(4) we would prefer to see language written with greater flexibility, such as the language now in the current Maryland Condominium Act. We feel that any contract entered into while the developer is in control should be voidable by the association, any time after homeowners have taken control, on 30 days' notice. This gives the homeowners time to determine the effectiveness of contracts which might be good, while giving them an early out for excessively one-sided contracts.

In section 5(5) we would suggest that any warranties should be guaranteed by a bond to avoid a developer's bankrupting the Shell Corp. under which he is operating in order to avoid responsibility for warranties.

With respect to the proposed National Standards for Disclosure, NCCF regards the abstract proposed in S. 2273, which would be given to all prospective purchasers, as an important first step in providing the basic information necessary for making an intelligent purchase.

We would suggest that section 6(a)(4) should include information on whether or not the loan is assumable at resale, and whether or not there is any prepayment penalty.

Section 6(a)(6) should be strengthened by specifically guaranteeing the assessment for a 1-year period, with a specified maximum percentage increase guaranteed for the second year.

In addition, we feel that the developer must be required to assume responsibility for any association deficits resulting from either intentional or unintentional lowballing.

We would also suggest that section 6(a)(7) be strengthened by requiring that a reserve fund, or sinking fund, be set up—whether funded by the developer or not—utilizing the accounting procedures set up by FHA for FHA projects, or other sound accounting procedures, based on a long-term maintenance cycle derived from an engineering report with 10-year or 20-year projections.

We regard the abstract as an important document that would acquaint the prospective purchaser with basic information regarding an offering, and we feel it should be given to all shoppers when they enter the sales office, or when they request an abstract, in a manner similar to the requirements for interstate land sales prospectuses, so that a consumer can use the abstract as a tool for comparison shopping.

In addition, however, we feel that it is extremely important that the purchaser, in order to be fully protected, should be provided with the

basic documents and contracts relating to his condominium no later than the date of the signing of the contract, so that the rescission rights created by section 4(b) will be truly meaningful.

These documents should include the charter and articles of incorporation, if applicable, and the master deed or declaration and bylaws, as well as any leases of real or personal property applicable to the condominium, and any management contract, employment contract, insurance policy or other contract affecting the use, maintenance or access to all or part of the condominium.

These documents, which are critical to the functioning of a condominium, and determine the relationship of the purchaser to the association, and his financial obligations over the long term, should be included in a second section available with the abstract, or at contract, as exhibits, so the prospective purchaser can examine them or turn them over to his personal attorney for examination and analysis. The exhibits should also include copies of all legal documents pertaining to the purchase and settlement of the condominium unit.

We have heard testimony earlier concerning 120-page purchase contracts. This is the kind of purchase contract that a personal attorney should be given the opportunity to read and review, so that the consumer will be fully protected.

We are pleased with the administrative plan proposed in this bill. We feel that the diversity of the States and localities means that enforcement plans are best set up and administered at the State and local level, as this act permits, except where the States, through inaction, leave enforcement in Federal hands. One of the weaknesses of second generation condominium laws in some States is the absence of effective enforcement. This proposal combines effective consumer protections with effective enforcement.

We have found that even where disclosure is required, that many owners and purchasers never receive the required documents and information.

We also favor the proposals for civil and criminal penalties, as well as the assurance of the right of the unit owners to sue the developer, although we would suggest that section 9(a) be expanded to include the net cost and net resale value, so that this protection will include fees, closing costs and additional expenses borne by the consumer as part of his purchase. There should be additional penalties to the seller if the unit has increased in value.

Lastly, we would propose that Section 17, the effective date, be moved up. We are dealing with ongoing abuses which must be ended as soon as possible. There is no reason for a year to elapse after passage for these protections to go into effect. The requirements of sections 4, 5 and 6, the Prohibitions, and the National Standards for Protection and Disclosure, should go into effect as emergency legislation no later than 90 days after passage. Ongoing abuses must be stopped.

We would also like to point out that there are other areas that need attention in the condominium field. We would like to see Federal requirements and Federal minimums, and review at the State or local levels, of association documents and site plans to assure their adequacy and to assure long-term association success.

We would also like to see some kind of consistent requirements for documentation by Federal and quasi-Federal agencies such as FHA,

FNMA, VA, GNMA, and the Federal Home Loan Bank Board. We would also like to see a system set up for the establishment of a management accreditation or certification program for condominium and planned-unit development (PUD) managers.

In addition, it is important for Federal, State and local governments to realize that condominiums and PUD's have many of the characteristics of both business enterprises and mini-governments, and that the officers and directors—or mayors and councilmembers, if you will—elected by the unit-purchasers usually have little or no experience in community management, government or operations. We feel that a national technical assistance plan, consisting of a research program, and information and assistance for developers and lenders, as well as for local association officials, is an absolute necessity to assure long run association success for condominiums and PUD's and thus to assure that they remain an asset for the communities in which they are located.

We also feel quite strongly that legislation is imperative to reverse the restrictive and discriminatory Internal Revenue Service rulings requiring taxation of condominium and HOA surpluses and reserve funds—double taxation for condominium and HOA residents.

In conclusion, I would like to restate the National Capital Condominium Federation's support for the Biden-Brooke-Proxmire Condominium Consumer Protection Act, S. 2273, as an important first step in assuring the success of condominiums.

We are convinced that condominiums are here to stay as an important segment of the housing market in this country. Disclosure and protection against the flagrant abuses that have been all too common in this field will be an immense help. Over the long run, however, we feel that the ultimate success of condominiums—and PUD's—will depend on the help and direction homeowner boards of directors and managers will receive from the operations' standpoint from Federal, State, and local officials.

From a public policy standpoint, and from the standpoint of someowners living in a community, we feel that disclosure and consumer protections must be matched by efforts from those concerned with housing to assure the long-term success of condominium and PUD developments.

[Complete statement and additional material follow:]

TESTIMONY FROM THE NATIONAL CAPITAL CONDOMINIUM FEDERATION

Mister Chairman, and members of the committee: My name is Richard Arkin. I'm president of the National Capital Condominium Federation. Accompanying me are James McIntyre, C. E. Bodwell and Michael Friedman. Thank you for inviting us to testify.

. . . . . .

Mr. McIntyre, chairman of the Federation's Legislative Committee and an NCCF Director, is a Certified Public Accountant with experience in condominium financial management. He is former President, and currently a Director, of the Marlow Towers Condominium in Silver Hill, Maryland. Mr. Bodwell, the Federation's Vice President and former Legislative Committee Chairman, is President of the Park Terrace Condominium in Rockville, Maryland. Mr. Friedman, who is also an NCCF Director, is an attorney in private practice in Maryland, and is a member of the Maryland Bar Association's Condominium Law Committee. Mr. Friedman is a director of the Inverness Forest Homeowners Association, a planned-unit development in Potomac, Maryland.

I am currently in my second term as President of the National Capital Condominium Federation, and I am a Director and former President of the Autumn Walk Condominium in Layhill, Maryland, a suburb near Silver Spring. I am also a Condominium Specialist for the Montgomery County, Maryland, Office of Consumer Affairs, the office charged with the enforcement and administration of Montgomery County's Condominium Disclosure Act, which is similar in many respects to the legislation currently before this Committee.

The National Capital Condominium Federation is an organization of condominiums, homeowners associations, planned unit developments and similar automatic membership community association developments in the Washington Metropolitan Region. Our membership consists of about 50 such organizations in the District of Columbia, Montgomery and Prince Georges Counties in Maryland, and Arlington, Falls Church, Fairfax and Alexandria, in Virginia. Approximately 20,000 residents live in roughly 7,500 units in the area's NCCF developments. The Federation was formed early in 1974 by leaders of these associations to serve as a communications clearinghouse for these developments, as an educational vehicle for neighborhood leaders and residents, and as a spokesman for those living in condominiums, HOA's and PUD's. NCCF is entirely homeowner controlled, and we are all volunteers donating our time.

NCCF has devoted considerable time toward study of S. 2273, including study by members of the Legislative Committee, and entire membership meeting devoted to the bill at which Elinor Bachrach of Sen. Proxmire's staff and Peter Wentz of Sen. Biden's staff spoke, sharing views—and listening to comments—with representatives of communities who have suffered through the kinds of abuses which this proposal would hopefully end.

In addition, officers of the federation participated actively in the HUD hearings held early this year, and assisted in the preparation of the HUD study by the Arthur D. Little and ICF research groups.

The Federation would like to applaud Senators Biden, Brooke and Proxmire for introducing this proposal, and the Committee for holding these hearings on the problems of condominium development. We support this bill whole-heartedly, with some suggestions for modifications which we will discuss below.

Condominium development, as the just-completed HUD study and other recent research projects have shown, has become a substantial segment of housing development in America, with housing starts this year estimated to be 16 percent condominium. In the Washington area, at the peak of the condominium boom, 85 percent of multi-family housing starts were for condominium units, and although the proportion of condominium starts has declined somewhat because of overbuilding and bad publicity, condominiums are still an extremely substantial part of the housing stock and of housing starts in this area. In addition, in the major metropolitan regions of this country, a much larger proportion of development is in the form of townhouse and single family planned unit developments with automatic membership homeowner associations created for the maintenance of common grounds, streets, recreation facilities and equipment, and for the enforcement of covenants and restrictions. These HOA's are subject to many of the same problems and abuses as condominiums, but have not shared the same glare of unfavorable publicity.

The National Capital Condominium Federation agrees with the observations of most astute researchers in the field in predicting that the current oversupply of condominium units is a temporary phenomenon related to overbuilding and over-converting and the general economic slump. Condominiums and planned unit developments, we believe, are, in fact, the wave of the future, because of the increasingly high costs of land, land development and building. Housing officials across the country have rapidly accommodated themselves to these forms of ownership because they mean more rational use of land, less cost-per-unit for services for government, and more opportunity for homeownership for families of moderate means. Most local governments, like the federal government, seek to encourage homeownership, because pride in ownership promotes neighborhood stability and quality.

Consumers are attracted to condominiums and PUD's for many of the same reasons. The economies of land development and building mean lower purchase costs, and in these days of high inflation and tight money, this means that the opportunities for homeownership remain open in condominiums and PUD's for moderate-income families who have been shut off from the single-family home market in conventional subdivisions. These families are able to enjoy the same

tax advantages and build equity in their living units, and to share in the pride of ownership denied residents of rental units. In addition, many are attracted by the recreational and park-like facilities that the economies of scale allow in condominiums and PUD's, while others are attracted by the shared maintenance burdens which are borne by the association as a whole, as opposed to the individual requirements for total maintenance characteristic of the conventional single-family unit.

As all of us here today realize, the condominium boom is very recent, with the first enabling legislation for condominiums going back only about a dozen years, and with the real development boom dating back only about five years. This boom, which occurred in a climate of little experience for developers, government agencies and purchasers, and at a time when consumer protections were nil, led to a get-rick-quick attitude on the part of many developers, and the problems and abuses which now plague the movement, and which this legislation addresses.

Some of the most flagrant abuses deserve special mention. It has not been uncommon in many areas for developers to retain title on important parts of a development. These can include recreational facilities, the parking garages or lits, the laundry rooms, or commercial units in residential buildings, for example. These may then be leased back to the condominium unit-owners—or the PUD unit owners—through their association, utilizing long-term, exceedingly one-sided agreements, which can net the developers incredibly high returns through such devices as automatic assessment increases tied to the cost of living.

Another common abuse is the long-term "sweetheart" management or maintenance contract which ties the unit-owners to one-sided contracts with firms connected to the developers, again assuring the developers a long-term income from the project, while tying the buyers to burdensome terms. In some communities, the developer hangs onto control of the association itself, long after most or all of the units are sold, so the cream can be skimmed from the top in on-going management and maintenance operations.

Lowballing—deliberately disguising the costs of maintenance to induce purchasers to buy—is another common abuse, as is the failure to disclose material information to prospective purchasers, such as the soundness of structural elements, electrical, mechanical, heating or plumbing equipment in conversions. Other condominium purchasers have been victimized by the failure of the developer to build promised facilities, the failure to honor warranties, the failure to pay the developer's share of condominium fees (thus destroying the financial soundness of the association), and the failure to educate purchasers in the management and maintenance of their development prior to turning over control.

The National Standards for Consumer Protection, as proposed in S. 2273, are a necessity if condominium development is to succeed in the long run, although we would like to suggest a few modifications.

We would like to see Section 5(2) more specifically written to assure that the entire property is offered as an entity, with all buildings, facilities, machinery, equipment and land in which the developer has any interest, and which is part of the property, offered in full. This recognizes the fact that the fiscal viability of a project with non-residential space can depend to a large extent on the income derived from the non-residential areas. If all non-residential space—including commercial units—is considered part of the common area, purchasers will receive the income derived therefrom and a measure of control over the maintenance and tenancy of non-residential units.

In Section 5(3), the word "occupied" should be replaced by the word "settled," as units occupied through a rental or presettlement agreement could end up being counted as part of the 80 percent required for owner control. During the sell-off period, the developer has a legitimate interest in retaining a measure of control over the project, to insure its marketability. Similarly, it is in the interests of the consumer that the project be marketed effectively, since the consumer's investment is tied up in the long-range success of the project. We would actually prefer to see a formula devised to assure that consumers are represented on a builder-controlled board long before the turnover of control takes place, so an orderly transition can be combined with a period of guidance and training for the owner-leaders. In a five-member board, for example, for each 20 percent of the units sold, a unit-owner should be given a seat on the board, with the developer retaining his veto power until settlement on, say, 75 percent of the units has taken place. In this respect, we feel that the one-year maximum for developer control proposed in the bill may actually be too restrictive and inflexible, since a project consisting

of several hundred units could take considerably more than a year to build and sell.

In Section 5(4), we would prefer to see language written with greater flexibility, such as the language in the current Maryland Condominium Act. We feel that any contract entered into while the developer is in control should be voidable by the association any time after homeowners have taken control on 30 days notice. This gives the homeowners time to determine the effectiveness of contracts which might be good, while giving them an early out for excessively one-sided contracts.

With respect to the proposed National Standards for Disclosure, NCCF regards the abstract proposed in S. 2273, which would be given to all prospective purchasers, as an important first step in providing the basic information necessary for making an intelligent purchase. We would suggest that Section 6(a)(4) should include information on whether or not the loan is assumable at resale, and whether or not there is any prepayment penalty. Section 6(a)(6) should be strengthened by specifically guaranteeing the assessment for a one-year period, with a specified maximum percentage increase guaranteed for the second year. In addition, we feel that the developer must be required to assume responsibility for any association debts resulting from either intentional or unintentional lowballing. We would also suggest that Section 6(a)(7) be strengthened by requiring that a reserve fund or sinking fund be set up—whether funded by the developer or not—utilizing the accounting procedures set up by FHA for FHA projects, or other sound accounting procedures, based on a long-term maintenance cycle derived from an engineering report with 10-year or 20-year projections.

We regard the abstract as an important document to acquaint the prospective purchaser with basic information regarding an offering, and we feel it should be given to all shoppers when they enter the sales office or request an abstract, in a manner similar to the requirements for Interstate Land Sales prospectuses, so that a consumer can use the abstract as a tool for comparison shopping.

In addition, however, we feel that it is extremely important that the purchaser, in order to be fully protected, should be provided with the basic documents and contracts relating to his condominium no later than the date of the signing of the contract, so that the recission rights created by Section 4(b) will be truly meaningful. These documents should include the Charter and Articles of Incorporation, if applicable, and the Master Deed and Declaration, and Bylaws, as well as any leases of real or personal property applicable to the condominium, and any management contract, employment contract, insurance policy or other contract affecting the use, maintenance or access to all or part of the condominium. These documents, which are critical to the functioning of a condominium, and determine the relationship of the purchaser to the association and his financial obligations over the long term, should be included in a second section available with the abstract, or at contract, as exhibits, so the prospective purchaser can examine them or turn them over to his personal attorney for examination and analysis. The exhibits should also include copies of all legal documents pertaining to the purchase and settlement of the condominium unit.

The Federation is particularly pleased with the administrative plan proposed in S. 2273. We feel that the diversity of the states and localities means that enforcement plans are best set up and administered at the state and local level, as this act provides, except where the states, through inaction, leave enforcement in federal hands. One of the weaknesses of second generation condominium laws in some states is the absence of effective enforcement. This proposal combines effective consumer protections with effective enforcement.

We also applaud the proposals for civil and criminal penalties, as well as the assurance of the right of the unit owner to sue the developer, although we would suggest that Section 9(a) be expanded to include the net cost and net resale value, so that this protection will include fees, closing costs and additional expenses borne by the consumer as part of his purchase. There should be additional penalties to the seller if the unit has increased in value.

Lastly, we would propose that Section 17, the effective date, be moved up. We are dealing with ongoing abuses which must cease. There is no reason for a year to elapse after passage for these protections to go into effect. The requirements of Sections 4, 5 and 6, the Prohibitions, and the National Standards for Protection and Disclosure, should go into effect as emergency legislation no later than 90 days after passage.

While this proposal, with or without our suggestions, is an important first step in assuring the success of condominium development in this country, we feel that there are certain other areas which need attention. We would like to see federal requirements or federal minimums, and review at the state or local level, of association documents and site plans to assure their adequacy and to assure long-term association success. We would also like to see some kind of consistent requirements for documentation by federal and quasi-federal agencies such as FHA, VA, FNMA, GNMA, and the Federal Home Loan Bank Board. We would also like to see a system set up for the establishment of a management accreditation or certification program for condominium and PUD managers.

In addition, it is important for federal, state and local governments to realize that condominiums and PUD's have many of the characteristics of business enterprises and mini-governments, and that the officers and directors—or mayors and council members, if you will—elected by the unit-purchasers usually have little or no experience in community management, government or operations. We feel that a national technical assistance plan, consisting of a research program, and information and assistance for developers and lenders, as well as local association officials, is an absolute necessity to assure long run association success for condominiums and PUD's, and thus to assure that they remain an asset for the communities in which they are located, rather than a problem and a liability.

We also feel quite strongly that legislation is imperative to reverse the restrictive discriminatory Internal Revenue Service rulings requiring taxation of condo and HOA surpluses and reserve funds—double taxation for condominium and HOA residents. Two recent IRS rulings have provided partial relief in certain circumstances for condominiums, but we feel that the status of condominium and HOA surpluses and reserve funds must be defined by legislation not subject to the everchanging whims of the IRS.

In conclusion, I would like to restate the National Capital Condominium Federation's support for the Biden-Brooke-Proxmire Condominium Consumer Protection Act, S. 2273, as an important first step in assuring the success of condominiums.

We are convinced that condominiums are here to stay as an important segment of the housing market in this country. Disclosure and protection against the flagrant abuses that have been all-too-common in this field will be an immense help. Over the long run, however, we feel that the ultimate success of condominiums—and PUD's—will depend on the help and direction homeowner boards of directors and managers will receive from the operations standpoint from federal, state and local officials. From a public policy standpoint—and from the standpoint of homeowners living in a community—we feel that disclosure and consumer protections must be matched by efforts from those concerned with housing to assure the long-term success of condominium and PUD developments.

If government recognizes the importance of these associations and their place in society, condominium and PUD success will be assured.

Thank you.

OFFICE OF CONSUMER AFFAIRS,
MONTGOMERY COUNTY,
Rockville, Md., July 30, 1974.

GUIDELINES FOR SUBMISSION OF A CONDOMINIUM PROPERTY REPORT PURSUANT TO CHAPTER 58 OF THE MONTGOMERY COUNTY CODE

PURPOSE OF THE DISCLOSURE LAW

The legislative intent of the Montgomery County Condominium Law is that buyers will be provided with an adequate factual basis from which to make a decision on whether or not to buy a condominium. It is, therefore, the intention of the Office of Consumer Affairs that all information in the required property report be presented as clearly and concisely as possible. While these guidelines will set a format for certain sections of the report, the presentation of other information will be left to the developer's discretion. Where a doubt exists as to how certain information might be presented, clarity and simplicity are the overriding factors.

If the developer is of the opinion that the inclusion of certain documents in their entirety in the property report will only serve to make the report unwieldly and confusing to consumers, the situation should be discussed in advance with the Office of Consumer Affairs. If deemed desirable, these documents can be incorporated by reference in the property report with their complete versions kept on file at the Office of Consumer Affairs and the sales office of the condominium, and made available to an individual recipient of a property report upon request.

SPECIFIC INSTRUCTIONS

Form of submission

1. The report is to be printed on paper no smaller than 6 x 9 inches and no larger than 8½ x 14 inches.
2. Five copies of the report are to be submitted to the Office of Consumer Affairs.
3. All information presented in the report must be clearly labeled.
4. Pages must be numbered.
5. All information must be clearly indexed.
6. No type used in the report may be smaller than standard elite except when photocopies of actual documents are included.

Cover (1st page)

The cover of the report shall contain the warning required by the Montgomery County Condominium Law. This shall be double-spaced and capitalized.

"MONTGOMERY COUNTY LAW SPECIFICALLY PROHIBITS ANY REPRESENTATION TO THE EFFECT THAT THE COUNTY HAS PASSED UPON THE MERITS OF, OR GIVEN APPROVAL TO THIS CONDOMINIUM. IT IS UNLAWFUL FOR ANYONE TO MAKE, OR CAUSE TO BE MADE TO ANY PROSPECTIVE PURCHASER, ANY REPRESENTATION CONTRARY TO THE FOREGOING, OR ANY REPRESENTATIONS WHICH DIFFER FROM THE STATEMENTS IN THIS PROPERTY REPORT."

Second page

The second page shall contain a notice of the purchasers recission rights under the Montgomery County Legislation. No other information may be included on this page.

Third page

The third page shall contain the index or table of contents.

Question and answer section

From page 4, and encompassing as many pages as necessary, the following "Highlights of the Property Report" shall be presented. Both questions and answers shall be included. Where applicable, references shall be made at the end of each question to the section and page number of the property report where detailed information on the topic can be found. It is anticipated that the "Highlights of the Property Report" will cover many of the requirements of the condominium law. It will not be necessary to repeat this information elsewhere in the property report unless the document containing it is specifically required by the condominium law. Any other information required by the law, not specifically highlighted, that is contained in required legal documents need not be repeated but should be referenced in the index.

1. Will purchase deposits be kept in "escrow"? Will deposits earn interest? If so, at what rate? (The required warning shall be inserted in this section where applicable.)
2. What is the earliest date at which occupancy of the property should be expected? What is the latest date?
3. How many units must be sold before closings will be allowed?
4. What is the maximum size the condominium can be?
5. What alternative uses can be made of the remainder of the site, if maximum size is not reached?
6. Will any of the land area on which part of the condominium is located not be a part of the condominium? If so, who owns this area? What uses will be allowed for this area?
7. What facilities to be used by the condominium owners will not be included with the individual units or controlled by the individual unit owners through

their condominium association? (For example, garage spaces, laundry facilities, swimming pool, and recreational facilities.)

8. What will be the charge to the owners to use the facilities which they don't control? Can these costs go up? Under what circumstances?

9. Explain any restrictions on the use of the condominium (identify source if applicable).

10. List the contracts (including leases) to which it is expected that the condominium association will be bound, along with the length of time the contract will run.

11. Will anyone with a financial interest in the condominium project be a party to a contract which will bind the condominium association? If so, explain the relationship.

12. When will control of the condominium project be transferred to the condominium owners?

13. Is there any pending litigation, liens, or judgments which will affect the condominium and/or the developer's ability to convey clear title?

14. What warranties or disclaimers are being made on the individual units and on the common and limited common areas?

15. Are there any outstanding building code violations?

16. What is included in the condominium fee? For what costs will the condominium owner be individually responsible?

17. Does the condominium fee include a provision for reserves? (Required warning should be inserted in this section where applicable.)

18. If a provision for reserves is included, has it been calculated to be adequate to cover all expected repairs and replacements anticipated in the operation of the condominium, or will special assessments be necessary?

Individuals With Financial Interest (*11A–3,a,1*)

Those only under contract with or in the employ of the developer need not be included in this section.

Professionals (11A–3,a,2)

Suppliers need not be listed.

Statement of Financial Capability (separate page) (11A–3,c,4)

The following wording shall be included unless qualification is necessary:

(Name of developer) has sufficient financial capability to complete the construction, renovation, and/or conversion of the condominium units, recreational and other facilities described in this property report by (date).

In making this statement the developer has taken into account the projected marketability of the proposed project, and other potential demands which may be placed on the resources available for its completion.

Presentation of the Budget (11A–3, f)

The budget should be presented in tabular form. Supporting documents may be requested by the Office of Consumer Affairs.

Statement of Condition of a Condominium Conversion (11A–3, g)

It is assumed that in order to properly evaluate the present condition of the condominium components it will be necessary to investigate the repair history of these components. Reference to that history should be made in the report.

It should be stated in the report that estimates of repair and replacement costs are in current dollars unless a rate of inflation (to be specified) has been considered.

Reference to any components either inoperable or considered to need major attention within a year after the establishment of the condominium should be capitalized and underlined.

Affirmation (separate page) (11A–3, i)

I hereby affirm that I am a senior executive officer of the developer of the condominium described herein authorized by the developer to complete this statement:

That the statements contained in this property report and any supplements, modifications and amendments thereto together with any documents submitted herewith are full, true, complete, and correct.

(That the report made pursuant to § 11A–3, g)[1] of the Montgomery County Code 1972, as amended, was prepared by a competent and qualified professional

[1] Where applicable.

and upon knowledge and belief was prepared in accordance with recognized professional standards.)

That the developer agrees to carry out the promises, warranties, and obligations set forth in this report or has delineated who is responsible for promises, warranties, or obligations for which the developer is not responsible and provided warnings where required by law.

BILL NO. 2–74

Introduced: January 15, 1974.
Enacted: June 4, 1974.
Executive: June 12, 1974.
Effective: November 22, 1974.

COUNTY COUNCIL FOR MONTGOMERY COUNTY, MD., JANUARY LEGISLATIVE SESSION 1974, CHAPTER 58

(As upheld on November 22, 1974, in Montgomery County Circuit Court, Judge Joseph M. Mathias presiding, Equity No. 50058. Six sentences struck down in this decision are herein marked out.) (The decision was not appealed.)

AN ACT to add a new Chapter 11A, title "Condominiums", to the Montgomery County Code 1972, as amended, to follow immediately after Chapter 11 thereof, to provide for the preparation of a property report and the filing of such report with the Office of Consumer Affairs prior to the offering for sale or notice to tenants of the conversion of condominium units in a condominium project; to specify the nature and extent of the information required to be contained in the property report; to provide for the furnishing of a property report to a prospective purchaser of a condominium unit and to allow the purchaser to rescind the purchase contract within fifteen (15) days after execution; to require 120 day notice to existing tenants to be given in the case of a conversion of rental property to condominium status; to permit tenants to terminate without penalty or termination payment existing leases upon notification of a conversion of their rental units to condominium status; to prohibit unlawful representations in connection with condominium property reports; to provide for the administration of this Chapter by the Office of Consumer Affairs; to provide for the application of this Chapter throughout areas of the County under jurisdiction of the County government and in incorporated municipalities who elect to bring themselves under provision of this Chapter; to specify that violations of the provisions of this Chapter may be subject to civil penalties not to exceed $500.00 and costs and criminal penalties not to exceed $1000.00; to provide for civil enforcement proceedings; to provide for definitions of terms used throughout this Chapter and to state legislative findings by the Montgomery County Council.

Be It Enacted by the County Council for Montgomery County, Maryland, that—

Sec. 1. There is hereby added to the Montgomery County Code 1972, as amended, a new Chapter 11A, title "Condominiums", to follow immediately after Chapter 11 thereof and to read as follows:

11A–1. *Legislative Findings.*

The County Council for Montgomery County hereby finds that there is an increasing percentage of construction of residential units in the County that are intended for condominium development and further that a considerable portion of the County's rental housing is being converted to condominium status; that prospective purchasers of these condominium units are often without knowledge of the unique concepts of ownership involved in condominium housing; that often there is unequal bargaining power between buyers and sellers of condominium units; that often the buyers have little factual basis presented to them on which to make a decision; that the Council is aware of reported abuses by sellers of condominium units; that in order to facilitate fair and equitable bargaining and to provide the buyers of condominium units with basic information by which to make an intelligent housing choice and promote the health, safety and welfare of the people, it is necessary and appropriate for the county to require that sellers of condominium units prepare and distribute information deemed relevant to the buyers of this type of residential property.

11A–2. *Definitions.*

For the purposes of this Chapter, the following words and phrases shall have the meanings respectively ascribed to them by this section:

(1) *Agent:* The word "agent" means any person, firm, partnership, association, joint venture, corporation or any other entity or combination of entities who represents or acts for or on behalf of a developer in selling or offering to sell any condominium units.

(2) *Blanket Encumbrance:* The phrase "blanket encumbrance" means a trust deed, mortgage, judgment or other lien or encumbrance including an option or contract to sell or a trust agreement affecting a condominium including any lien or other encumbrance arising as a result of the imposition of any tax assessment by a public authority.

(3) *Closing of the Sale:* The phrase "closing of the sale" means the operation of transferring ownership of a condominium unit to the prospective purchaser from the developer through a deed of conveyance.

(4) *Common Elements:* The phrase "common elements" means all of the condominium except the condominium units.

A. *Limited Common Elements:* The phrase "limited common elements" means those common elements identified in the declaration or on the condominium plat as reserved for the exclusive use of one or more but less than all of the condominium unit owners.

B. *General Common Elements:* The phrase "general common elements" means all of the common elements except the limited common elements.

(5) *Condominium:* The word "condominium" means property subject to the condominium regime established pursuant to the Horizontal Property Act of the State of Maryland.

(6) *Condominium Project:* The phrase "condominium project" means a plan by a developer to sell residential condominium units in a building or buildings either through conversion to condominium status or construction of new buildings with condominium ownership.

(7) *Condominium Unit:* The word "condominium unit" means a three dimensional area identified as such in the declaration and on the condominium plat and shall include all improvements contained within the area except those excluded in the declaration. A condominium unit may include two or more non-contiguous condominium units.

(8) *Conversion:* The word "conversion" means the offering for sale by a developer or the developer's agent of condominium units that were previously rental units.

(9) *Developer:* The word "developer" means any person, firm, partnership, association, joint venture or corporation or any other entity or combination of entities or any successors thereto who at any time after the effective date of this Chapter undertakes to develop a condominium project either by conversion to condominium status or construction of new buildings.

(10) *Offering:* The word "offering" means any inducement, solicitation, advertisement, publication or announcement to the general public to encourage a person to acquire a condominium unit in a condominium.

(11) *Prospective Purchaser:* The phrase "prospective purchaser" means a person who visits the condominium project site for the purpose of inspection for possible purchase or who requests the property report.

(12) *Site:* The word "site" means any land area on which a part of the condominium is located.

11A–3. *Property Report; required; contents.*

Prior to offering for sale any condominium units in a condominium project a developer must prepare a property report which shall contain the following information about the condominium project:

a. A statement indicating name and address of the developer and owner including all partners of a partnership or all officers and directors of a corporation as well as the following:

* * *[1]

b. A description of the condominium project in addition to the legal documents described in paragraph d. of this subsection:

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[1] Not required according to 11/22 Circuit Court Decision.

(1) Map or plat showing size and dimensions of the condominium project together with all improvements, including recreational facilities, proposed construction and present and planned location of streets and roads.

(i) Description of the condominium units offered and the nature and extent of individual ownership in such condominium units.

(ii) Description and nature and extent of ownership of all common elements, general and limited.

(iii) Description, nature and ownership of all property and facilities on the site which are not part of the condominium.

(iv) Description of all existing and proposed recreational facilities and other facilities within the condominium project.

(v) Location, nature and ownership of streets and roads on and contiguous to the site.

(vi) Drawings, architectural plans or other suitable documents setting forth the necessary information for location, maintenance and repair of all condominium facilities. (Such items shall be incorporated in the property report by reference, shall be located at the sales office site and shall be turned over to the council of condominium unit owners upon transfer of control by the developer.)

(2) Projected completion dates for proposed construction, renovation or conversion.

(3) Uses permitted for individual condominium units by the declaration, bylaws of the condominium association or organization and applicable zoning provisions.

(4) Statement as to whether or not the condominium units may be rented.

* * *[1]

(6) Method and timing of transfer of control over the condominium project to a council of condominium unit owners, the association's relationship with the developer and the nature and extent of any interest retained by the developer.

c. A statement of all financial aspects of the condominium project, including but not limited to:

(1) Name of construction mortgagor or the interim mortgagor.

(2) Institution offering long term mortgage financing, if available, and terms and conditions of such mortgage.

(3) Nature and extent of any protection of purchaser's deposits in escrow accounts. In the event that purchasers' deposits are not being placed in an escrow account the following statement must be inserted: "The developer has made no arrangements for protecting deposits for the purchase of a condominium unit. Accordingly, there is a risk that you will lose your deposit if the developer becomes insolvent."

* * *[1]

(5) Nature and extent of any protection to a prospective purchaser if the developer defaults on blanket encumbrance. If there is no protection to purchasers from a developer's default on a blanket encumbrance the following statement must be inserted: "The developer has made no arrangements to protect the purchaser of a condominium unit from its possible default on a blanket encumbrance. Accordingly, there is a risk of losing your financial interest in the event of the developer's failure or bankruptcy."

(6) Statement of any pending litigation which would affect the condominium and/or the developer's ability to convey clear title.

d. Copies of the sales documents and literature including but not limited to:

(1) Copy of purchase contract.

(2) Copies of sample forms of conveyance.

(3) Copies of sample deed of trust, mortgage and promissory note.

(4) Statement of sale prices.

(5) Copy of sales brochure and floor plans.

(6) Statement of terms and conditions of sale including estimated closing and settlement costs, taxes and expected special assessments levied either by the condominium or a governmental entity.

(7) Statement of monthly payments to be itemized as to principal, interest, taxes, condominium fee and utilities.

e. Copies of all required documents binding or to be binding upon the condominium (proposed documents acceptable until final version is available) including:

(1) The declaration or master deed.

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[1] Not required according to 11/22 Circuit Court Decision.

(2) The articles of incorporation or charter of the condominium association.
(3) The by-laws and regulations of the condominium association.
(4) Any leases of real or personal property applicable to the condominium.
(5) Any management contract, employment contract, insurance policy, or other contract affecting the use, maintenance or access to all or part of the condominium.

f. A statement of management and expected operation costs of the condominium.

(1) Copy of the projected annual operating budget for the condominium including, but not limited to, the following:

(i) *Operational Costs*
Utilities.
Heating Fuels.
Janitorial Services.
Trash and Garbage disposal.
Ground and Building Maintenance.
Security.
Maintenance and operation of recreational and other facilities.
Answering Service.
Other operating costs.

(ii) *Management Costs*
Legal and accounting services.
Bookkeeping services.
Management fees.
Other management costs.

(iii) *Fixed Costs*
Building Insurance.
Elevator Maintenance.
Sidewalks and Street Maintenance.
Other fixed costs.

(iv) *Reserve Costs*
Reserve for unexpected repair work.
Reserve for replacement and upkeep of common area and facilities including basis upon which reserves are calculated.
Reserves for improvements.
Other reserve funds.

If no reserve is provided for any one or more of the costs listed in this item, the following statement must be inserted in the property report: "The developer has not provided a reserve for certain possible future costs of the condominium in his budget. Accordingly, it may be necessary to provide for a special assessment to all condominium unit owners to pay for such costs should they occur."

g. In the case of a conversion from rental or other legal status to condominium, a report from a qualified licensed engineer or other qualified professional stating the condition and the useful life of all appliances, the roof, foundation, external and supporting walls, mechanical, electrical, plumbing and structural elements and all other common facilities together with an estimate of repair and replacement costs and a list of any outstanding building code violations.

h. A statement of all warranties and disclaimers being made to the purchaser.

i. A senior executive officer of the developer shall sign the property report and affirm that it and any supplements, modifications and amendments are true, full, complete and correct.

j. Each property report shall contain on the first page the following warning in capital letters:

"MONTGOMERY COUNTY LAW SPECIFICALLY PROHIBITS ANY REPRESENTATION TO THE EFFECT THAT THE COUNTY HAS PASSED UPON THE MERITS OF, OR GIVEN APPROVAL TO THIS CONDOMINIUM. IT IS UNLAWFUL FOR ANYONE TO MAKE, OR CAUSE TO BE MADE TO ANY PROSPECTIVE PURCHASER, ANY REPRESENTATION CONTRARY TO THE FOREGOING, OR ANY REPRESENTATIONS WHICH DIFFER FROM THE STATEMENTS IN THIS PROPERTY REPORT."

11A–4. *Property report; submission to prospective purchaser; filing.*

a. A developer or agent shall not enter into a binding contract or agreement for the sale of any condominium unit unless:

(1) A copy of the property report is filed with the Montgomery County Office of Consumer Affairs at least ten (10) days prior to the first offering or at least ten (10) days prior to the notice of conversion to tenants.

(i) * * *[1]

(ii) Any amendments, modifications or supplements must be filed immediately with the Office of Consumer Affairs and attached to any property reports distributed after the date of filing.

(2) A copy of the property report and any amendments, modifications and supplements thereto have been given to the prospective purchaser.

b. Within fifteen (15) days after the signing of the contract of sale for a condominium unit, the buyer may rescind, in writing, the contract of sale without any liability on the buyer's part, and shall thereupon be entitled to the return of any deposit made on account of the contract.

c. After the signing of the contract of sale for a condominium unit and prior to the closing of the sale, the developer must deliver to the buyer a copy of any amendments, supplements or modifications to the property report. The prospective purchaser may rescind, in writing, the contract of sale within five (5) days after receiving any of the aforesaid items without any liability on the buyer's part and shall thereupon be entitled to the return of any deposit made on account of the contract.

d. If the developer fails to comply with any of the requirements of this Chapter, the buyer may, at any time prior to the closing of the sale, rescind, in writing, the contract of sale, without any liability on the buyer's part and shall thereupon be entitled to the return of any deposits made on account of the contract.

e. The rights of prospective purchasers under this section may not be waived and any such attempted waiver is void.

11A–5. *Notice; property report to tenants; right to terminate.*

a. Prior to conversion of the first condominium unit to condominium status from rental or other legal status, the developer shall give 120 days written notice to all tenants as required by State law. At the time of receiving notice of conversion tenants shall be provided with a property report as described in Section 11A–3 of this Chapter.

b. * * *[1]

11A–6. *Unlawful representations.*

The fact that a property report has been filed with the County shall not be deemed a finding by the County that the property report is true and accurate or that the County has in any way passed upon the merits or given approval to the condominium project. It shall be unlawful to make or cause to be made to a prospective purchaser any representation contrary to the foregoing. It shall likewise be unlawful for any person to make or cause to be made in a property report to a prospective purchaser any statement or representation that is knowingly false or misleading.

11A–7. *Complaints, Penalties and enforcement.*

a. Any person subjected to any unlawful practice as set forth in this Chapter may file a complaint in writing with the Montgomery County Office of Consumer Affairs pursuant to the provisions for filing such complaints as set forth in Chapter 11 of this Code.

b. The Office of Consumer Affairs is hereby authorized and directed to receive complaints filed pursuant to this Chapter and to conduct such investigations and hearings as it deems necessary pursuant to the authority vested to that office by Chapter 11 of this Code.

c. Whenever it is determined by the Office of Consumer Affairs that there has been a violation of this Chapter or any duly adopted rule or regulation of the County, that office is authorized, at its discretion to commence with one or more of the following procedures:

(1) Attempt to conciliate the matter by conference or otherwise and secure a written conciliation agreement; or

(2) Seek a written assurance of discontinuance which shall be signed by the developer and the Director of the Office of Consumer Affairs; or

(3) Issue appropriate cease and desist orders; or

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[1] Not required according to 11/22 Circuit Court Decision.

(4) Refer the matter to the County Attorney for injunctive or other appropriate legal action.

d. Any person who violates any provision of this Chapter, or who makes an untrue or misleading statement of fact in a property report, or fails to state any fact required to be stated therein shall be liable for the payment to the County of a civil penalty, recoverable in a civil action, in the sum or not more than Five Hundred Dollars for each such violation. Each copy of a property report containing an untrue or misleading statement of fact or omission of any fact required to be stated therein shall constitute a separate offense.

e. It shall be unlawful for any developer to offer for sale any condominium unit in any condominium unless such developer has first filed a property report with Montgomery County in accordance with the terms of this Chapter. Any developer who violates this provision shall be guilty of a misdemeanor and upon conviction shall be subject to a fine of not more than $1000 or imprisonment for a period of not more than six (6) months, or both.

f. In addition to any criminal or other penalty herein provided, injunctive or other appropriate action or proceeding to correct a violation of this Chapter may be instituted by the County Attorney's Office and any court of competent jurisdiction may issue restraining orders, temporary or permanent injunctions or other appropriate forms of relief.

g. Nothing herein shall prevent any person from exercising any right or seeking any remedy to which such person might otherwise be entitled or from filing an appropriate complaint with a court of law or equity.

11A–8. *Administration.*

The Office of Consumer Affairs shall be responsible for administration of this Chapter and the County Executive shall, from time to time, issue such written regulations as may be necessary to put into effect and to administer the provisions of this Chapter.

11A–9. *Application.*

a. This Chapter shall be effective throughout the County except in any incorporated town, village, or other municipality which by law has authority to enact a law on the same subjects as covered by the sections of this Chapter. If any such incorporated town, village, or other municipality shall adopt this Chapter and request the County to enforce the provisions thereof within its corporate limits, the County shall thereafter administer and enforce the same within such incorporated town, village or municipality.

b. The provisions of the Chapter shall apply to:

(1) Any condominium offering made after the effective date of this Chapter.

(2) In the case of condominium offerings in which fifty (50) percent or 25 condominium units, whichever is less, remains to be sold as of the date this Act becomes law, the developer shall be required to file a property report with the Office of Consumer Affairs by the effective date of this Chapter.

(3) Any purchaser who signs a contract between the date this Chapter becomes law and the effective date hereof shall be provided with a property report on the effective date of this Act. Any such purchaser who has not closed the sale prior to the effective date of this Chapter shall have fifteen (15) days after receipt of the property report in which to rescind the contract of sale, in writing, without any liability on his part, and shall be entitled to the return of any deposit made on account of the contract.

Sec. 2. Severability.

The provisions of this Act are severable and if any provision, clause, sentence, section, word or part thereof is held illegal, invalid or unconstitutional, or inapplicable to any person or circumstances, such illegality, invalidity or unconstitutionality, or inapplicability shall not affect or impair any of the remaining provisions, clauses, sentences, sections, words, or parts of the Act or their application to other persons or circumstances. It is hereby declared to be the legislative intent that this Act would have been adopted if such illegal, invalid, or unconstitutional provision, clause, sentence, section, word or part had not been included therein, and if the person or circumstances to which the Act or part thereof is inapplicable had been specifically exempted therefrom.

Sec. 3. Effective date.

60-564 O - 75 - 20

This Act shall take effect on the 76th day following the date on which it becomes law.

Approved:
JUNE 7, 1974.

NEAL POTTER,
President, Montgomery County Council.

JUNE 12, 1974.

JERRY T. GREAR,
County Executive.

Attest: June 13, 1974,

ANNAP SPATES,
Secretary of the County Council.

[Excerpts From the Maryland Condominium Act]

§ 11–102.1. NOTICE PRIOR TO CONVERSION OF RESIDENTIAL PROPERTY TO CONDOMINIUM

(a) At least 180 days before property is subjected to a condominium regime, the owner shall give to each tenant then occupying any portion of the property as his residence a notice in the form specified in subsection (f) and shall deliver a copy of the notice prior to entering into a lease to each tenant who thereafter leases any portion of the property for his residence.

(b) The notice shall be considered to have been given to each tenant if delivered by hand or mailed, postage prepaid to the tenant's last known address.

(c) A tenant leasing any portion of the property as his residence at the time the notice referred to in subsection (a) is given to him may not be required to vacate the premises prior to the expiration of 180 days from the giving of the notice except for:

(1) Breach of a covenant in his lease; or

(2) Nonpayment of rent.

(d) Any tenant leasing any portion of the property as his residence at the time the notice referred to in subsection (a) is given to him and whose lease term would ordinarily terminate during the 180-day period is entitled to have the term extended on the same terms and conditions until the expiration of the 180-day period.

(e) Any tenant leasing any portion of the property as his residence at the time the notice referred to in subsection (a) is given to him may terminate his lease, without penalty for termination upon at least 30 days' written notice to his landlord.

(f) The notice referred to in subsection (a) shall be sufficient for the purposes of this section if it is in substantially the following form:

NOTICE OF INTENTION TO CREATE A CONDOMINIUM

_____(Date)

This is to inform you that the premises known as_____
_____
_____may be subjected to a condominium regime in accordance with the Maryland Condominium Act following the expiration of 180 days from the date of this notice.

If you are a tenant of these premises, you are entitled to remain in your leased premises until the expiration of the term of your lease or the 180 day period, whichever is longer, unless you breach a covenant in your lease, or fail to pay your rent. If the term of your lease expires during the 180 day period, you may have it extended, on the same terms and conditions, until the expiration of the 180 day period.

If you are a tenant in these premises, you may terminate your lease upon at least 30 days' prior written notice to your landlord.

(g) A declaration may not be received for record unless there is attached thereto an affirmation of the developer in substantially the following form:

I hereby affirm under penalty of perjury that the notice requirements of section 11–102.1 of the Real Property Article, if applicable, have been fulfilled.

Developer
By_____

(h) Failure to fulfill the provisions of this section does not affect the validity of a condominium regime otherwise established in accordance with the provisions of this title. (1974, ch. 704; 1975, ch. 786, § 1.)

Effect of amendment.—The 1975 amendment, effective July 1, 1975, rewrote this section.

Editor's note.—Section 2, ch. 704 Acts 1974, provides that the act shall take effect July 1, 1974.

Section 5, ch. 786, Acts 1975, effective July 1, 1975, provides that: "That act shall be construed only prospectively and shall not be applied or interpreted to have any effect upon or application to any event or happening occurring prior to the effective date of this act."

§ 11–124. Disclosure Requirements

(a) *Material to be furnished by vendor to purchaser before closing.*—Not later than 15 days prior to the closing of the initial sale of each unit to a member of the public, the vendor shall furnish to the purchaser the following:

(1) A copy of the proposed contract of sale for the unit;

(2) A copy of the proposed declaration and bylaws;

(3) A copy of the proposed articles of incorporation of the council of unit owners, if it is to be incorporated;

(4) A copy of any proposed management contract, employment contract, or other contract affecting the use, maintenance, or access of all or part of the condominium to which it is anticipated the unit owners or the council of unit owners will be a party following closing;

(5) A copy of the projected annual operating budget for the condominium including reasonable details concerning the estimated monthly payments by the purchaser for assessments, and monthly charges for the use, rental, or lease of any facilities not part of the condominium;

(6) A copy of any lease to which it is anticipated the unit owners or the council of unit owners will be a party following closing;

(7) A description of any contemplated expansion of the condominium with a general description of each stage of expansion and the maximum number of units that can be added to the condominium;

(8) A copy of the floor plan of the unit;

(9) A description of any recreational or other facilities which are to be used by the unit owners and maintained by them or by the council of unit owners and a statement as to whether or not they are to be part of the common elements;

(10) A statement as to whether streets within the condominium are to be dedicated to public use or maintained by the council of unit owners; and

(11) In the case of condominiums containing buildings substantially completed more than five years prior to the recordation of the declaration, a statement of the physical condition and state of repair of the major structural, mechanical, electrical, and plumbing components of the improvements to the extent reasonably ascertainable. The vendor is entitled to rely on the reports of architects or engineers authorized to practice their profession in this State.

(b) *Change in material following delivery to purchaser.*—Any material furnished pursuant to subsection (a) may not be changed or amended following delivery to the purchaser, if the change or amendment would affect materially the rights of the purchaser, without first obtaining approval of the purchaser. A copy of any amendments shall be delivered promptly to the purchaser.

(c) *Purchaser's right to rescind contract of sale.*—Any purchaser may at any time (1) within 15 days following receipt of all of the information required pursuant to subsection (a) and (2) within five days following receipt of the information required pursuant to subsection (b), rescind in writing the contract of sale without stating any reason and without any liability on his part, and he shall be entitled to the return of any deposits made on account of the contract.

(d) *Untrue statement or omission of material fact.*—Any seller who, in disclosing the information required pursuant to subsections (a) and (b), makes any untrue statement of a material fact, or omits to state a material fact necessary in order to make the statements made, in the light of circumstances under which they were made, not misleading, shall be liable to any person purchasing a unit from him. However, no action may be maintained to enforce any liability created under this section unless brought within one year after the facts constituting the cause of action are or should have been discovered.

(e) *Waiver of purchaser's rights.*—The rights of purchasers under this section may not be waived in the contract of sale and any attempted waiver is void. However, if any purchaser proceeds to closing, his right under this section to rescind is terminated.

(f) *Sale of unit for nonresidential purposes.*—The requirements of this section do not apply to the sale of any unit which is to be occupied and used for nonresidential purposes.

(g) *Location of condominium immaterial.*—The requirements of this section shall apply to the sale of any unit offered for sale in the State without regard to the location of the condominium. (1974, ch. 641; 1975, ch. 786, § 1.)

COMMENT

Section 11–124 contains entirely new material and represents one of the most comprehensive disclosure and anti-fraud provisions found in the Condominium Act of any jurisdiction. The requirements of this section apply to condominiums offered for sale in the State of Maryland without regard to the location of the condominium. Subsection 11–124 (f) provides that the requirements of this section do not apply to offers for the sale of units intended to be used for nonresidential purposes such as industrial space, commercial space, offices, etc.

Since subsection 11–101(f) of this Title defines "developer" as the person who actually *creates* the condominium regime, subsection 11–124(a) imposed the disclosure requirements on the "vendor" who *initially* offers the condominium unit for sale "to a member of the public." A transfer of the entire condominium project by the "developer" to another person for the purpose of the resale of the individual units to members "of the public" in the ordinary course of that person's business, or for purposes of avoiding the requirements of § 11–14, will not eliminate the requirements for disclosure when units are later offered for sale to the public.

Section 11–124 does not necessarily require that the disclosure provisions shall be complied with prior to or at the time the condominium units are offered for sale, or even at the time that an agreement for the sale of a unit is executed. The section does provide for a 15-day "cooling off" period, however, and, pursuant to subsection 11–124(c), any "purchaser" has an unqualified right to rescind his agreement to purchase a condominium unit, by notice in writing to the "vendor" within 15 days "following receipt of all of the information required" to be disclosed pursuant to subsection 11–124(a), provided he has not elected to close without such information.

Section 11–124(a) is not intended to provide that recorded or even executed copies of the materials described in subsections 11–124(a)(1), 11–124(a)(2), 11–124(a)(3) or 1–124(a)(5) be furnished to the purchaser. These materials may be in the nature of unrecorded unexcuted drafts. However, in the event of any change or amendment which would *"materially"* affect the rights of the purchaser" then the purchaser must be furnished with the changes or amendments and shall have 5 days following his receipt of the amended materials within which to rescind his agreement of sale. If the purchaser does not elect to rescind within the time provided in subsection 11–124(c), then the amendments shall be considered approved.

The right to rescind created pursuant to subsection 11–124(c) may be exercised by the purchaser without liability. Subsection 11–124(e) prohibits attempts to waive the "rights of the purchaser" to receive the information and materials required to be disclosed pursuant to this section and prohibit attempts to waive the "rights of the purchaser" to rescind. However, the purchaser may elect to waive his right to rescind by proceeding to close. This provision avoids possible clouds on title. It also permits the purchaser to obtain mortgage financing to enable him to close if he wishes. If the purchaser waives his statutory right to rescind under subsection 11–124(e), he does not thereby waive any rights he may have under subsection 11–124(d) or any rights (including the right of rescission) he may have at common law.

Cross reference.—See § 11–128(e) of this article.

Effect of amendment.—The 1975 amendment, effective July 1, 1975, inserted the present paragraph (1), redesignated former paragraphs (1) through (7) as paragraphs (2) through (8), added paragraphs (9) through (11) and eliminated in present paragraph (8) the provisions relative to furnishing information necessary to show location of common elements and other facilities.

Editor's note.—Section 5, ch. 786, Acts 1975, effective July 1, 1975, provides that: "This act shall be construed only prospectively and shall not be applied or interpreted to have any effect upon or application to any event or happening occurring prior to the effective date of this act."

§ 11–125. Termination of Leases or Management and Similar Contracts

Within three years following the date on which units have been granted by the developer to unit owners having a majority of the votes in the condominium, any lease, and any management contract, employment contract, or other contract affecting the use, maintenance or access of all or part of the condominium entered into prior to the date to which the council of unit owners is a party may be terminated by a majority vote of the council of unit owners without liability for the termination. The termination shall become effective upon 30 days' written notice of the termination from the council of unit owners. (1974, ch. 641.)

COMMENT

Section 11–125 contains entirely new material relating to the protection of the consumer. This section gives the council of unit owners, by a majority vote, the power to terminate any lease and any management and similar contracts which the council may have entered into while the "developer" controlled the council. This power to terminate expires three years following the date upon which the "developer" last had a majority of the votes in the council.

Cross reference.—See § 11–128 (f) of this article.

§ 11–126. PROVISIONS REQUIRING EMPLOYMENT OF DEVELOPER OR VENDOR TO EFFECT SALE

Any provision of a declaration or other instrument made pursuant to this title which requires the owner of a unit to engage or employ the developer or any subsidiary or affiliate of the developer for the purpose of effecting a sale or lease of any unit is void. Any provision of any contract for the sale of any unit which requires the purchaser to engage or employ the vendor or any subsidiary or affiliate of the vendor for the purpose of effecting a sale or lease or any unit is void. The provisions of this section apply to declarations, instruments and contracts made prior to and after July 1, 1974. (1974, ch. 641.)

The CHAIRMAN. Thank you, Mr. Arkin.

Our next witness is a representative of Mr. Cruikshank, Mr. Marlin, I take it you and whoever is with you will share the presentation.

Mr. MARLIN. I express Mr. Cruikshank's regrets for not being able to be here this morning.

The CHAIRMAN. His statement will be printed in full in the record.

[The complete statement follows:]

TESTIMONY ON S. 2273 by NELSON H. CRUIKSHANK, PRESIDENT,
of the NATIONAL COUNCIL OF SENIOR CITIZENS,
1511 K STREET, N.W., WASHINGTON, D.C.
submitted to the
COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS,
UNITED STATES SENATE
October 7, 1975

A. Introduction

Good morning, I am Nelson Cruikshank, President of the National Council of Senior Citizens. The National Council consists of over 3,500 clubs, with a membership of more than three million older persons. It was instrumental in the fight to enact Medicare in the early sixties and has remained an effective, nonpartisan forum for political and social action for the elderly.

We are here today because we care about housing for the country's almost 22 million older citizens. We are convinced that the condominium trend has become a permanent part of the elderly housing picture -- and indeed of the nation's entire urban and metropolitan housing pattern. The Department of Housing and Urban Development recently found that approximately four million Americans now live in condominium and cooperative housing, and that condominiums have increased in number nearly 15-fold since 1970. We have been giving much thought to how this growing phenomenon is affecting the elderly, and what must be done to ensure that many will benefit, and that none will be harmed.

The effect is two-fold. Elderly persons with an adequate income are increasingly choosing condominiums for retirement living because they combine many of the conveniences of rental living with the independence, tax advantages and equity of owning a home. However, the median income of older persons living alone in 1973 was $2,725; and half of the families headed by an older persons had incomes of less than $6,426.

For these elderly persons, purchase of a condominium unit is next to impossible. And even if they could afford it, some feel they are simply too old to take on the responsibilities of homeownership. For thousands of older tenants, the conversion of rental units into condominiums represents a severe economic and psychological dilemma.

We have reviewed S. 2273 with great interest. We found that while the consumer protection aspect of the condominium phenomenon is treated quite comprehensively, the conversion aspect -- so critical to the elderly -- is not addressed at all.

B. Regulation of Condominium Sales

The proposed Act goes a long way in providing full disclosure and protection to the prospective buyer and the public. It could prevent many of the most common deceptive practices against vulnerable elderly and other purchasers. We have only two additional suggestions.

First, section 6(a)(6) requires a two-year projection of annual operational and maintenance expenditures. A developer should also be required to provide a statement of the actual expenses for the past three years or the period of operation, which ever is longer. This would provide the prospective buyer with some idea of the accuracy of the projection and a realistic picture of what he would immediately have to begin paying.

Second, the Bill provides for full disclosure by the developer to initial purchasers. But it is silent as to subsequent purchasers. Both the District of Columbia and Virginia currently regulate condominium resales in this manner. Full disclosure in resale should be added to S. 2273.

C. Condominium Conversion: Its Effects

Conversion of rental units into condominiums has a two-tiered impact. First, it affects the total urban and metropolitan housing market. This in turn affects the elderly, and other low and moderate income residents. Second, it affects elderly tenants directly in a personal and often

dramatic way -- it forces them to uproot themselves, compete for a dwindling number of rental units, relocate and reestablish patterns of daily living and social networks.

1. Effects on Housing Market. The Department of Housing and Urban Development found that approximately 100,000 rental units were converted to condominiums from 1970 through March, 1975. This means the nation's supply of rental units has been permanently diminished by 100,000. Dispersed evenly across the nation, this loss may seem of little consequence. But instead, conversions are concentrated in metropolitan areas already experiencing a serious rental housing shortage. In cities like New York, San Francisco and Washington, D.C. conversion has served to exacerbate an existing housing crisis. For example, in the District of Columbia, a city with an overall vacancy rate of under two percent, close to 5,000 rental units had already been lost to condominium conversion when the city enacted a moratorium in August, 1974.

At the same time, most of these same urban areas are experiencing a decline in the constrution of new rental housing, skyrocketing rental and housing costs, and an increasing number of households in need of housing assistance. Continued conversion in such areas could pose an alarming housing threat.

2. Effect on Elderly. There is no doubt that this threat falls disproportionately on the elderly. They often live in buildings which are prime targets for conversion -- old but substantial buildings in good locations. And yet they are least able to cope with choices and the changes which conversion can bring.

Many settled into their apartments long ago, often chosing them for their proximity to shopping areas, doctors, family and transportation. When they receive notice of conversion, they want to stay. But generally, they are on fixed incomes, feeling the bite of inflation, and cannot afford to pay for apartments that often cost more than 150 times their monthly rent. When interest, maintenance fees (apt to be 30% higher in conversions than in new developments, according to the

HUD study) and taxes are included, the monthly payment for a condominium purchaser may be well over 35% higher than the former rental payment (HUD). A recent National Council survey of 97 renters who moved from converted buildings in the District of Columbia took as a criterion of a respondent's ability to purchase a factor of 2.5 times his annual income -- we found that 73% of the low and moderate income elderly would have had to pay more than 2.5 times their income, and thus were priced out of the market. Moreover, old age often makes arranging a mortgage difficult or impossible.

In the end, thousands of older persons are often relocated into units which may not be comparable to their old apartments in terms of rent and convenience. In NCSC's survey in the District of Columbia, 72% of the low and moderate income elderly who were displaced due to conversion experienced a 20% or greater increase in rent as they moved to their new location. Eighty-two percent were forced to spend a fourth or more of their income on rent.

The conversion process means not only serious economic strain for the elderly, but great psychological trauma. Relocation of aged persons means the disruption of long-established life patterns, a debilitating shock from which they may never fully recover.

A summary of ten research studies done nationwide on the effects of relocation on the elderly was recently published by the American Psychological Association. Although many of the subjects of these studies were residents of nursing homes, many were healthy, independent tenants of apartment houses. Of the ten studies, seven showed excess mortality rates associated with relocation from the familiar environment. The other three showed negative effects such as depression or decline in health.

In the NCSC study, low and moderate income elderly respondents consistently reported such disruption: 92% found it harder to see their families after moving; 81% found it harder to get to church, and 70% found it harder to see their doctor. Forty-five percent experienced ill health effects, which were often described more particularly as

depression, mental distress and great anxiety. Several felt the continuing fear that their new building would go condominium and they would again be uprooted.

D. Condominium Conversion: Alternative Legislative Solutions

What is the answer to the conversion problem? Certainly not to ban all conversion, for it offers many advantages -- it means needed rehabilitation of older urban sections, a greater tax base for cities, and a new form of ownership ideal for small city and suburban households. But in order to protect tenants, maintain a sufficient supply of rental units, keep a healthy balance of owned vs. rental housing, and foster economic and social stability, reasonable controls must be placed on the conversion process.

The National Council has made an extensive examination of federal, state and local legislation regarding condominiums. This study revealed that very little attention has been given to the conversion aspect. Few jurisdictions have addressed the problem at all. Several cities -- San Francisco, San Jose, Tiburon and Washington, D.C. -- enacted a moratorium while a conversion policy was being formulated. New York, and now San Francisco, allow conversion to proceed only when 35% of the tenants in a project agree to purchase their unit. This method, however, can produce haphazard and inequitable results, gives no assistance to the other 65% of the tenants, can lead to landlord intimidation, and is of questionable constitutionality.

Instead, what is needed is a solution which ties conversion into a city's housing and land use goals. Two places in California, Palo Alto and Marin County, prohibit conversion when the rental vacancy ratio falls below a specified percentage. The National Council has recommended a similar provision for the District of Columbia and is now designing a model statute incorporating this idea.

The statute would allow conversion to proceed only when the low and moderate income rental housing vacancy rate is above 3%. It would provide, as well, realistic options for low and moderate income elderly tenants displaced when the vacancy formula does allow conversion. A

long-term older tenant who wished to remain in his apartment as a renter would be allowed a life tenancy, and might be eligible for a rent subsidy. An older person who wished to purchase but could not obtain conventional financing would be given a low-interest, long-term loan. Finally, tenants electing to move would receive relocation payments and assistance.

E. Condominium Conversion: The Federal Role

The federal government must take a leadership stance in regard to conversion. While conversion control may ultimately be to some extent a state and local matter, conversion consequences are too serious for federal decision-makers to ignore. The federal government could meet these consequences primarily in three ways.

First, it could assist in the financing of state conversion control. Federal funding participation would encourage states and localities to focus on conversion as a problem and stimulate them to forge their own plans for regulation of the conversion process.

It could work this way: The state or city could pass conversion control legislation, to be financed by a "condominium fund". The fund could be composed of both state and federal monies, which could be used to administer the law, give low-interest loans, provide rent subsidies and relocation assistance. Some federal money, theoretically, is already available for such purposes from the Housing and Community Development Act and from Revenue Sharing. In reality, the money has not been spent in this way. Funding directly for conversion control would provide a strong impetus for enactment of state and local measures such as we have described above.

Second, more federal funding is drastically needed for the construction of new rental units. With the availability of more rental units, the condominium conversion process will lose some of its sting for elderly and other tenants, and the cities will have a better balanced housing market in which conversion will take its place among other competing forces. But as it stands now, new constrution has slowed almost to a halt, and this fact makes the conversion process a

devastating one.

Third, the federal government must take responsibility for older persons and other tenants displaced due to conversion. The Uniform Relocation Assistance Act presently provides assistance to persons displaced because of federal or federally assisted programs. Why couldn't the Act be extended to cover those displaced as a result of conversion? Certainly the hardship to tenants forced to move as their buildings go condominium is equal to -- in fact, is virtually the same as -- the hardship the Act was intended to alleviate.

F. Conclusion

Condominiums, both converted and new, are here to stay. Basically, the concept is a good one, in that it offers a new choice. S. 2273 would assure that the choice is a real one for prospective purchasers. But what about poor and elderly tenants enmeshed in the conversion dilemma? The federal government must join with the states and localities in a policy which would allow them a choice, too.

STATEMENT OF DAVID H. MARLIN, NATIONAL COUNCIL OF SENIOR CITIZENS, ACCOMPANIED BY ERICA WOOD, STAFF ATTORNEY

Mr. MARLIN. We will summarize. What we want to talk about this morning is an area that has been overlooked in the bill.

That issue to the conversion of existing rental units into condominium ownership. It affects the 22 million older persons in the country more profoundly than the consumer protection issues in the bill could.

Mrs. Wood will make a brief statement.

The CHAIRMAN. All right. Tell us your qualifications.

Mrs. WOOD. I am a staff attorney for Legal Research and Service for the Elderly, the legal unit sponsored by the National Council of Senior Citizens. Over the past year I have spent quite a lot of time examining the effects of condominium conversion on the Nation's elderly.

We have found that the conversion of rental units into condominiums has two separate, but interlocking dimensions. First, it affects the total urban, metropolitan housing market which in turn has a great deal of effect on elderly and other low- and moderate-income residents.

Second, it affects the elderly tenants directly in a personal and dramatic way, forcing them to uproot themselves and compete for a dwindling number of rental units.

The Department of Housing and Urban Development has found that 100,000 rental units were converted to condominiums from March 1970 to March 1975. Dispersed evenly across the Nation, this loss may seem of little consequence. Instead conversions are concentrated in metropolitan areas already experiencing a serious rental housing shortage, skyrocketing rental and housing costs in an increasing number of households.

Conversion in such areas can pose an alarming housing threat. There is no doubt this threat falls disproportionately on the elderly. Many of the elderly settled into their apartments long ago, often choosing the area for its proximity to shopping areas, doctors, transportation, and family.

When they receive notice of conversion, they want to stay, but they can't stay because they are on generally fixed incomes, feeling the bite of inflation, and cannot afford to pay for apartments that often cost over 150 times their monthly rent, or for monthly payments which may well be over 35 percent higher than the former rental payment. Moreover old age often makes arranging a mortgage difficult or impossible.

In the end, thousands of older persons are often relocated into units that may not be comparable to their old apartments in terms of rent and convenience.

We in the national council did a survey of such elderly residents in converted buildings in the District of Columbia and found that 72 percent who were displaced experienced a 20 percent or greater increase in rent as they moved to their new location.

Aside from the economic strain, conversion means great psychological trauma for the elderly. It means the disruption of long established life patterns, a debilitating shock from which they may never recover.

In the NCSC study, we found that 92 percent of the low- and moderate-income respondents found it harder to see their families after moving. Eighty-one percent found it harder to get to church and 70 percent found it harder to see their doctor. Forty-five percent said they experienced ill health effects, including depression, mental distress, great anxiety, and continuing fear that their new building would go condominium.

The National Council has made a study of Federal, State, and local legislation regarding condominium conversion. We found that little attention has been addressed to this issue.

Several cities have enacted a moratorium while they formulate a policy for conversion. New York and San Francisco allow conversion to proceed only when 35 percent of the tenants in a project agree to purchase their unit. This method, however, can tend to produce haphazard and inequitable results, provides no solution for the 65 percent of the tenants who do not agree to buy, and it is of questionable constitutionality.

Instead, what is needed is a solution which ties conversion into a city's housing and land use goals. Two places in California, Palo Alto and Marin Counties, prohibit conversion when the rental vacancy ratio falls below a specified percentage. The National Council has recommended a similar provision for the District of Columbia and is providing a model statute incorporating this idea; and providing, as well, realistic options for low- and moderate-income elderly, displaced tenants.

The Federal Government, we feel quite strongly must now begin to take a leadership stance in regard to conversion. While conversion control may be a State and local matter, the consequences, as we have detailed, are far too serious for Federal decisionmakers to ignore.

There are three ways that the Federal Government may begin to meet these consequences. First, it could assist in the financing of State conversion control. Federal funding participation would encourage States and localities to focus on conversion as a problem and stimulate them to forge their own plans for regulation of the conversion process.

Second, more Federal funding is needed for the construction of new rental units. With the availability of more rental units, the condominium conversion process will begin to lose some of its sting for elderly and other tenants. The city will have a better balanced housing market where conversion will take its place among other competing forces.

Third, the Federal Government must take responsibility for the older, displaced tenants. The Uniform Relocation Assistance Act provides assistance to persons displaced because of Federal or Federally-assisted programs. We feel this Act could be extended to cover those displaced as a result of conversion. Certainly the hardship to the tenants forced to move as the buildings go condominium is similar to the hardship that the act was intended to alleviate.

We will be happy to respond to any questions.

The CHAIRMAN. Mr. Marlin, would you like to add anything?

Mr. MARLIN. No.

The CHAIRMAN. I'm glad we have this as a panel. It may seem unorthodox, but I think all of you have expertise which will be helpful.

The issue of developer control and the transfer of control to unit owners is one of the great concerns in condominiums. The bill requires the control be turned over when 80 percent of the units are occupied or after 1 year, whichever is sooner.

Several witnesses have suggested that 1 year is too short a time. On the other hand, some definite prescribed time period may be advisable.

Mr. Hyatt, what do you think would be the optimum method of determining transfer control to unit owners?

Mr. HYATT. The problem with 1 year is we may not have enough units sold to provide the work force of homeowners to manage the project. In our prepared testimony we suggested a proposal much like that suggested by Mr. Arkin. We didn't know we were both doing it.

The phased turnover on percentage of units sold so that approximately 20, 25 percent of the board would be made up of homeowners when that same percentage had been sold. In the Georgia statute, we have enough people in there, or they should know by then that the program will not go.

The CHAIRMAN. You suggest two things: No. 1, a proportional representation of the owners as they move into the condominium. No. 2, an outside limit of 3 years at the end of which time the owner who occupies would have control.

Mr. HYATT. Three years and 75 percent, whichever comes sooner; 75 or 80 percent is clearly a maximum time to turn over.

The CHAIRMAN. Do you agree, Mr. Arkin?

Mr. ARKIN. I suggest 2 years as an outside limit; 2 years or the 75 percent, as I discussed in my testimony. If you have a development which takes longer than 2 years to go from first settlement to 75-percent settlement, you probably have a development which is not going to be economically feasible.

This brings up one question not addressed in this proposed legislation at all—that is, what happens to a development that partially sells out and then the sales slow down or stop after settlements have already begun to take place?

This can leave the consumers hung up. They are then in a situation which is neither here nor there. They are in an apartment or complex which is partially owner occupied and partially owned by developers who are probably renting out other units as rentals. Although we have taken no position on how the problem could be addressed, it is a real problem in some parts of the country and has been a serious problem in this area. It deserves some thought by the committee.

The CHAIRMAN. The Secretary of Housing and Urban Development yesterday testified that the developer should not have to pay total condominium fees for unoccupied units as provided in S. 2273.

Do you agree and do you see the possibility of allocating to the developer a fair prorated share of the unsold units?

Mr. ARKIN. I think an argument could possibly be made that because a developer-owned unit is not occupied, that certain costs which may be condominium costs are not proper to charge to the developer, such as water or gas heat or electricity, where these are centrally metered.

However, certain other costs of running the development, relating to maintenance, management and, essentially, the care of the facility, are ongoing costs. If they are not borne by the developer, they have to be borne by the association. If they are borne by the association, then the developer should be responsible for his share.

The developer—where there is central metering—could be made responsible for 80 percent as his proportionate share, for his unoccupied units. If you went below that kind of figure, you'd be jeopardizing the fiscal viability of the project. For noncentrally metered projects, he should pay the full share.

The CHAIRMAN. Well, of course, he is the man who takes the risk, who builds the condominium. He makes the gain, makes the profit. Why shouldn't he assume the full burden of losses since he assumes the full burden of profits? If he makes a killing on this, he doesn't hand it out to the condominium owners.

Mr. ARKIN. I feel that as far as losses are concerned, or for any deficits resulting from intentional or unintentional lowballing—or from unfair cost allocation—the developer should be fully responsible. He takes risks. His risk is matched later on by a similar risk for the consumer as soon as he takes title. They are then in a mutual risk position.

If the development doesn't sell out, the consumer is also hung up. But I think it is important to stress, along this line, that no matter what formula is devised for developer share of expenses, if the planning goes awry, the developer must be responsible for any deficits that result.

The CHAIRMAN. Mr. Hyatt, what about it?

Mr. HYATT. I agree that the developer should carry the loss totally in the event something goes awry. I think as a practical matter that the developer should pay the full tariff.

The costs that are incidents of ownership are generally small. In our part of the country, most condominium developments are of the townhouse variety. Most utilities are billed to the unit for internal gas, electricity—whatever.

The only real charge or common expense which is a function of occupancy is the sewerage which is not—about but a couple of dollars a month.

The CHAIRMAN. We are going over a little.

Mr. HYATT. Yes, but the loss to the association when the developer says, "I will not pay anything," is so great that too often at turnover time, the association finds a substantial deficit and often a substantial number of unpaid bills.

If you don't have some control to make sure there is a constant cash flow, particularly requiring there be a reserve set aside, assuming legislation will protect those reserves from the ravages of the Internal Revenue Service, the associations will not be able to function.

The CHAIRMAN. Mrs. Wood, your statement gives suggestions as to how the Federal Government could become involved in condominium conversion and displacement of elderly persons. In view of the fact that condominium conversion is a highly localized phenomenon, widespread in a few large urban areas, wouldn't it be better to handle the problem on a local or State level rather than involve the Federal Government?

Mrs. WOOD. I think it is important that the Federal Government encourage conversion control in the areas which need it. In areas that don't need it, many of the rural areas across the country would choose not to adopt this kind of control.

The CHAIRMAN. If we incorporated this into the legislation, the option would be exercised by the locality, city, or State.

Mrs. WOOD. I think we would provide—there would be certain guidelines for the adoption of State legislation. If those guidelines were met, then the Federal funding participation would be forthcoming.

Mr. MARLIN. I agree with Mrs. Wood. It would be optional upon the States to enact legislation that would pick up the Federal interest and the Federal programs that would be available under the statute.

It is our belief that it is primarily a local matter. It must be dealt with, at least at this stage of the process, on that level.

The CHAIRMAN. What would be the incentive for the State to act?

Perhaps I misunderstand you. You wouldn't have any necessity for compliance unless the State wanted to take full initiative, or where they could only opt out of it, or they could only opt that way by meeting certain standards.

Mr. MARLIN. The incentive would be money. States and cities that are burdened by the conversion process are finding it very difficult, particularly with the decline in housing construction and the ravaging of Federal programs over the last few years, to do anything about stimulating the construction or even renovation of existing buildings.

The rental housing vacancy rate in a city like Washington has declined to 1.8 percent. In San Francisco, it is 2 percent. That is the extent of vacant rental housing without new rental housing being built. In order to bring the conversion problem under control, the Federal Government, by programs such as the ones we have suggested or hinted at, would be able to supply the financial incentive to get the States moving in this direction. So far the only legislation has been city legislation, in New York City, San Francisco, and several cities in California that have had conversion problems.

The CHAIRMAN. You are saying the Federal Government should step in as the means of conserving housing?

Mr. MARLIN. That is correct.

The CHAIRMAN. For the elderly, particularly, who find themselves in a position where there is very little available. Vacancy rates are extremely low in some areas of the country.

When these units convert from rent to condominium, the people who had occupied the rental units, usually low income or modest income people are in a very difficult and discriminatory position.

Mr. MARLIN. That is correct, and a very hazardous, precarious position. They must sometimes relocate miles from where they have been.

The CHAIRMAN. This legislation will have enough trouble as it is.

I wonder if there is another way to meet this problem. The administration decided in January 1973 to kill the Government assisted housing programs, all of the programs that are so essential, including 236 which is appropriate here.

Then the condominium situation aggravated this.

Mr. Arkin, do you think this legislation can cope with that, that very serious problem?

Mr. ARKIN. I think it is an extremely serious problem. It has been a particularly serious problem in the Washington area, where a large proportion of the condominium housing stock on the market in the past 5 years has come from conversion rather than from new building. The city of Washington has answered the problem partially by moratoriums.

To a certain extent, in some of the surrounding jurisdiction——

The CHAIRMAN. Moratorium on conversion so they would be unable to convert to condominiums?

Mr. ARKIN. In the District of Columbia, one that has received, I believe, two renewals so far. The problem may have been alleviated somewhat because the bloom is now off the rose, to a certain extent, in condominium conversion.

So many condominiums have converted with nothing more than cosmetic rehabilitation. The problems which have emerged as a result—and resulting publicity—has scared off buyers and reduced the incentive to convert.

An engineering report, as suggested by the proposed legislation, would show a prospective purchaser whether a unit in a conversion will be a good purchase or not. It would tend to remove some of the questionable conversions from the market.

From a practical standpoint, I am afraid of lumping too much into one bill, of putting too many public policy questions into the same bill, because the bill then becomes wide open for attack from any angle.

I think essentially that the conversion problem is a local problem, but that the abuses——

The CHAIRMAN. The only local instrument that seems to be available is moratorium, and that is not satisfactory.

A good deal of the motivation behind this bill was on the part of many of us—was the fact we found modest and low income people with no place to go.

Mr. ARKIN. I think part of the answer may be in uncorking the Federal subsidies on housing and revitalizing some of the Federal housing programs.

Part of the problem with the shrinkage of rental housing is that rental housing is no longer an attractive investment.

The CHAIRMAN. The administration has taken the big section 8 program—a program into which an enormous amount of money is authorized—we provided $600 million for this year to fund only on a 1-year basis.

The first year contracts alone are estimated to cost $17 billion in the next several years, to provide funds to people who have modest incomes so they can go out and rent.

If the units are going to be converted to condominiums, they won't have the opportunity because the vacancies will be so few that rents will go right up through the ceiling.

Mr. ARKIN. Rents are already going up through the ceiling because of the low vacancy rates, and because rental units are no longer attractive to investors.

The CHAIRMAN. We have to take things one at a time. One of the elements that aggravates that would be the continued conversion from rental unit to condominium. This diminishes the available rental market.

Since the only laws the administration will administer that will help housing for low income people is to give them the opportunity to rent more. Secretary Hills in a speech a couple of weeks ago, said people with modest and low incomes can't afford to buy homes and we shouldn't help them.

Since that is the policy of the administration, it is hard for Congress to overturn it in view of the veto power of the President.

We have to deal with reality here.

Under those circumstances, don't we have a difficult situation in condominium legislation? It may do little to help or it may even aggravate the situation if it makes it easier.

Mr. ARKIN. You stated earlier that the only authority that the local government has is to legislate a moratorium on conversion. You seem to be saying the same thing with respect to the Federal Government now.

The CHAIRMAN. The administration has put a moratorium on Government-assisted construction as you know, since 1973.

Mr. ARKIN. A moratorium on conversion may be the only answer to the dilemma we've been discussing. I would warn, however, in looking at any kind of moratorium, we have to look at the example of New York City, where rent control and moratoriums have resulted in abandonments. When you have abandonments, you are losing both housing units and tax money.

The CHAIRMAN. Mr. Hyatt, would you give us your views on this?

Mr. HYATT. We have had very, very little experience in my area in the conversion process. Most of the conversions have gone smoothly.

I am not experienced enough to have substantive comments.

Speaking from my constituency and taking the approach one step at a time, I would like to see condominium legislation. If you put too many things on it, you are increasing problems with the bill.

The CHAIRMAN. In view of the IRS problems, there has been controversy about requiring condominiums to set up reserve funds.

Do you think the Federal legislation should address the question beyond requiring the disclosure of the existence of the fund or lack of it?

Mr. HYATT. First, Federal legislation should get rid of the tax problem by providing an exemption for associations. The House Ways and Means Committee has reported out a bill that would carry a tax exemption for condominium and homeowner associations, and it needs to be enacted. Then I think the Federal legislation should require a reserve fund.

I would like to see that enacted with 2273. I think we should assure a reserve fund not subject to taxation.

The CHAIRMAN. Should we tell these owners associations how to run their lives?

Mr. HYATT. No. In that regard, Senator, I think you are correct. You can't go too far in running the business of an association. It should be stated whether there is a reserve fund in the disclosure package.

If the budget that is presented in accordance with section 6 or the operating projects includes a reserve, there should be some burden upon the developer to insure that the reserve fund is intact.

There is a limit to what the Federal legislation should do. You shouldn't say, however, you have to budget $5 every month for this.

The CHAIRMAN. HUD proposes to develop educational materials and classes in order to increase knowledge about condominiums and how they should be developed and managed.

The Secretary feels strongly in this area.

Would you support this idea? Do you think an educational program would be a major and significant help in clearing up the problems in condominiums?

Mr. ARKIN. From the standpoint of operations and management, yes. We would support it fully and enthusiastically. Part of the problem—and this relates to the business of telling an association how to run itself—part of the problem we are dealing with is the turning over of control of a real estate property and considerable grounds—and a measure of control over the lives of scores or even hundreds of individuals—to people who basically know nothing about property management, operations, or government.

If they employ a good management firm, they will get support and assistance from the management firm. This support and assistance will go primarily to the directors, however, not the purchasers.

The purchasers in general know nothing about reserve funds. They know nothing about the tax problems that Mr. Hyatt just addressed and don't understand them. They know nothing about the problems of running a condo or PUD.

I think that an education and research program to provide technical assistance regarding management operations for condominiums and planned-unit developments (which are subject to many of the same abuses as condominiums) is an absolute necessity if we are not going to be here 10 years from now discussing the problem of condominiums and PUD's going defunct.

The CHAIRMAN. Do you agree with that?

Mr. HYATT. Senator, I think the most serious problem dealing with condominiums and PUD's is a lack of understanding of what it's all about, both on the lender and developer and the consumer and operator.

There is a serious need for a technical assistance program. I think it is one that uniquely should be run from Washington. There is a need for uniformity on a high level so we have good quality educational programs that the State and homebuilders and consumer groups can turn to for assistance.

The CHAIRMAN. I wonder if this is something that the Federal Government should pay for. You are sending the condominium owners to business school. They will benefit from it.

I went to Harvard Business School. My family paid the tuition. It wasn't paid for by the Federal Government. Why should we give owners a course in technical education for nothing?

Mr. HYATT. I think organizations such as Mr. Arkin's and Georgia Association of Condominium Owners and a lot of other State and local organizations around the country have paid and would be delighted to pay what they could to learn about managing their associations.

I think the State should pay what they should. But there has got to be a start, and there has got to be somebody that can carry the burden and begin the process.

We condominium owners are suffering from the same disease that too many are. That is looking to Washington to find and to pay for the solution. Maybe that is not a solution, but in this instance, the Federal Government can best begin and control the process.

The CHAIRMAN. It is good. I think we agree it is desirable. I think at least a reasonable part of it might be paid by the people who would really benefit.

This would enable them to earn more.

Mr. HAYTT. That is right.

The CHAIRMAN. Finally, Mr. Hyatt, some people have suggested contrary to your views that if the Federal law is passed, that it will revive incentive for States to act on their own to pass laws to meet the particular problems.

What is your answer to that?

Mr. HYATT. I agree to some extent with the State representative from Florida who said his State had tried and not reached the level they wanted and therefore there is a need for Federal legislation.

In Georgia, there was a great deal of pride when they were about the fourth or fifth State to come along with the second generation statute that contained meaningful consumer protection provisions. Other States with Federal assistance, will have this same pride in addressing local problems.

The Federal Government encourages the States to act. A lot of them will, if for no other reason than the preemption, to avoid having Federal law imposed in their State.

The CHAIRMAN. Mr. Marlin and Mrs. Wood, I don't want you to feel neglected. You have a good point. I would like to give you an opportunity to perhaps summarize your position, and in light of our discussion and questioning, you may say what you think we should do.

Mr. MARLIN. Thank you, Senator. One thing we neglected to say at the outset was that the National Council of Senior Citizens is very much on record in support of the bill.

We are familiar with the bill. We have worked on consumer protection provisions in a number of States. Our legal program gives technical assistance in 19 States. We worked on the bill in Virginia and the District of Columbia. We didn't come prepared this morning with detailed comments on the bill. We support it in principle, and we are familiar with it.

With respect to the conversion process that we decided we want to emphasize because of its impact on older persons and because it is an area not covered by the bill, the legislative judgment as to whether or not the bill would be burdened by an extension into that area is one to which we would defer. It may be this is not the year to add the conversion process to the bill.

We think Federal leadership is needed and a Federal role is required to bring the conversion process into conformity on an interstate basis.

We would be willing and anxious to work with your committee, sir, in any efforts you may take to study the problem more extensively.

We anticipate publishing this year, probably through the auspices of the Senate Special Committee on Aging, a model State statute relating to the conversion process.

One final thought that I have is in regard to the discussion about a moratorium being the solution to the conversion problem. We don't consider moratoria a solution to conversions. It is a temporary expedient which if extended indefinitely would raise a serious constitutional question of impeding someone's ability to alienate his property under traditional real property concepts.

The moratorium is simply a way of halting the conversion process until a more reasoned legislative solution can be found.

It is that reasoned solution that New York, San Francisco, and now Washington are considering. We are interested in developing such solutions and interested in Federal legislation making that possible.

Thank you.

The CHAIRMAN. That is very, very helpful. I think this conversion situation is really a victim of timing. We are all such creatures of whatever is the immediate pressure of the time.

The fact was a year or so ago we could see the conversions right and left. We could see what is happening to people.

In running down to work in the morning I would pass a big area that had all kinds of children, minority children, in a big rental apartment complex. That complex has been converted to a condominium for upper-income people now.

That is the reason I was interested in this kind of legislation.

Now, however, we have a situation in which condominiums have had this delay put on them, this moratorium.

As you say, the bloom is off the rose for condominiums, so restrictions to prevent conversions don't seem as urgent now. We have lost that force and motivation. A year from now we may have it more forcefully than we had it before.

I want to thank all of you very, very much for your helpful testimony.

The committee will stand in recess until tomorrow morning at 10 o'clock, when we complete our testimony on the Condominium Consumer Act.

[Whereupon, the hearing was recessed until 10 a.m., Wednesday, October 8, 1975.]

CONDOMINIUM CONSUMER PROTECTION ACT OF 1975

WEDNESDAY, OCTOBER 8, 1975

U.S. SENATE,
COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS,
Washington, D.C.

The committee met at 10:10 a.m., pursuant to adjournment, in room 5302, Dirksen Senate Office Building, Senator Joseph Biden presiding.

Present: Senators Biden, Brooke, and Garn.

Senator BIDEN. The hearing will come to order.

Our first witness this morning is Mr. James Dowden, Community Associations Institute. Mr. Dowden, welcome, and you can proceed. I guess I shouldn't say proceed at your own risk, but proceed at your own pace and we are anxious to hear what you have to say.

STATEMENT OF C. JAMES DOWDEN, EXECUTIVE VICE PRESIDENT, COMMUNITY ASSOCIATIONS INSTITUTE; ACCOMPANIED BY KENNETH S. GIRARD

Mr. DOWDEN. Thank you, Senator. I submitted a prepared text to the committee and I don't intend to reread it. I am available to answer questions now or subsequently at your pleasure. I do ask that the clerk correct a portion at the very beginning where I indicate that Arthur Schreiber, CAI's attorney, is with us. He was not able to be with us this morning. I do have with me Mr. Ken Girard, who is senior researcher for the institute on my right.

Senator BIDEN. Your entire statement will be entered in the record and any portion which you refer to is at your discretion.

Mr. DOWDEN. Thank you.

[Complete statement follows:]

Testimony of C. James Dowden

Community Associations Institute

Senate Hearings on S. 2273 -

"Condominium Consumer Protection Act of 1975"

Mr. Chairman and members of the committee, my name is James Dowden and I am Executive Vice President of the Community Associations Institute. I have with me today Arthur Schreiber of Silverstein and Mullens who serves as Legal Counsel to the Institute. CAI is a nonprofit research and educational organization created to help the homeowners, builders, public officials and others in their efforts to establish and operate viable homeowner associations in condominium, townhouse cluster, and planned unit developments. CAI was formally incorporated in the fall of 1973 and has been staffed since September, 1974. The Institute received start-up support from the Urban Land Institute, U. S. League of Savings Associations, National Association of Home Builders and a number of individual leaders and professionals who recognized the need for a neutral service organization to meet the important needs in the growing condominium and PUD field.

CAI's ongoing program today is supported through a growing membership of homeowners, builders, managers, lenders, public officials, and others involved in this field. In addition, the Institute is involved in contract research activities

and currently has a contract with HUD to provide certain handbooks for builders and public officials on the best approaches to developing condominium and homeowner associations. CAI recently completed a contract with the Veterans Administration to produce a number of informational brochures on condominiums. We are pursuing other contract research possibilities.

To properly understand the context of my remarks today, I must also explain the balanced nature of CAI's organizational structure. The organizers of CAI recognized the diversity of the interests which would exist among the builders, homeowners, public officials, managers, etc., who would make up CAI's membership. Therefore, CAI's Articles of Incorporation and Bylaws provide that at all times these groups must be equally balanced and represented on the Board of Trustees, Executive Committee and other policy arms of the Institute. We are not, therefore an advocate organization for any one client group but, rather, CAI is an advocate for the successful creation and operation of the associations of homeowners which eventually manage the condominium, townhouse project, or PUD.

I am speaking today at the direction and on behalf of the Board of Trustees of CAI and my comments reflect the views of that body adopted unanimously on September 26, 1975.

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Mr. Chairman, the earlier testimony of Secretary Hills and the accompanying report of the HUD condominium study amply documents the explosive growth in condominium development over the last five years. A fifteen fold increase from

85,000 units in 1970 to more than 1 1/4 million units in early 1975 has been found by the HUD study. To fully appreciate many of the problems that have been experienced today in the condominium field we have to keep in mind this level of growth.

The sudden boom in condominium development reflects a popularity with the builder and the owner that arises for a number of reasons. Notable among these are economics achieved as a result of the more efficient use of land and facilities. Because of these economics and the generally more diverse and abundant amenities which can be provided economically on a group ownership basis, condominiums have begun to capture a major portion of the new housing market. Much has been said, already, regarding the consumer's interest in the condominium because of changing lifestyles, generally lower unit price, desire for homeownership without all the burdens of ownership, etc. Whatever the reasons, the effect of the consumer demand has been dramatic.

The suddenness of the condominium "boom" has caught most of the industry, government and indeed, the consumer, unaware and there have been problems. The media and government agencies at all levels have begun to give condominiums greater attention because of these problems. Most of that attention has centered on providing consumer protection for the buyer. With the suddenness of the growth of condos, the relatively unaware consumer has found himself in occasional difficulty, as much a function of his own ignorance as that of the builder.

One of the purposes of the HUD study of condominiums was to more accurately provide a true measure of the problems which have been experienced and the extent to which they pervade the market. Clearly, the results of that study indicate

that condominium development is a relatively localized activity, concentrated in certain growth areas, and that the overwhelming number of condominium owners are satisfied with their purchases. This is not to say that there have not been problems, certainly the "horror stories" have been fully covered in the media, and elsewhere. There have been problems and abuses. However, the results of this study clearly indicate that the problems of recreation leases, sweetheart contracts, long term management contracts, etc., do not pervade the market. In fact, these practices appear to be relatively localized to a few markets in one or two states.

Increasingly, Mr. Chairman, we feel that more information and education for the consumer, the builder, and the state and local government official is the answer to these problems. All to frequently, the early condominium efforts reflect ignorance of the process rather than sound logic based on long years of experience with condominiums. The "state of the art" of condominiums has only recently begun to reflect the short experience we have had with this form of housing. Legal documents are too complex and cumbersome; insurance policies are frequently amended versions of renter policies; appraisers, lenders, accountants, planners and others are only now beginning to reflect experience gained over these last few years. Likewise, the consumer has not had reliable information to guide him in making a purchase, and state and local governments have not fully understood the nature and form of regulation that might be required.

Increasingly, however, the condominium form of housing has been "coming of age" in recent times. The initial state enabling acts have been undergoing revision in states with heavy condominium activity and the changes are reflecting

the experience in those states and the problems they have encountered. Even in Florida, there are signs that the "horror stories" in that state are having an impact in new legislative and enforcement initiatives. The initial rash of ordinances placing a moratorium on conversion activity is now subsiding and is being replaced with more reasoned legislation incorporating appropriate safeguards for the renter and the buyer while still providing this housing option. In fact, in this metropolitan area, one major political subdivision is in the process of devising a program to encourage more condo conversions.

As the consumer's knowledge expands, as the builder gains more experience in this area, and as state and local governments catch up, in terms of regulation and legislation for condominiums, we feel confident that many of the "abuses" and "horror stories" cited here and elsewhere will be a thing ot the past. Hopefully the legislation under consideration today will provide support and encouragement in this regard, not further impediments.

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Mr. Chairman, CAI is pleased to see that the current condominium legislative proposal before you has moved away from an approach involving a national program of registration and regulation. We have grave concerns regarding the practicality of any such approach adequately serving the needs of the consumer or providing appropriate safeguards to permit the condominium process to continue. Certainly a new large bureaucracy in Washington would not be desireable unless it served a useful purpose.

S. 2273 reflects a more appropriate role for the National government in our judgement -- that of establishing national guidelines and policies which provide leadership to the states in meeting their responsibilities in regulating and enforcing the real estate laws of the state. CAI endorses this approach to condominium legislation coupled with a viable, well funded national program of information and technical assistance which can make the information available to the consumer as well as to the professional builder, attorney, local official and others on the best approaches to achieve successful condominiums. If properly administered, Mr. Chairman, such a program of technical assistance and information would begin to provide the means to assure the sound, appropriate development of this segment of the housing field and to meet the needs of that proportion of the population for which condominium housing is suitable.

With regard to the state government role, Mr. Chairman, CAI has seen, and to some extent the HUD study documents, the trends in the state legislatures to upgrade and improve their laws relating to condominiums based on their own localized experience. There is a long history and practice in each of the separate fifty states regarding the regulation of real estate transactions in general and condominiums in particular.

This fragmentation and the diversity of state approaches is as much a reflection of an attitude of states rights as it is a function of the character of the real estate and housing industry. Most realtors and most builders never do business beyond the boundaries of a single city or county in any given year, let alone beyond the boundaries of more than one state. Most lenders, lawyers, property managers, and other professionals involved in the housing industry and real estate field likewise operate within a single state.

CAI believes the states, guided by certain national standards and recommendations are best able to achieve the level of consumer protection necessary in the condominium field and, are best able to develop legislative requirements and regulations which are workable in their own context and based on their own localized experience. Congress should encourage the states and, to some extent localities, to assume this responsibility and role.

Mr. Chairman, regarding the general approach to condominium regulation as reflected in this bill, the CAI Board of Trustees

-- supports the approach of setting certain national guidelines and standards. Those standards should be established as minimum requirements in the area of disclosure (Sec. 6) and as voluntary recommendations to the state on operational matters contained in Section 5 of the bill.

-- supports the approach of relying on the state government for actual regulation and enforcement through processes established by state law and procedure.

-- supports and strongly urges the establishment and funding of a national program to provide education and information to the consumer, builder, property manager, state and local official and others involved in the condominium process.

Specific Comments on S. 2273

The Board and staff of CAI have carefully reviewed the detailed provisions of the proposed bill and, while the general approach has been found to be a

considerable improvement over previous versions of the legislation, there are a number of areas which present some difficulty and which can be improved. We will comment below on each of these sections.

First, Mr. Chairman, it is important that we briefly discuss the question of mandatory and voluntary standards. It is the position of CAI's Board that the national government has a clear responsibility and obligation to assure that the consumer has the right to know certain factual conditions relating to his purchase. Subject to the specific considerations mentioned later, CAI's Board does support the establishment of minimum disclosure requirements concerning essential legal, construction and financing information on a particular project, provided this can be accomplished without onerous paperwork and costs. Many state laws and most developers are already meeting this requirement.

On the other hand, the CAI Board believes that the operational type provisions contained in Section 5 of S. 2733 should be adopted as suggested guidelines for the states to consider incorporating and not as mandatory requirements. We suggest this voluntary approach to the handling of the operational procedures, Mr. Chairman, because these are items of such detail and divergent opinion that they can better be handled in each state based on local conditions and local experience. With fifty different state approaches to the practice and regulation of real estate and condominium operational matters, CAI's Board feels that the states with the advice of this legislation, should determine the best way to deal with the concerns and issues which are delt with in Section 5. One of our concerns, Mr. Chairman, is that some states have apparently worked out arrangements to provide the safeguards sought in Section 5 but through means and techniques not encompassed here.

The effect of a prescriptive approach would preclude such initiatives in those states where they feel they have adequately addressed the problem through other means. Moreover, experts in the field are not yet agreed on a single approach to such matters as transition, warrantees, appropriate builder's assessment responsibilities and others. To prescribe an approach in this legislation which may work well in some states and not in others would be disfunctional.

Disclosure Requirements -- Section 6

Turning now to our specific comments regarding Section 6 -- National Standards for Disclosure. As I indicated, the CAI Board does support the general intent and purpose of this section as minimum standards for state laws. We are concerned that the enforcement of these provisions not become onerous or excessive in costs to the builder or the consumer. Many of these provisions are currently required under state laws and are practiced by many condominium developers today.

One specific problem area, however, is subsection 6 which requires a two-year projection of annual expenditures for the common expenses. We would recommend this provision be revised to a one year projection which is more realistic given current economic conditions and that revisions be required each year or whenever there is a material change in conditions. The problem, of course, is that everyone in today's economy is having difficulty accurately forcasting future expenditures and a two year forcast may be more misleading and harmful than if the forcast is changed each time conditions change or each year.

We would also suggest that any projection of costs per unit be based on full occupancy of the project to eliminate confusion and possible underbudgeting.

We have difficulty with the terminology in this section which says "certified to have been based on generally accepted accounting principles." We would suggest removal of the word "certified" which seems to suggest the use of a C. P. A. which rarely, if ever, certifies future acts. The intent is clear but this word could force additional unnecessary costs and problems in enforcement.

In subsection (6) (A) we would suggest the work "basis" instead of "formula" in order to more accurately describe the procedure.

We would suggest the explicit statement in subsection (7) that this provision applies to condominium conversions. To impose this provision on newly contructed projects, which are more than one year old at offering is an unnecessary burden and cost in addition to the budget requirements and warranty provisions already suggested. We are also concerned about the practicallity of obtaining the opinions of a certified engineer regarding the remaining life of common facilities. We would urge the Committee to explore this further with appropriate professional engineering societies.

The potential scope of subsection (10) is limitless particularly as it deals with interpreting the potential impact of activities beyond the control of the developer. We would recommend that the subsection be restricted to providing a description of such developments by placing a period at the end of the third line of that section following "... or near the condominium project."

Specific Comments on Section 5 -- National Standards for Consumer Protection

Mr. Chairman, as I indicated earlier the CAI Board understands and supports the effort in this section to deal with several problem areas which have

arisen in the past. However, the Board does believe that these operational provisions should be provided as suggested guidelines to the states, not as minimum standards. Each state in its regulation of condominium and real estate matters has developed experience and practice which may suggest other techniques to handling the problems addressed here and we should not impose detailed requirements of this type until the states have had the opportunity to address these concerns.

For the most part CAI's Board agrees with the general appraoch in this section if enacted as voluntary guidelines. The specific comments on each item which follows will outline specific concerns on each item and provide further support for the voluntary state approach to these itmes.

Subsection (1) would suggest that any deposit or downpayment be held in trust or escrow until closing. This is directed at the problem of the builder or firm going out of business and the consumer losing his downpayment or deposit. The specific provision in this subsection is too limiting.

The premise of many developers who in the past have utilized the recreation lease was that it served as a means for providing certain facilities without including the costs of those facilities in the purchase price of the unit. Theoretically, then, the lease arrangement lowers the initial purchase price to the consumer and he pays for the cost of the recreational facilities over time. In theory, then, if there is proper disclosure to the purchaser and if the cost features of the lease are not "onerous", there are possible beneficial features to such leases for some purchasers.

There is another problem in this area, Mr. Chairman. As you may know the constitutionality of the prohibition of recreation leases in Florida law is being tested in the courts. Outright prohibition may not be possible. Therefore, CAI's Board recommends that the recreation lease issue be dealt with by requiring disclosure of such leases under Section 6 and suggesting in Section 5, subsection (2) the state be advised to determine the parameters to prevent all onerous recreation leases. It would necessarily be left to the states and conceivably the courts to determine what indeed in onerous.

There are other possible techniques for protecting the consumer against the potential loss of his money at this stage of the process. For instance, in New York state and apparently in some other areas, the builder can provide a bond to guarantee these funds from loss. We would suggest that language be included in this subsection outlining the desired goal of providing safeguards for these monies and to incorporate the alternative of bonding in addition to the escrow or trust approach. The states may indeed have other techniques to achieve this goal and as a guideline rather than a requirement they will have the flexibility to accomplish that without being limited to these two or three approaches.

Subsection (2) prohibits the builder or developer from maintaining an interest in any common element after control has shifted to the homeowners association. This provision appears to be directed at the practice of recreational leases that was common in some areas. The particular problem of these leases has been the failure to disclose the existence of these leases at the time of sale and to onerous provisions which are occasionally found in such leases such as cost of living escalator clauses, etc.

Subsection (3) provides that the builder transfer control of the homeowners association one year following initial occupancy or at 80% of the units are occupied, whichever is first. As a practical matter, Mr. Chairman, this provision would be calamitas, particularly today, when we find many condominium projects which are not even 50% sold at one year following initial occupancy. Linking time and percentage of sales when sales are brisk may not even be possible since it is not uncommon to have a sellout period to extend well beyond one year.

The Board of CAI recommends that the states be encouraged to adopt a policy of gradual transition of control, involving homeowners on the Board from the early stages of the project, with majority control shifting to the homeowners at 75-80% sellout.

Subsection (4) permits the cancellation of any management contract six months following the takeover of control by the homeowners. This is directed at the problem of homeowners being saddled by multi-year contracts which may or not be in the best interest of the homeowners. The CAI Board would suggest this provision be effective at one year following takeover and apply to all service contracts. This time frame more nearly fits the contract cycle in practice today, while still providing the protection sought. Moreover, we would recommend such contract or agreement be renewed or rescinded by vote of the Board of Directors of the Association not by the full membership of the association. As a practical matter contracts are rarely voted on by all homeowners. The Board is provided the necessary authority to act on contracts in the legal documents.

Subsection (5) requires the developer to furnish a two year warranty on common areas and facilities and a one year warranty on the individual unit. The developer is already required under Section 6 to disclose all warranties under subsection (5) of that section.

In our judgement this warranties section has a number of problems. First, in many instances the consumer can currently receive warranties in excess of those contained here and the effect of this provision would be to limit existing warranties. Many manufacturer warranties currently are for three or more years and the NAHB HOW insurance program provides up to ten years coverage for major items. Moreover there is a defect in this subsection which only provides two year coverage from the initial occupancy of the project rather than from the time of completion or use of the particular item.

. Therefore, CAI's Board urges that the states be advised to consider the need for warranty provisions and protection incorporating the various considerations already mentioned and let the states, based on their experience develop appropriate warranty provisions.

Subsection 6 would require the developer to assume the rights and obligations of a unit owner for all units not sold. This provision appears to be directed at requiring the developer to meet the monthly assessments for each unsold unit. The practice and law on this matter differs considerably aroung the country. In some states, the developer must pay 100% of the monthly assessment on all constructed but unsold units. However, in many areas and projects, particularly when the maintenance, utility and other costs of the unsold, unoccupied units, are not proportionate to those of the owner occupied unit, the practice is for the developer to pay some lesser

percentage or to make up the difference in operating costs of the association. The practice with other types of projects involving homeowner associations, the practice is to require the developer to pay some lesser percentage, 25% for instance, of the monthly assessment on constructed, but unsold units.

CAI Board recommends that the states be encouraged to develop a policy which would require the developer to pay the net difference between the assessments set forth in the disclosure statement and collected from occupied units, and the amounts necessary to operate the association consistent with the budget.

Subsection 7 would require certain timed notices to the tenants of units which are to be converted to condominiums. As a matter of policy, the CAI Board feels the time limits outlined in this section are acceptable as a recommended approach to the states. However, again these types of requirements are being tested in the courts in at least two states and the Constitutionality of such provisions is open to question. Moreover, these provisions would prohibit the conversion of a project which would require complete evacuation of tenants in order to carry out extensive renovations that may be required to make the project acceptable for sale. Therefore, the CAI Board recommends that the states develop appropriate standards and guidelines in this area subject to local conditions.

Mr. Chairman, we have devoted considerable discussion and effort in the area of standards and practices because these provisions even have a major effect in guiding practices and state laws in this area. We do want to emphasize again, however, our concern, and desire and support for a program of education and technical assistance to be provided to the builder, developer, homeowner, manager and others to assure the long-term viability of condominium and homeowners associations.

To some extent this activity is provided for in this legislation. However, we strongly recommend that this educational and technical assistance program be carried out and delivered by HUD utilizing the best available resources to do that. In that regard, the legislation limits grants and contracts to the states which in our opinion seriously limits the flexibility of HUD to provide assistance to cities, counties, or wherever else it may be required in this regard. Moreover, the provision which limits the federal grant to 25% of cost appears to be more of a disincentive given the track record of most federal grant-in-aid programs.

CAI's Board feels strongly that the technical assistance and education program be developed and administered at the national level, directed at those states or situations where the greatest needs exist without limitation on who or what agency might be best able to produce materials or have the greatest need for technical assistance. Again, in our judgment the expenditure of funds in supporting a national program of technical assistance and education may do more to resolving the problems we've discussed here than any other single activity, including regulation.

Conclusion:

The current proposed legislation, S2273, is a considerable improvement over earlier versions of such legislation which would have involved national regulation

and registration of all condominium projects. However, while this bill does address certain important issues and problems, operationally certain provisions will hinder more than help the condominium process across the country. The CAI Board of Trustees endorses the need for legislation and national standards and guidelines which would:

-require a minimum disclosure statement of certain key features of the condominium transaction.

-encourage the states to consider the adoption of certain operational standards subject to local conditions and experience.

-establish and fund a national program of education and technical assistance

Thank you, Mr. Chairman. We are available for any questions.

Mr. DOWDEN. I'd just like to summarize, Mr. Chairman, the approach that the institute has taken and the background behind our statement, and then hold myself for questions.

The Community Associations Institute is a unique organization. We are a nonprofit organization that is made up of the actors in the process involved with condominiums and PUD's or automatic membership associations. We are required by our articles of incorporation and our bylaws to maintain an equal balance of builders/developers, homeowner association leaders, property managers, professional colleagues, and local and State public officials who are involved with condominiums and planned unit developments.

Our advocacy position is the successful creation and operation of condominium homeowner associations. That's our only advocacy position. Our board of trustees met toward the end of September for the specific purpose of reviewing this legislation and offering to the committee our views on the specific proposals in the legislation as it impacts on our advocacy position.

Mr. Chairman, the position that you have before you and that I will refer to briefly was unanimously adopted by that equally balanced board of trustees representing the homeowner, builder, property manager, and others involved in the condominium process.

Just to quickly summarize our approach, we have reviewed the key issue, that is the national role as it relates to condominium regulation. We feel and the board has adopted the position that the appropriate national role is one of setting guidelines and standards to be practiced. We feel this specifically as it relates to the disclosure elements and the intent of the bill as it relates to disclosure.

Senator BIDEN. I'm sorry. You said set guidelines and what?

Mr. DOWDEN. Standards. Moreover, Mr. Chairman, on reviewing the specifics that we have characterized as operational provisions—that is section 5 of the bill—the board was troubled because the state of the art is such that there are no clear practices that are deemed successful in every instance and in every State on several of those items.

More importantly, it's clear that a number of States have worked out agreements where some of the provisions—escrows, for instance, and warranties in some cases, are successfully handled through other techniques than contained in the bill. The board was troubled with the prescriptive approach in that particular section and suggests instead that the committee consider enacting those provisions as guidelines to the States on a permissive basis until such time as we can determine either the correct and appropriate approach or until we can determine whether or not the States indeed can meet that responsibility.

Our most serious concern, Mr. Chairman, frankly, is in the education and technical assistance area. We have maintained at several hearings that have been conducted so far that in our short history every indication we have is that much more technical assistance and information is needed to clear up many if not all of the problems and difficulties that have been encountered by the consumer and the builder and the property manager and others involved in condominiums across the country.

We can't emphasize too much our feeling that a major national role is in the area of providing technical assistance and information and education on how to go about buying, selling, building, creating, and managing condominiums and planned unit developments.

In this regard, Mr. Chairman, we have ourselves undertaken a relatively preliminary effort in the education and information field. We have had a contract with the Veterans' Administration to produce consumer booklets. We are under contract at the moment with the Department of Housing and Urban Development to produce certain handbooks and manuals. Separate from that, we have joint ventured with the Urban Land Institute to produce certain handbooks to help guide the homeowners association leader through his management of the association.

We feel that many of the problems and abuses you have heard about these last 2 days and in the hearings a year ago and the hearings that HUD conducted and cited in the 10 problem areas that the HUD report deals with could have been dealt with more effectively and can be dealt with more effectively in the future with appropriate education and information. We think this is a critical feature of the bill.

The disclosure elements are also critical and we have offered some suggested changes in several areas where we think there's some mechanical defects or mechanical problems, and then in our statement, Mr. Chairman, we have dealt one by one with the particular operational provisions.

Again, we view them as more appropriately guidelines at this point, but we have offered suggested changes whether they become guidelines or requirements.

I would like to conclude, Mr. Chairman, by again emphasizing that we have tried to strike a balance on what we think will work and what we think will serve the best interests of all the individuals and actors involved in condominium developments across the country.

Thank you.

Senator BIDEN. Thank you very much.

I should say before I begin to question you that when I looked down at your statement—it's amazing the tricks that your eyes play on you—I looked down and I thought what in the devil is the CIA involved in this? I thought, my Lord, they're in the condominium business?

Mr. DOWDEN. We only have that problem on the Hill, sir.

Senator BIDEN. It's been argued that the States do a good job in regulating condominiums. First of all, do you think this is true and if you do think it's true, why do we need this bill?

Mr. DOWDEN. Well, I think that I would characterize it somewhat differently rather than an all-encompassing statement. I think most of the condominium developments that have occurred in the last 5 years, almost all of the people involved were acting out of ignorance or lack of knowledge and understanding and everybody has been, over these last 2 years certainly for both economic and other considerations, getting their education.

What we are seeing in second and third generation State laws are considerable improvements over what has been on the books in the past. Certainly, the experience in Virginia and Georgia that the committee heard about yesterday, and the District of Columbia's effort

underway at the moment, and several other cities, are marked improvements toward the State fulfilling its role and responsibility.

I think the biggest problem the committee has is that HUD's report indicated that the bulk of condominium development is occurring in relatively few States and many, if not all, of those States are into second and third generation laws directly dealing with some of these very problems. The problems that troubled our board the most are the operational provisions. There are no nice, neat, clean, golden rules on handling several of those provisions and national legislation at this time unguided, if you will, by those rules may be premature and may be more disruptive than productive.

Senator BIDEN. So I'm not sure I understand your answer then. Do you think the bill is needed or not?

Mr. DOWDEN. I think that certainly the disclosure provisions are appropriate, Mr. Chairman, and as it relates to the national TA and education we think it's vitally needed.

As it relates to the operational provisions, we are less clear and less adamant both because we are not sure what the appropriate requirements should be in every case nor are we sure that the States have not already begun to address those issues and the States would preempt on condominium development.

Senator BIDEN. When Secretary Hills testified, she advocated some minimum disclosure for use in sales in interstate commerce. In this way, the developer in Florida who wanted to solicit sales in Northern States would not have to comply with various requirements of all the States and instead just comply with the Federal requirement. What do you think about this idea?

Mr. DOWDEN. I think there has to be some uniformity involved, Mr. Chairman, whether it's achieved through HUD, through this legislation, or through the efforts at the moment to develop uniform State acts regarding this. I'm not sure which will happen first or which is more productive, but I think the uniformity is necessary.

Senator BIDEN. Does the uniformity have the effect of precluding States which have decided on their own to have a tighter or a tougher disclosure requirement—preclude them from having that? Do you think we should do that?

Mr. DOWDEN. I don't think it precludes them. I think the language in this legislation is couched so these are minimums and certainly the States can go beyond them.

Senator BIDEN. Well, the whole idea, though, is to preclude a builder who is doing business in more than one State from having to file a number of forms. The idea, as I understand it, of Secretary Hills is just one single form, one single set of regulations that will give the builder sort of free passage in every State.

The rationale for her approach is that we want to eliminate the redtape, paperwork, and additional costs of putting the builder in the position of having to comply with more than one set of regulations. Ergo, we could have a single Federal standard which, in fact, applies in every State and which by definition would neither be a minimum nor a maximum but would be the only regulation. Otherwise, if you allow there only to be a minimum, then each State can come in and do something differently and then you would abrogate the intention of having a single standard. You put the builder back in the position of having to file more than one set of disclosures, for example.

So assuming I'm correct about HUD's position, what is your position with relation to this position?

Mr. DOWDEN. As I understand what you're saying, Mr. Chairman, that is my understanding of HUD's position. Our position at the moment is that HUD establish or there be a national minimum disclosure standard whether through this act or through some effort to bring the State actions into uniformity. I don't believe that our membership or the States would accept the suggestion that the State of New York, for instance, could not make additional requirements which are uniquely suited to their State law.

Senator BIDEN. Your position then is that any Federal standard probably should not be exclusive or preemptive—and not preempt a State's right to apply tougher standards if it wants?

Mr. DOWDEN. At this point, Mr. Chairman, that's the extent of our position, that's correct, in the area of disclosure.

Senator BIDEN. How about interstate versus intrastate offerings?

Mr. DOWDEN. The position is the same, Mr. Chairman.

Senator BIDEN. Prior to coming here I was a county councilman and all I did was just seem to deal with PUD's and zonings generally and condominiums and the problems related to construction. And if you're able to, which apparently you are, give advice to builders and owners, lessee and lessor and everybody in between with some degree of impartiality, you are better than Solomon.

At any rate, in giving advice to your group, which you do in working with condominiums, what have you found to be the biggest problems and abuses that exist with regard to the sale of condominiums? I'm looking at it for the first part of my question with regard to the consumer side. What do you see as the biggest abuses?

Mr. DOWDEN. I would rather characterize them as problems. I think the biggest single problem in the sale of condominiums is the lack of understanding of what is being purchased and what's being sold. I think an unfortunate number of consumers have bought something that they weren't fully familiar with, didn't understand what they were buying, or what the responsibilities that went with buying were, and I'm afraid—and I have told the builders this—I think an unfortunate number of their salesmen have not known fully what it was they were selling and have not either sold the condominiums as a true condominium and fully explained all that's involved. Consequently, 6 months or a year or further down the road many of the complaints that are heard from among the residents are complaints that arise out of a lack of understanding of what exactly it was that they purchased.

Senator BIDEN. So it relates in large part to inexperience in dealing with this kind of transaction on the part of both the salesman in one instance and the consumer on the other side?

Mr. DOWDEN. Both inexperience and lack of education or information available. Right.

Senator BIDEN. I'm in the anomalous position of having introduced a bill similar to this over a year and a half ago and then cosponsored this legislation. In the meantime, my father is a real estate salesman and was put in charge of a large condominium sales operation in Delaware and we don't speak much any more. But anyway, the condominium industry, at least in the Northeast, it's my understanding, has been in a bit of a recession in the past year or so,

maybe more. It's been speculated that one of the reasons is the lack of confidence in condominium purchases because of the reported or alleged abuses that exist either because of inexperience or lack of knowledge or direct attempt to mislead.

First of all, has it been in a recession?

Mr. DOWDEN. Oh yes, definitely.

Senator BIDEN. Secondly, do you think that is totally a consequence of the economy or do you think it has anything to do with a lack of consumer confidence in that type of transaction?

Mr. DOWDEN. Well, it's obviously difficult to separate. The whole housing industry is in a recession.

Senator BIDEN. I understand. Is lack of confidence any part, any element?

Mr. DOWDEN. I think confidence in the condominium concept has been shaken. It's not been destroyed but it has been shaken.

Senator BIDEN. Now do you think that national legislation of the nature that we have proposed here, that Senator Proxmire, Senator Brooke, and myself have offered—do you think legislation of this nature would help restore that confidence, the mere fact that there has been a recognition on the part of the Federal Government of the abuses and an attempt to correct some of them? Do you think that will have any impact? I'm really not looking for a solicitous answer. Your colleague to the left has been shaking his head and I'd like to know from you what you honestly think.

Mr. DOWDEN. I think an unfortunate part of the national role as it relates to condominiums is that until today, for the most part, Federal agencies and lending institutions have only dealt with condominiums at the time of mortgage or at the time of foreclosure.

The current HUD study, if properly circulated—and certainly this legislation as it relates to technical assistance and information would go a long way toward restoring confidence in the condominium concept. That 95-percent number I think was a shock as much to some people on the Hill as it may have been to some of the builders and others of us who are working closely in the condominium field, and was certainly what many people felt in their hearts. It wasn't as bad as the Reader's Digest and Wall Street Journal and some of the others who cited the horror stories said. It's clear that that 95-percent number ought to restore some confidence and this education and TA would do the same.

Senator BIDEN. Some of us believe and I have believed from the beginning that the vast majority of the reputable builders or the vast majority involved in construction are reputable, and in fact have handled condominium sales, as the young kids say, in an "up front" manner from the beginning. I even had builders in my State come to me and support legislation along these lines because they felt that they were being hurt by a reputation which was deserved by some within their community—the fly-by-night operators who were converting and running. It was affecting them and they thought this kind of legislation, although initially directed at protecting consumers, would have the effect of protecting them.

I think there's less of that kind of feeling that I have heard nationally than I heard locally and I'm just wondering from your experience representing builders, whether or not they feel there's a need

to police their own industry and eliminate some of the sharks who have been I think responsible for the abuses. They may be minimum abuses, although when the abuse hits you it's significant for the person it hits. Do you get any of that kind of feeling from those you represent or is it just a flat out——

Mr. DOWDEN. No. We have one of the gentlemen on our board who is a Florida condominium developer in several cities in Florida and he feels very strongly about this and indicates he's supported State legislation as well as national—this legislation, as it relates to improving the developer's image in doing business in the State.

There are a number of abuses which he does not practice that he feels need to be corrected. I think the more serious thing is an understanding of what is involved. Converters are not builders.

Senator BIDEN. I understand that, but that distinction is not understood by the American public. What happens, it seems to me, in my limited experience as an attorney in dealing on the county level with the very thing that you do all the time, is that the average person out there doesn't make that distinction and what happens is you get an entire building community tarred by that blush. For example, in my State, there was some significant investigation going on as to whether or not builders were involved in altering the zoning process through the legislative process, through campaign contributions. I suspect that kind of investigation has gone on in every State. Any by and large, overwhelming number of builders involved in developing and rezoning are no party to that, but to almost a man in my State, they now tell me that they are in fact viewed by the people who come in to buy a house as if they were involved. Prospective buyers say, "Well, you're one of the guys," and it starts out that way.

So I think that the building community, at least in the East—I'm very familiar with Pennsylvania and New Jersey and Delaware—is not held in particularly high regard by the average consumer. They blame the builder, it seems to me, for the escalation of costs which, in large part, is not the fault of the builder. They blame the builder for shoddy workmanship which, in many instances, is not the fault of the builder—for things beyond his control—and they blame the builder for the abuses regardless of whether or not that builder is engaged in the kind of activity that is subject to the abuse.

Well, anyway, I have gone too far. One last question and then you can comment on anything I said.

Mr. DOWDEN. If I could just comment quickly, I think the industry has made an earnest effort to begin to address some of these problems. I'm not here to plug homebuilders or the homebuilding industry, but they were participants in a hands-off fashion in getting CAI started specifically for the purpose of setting something up that would be in a position to help the homeowner association once it was created.

I know that—and you may hear later in their testimony about some of the other things that NAHB and the other industry groups are trying to do. Around the country, it is typically the builder and the property manager who are trying to get our local chapters underway and trying to support the effort to educate the consumer.

Senator BIDEN. I would think it would be. It's in their self-interest to do that. I think people move into these condominium complexes or get involved in homeowners associations and not only view themselves

in an adversary position but assume from the beginning that every builder is out to nail them and therefore their only responsible position to take is to go out and try to nail the builder. There's a minimum of cooperation.

Mr. DOWDEN. Our staunchest supporters, Mr. Chairman, across the country are the builders who intend to remain in the community and need to make this condominium a success in order to help them with their next condominium.

Senator BIDEN. One last question. You mentioned that education and technical assistance in the area of knowing how to go about buying, building, selling, creating PUD's, condominiums, is essential, and then you say that there is a national role in setting guidelines and giving some direction in this area. That sounds fine, but I wonder whether or not you could give me a little more detail as to how you think that could be done because I'm not sure that it can be done.

We talk about educating the public. How do we educate the public through national legislation? How do you really do that?

Mr. DOWDEN. Well, I think what the national legislation does is set up the mechanism to provide the TA and education and assistance. There is no mandated program in HUD to do some of the things they have already done. Their publication on questions and answers for the condominium purchaser has been printed on the order of 300,000 or 400,000 copies. For a long time—an unfortunately long time—it was the only publication to which you could refer potential purchasers of a condominium.

Senator BIDEN. Implicit in your statement is the idea that maybe the Federal Government can give grants to groups like yours to aid in that education.

Mr. DOWDEN. CAI has an obvious interest here. If the occasion arises where we could provide that service, we are available to do it. I think the more important thing—as we have explained to the HUD people—is that the job needs to be done and we're going to do it whether or not HUD does it.

Senator BIDEN. I tell you what—the gentleman to your left, you and he should get together, because he goes no every time you say yes.

Mr. KEEN. I'm a builder and he's an institute representative.

Senator BIDEN. I thank you very much and, Senator Brooke, thank you for letting me go on that long.

Senator BROOKE. Mr. Dowden, I have a brief statement and then I think we ought to go on perhaps with the next witness if we may, unless my good friend, Senator Garn, has questions.

Senator GARN. I'm going to give the chairman a break today and be quiet.

STATEMENT OF SENATOR EDWARD W. BROOKE

Senator BROOKE. Over the last 5 years there has been a 15-fold increase in the number of condominiums in the United States. Almost one-fourth of the newly constructed housing units offered for sale this year will be condominium units and already some 4 million Americans live in condominiums.

Unfortunately, as condominium production has burgeoned, abuses in the sale and management of these units has also developed. These include such practices as sweetheart contracts, unfair recreation leases and deliberately unstated maintenance charges.

These abuses have been revealed by the media and documented in testimony before this committee. Despite these abuses, condominiums can be expected to continue to serve as an important source of housing for those who want to own their own units and S. 2273 that Senators Proxmire, Biden, and I introduced on August 1 is designed not to discourage the development of the condominiums, but to restore consumer confidence in this form of ownership. The sponsors of S. 2273 have four basic objectives:

First, to correct the abuses which have developed in the marketing and management of condominium units which are very often sold in interstate commerce; second, to increase consumer confidence in the condominium form of ownership; third, to provide condominium consumer protection with the minimum of paperwork and bureaucratic redtape; and fourth, to leave to State and local governments to regulation of those aspects of condominium ownership which are best dealt with at the State and local level.

Mr. Chairman, I want to make it clear for the record that I have an open mind so far as this legislation is concerned. We scheduled these hearings so that we could hear witnesses who work with the condominium developers and builders and consumers and others, and I think that the hearings already have been very helpful to this committee, certainly to me, even though, unfortunately, with the conflicting schedules, I have not been able to participate at great length.

I do say, however, that I must be one of the 5 percent of discontented owners that was spoken about. I live in a cooperative. I don't know how many on this committee do, but I do, and I have had serious problems in the construction of the cooperative in which I live. Every time I turn around, we're having to spend additional money. We're being assessed additional money for construction of floors which were built incorrectly. The balconies have the leaks and the floors are coming up. I wouldn't even admit where I lived a year ago, but it's the Watergate, and it's just about the worst construction that you could find.

I'm not here to indict the builder of it, but I'm sure that similar problems exist elsewhere, and I'd like some time to find out where that 95 percent who are satisfied comes from. I just happen to fall in that 5 percent, and that worries me quite a bit. It might be true that it's just my misfortune to have fallen in that 5-percent category.

Senator BIDEN. It's the 95 percent that don't live in condominiums that are satisfied.

Senator BROOKE. It may very well be that, but I'm not here to plead my own case, and that was not my purpose for filing the legislation. Now, Mr. Dowden, I take it that you feel we should not have Federal legislation in this field. Is that the sum and substance of it? I know you say regulations and guidelines, but I take it that your institute is generally opposed to Federal legislation in the field of condominiums.

Mr. DOWDEN. No, sir. Our institute has supported the legislation before you as it relates to requiring standards for disclosure. Our institute is unclear whether or not either we have at the national level the wisdom or the correct answer on those specific seven items that are encompassed within section V and have suggested that they are addressing meaningful problems in the condominium area, but

that at this stage in the development of the state of the art, if you will, that we best hold our options open on how we can deal with those particular abuses.

We are very concerned about the loss of downpayments and deposits, but escrowing alone is not the answer. There are some States where escrowing is not the practice and bonding is the practice, and we need to show greater flexibility in those specific items, and it may be necessary to open this on a permissive basis to the States.

In the other areas, Mr. Brooke, with regard to the 80 percent turnover to homeowners or 1 year after the first sale, 1 year is unworkable for most condominium projects across the country. Although 80 percent may be an appropriate figure, frankly we'd rather see homeowners involved in the board even earlier than that even if only on a minority position and transfer of majority control of the board at 75 or 80 percent. But the 1-year figure included in the draft is unworkable for most condominium projects, and I can go down the list of other items which present similar problems.

We are not at all opposed to an effort to try to address those abuses. We are very troubled because those seven items are relatively detailed operational provisions. In some States, they are addressed in other more successful ways that may be envisioned there, and the committee, we think, should be well advised to provide some flexibility in that area.

Senator BROOKE. Well, I just reread the final paragraph of your statement. I read your whole statement, but the final paragraph of your statement states that the CAI board of trustees endorses the need for legislation and national standards and guidelines which would require a minimum disclosure statement of certain key features of the condominium transaction, to encourage the States to consider the adoption of certain operational standards subject to local conditions and experience, and to establish and fund a national program of education and technical assistance.

Let me say to you, I just question whether that alone would be sufficient to assure protection against the abuses that I mentioned.

Mr. DOWDEN. Well, I would hope—I cannot help you with your Watergate construction problem, and I'm not sure that any legislation will, but if we're talking about the kind of abuses that are in section 5 of the bill, including the escrow area, in the conversion dates, if we're talking about those seven specific items, Mr. Brooke, I'm not sure that you aren't already seeing revisions in State laws to address these areas, and I think the attitude of our board was if the National Government or the Congress has suggested approaches to those problems, let's try them, but we're not sure at this point that we've got the answers to the warranty provisions that are contained in this proposal or that we've got the appropriate answer to the manner in which we best handle the management contract provision.

I think, again going back to the specifics in our statement, we tried to suggest that there are other ways that these are being done in some States and that maybe at this stage Congress would be well advised to try the guideline approach on those operational provisions subject to State experience, and if it doesn't work, we'll come back and make some other change.

Senator BROOKE. How much consumer input is there in your institute?

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Mr. DOWDEN. Roughly 45 percent of my total membership at the moment is homeowner association leaders or the homeowner association itself. In addition, I am required to have the CAI board and among the various policy committees an equal balance of builders and homeowners and property managers and others. So that one of our trustees who was before the committee yesterday also serves as president of the association of condominium owners, and he delivered a statement on their behalf.

Senator BROOKE. Thank you.

Senator BIDEN. Thank you, Senator.

I'd like to mention three things in closing this portion. One, it always surprises me that sometimes the press and witnesses fail to understand the purpose of a hearing. By that, I mean as Senator Brooke pointed out, we do come to these hearings with an open mind. Otherwise, there's no sense in having a hearing. We'd just introduce the legislation and take it to the floor. Obviously, we want to hear witnesses in order to alter what is wrong with our legislation, assuming it's just not a basic philosophic difference. Second, Senator Garn had to go testify before the Agriculture Committee on a matter and he will be back.

Third, since I have put myself once again in a position of being in a distinct minority on the Sinai issue in the Foreign Relations Committee, I have been assigned to handle the minority position on that. I'm going to have to leave very shortly and I don't want that to be taken as a reflection of a lack of interest in my own legislation and the testimony of the following six people at which time I'd like to call them up.

Thank you very much, Mr. Dowden.

Mr. DOWDEN. Thank you.

Senator BIDEN. I hope I pronounce all the names correctly. Mr. Carl A. S. Coan, Jr., National Association of Home Builders; Mr. Gary A. Terry, American Land Development Association; Ms. Phyllis O'Connell, executive director, Florida Condominium Developers Association; Mr. Hunter W. Wolcott, Florida Home Builders Association, Miami, Fla.; Mr. Stephen G. Johnakin, Lawyers Title Insurance Corp.; and Mr. J. Jackson Walter, Walter & Sonnenschein, Boston, Mass.

Ladies and gentlemen, for purposes of the panel, we appreciate you all participating in this. I'd like you to begin to testify in the order that I called you and that is listed on the hearing witness list which some of you may have a copy of, and if you would all please limit your oral statements to 5 minutes your entire written statement will be entered in the record completely and then you will have an opportunity during the question-and-answer period to expand upon your 5-minute oral statement. But in the interest of seeing that everybody gets an opportunity to testify—and I know that's a tough thing. Some of you have come a long way and you get to a hearing and then they tell you you have 5 or 7 minutes or 10 minutes, but unfortunately, we have no alternative. If you will limit your comments to 5 minutes I'm going to ask the clerk of the committee to inform us as to when your 5 minutes is up and if you go beyond the 5 minutes we will have you arrested and dragged out of here—and I'm only kidding. If you could try to keep it to 5 minutes, I would appreciate it.

Mr. Coan, where is Mr. Coan?

Mr. KEEN. Keen is the name, Senator.

Senator BIDEN. I beg your pardon.

Mr. KEEN. Mr. Coan is the NAHB staff vice president and legislative counsel. I'm the witness this morning. I'm a builder.

Senator BIDEN. OK. Proceed.

STATEMENT OF EMIL KEEN, HOMEBUILDER, ON BEHALF OF THE NATIONAL ASSOCIATION OF HOME BUILDERS, ACCOMPANIED BY CARL A. S. COAN, JR., STAFF VICE PRESIDENT AND LEGISLATIVE COUNSEL

Mr. KEEN. My name is Emil Keen and I'm a builder in northern Virginia. I reside in Alexandria and I'm actively engaged in the construction of condominium projects.

However, while I have personal opinions on this subject matter, I'm appearing here today on behalf of the National Association of Home Builders which represents a substantial membership throughout the country and represents the basis of our homebuilding industry.

We appreciate the opportunity to appear today and present our comments on S. 2273. While we share the committee's concerns about abuses which may have occurred in some condominium transactions, we are disturbed about the route that S. 2273 would take to deal with these problems.

This bill would add one more Federal regulatory program to the plethora of programs that already impact on the small businessman homebuilder. Even though the Federal regulations would be somewhat self-implementing in that there would be no provision for prior review and approval by HUD, we fear that we may well wind up with the same burdensome experiences that have plagued the implementation of the Real Estate Settlement Procedures Act.

The regulation of real estate transactions and the development of land has historically been a matter primarily within the province of the States. The Federal Government has normally only stepped in when there has been demonstrated to be an overriding Federal interest because of a substantial amount of interstate activity, or a demonstrated failure of the States to accept their responsibility. We do not believe that either situation is true in this case. In the first place, the overwhelming majority of condominium sales activity takes place within the boundaries of the State in which the condominium project is located. Most condominium units serve as principal residences of their owners and these owners purchase their units in the same general fashion that they purchase a single family home.

The States have not been derelict in moving to assert their responsibility to provide protection to the purchasers of condominium units within their borders. According to HUD, over 43 percent of the condominium inventory is located in three States, Florida, California, and New York. Each of these States has enacted strong condominium regulatory statutes. They and six other States plus the District of Columbia, which have enacted such statutes, account for over 50 percent of the total condominium inventory in the country at this time.

In addition, the State of Maryland has enacted a strong disclosure act with many basic consumer protections written into it. It is one of the top 10 States in inventory of condominium units.

We believe that this is an outstanding record by the States in view of the fact that widespread use of the condominium form of ownership has only developed over the past 5 years. Where activity has been substantial, the State has generally recognized its responsibility and enacted appropriate legislation. This pattern, we believe, can be expected to be followed in the other States over the next few years as they perceive the need as a result of increased condominium activity within their borders.

Just as the States have demonstrated responsibility in dealing with condominium sales, so, we believe, has the homebuilding industry demonstrated its concern that the increasing use of this form of homeownership required special attention. The first effort was the formation some time ago by NAHB, in conjunction with the Urban Land Institute, of the Community Associations Institute, as the first witness today testified.

NAHB has also undertaken educational programs for its members and the general public on the problems involved in both condominium construction and purchase. Not long ago we published a consumers guide for use by prospective condominium purchasers. A copy of this guide has been supplied to each member of the committee.

In addition, the NAHB-sponsored, voluntary warranty program administered by the Home Owners Warranty Corp. provides protection against construction defects for purchasers of condominium units in both low-rise and high-rise structures. Basically, the HOW program provides the purchasers of newly constructed condominium units with 10 years' protection against major structural defects.

Aside from our belief that there is no need for Federal intervention into the sale of residential condominium units, we are also deeply concerned that the provisions of S. 2273 would, in many cases, impose uncalled-for and undue burdens on condominium developers. In the first place, the threshold limits of coverage are so low that almost all condominium projects would be covered. The developers of these covered projects would then be subjected to a whole range of inflexible requirements which, like those imposed under RESPA, would have the effect of hamstringing condominium sales and significantly increasing the cost of those units sold.

I have been informed, Senator, that my time is up and, of course, this written statement has been presented and is available. Before I am relieved of my time, may I add a couple of personal comments that have been raised by questions of the chairman and yourself, sir, in regard to this proposed bill?

Senator BROOKE. May I ask you to do that at the conclusion of the other panel witnesses because I would like to hold to the 5-minute rule since we do have a time constraint. You will have an opportunity to answer questions later. Thank you very much for your testimony.

[Complete statement follows:]

STATEMENT OF

THE NATIONAL ASSOCIATION OF HOME BUILDERS

before the

COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS

UNITED STATES SENATE

on

S. 2273, CONDOMINIUM CONSUMER PROTECTION ACT OF 1975

OCTOBER 8, 1975

Mr. Chairman and Members of the Committee:

My name is Emil Keen. I am a home builder in Virginia actively engaged in the construction of condominium projects. I appear here today on behalf of the National Association of Home Builders which represents some 74,000 member firms in 603 state and local associations throughout the country.

With me today is Carl A. S. Coan, Jr., NAHB Staff Vice President and Legislative Counsel.

We appreciate this opportunity to appear today and present our comments on S. 2273. While we share the Committee's concerns about abuses which may have occurred in some condominium transactions, we are disturbed about the route that S. 2273 would take to deal with these problems.

This bill would add one more Federal regulatory program to the plethora of programs that already impact on the small businessman home builder. Even though the Federal regulations would be somewhat self-implementing in that there would be no provision for prior review and approval by HUD, we fear that we may well wind up with the same burdensome experiences that have plagued the implementation of the Real Estate Settlement Procedures Act. As you know, that Act provided for HUD to establish certain guidelines and criteria with respect to the provision of information in connection with real estate settlements but did not otherwise provide for HUD intervention in individual real estate settlements. Nevertheless, the problems that arose in RESPA's implementation were so many that this Committee last week, on October 2, unanimously approved a bill to suspend the operation of its principal sections for a one-year period. We hope that the Committee would apply the lesson of RESPA to this situation and reject S. 2273.

The regulation of real estate transactions and the development of land has historically been a matter primarily within the province of the

states. The Federal Government has normally only stepped in when there has been demonstrated to be an overriding Federal interest because of a substantial amount of interstate activity, or a demonstrated failure of the states to accept their responsibility. We do not believe that either situation is true in this case. In the first place, the overwhelming majority of condominium sales activity takes place within the boundaries of the state in which the condominium project is located. Most condominium units serve as principal residences of their owners and these owners purchase their units in the same general fashion that they purchase a single-family home.

Where there is any interstate activity of any substantial amount it generally only takes place under two sets of circumstances. The first would be in those housing markets which are located in two or more states, such as is true here in Washington, D. C. metropolitan area. Yet there would seem to be no more reason to regulate the sale of condominium units to be used as principal residences in such markets, than there would be to regulate the sale of single-family homes.

The second would be in connection with those condominium units which are designed primarily for use as a second home or for recreational purposes. While these are not inconsequential in number, they would seem to be predominantly located in those states such as Florida, Arizona, California and Hawaii, which have already enacted strong condominium statutes protecting the consumer. Thus, where problems may have

already arisen, the states have moved to deal with them. Furthermore, there appears to be no widespread sale of condominium units by telephone or through the mails with the types of misleading information and other abuses which led to the enactment of the Interstate Land Sales Full Disclosure Act in 1968.

Nor have other states been derelict in moving to assert their responsibility to provide protection to the purchasers of condominium units within their borders. According to HUD, over 43 per cent of the condominium inventory is located in three states, Florida, California and New York. Each of these states has enacted strong condominium regulatory statutes. They and six other states plus the District of Columbia, which have enacted such statutes, account for over 50 per cent of the total condominium inventory in the country at this time. In addition, the state of Maryland has enacted a strong disclosure act with many basic consumer protections written into it. It is one of the top ten states in inventory of condominium units.

We believe that this is an outstanding record by the states in view of the fact that widespread use of the condominium form of ownership has only developed over the past five years. Where activity has been substantial, the state has generally recognized its responsibility and enacted appropriate legislation. This pattern, we believe, can be expected to be followed in the other states over the next few years as they perceive the need as a result of increased condominium activity within their borders.

The need for the states to act in this area has also been perceived by the National Conference of Commissioners on Uniform State Laws, which is the principal developer of uniform laws in areas in which there is a fairly common concern to all the states. The Conference for sometime has been working on a Uniform Land Transactions Act. Included in the draft being considered by it was an article on condominiums. At the urgings of NAHB, a participant in the advisory committee on this uniform act, and others, the Conference in August voted to remove the condominium article, which was basically procedural in nature as to the formation of condominium entities, from the Land Transactions Act. It was referred to a separate committee to be combined with an act being drafted on "Condominium Sales and Sales Practices."

Thus, the Conference can be expected to develop a broad-scale, uniform condominium statute which it would then recommend to the states for their adoption. If the substantial use of the condominium form of ownership now prevelant in a relatively few states should spread to all the states in the future, the uniform law being developed by the Conference will be available for their use.

Just as the states have demonstrated responsibility in dealing with condominium sales, so, we believe, has the home building industry demonstrated its concern that the increasing use of this form of home-ownership required special attention. The first effort was the formation some time ago by NAHB, in conjunction with the Urban Land Institute, of

the Community Associations Institute. The purpose of CAI is to assist homeowner and condominium associations, through advice and counsel in such areas as the financing, operation and maintenance of the common facilities, to deal with this new type of real estate ownership. CAI is an independent entity entirely separate and distinct from NAHB, and its membership represents community association managers and officials, association members, and public interest groups, as well as developers and builders.

NAHB has also undertaken educational programs for its members and the general public on the problems involved in both condominium construction and purchase. We not long ago published a consumers guide for use by prospective condominium purchasers. A copy of this guide has been supplied to each member of the Committee.

In addition, the NAHB-sponsored, voluntary warranty program administered by the Home Owners Warranty Corporation provides protection against construction defects for purchasers of condominium units in both low-rise and high-rise structures. Basically, the HOW program provides the purchasers of newly constructed condominium units with ten years protection against major structural defects. Additionally, during the first year full protection is provided against defective materials and faulty workmanship, with protection against malfunctioning systems such as plumbing and wiring being provided during the first two years.

The home owners warranty is backed by the American Bankers Insurance Company of Florida which insures that, if a builder does not honor the warranty during the first two years of coverage, the purchaser will receive payment for necessary corrective work from the insurer. American Bankers is also responsible for warranty coverage for the third through the tenth years.

Aside from our belief that there is no need for Federal intervention into the sale of residential condominium units, we are also deeply concerned that the provisions of S. 2273 would, in many cases, impose uncalled for and undue burdens on condominium developers. In the first place, the threshhold limits of coverage are so low that almost all condominium projects would be covered. The developers of these covered projects would then be subjected to a whole range of inflexible requirements which, like those imposed under RESPA, would have the effect of hamstringing condominium sales and significantly increasing the cost of those units sold.

I should like to comment on some of the specific provisions of the bill. We see no need to give a purchaser as long as 15 days after he has executed his purchase contract to rescind that contract. The bill makes no allowance for situations in which the purchaser has been provided adequate information long before he has entered into his purchase contract. The time limits provided for transfer of common elements and the

termination of management contracts may well be too rigid in many circumstances, not allowing for special conditions that arise out of the particular nature of a given project. We see no need for a federally mandated warranty, especially in view of the action that the industry has taken on its own to provide warranties for new home purchasers.

The detailed two-year budget projection, including the estimated monthly cost of utilities, with its required CPA certification would probably be impossible to obtain. The type of report contemplated from an independent certified engineer would be extremely difficult to obtain, as well as most expensive. The proposed statement of the impact of commercial or other nonresidential development in the neighborhood of the project on the interests of the condominium unit owners is so subjective as to be probably worthless. And, of course, the format in which these and other disclosures must be presented to prospective purchasers will probably ultimately result in a detailed type of form, such as that which drove all who came in contact with the RESPA form up the wall.

We have had some bad experiences with HUD deciding whether state requirements fully met Federal requirements. Under the Interstate Land Sales Full Disclosure Act, HUD, not too long ago, came to the conclusion that no states met its standards and therefore decided not to accept any state registrations as complying with the Federal law, even though several states had been so certified for many years. The same would probably occur if S. 2273 is enacted.

We have also had very unfortunate experiences with the exercise of the broad investigatory powers that HUD has under the Interstate Land Sales program. It has not been uncommon for HUD to willy nilly subpoena developers to come to Washington with all their records for the purpose of proving that they are not subject to the Act, without HUD's first trying on its own to determine whether the developer is making land sales covered by that Act. Yet Section 12 of S. 2273 proposes to give HUD the same authority it has under the Interstate Land Sales Act.

While S. 2273 is billed as a relatively limited proposal, Section 13 would give the Secretary of HUD unlimited authority to prescribe additional standards for consumer protection and additional disclosure requirements that would be applicable to all condominium projects. This is an open invitation to the regulatory bureaucracy to continuously devise new reasons for its existence. Without even such authority in the Interstate Land Sales Full Disclosure Act, HUD, in recent years, has expanded the requirements under that Act far beyond the contemplation of all concerned when that Act became law. Imagine what could happen if Section 13 of S. 2273 is enacted.

S. 2273 is unnecessary. While there has been an explosive growth in the condominium form of home ownership over the past five years, there has also been an acceptance by the states, where this growth has primarily taken place, of their responsibilities to supervise condominium sales. We believe that this is how condominium sales should be continued

to be supervised, by those units of government which are most directly concerned and knowledgeable about the particular nature of real estate transactions within their jurisdiction -- the states. This is the view expressed by our Board of Directors at its most recent meeting two weeks ago, when it adopted a resolution in opposition to S. 2273 as an unnecessary intrusion by the Federal government into an area which is primarily a matter of state responsibility. A copy of this resolution is attached.

Nor would there seem to be any great outcry by the public for enactment of S. 2273. The recent study completed by HUD indicates that 95% of the condominium residents interviewed for HUD are either satisfied or very satisfied with their unit. We realize that this does not mean that there have been no problems or complaints but this degree of satisfaction, and the evident move by the states to provide appropriate supervision, are strong arguments against the open-ended and complex regulatory scheme proposed by S. 2273. We urge the Committee to reject S. 2273 as unnecessary.

Thank you for this opportunity to present our views to you today.

ATTACHMENT

NAHB RESOLUTION

Honolulu, Hawaii
September 23, 1975

EXECUTIVE COMMITTEE

REGULATION OF CONDOMINIUM SALES

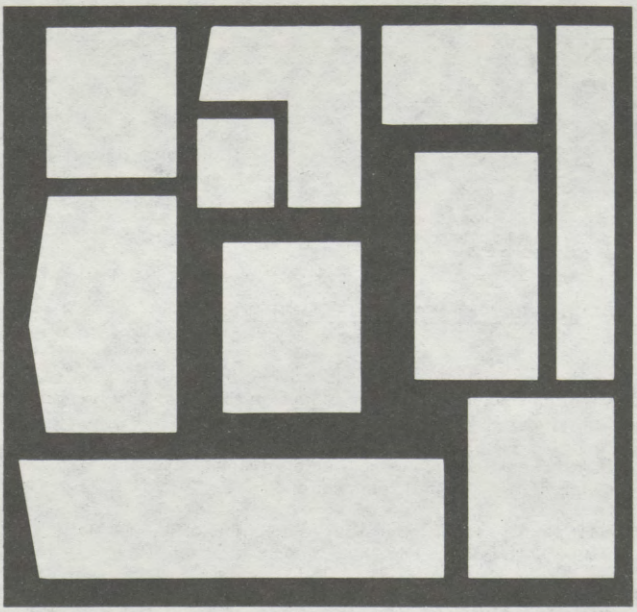
WHEREAS, legislation has been introduced in the U. S. Senate (S. 2273) to establish Federal standards to govern the sale of residential condominium units; and

WHEREAS, the regulation of real estate transactions has historically been a matter of state concern; and

WHEREAS, most states, where large numbers of residential condominium sales have taken place, have moved to assert their responsibility over such condominium sales to assure adequate protection of consumer interests;

NOW, THEREFORE, BE IT RESOLVED, that the National Association of Home Builders express opposition to S. 2273 as an unnecessary intrusion by the Federal Government into an area which is primarily a matter of state responsibility, namely the regulation of the sale of residential real estate.

APPROVED BY THE BOARD OF DIRECTORS



CONDOMINIUM BUYERS GUIDE

con-do-lence \kon-'do-len(t)s, 'kän-de-\ *n* 1 : sympathy with another in sorrow 2 : an expression of sympathy **syn** see PITY

con-do-min-i-um \,kän-de-'min-e-um\ *n* [NL, fr. L *com-* + *dominium* domain] 1 a : joint dominion; *esp* : joint soverignty by two or more nations b : a government operating under joint rule 2 : a politically dependent territory under condominium 3 : a home you own in a multi-unit building, such as an apartment complex or town-house cluster

con-do-na-tion \,kän-do-na-shun, -de\ *n* : implied pardon of an offense by treating the offender as if it had not been committed

con-done \ken-'don\ *vt* [L *condonare* to forgive, fr. *com-* + *donare* to give — more at DONATE] : to pardon overlook voluntarily **syn** see EXCUSE — **con-don-er** *n*

con-dor \'kän-der, - do(e)r\ *n, pl* **condors** [Sp *condor*, fr. Quechua *kuntur*] 1 : a very large American vulture (*Vultur gryphus*) of the high Andes having the head and neck bare and the plumage dull black with a downy white neck ruff and white patches on the wings 2 *or pl* **con-do-res** \ken-'dor-(,)as, -'dor-\ : any of several So. American coins bearing the picture of a condor

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prepared by
National Association
of Home Builders



Foreword

Home ownership is a sound investment. "A place of your own" provides security and personal satisfaction. And the purchase of a home is probably the largest single financial transaction you'll ever encounter.

In recent years a new option has been added to the choices offered potential home buyers: the condominium. Just when you may think you've mastered the delicate process of buying a house, perhaps with the help of NAHB's popular "Home Buyers Guide," a new element—the condominium—raises new questions.

Condominium ownership is an excellent investment. It's home ownership with many of the worries of maintenance and upkeep removed. The pitfalls, as with any major financial investment, *are* there—but they are avoidable if you exercise the same prudence you would exercise in purchasing any home.

The National Association of Home Builders and its 78,000 members believe this Condominium Buyers Guide can help. It should encourage you to examine the product carefully—to understand the condominium concept—and, most important, to *ask meaningful questions.*

Remember: it is a *home* you are buying. And while there have been instances of questionable practices that have placed buyers at a disadvantage, the basic legal, sales, and technical information offered in this booklet should be

sufficient to make your condominium purchase a wise investment—and a satisfying one.

In addition to the built-in advantages of home ownership, here are a few of the advantages unique to condominium ownership:

Maintenance

Your condominium Owners Association takes care of all common areas, facilities, and all exterior maintenance and landscaping.

Management

The owner of each condominium unit has a vote in the affairs of his community. The day-to-day business affairs of the condominium handled by a managing agency.

Ownership

You own your own home; you and your neighbors jointly own the common elements of the building and the land around the buildings, as well as recreation* and parking areas, with shared responsibility through the Owners Association.

Replacements

Most condominium Owners Associations maintain a reserve fund to replace roofing, repaint the exteriors, and even repave all drives and streets if they wear out.

*Recreation facilities are sometimes leased to the condominium Owners Association. Check your Master Deed to see whether it is an ownership or lease arrangement.

What's a Condominium?



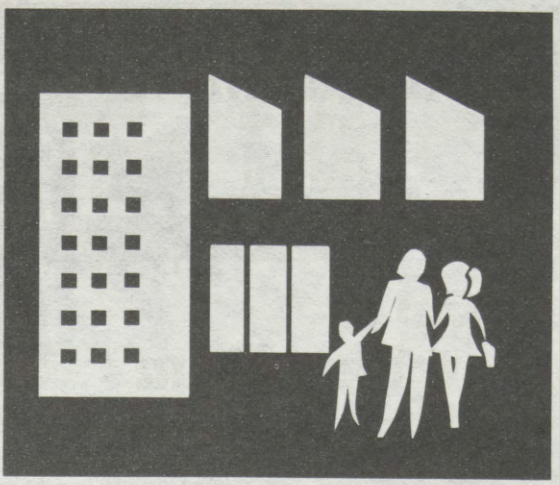
A condominium is a form of ownership.

It's a home you own in a multi-unit building, such as an apartment complex or townhouse cluster. As a condominium owner, you hold the deed exclusively to all of the enclosed space precisely described in your title. You are responsible for the maintenance and upkeep of that space—the walls, oven, refrigerator, etc.

Besides these features, you own—in conjunction with your neighbors—an undivided interest in the *common elements* of the condominium property. These elements are described in the Master Deed (which we'll discuss later). They include the building's exterior, the hallways, the utility pipes, the land under the building, the grounds, and the recreational facilities.

You will note three basic areas that distinguish between the ownership of a condominium dwelling and the ownership of, say, a single-family house:

- The condominium dweller is *sole* owner of only the inner living space. The fellow with the house owns not only that space but the exterior of the house and the land under and around it as well.
- The owner of a house owns his lot outright, while *all* condominium owners jointly own the grounds and exterior facilities, maintaining them through a "co-owners association."
- The owner of a house bears all the costs of maintenance and exterior decoration of his home, while the condominium owner contributes a monthly fee for the upkeep of the jointly owned "common elements."



The basic financing is generally similar in both cases. Whether you're buying a house or a condominium unit, the lender (or mortgagee) secures his long-term loan to the buyer with a mortgage, or a deed of trust. The buyer in both cases is solely responsible for the principal and interest payments on his home, as well as local real estate taxes on his unit and personal property and liability insurance for occurences within the homeowner's unit.

For the condominium owner, there will also be a fee to be paid into the co-owners association, covering operating expenses of the property and providing a reserve for replacements and improvements.

As a co-owner of the grounds, recreational facilities, and other amenities and common elements, you have a voice in the maintenance and management of these facilities. They may be improved, changed, or preserved only as you and your co-owners see fit.

Your building—your home—is just what you and your co-owners association make it.



How to Buy a Condominium

Pardon the repetition, but remember: It is a *home* you are buying. As with the purchase of any home, great care must be exercised.

The condominium you choose should reflect the life style you and your family desire. Its convenience, comforts, and space should match your needs and tastes—and budget.

Have the children grown and left home? You might prefer an all-adult condominium community, perhaps a high-rise.

Are you a young couple, just starting out? A garden-condominium community, occupied by new families like yours, might be the thing.

Is the family about to grow? A townhouse might be the answer.

The range of selection varies widely—and with it, the choice of amenities and facilities. Think carefully about what pleases you. A swimming pool? Tennis courts? Finished basement? Teen center or clubhouse? The choices are yours.

Take your time. Investigate the neighborhood.

Before we focus on the condominium, let's list some of the basic points you should consider in choosing a neighborhood and a home, be it house or condominium.

First, the neighborhood:

Consider practical aspects, such as time and distance to place of work, to schools, and the availability of transportation, as well as considerations such as "atmosphere" or "lifestyle." These are important when selecting the right location and neighborhood for you. As you shop, compare neighborhoods as much as homes.

CHECKPOINTS FOR OUTSIDE THE HOME

Make your own personal observations, but also consult your builder, local government, and knowledgeable people. As you explore various homes and neighborhoods, use these checkpoints to compare them and see whether the housing environment matches your wants and needs.

	Home 1	Home 2	Home 3
Shopping Are there adequate facilities close by?	■	■	■
Community Is the community well-planned?	■	■	■
Neighbors Are they likely to be compatible with your tastes and lifestyles?	■	■	■
Police and Fire Protection Are they adequate for the area?	■	■	■
Schools Are the schools your children will attend located to suit you?	■	■	■
Hospital Is there a hospital or medical center nearby?	■	■	■
Hazards Are hazards such as gas or oil tanks and streams that might overflow at a considerable distance?	■	■	■
Recreation Are there suitable facilities for young and old within walking distance?	■	■	■
Places of Worship Are they available and convenient?	■	■	■
Trash and Garbage Disposal Are the arrangements adequate and frequent enough?	■	■	■
Traffic Are streets likely to be busy or quiet? Does the speed limit suit you?	■	■	■
Parking Are there enough parking spaces and garage facilities for your needs?	■	■	■
Transportation Is public transportation adequate and handy?	■	■	■

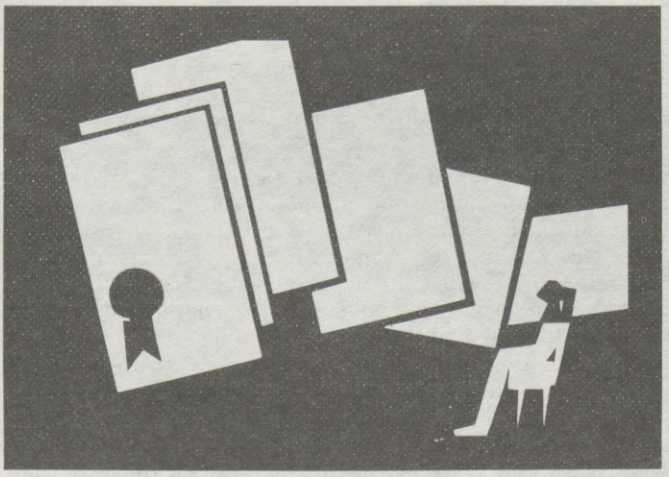
	Home 1	Home 2	Home 3
Lay of the Land Is land well-drained? And do you like the "micro climate"? For example, in a valley you may have a great deal of fog; on a hill, it may be windy!	■	■	■
Landscaping Has proper landscaping been done to prevent erosion?	■	■	■
Water Is there a reliable source of drinkable water with adequate pressure to fit present and future community needs?	■	■	■
Sewerage Is the sanitary sewage disposal system reliable and adequate and does it meet present and anticipated future community needs?	■	■	■
Privacy Are units arranged to suit your family lifestyle?	■	■	■
Nuisances Are there nearby sources of excessive noise, smoke, soot, dust, or odors that will degrade your housing environment or endanger members of your household?	■	■	■
Assessments Are there special assessments covering a portion of the lot, street, or community development costs which will mean added monthly charges to you for a specified number of years?	■	■	■

CHECKPOINTS FOR INSIDE THE HOME

What you should look for inside the living space depends on what you personally need and want, so it's a good idea to compile your own list of features to check. Here are some questions to start you off, but you should add checkpoints according to your personal concerns. Rate the homes you're comparing as good, fair, or poor.

	Good	Fair	Poor
Do walls seem sound and smooth, floors firm and level, carpentry well-fitted and joined?	■	■	■
Is the basement clean and dry?	■	■	■

	Good	Fair	Poor
Is lighting good, in daylight and at night?	■	■	■
Are rooms large enough for your furniture and is there sufficient useable wall space for arranging furniture?	■	■	■
Is the floor plan well-laid-out with separate areas for living, working, and sleeping?	■	■	■
Do bedrooms and baths provide quiet and privacy away from the living area?	■	■	■
Is sound insulation adequate between individual home units?	■	■	■
Can you get from entry doors to other parts of the house without crossing the living room?	■	■	■
Does the kitchen suit you—does it have good light and ventilation and are there enough outlets for plugging in all your kitchen appliances?	■	■	■
Are there ample cabinets and counter work space for your family needs?	■	■	■
Have all interior wall, ceiling, and floor surfaces been properly finished?	■	■	■
Is there adequate and convenient closet room and storage space for linens and equipment?	■	■	■
Do doors, windows, and drawers work easily?	■	■	■
Does plumbing work well and quietly, with adequate water pressure and free-flowing drains?	■	■	■
Is heating, cooling, and ventilating equipment satisfactory and convenient?	■	■	■
Are there enough well-arranged electric outlets with sufficient amperage for your equipment?	■	■	■
Are bathrooms and lavatories conveniently located?	■	■	■
Are the rooms located to take advantage of sun and shade?	■	■	■
Are the views from the windows to your liking?	■	■	■
Are the temperature controls located in safe and convenient places?	■	■	■
If there are stairs, are there landings and adequate handrails?	■	■	■



DON'T BE OVERWHELMED

Many prospective condominium buyers are taken aback by the formidable array of legal documents associated with this transaction. On top of that, many have read negative newspaper stories about consumers who have been misled or cheated by unscrupulous developers.

True: the paperwork in condominium transactions is heavy—but it's necessary *for your protection*, and it's to your advantage to deal with these documents carefully and conscientiously.

Also true: there have been abuses in the condominium market. In some cases, promises have been broken, and major items affecting the buyer (and his wallet) have not been disclosed.

The developer who has covertly and intentionally misguided the public gives *all* homebuilders a bad name. NAHB believes that consumers and builders alike are best served by fair and open disclosure of the scope, services, and dimensions of the dwelling—be it condominium, single-family house, or apartment—and all of the provisions of the transaction.

Remember, it is a *home* you are buying. Ask questions, such as:

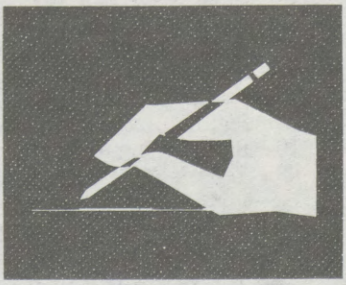
- What's the builder's reputation? Does he guarantee his work? How long has he been in business? Be sure you are dealing with a professional builder.
- How is the quality of the construction? Is the sound-proofing effective? Design satisfactory? What is under warranty? Are you satisfied with the overall structure and the finished workmanship? How does it look?

- What is included in the condominium, the part solely owned by you, and where will it be located? Size and make of stove/oven? Refrigerator? Precisely where will your unit be located in the project?
- What recreation facilities will there be--and *when will they be finished?*
- How will the recreation facilities be operated and controlled? Will they be turned over to the co-owners association--and when? Will outsiders share in their use—and will they be charged? If so, who will realize the income? What will your financial obligations be? If the facilities are *leased* to the association, what are the terms and conditions? Can the lease be terminated?
- When will the developer transfer control to the association? What happens to the monthly fees meanwhile?
- Who is the *managing agent*—the person or group who actually runs the project? Reputation? Terms of his contract? Can your association choose another? If the management contract term seems excessively long, includes huge fees, and the Owners Association is restrained from selecting another agent—*BEWARE.* That's called a "sweetheart" contract, and likely does not favor the consumer. Find out how much of your monthly dues goes to the agent for services performed.
- Are the common elements adequately insured? Check the extent and values of coverage. Remember, your association is responsible for fire, theft, workmen's compensation, director's bonds, and liability. *The individual owner should carry a personal insurance package* covering his unit and belongings, as well as any personal liability insurance he might need.
- Is there a pre-sale agreement with a financial institution? Such an agreement often prohibits the builder from "closing" on your home until a specific number of condominiums have been sold or reserved. Should sales fall below the required number, the builder should return your deposit and the purchase should be voided.
- Are there any unusual conditions or restrictions of which you should be aware? Can you sell your unit without undue co-owner approval? Who owns the utility systems? Can you keep a pet? Do you own a parking space? Can you rent out your unit? Can you remodel your kitchen? Who removes the snow?

Don't be afraid to ask these questions and any others that come to mind as you explore the situation. And be sure the answers you receive are supported by the basic condominium documents.

Always ask for the basic condominium documents—Master Deed, by-laws, contracts, floor plans, etc., and read them thoroughly.

About those Documents...



Again, be sure you get them all and read them thoroughly. If you don't understand them, don't hesitate to seek professional help.

THE MASTER DEED

The Master Deed, as it is usually called, is the controlling condominium document. It states the intention of the builder to create condominium units and sell them, subject to the legal and technical obligations imposed by local authorities. In addition, an exhibit attached to the deed records with the city, state, or county a description of the property and facilities.

The Master Deed should fully describe the size, location, and mechanical equipment in each condominium home. For your protection, look for definitions and detailed descriptions of these additional items:

1. The scope of the project itself.
2. The co-owners association.
3. General common elements.
4. Limited common elements.
5. Easements by utilities and other parties.
6. An explanation of the undivided interests and values of the co-owners.
7. The purposes for which the building and each of the units may be used.
8. Provisions for assessments and charges.
9. A management agency agreement.

The by-laws, usually an exhibit to the Master Deed, provide for administration and maintenance of the condominium. Look for these items:

The Co-Owners Association

This section should define the association and the rules and regulations governing the condominium. It includes the size and duties of the board of directors, requirements for meetings, and voting powers. The co-owners elect the board to direct the affairs of the condominium, to administer policies outlined in the by-laws, and to oversee the upkeep and budget of the condominium.

Fiscal Management Policies

The board of directors should adopt a budget for each calendar or fiscal year, to be submitted to the owners at an annual meeting. The budget process should consider not only costs of maintaining the common elements, but also the need to reserve funds for changes and capital improvements. A typical budget will provide payment for landscaping, maintenance, utilities, management, taxes, and insurance. As a prospective buyer, you should know what the annual expenses will be.

Assessments

The assessments, which are to be your pro rata share of the annual expenses, should be clearly stated.

Insurance Policies

All insurance policies covering the common elements should protect the co-owners from loss or damage by fire and other hazards. They should include coverage for liability. Recoverable sums should be made payable directly to the co-owners association. Individual insurance covering each owner's property is not included in the master policy.

Use and Transfer of the Unit

To provide for a congenial project and to protect the value of the units, the use of each condominium should be clearly defined. You assume you are purchasing a residential unit. Make sure the document says so. Purchasers have sometimes used their units for offices or other purposes, to the displeasure and inconvenience of their neighbors. Also, be sure you know whether you can sell or rent out your unit without complicated approval procedures by the board of directors.

Default

Each co-owner should be put on notice as to what constitutes a default in favor of the board of directors or the co-owners association. Specifically, what happens if your neighbor fails to pay his condominium fee? Does this constitute a lien on his property—and, if so, what are the association's remedies?

Contributions for Extraordinary Expenses

In a prepared paragraph, the by-laws should apportion common expenses, based upon the projected operating budget. These charges do not take into account special or extraordinary fees that might be assessed against all the co-owners. These special charges, which may be assessed from time to time, could be an extraordinary increase in real estate taxes, construction of a new swimming pool, or some other one-time capital improvement that might be approved by the board of directors.

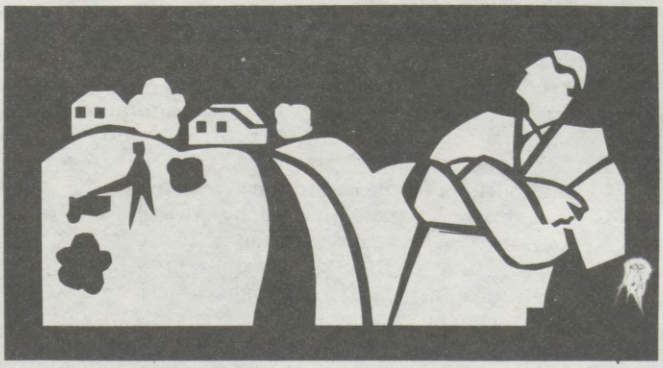
The Condominium Unit Sales Contract

This is the first document you will be asked to sign. You should be quite particular about the terms and conditions stated in the contract. This agreement should *completely* describe your unit, the purchase price, the method of payment, and the time and place where the closing of purchase will occur. Find out what the closing costs will be. When you sign this purchase agreement the sales representative will usually require an "earnest money" deposit to show your "good faith" and reserve the unit. At closing you will complete the purchase of your home with additional cash, payment of "closing" costs, and usually assumption of the mortgage note. Closing costs, or settlement charges, are fees, taxes, and prepayments, and will vary in amount. Your settlement sheets should clearly show the total sum and categories of charges.

Management Contract

The Master Deed should provide for the employment of a managing agent. Initially the developer, or a subsidiary, acts as the management, but the co-owners should be given the right to select the association's agent.

Let's explore the management contract and the duties of the managing agent. Technically, the association arranges for management. This can be an individual or management concern. The duties of the management are clearly described as are the authority and powers to carry out those duties.



The responsibilities of management should include:

1. The maintenance and upkeep of the common elements; including hiring the lawn care company and the swimming pool operator, and generally supervising the building operations.
2. The hiring of building employees, such as the superintendent, guard, or switchboard operator.
3. The preparation, for the co-owners approval, of the insurance package and the operating budget.
4. Control of a limited fund to be used without prior consent in emergencies. Find out the limit of this fund.
5. The accounting and record-keeping procedures, which will detail the income, expenses, and reserves. Management can also be responsible for the collection of delinquent assessments.

In summary, management functions as the association representative. It oversees the details of the project, from lawn care and swimming pool to replacement reserves and budgeting. Management must enforce the association's policies in a professional and judicious manner.

The structure of the condominium and the condominium documents outlined above are typical but may vary according to local law and practice. The legal documents used in forming and selling condominiums can be very complex. If you have any questions or doubts regarding your rights and responsibilities as a condominium owner, consult an attorney.

How Much can you Buy?



WHAT CAN YOU SPEND FOR MONTHLY HOUSING?

1. Your Average Monthly Income

Take-home pay* (gross pay less taxes)	$_____
Rents, dividends, interest**	_____
Other income	_____
Net Average Monthly Income (add) (1)	$_____

2. Your Average Monthly Non-Housing Expenses

Food, household supplies	$_____
Clothing	_____
Medical costs and insurance	_____
Life and casualty insurance	_____
Automobile and insurance	_____
Education	_____
Commuting	_____
Installment payments/interest charges	_____
Recreation, hobbies (adjust realistically)	_____
Telephone	_____
Contributions, dues, fees, etc.	_____
Personal (cleaning, barber, etc.)	_____
Savings/investment program (adjust realistically)	_____
Other miscellaneous expenses	_____
Total Average Monthly Non-Housing Expenses (add) (2)	$_____

3. Your Monthly Income Available for Housing

Net average Monthly Income (total 1)	$_____
Subtract Non-Housing Expenses (total 2)	_____
Average Monthly Income Available for Housing Expenses (3)	$_____

** You may include wages of a spouse who is working, or of other members of the family who live with you.*

***Do not include dividends and interest from savings and investments you will use for down payment. Include only stable income sources.*

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4. Average Monthly Housing Expenses*

Condominium Association fee	$_____
Mortgage repayment (principal and interest)	_____
Personal property and liability insurance (if not included in mortgage loan repayment)	_____
Unit property taxes (if not included in mortgage loan repayment)	_____
Utilities (heating, electricity/gas/oil, water)	_____
Other monthly housing expenses (decorating, appliances, etc.)	_____
Average Monthly Housing Expenses (add)	$_____

HOW MUCH DOWN PAYMENT CAN YOU AFFORD?

5. Available Funds

Equity (see Glossary in back) in present home/lot	$_____
Savings, savings certificates	_____
Investments/mutual funds (current value)	_____
Insurance (cash surrender value)	_____
Other available funds (such as a personal loan)	_____
Total Available Funds (add)	_____
Subtract Amount you must keep in reserve	_____
Adjusted Total Available Funds	(a) $_____

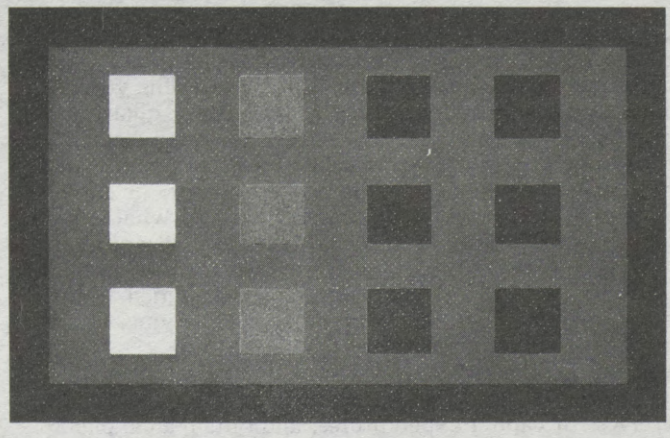
6. Expected Cash Expenses

Cash costs for *closing* and *settlement*	_____
Furniture, furnishings (if any)	_____
Moving expenses	_____
Other expected expenses	_____
Total Expected Expenses (add)	(b) $_____
Now subtract total (b) (your expected expenses) from total (a) (your available funds) to get **amount you can afford to spend for your down payment:**	_____ (c) $_____

Subtract the down payment from the sales price of the home you wish to buy and you will know how much of a mortgage you will need to finance.

** Your builder's representative can probably approximate these costs for you. Now double-check your estimates. Check total 3 (what you can spend each month for housing) against total 4 (what you will need to spend each month for housing) to make sure that the home you are considering is within your means.*

What about Condominium Conversions?



We have concentrated so far on the legal and technical aspects of purchasing a new or imminent condominium home. Consider now the condominium *conversion.* What is it? What should you know before you buy?

A condominium conversion is an existing rental apartment structure that is changing its form of ownership by selling the units to the present tenants and/or to new occupants. The reason is that the owner(s) of the building have decided not to operate the structure as a rental apartment house, and are offering each apartment for sale. In essence, they are "converting" the ownership from themselves to others.

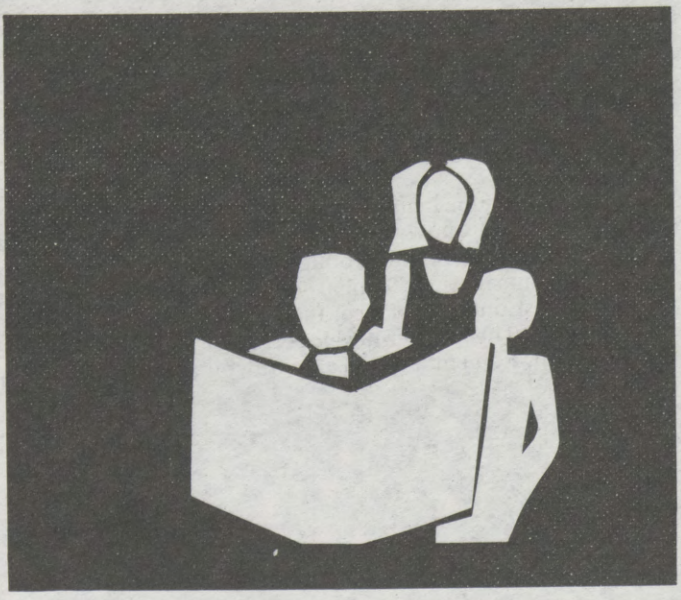
In a typical situation an apartment building is owned by a group of investors who receive a return on their investment in the form of tax saving and cash distributions. For various reasons they may decide that the best method of selling their building is to "convert," and dissolve their method of ownership. They must deal with the special problems of conversion: market needs, renovating the structure, budget, financing, and all the details that will present a saleable, attractive product to the

consumer. A team of professionals, which may include attorneys, architects, landscape planners, painters, dry wall contractors, heating and air-conditioning contractors, electricians, and more, descend to breathe new life into a seasoned building. And after the dust has cleared and the paint is dry, the potential purchaser has yet another choice. Should you choose to buy a condominium home in a "conversion," you must use all the same criteria you would if you were buying a "new" home—and then some. Again, be selective, ask questions, get the facts.

HERE ARE SOME GUIDELINES BEFORE YOU BUY:

1. **Understand what you are buying.** If the building you are considering is seasoned, and the extent and quality of renovation will give each unit and the common elements new economic value. Find out the condition of the mechanical elements (i.e., plumbing, heating, air conditioning). What about sound transmission? What's the condition of the roof? The walls? Are the utility pipes in good condition? Are new windows being installed and are they insulated? What equipment is included in the kitchen? Remember, it is a home you are buying. Learn as much as you can about it.
2. **Ask for a copy of the proposed condominium association budget.** Pay special attention to the projected reserves for capital expenditures, and obtain an explanation for their uses.
3. **Determine which elements of the building are restored and which are improved.** Restored components should be brought up to "like new" condition and have an extended usable "life." Improvements enhance the design and value of the building. Find out if structural, mechanical, and electrical systems have been repaired or replaced.
4. **Make sure the building and the unit conform** to local governmental requirements. A refurbished heating system *not* in compliance could be costly and inconvenient to the new unit owners association.
5. **Select your neighborhood with care.** Consider location, access to facilities such as shopping and transportation, and all the other factors that suit your personal tastes and lifestyle.

The condominium conversion provides the potential buyer an opportunity to live in an established neighborhood, sometimes at a price below that of a newly constructed condominium.

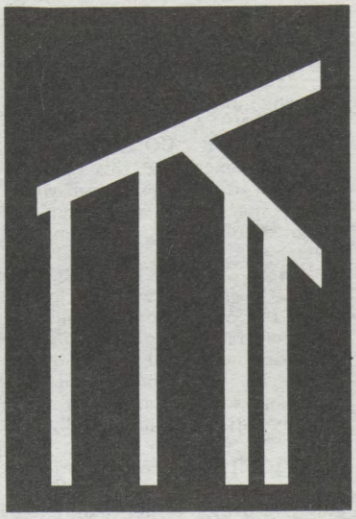


22

in Summary

Condominium living can be an attractive and worthwhile investment. By now, you probably have rightly concluded that what this booklet boils down to is *common sense.* Allow yourself time to plan your purchase carefully. Plan your questions in advance; read them from this booklet, if you wish. The builder-developer, after all, is in business to serve you. Remember, it is a *home* you are buying.

Glossary



WORDS YOU SHOULD KNOW

ABSTRACT—A summary of the history of the legal title to a piece of property.

AMORTIZATION—Provision for gradually paying off the principal amount of a loan, such as a mortgage loan, at the time of each payment of interest. For example, as each payment toward principal is made, the mortgage amount is reduced or amortized by that amount.

APPRAISAL—An evaluation of the property to determine its value. An appraisal is concerned chiefly with market value—what the unit would sell for in the market place.

ASSESSMENT (Operating)—Proportionate share of the budgeted annual cost to maintain physically the common areas and elements of a condominium and to maintain sufficient reserves to assure financial stability. The annual assessment is reduced to monthly charges payable to the Owners Association.

ASSESSMENT (Special)—An assessment for some special purpose or because of inadequate budgeting of operating expenses.

BINDER—A receipt for earnest money or a deposit paid to secure the right to purchase a home at terms that have been agreed upon by both buyer and seller.

BYLAWS—The rules or code of regulations providing for the administration and maintenance of the condominium project or a Planned Unit Development. Often the bylaws are inserted in or appended to and recorded with the master deed.

CC and Rs—Conditions, covenants, and restrictions. See Declaration.

CAVEAT—A warning or notice to take heed, such as a clause in a document which is meant to be a warning.

CERTIFICATE OF TITLE—Like a car title, this is the paper that signifies ownership of a unit. It usually contains a legal description of the unit and its relationship to the condominium.

CLOSING COSTS—Cost usually in addition to the price of a unit and its undivided interest in the common estate including mortgage origination fee, title search, personal property and liability insurance, and transfer of ownership charges paid each time the unit is resold or refinanced.

CLOSING DAY—The date on which the title for property passes from the seller to the buyer and/or the date on which the borrower signs the mortgage.

COMMON AREA, COMMON ESTATE, OR COMMON ELEMENTS—Generally, this encompasses all of a condominium which is not specifically delineated and described as dwelling or commercial units.

COMMON OR UNDIVIDED INTEREST—Joint ownership with other fee owners of all land and areas within the structures that are not described as individually owned units. The interest is defined by a percentage of a total area but not actually divided into individual parts.

CONDOMINIUM—An apartment house or complex where individual units are owned rather than rented, with each homeowner holding an undivided interest in the common areas and facilities. Dwelling units are mortgaged separately, and each owner contributes a share of the expense for maintenance and operations of common facilities, which are administered by an elected board of owners.

CONDOMINIUM ASSOCIATION, ASSOCIATION OF OWNERS, CONDOMINIUM ASSOCIATION BOARD OF DIRECTORS, OR COUNCIL OF CO-OWNERS—See Owners Association.

CONDOMINIUM REGIME—The mode of self-rule established when condominium documents are recorded. The term also refers to all the documents necessary to legally constitute a condominium and to permit it to operate as such.

CONDOMINIUM UNIT—The enclosed space in a condominium project as described by the condominium documents.

CONVEY—To transfer title from one person to another.

COOPERATIVE HOUSING—A housing corporation or a group of dwellings owned by residents and operated for the benefit of resident members of the corporation by their elected Board of Directors. The resident occupies but does not own his unit. Rather, he owns a share of stock or membership certificate in the total enterprise.

COVENANT—A written agreement generally relating to land use conditions or restrictions. It usually binds subsequent owners.

DECLARATION—A document which contains conditions, covenants and restrictions governing the sale, ownership, use and disposition of a property within the framework of applicable State condominium laws.

DEED—A document used to transfer a fee simple interest in the unit together with an undivided interest in the common estate in the case of condominium title transfers.

DELINEATE—To describe the physical boundaries of a dwelling unit in a condominium.

DEPRECIATION—A decline in the value of a dwelling unit as the result

of wear and tear, adverse changes in the neighborhood and its patterns, or for any other reason.

DISCOUNT POINTS—The amount of money paid to the lending institution in order to obtain a mortgage loan. Each point is equal to 1 percent of the loan. See "Points."

EARNEST MONEY OR SUBSCRIPTION MONEY—The deposit money given to the seller by the potential buyer to show that he is serious about buying the dwelling. If the deal goes through, the earnest money is applied against the down payment. If the deal does not go through, through no fault of the seller, it may be forfeited.

EASEMENT—A right or privilege a person or group of people may have to property owned by one or more other persons.

ENCUMBRANCE—A claim or lien attached to real property, such as a mortgage or unsatisfied debt incurred with respect to the property.

EQUITY—Increase in value of ownership interest in the unit as the owner reduces his debt by paying off his mortgage, and from market value appreciation.

ESCROW FUNDS—Subscription or down payments required to be held unused, until the condominium regime is recorded on the property and titles are conveyed to each buyer. Escrows are usually used in each resale situation. The deed is held in escrow until all conditions of the sale (including any prepayments) have been met. Other escrow accounts are used to accumulate monthly property tax and personal insurance payments until the taxes and insurance are actually due.

FHA—Federal Housing Administration. This federal agency, established by Congress in 1934, insures mortgage loans made by FHA-approved lenders on homes that meet FHA standards in order to make mortgages more desirable investments for lenders.

FEE SIMPLE—The absolute ownership of land with no restriction on transfer of ownership.

GRANTOR—The owner of the property which is being subdivided into a multiple number of individual unit estates under a condominium regime.

INTEREST—The cost paid by a borrower for use of money borrowed to purchase a home.

LEASEHOLD INTEREST—The right to use a property under certain conditions which does not carry with it the rights of ownership of the land.

LIABILITY AND HAZARD INSURANCE (Association)—Insurance to protect against negligent actions of the Owners Association and damages caused to property by fire, windstorm, and other common hazards. This policy differs from the homeowner's personal insurance on his unit and furnishings.

LIEN—A claim recorded against a property as security for payment of a just debt.

MASTER DEED—The basic document used in the creation of a

condominium. It is occasionally referred to as "Matrix Deed," "Enabling Declaration," or "Deed of Constitution." The recorded Master Deed indicates that the property is submitted to a condominium regime and describes the division of the project into units and common elements.

MORTGAGE—The security instrument, the obligation secured thereby, the title evidence, and all other documents and other papers pertaining to a mortgage loan.

MORTGAGE (Home)—A mortgage which is secured by real property upon which is located a dwelling unit designed for residential use by not more than one family and where the real estate is owned in fee simple or consists of an acceptable leasehold interest.

MORTGAGE (Unit)—A mortgage which is secured by real property consisting of a dwelling unit designed for residential use by no more than one family and which is owned in fee simple or consists of an acceptable leasehold interest. A unit mortgage is secured by the unit itself and an undivided interest in an association having title to the common areas.

MORTGAGE INSURANCE PREMIUM—The payment made by a borrower to the lender for transmittal to HUD-FHA to help defray the cost of the FHA mortgage insurance program and provide a reserve fund to protect lenders against loss in insured mortgage transactions. In the case of an FHA insured mortgage this represents an annual rate of one-half of one percent paid by the mortgagor on a monthly basis to FHA. Nongovernment mortgage insurance companies have a similar premium.

MORTGAGE LOAN (Individual Units)—A contract in which the borrower's property is pledged as collateral and which can be repaid on an installment basis (usually monthly) over a long period of time. The mortgagor (the buyer) promises to repay principal and interest, to keep the home insured, to pay all taxes, and to keep the property in good condition.

MORTGAGE LOAN (Project)—Provides money to the builder/developer to acquire the land and construct the condominium. This loan should be paid off in full by the cash and individual mortgage loans that come into existence when all sales have been consummated. At such time the condominium individual units must be free and clear of all liens and all individual unit mortgages must be first mortgages assumed by owners of the units.

MORTGAGEE—The bank or lender who loans the money to the mortgagor.

MORTGAGOR—The homeowner who applies for, receives and is obligated to repay a mortgage loan on a property he has purchased.

ORIGINATION FEE—A charge by the lender for originating the mortgage.

OWNERS ASSOCIATION—A corporation or association as author-

ized by law, composed of the individual owners of units in a condominium project, which manages and has no ownership interest in the common areas. Its authority to operate comes from the Declaration.

PMI—Private mortgage insurance. A private company providing insurance to a mortgage lender on specific real estate loans. Such insurance protects the lender against loss in the mortgage transaction. It usually enables the mortgagor to make a lower down payment.

PLANNED UNIT DEVELOPMENT (PUD)—A real estate development which consists of separately owned lots with contiguous or noncontiguous areas of facilities owned by an Owners Association in which the owners of the lots have a stock or membership interest. Title to the real estate under the dwelling units is in the individual lot owners and not in the Association. The Association has title to and administers the common areas, and levies monthly charges against the lot owners for common area expenses. Membership in the Owners Association cannot be severed from the ownership of an individual unit.

PLAT AND PLANS—Drawings used by surveyors and architects to show the exact location of utilities, streets, buildings and units within the buildings, in relation to the boundary lines of the total property. They may also show units, common areas and restricted areas.

POINTS—A point is a charge of 1 percent of the mortgage value, a onetime charge assessed by the lender to increase the yield from the mortgage loan to a position competitive with the yield from other types of investments. The government prohibits the buyer from paying more than 1 point on FHA-VA insured mortgage loans. See "Discounts."

PREPAID EXPENSES—The initial deposit at time of closing for property taxes and the subsequent monthly deposits made to the lender for that purpose. Hazard insurance is not included in the mortgage payment under the individual unit mortgage.

PRINCIPAL—Amount of money borrowed in a mortgage loan, excluding interest and other charges.

REPAIR AND MAINTENANCE—The costs incurred in replacing damaged items or maintaining housing systems to prevent damage. In a condominium the owner is responsible for repairing and maintaining the dwelling unit and the condominium Association is responsible for repairing and maintaining the common areas. The owner only pays his proportionate share of the cost to the Association.

RESERVE FUNDS (Replacement)—Funds which are set aside in escrow from monthly Association payments to replace common elements, such as roofs, at some future date.

RESERVE FUNDS (General Operating)—Funds which are accumulated on a monthly basis to provide a cushion of capital to be used when and if a contingency arises.

SECOND MORTGAGE—A mortgage or deed of trust on property placed subsequent to an existing mortgage. The second mortgage holder's interest is secondary to the first (existing) mortgage holder's.

SETTLEMENT EXPENSE—This is different from closing costs but it also involves charges that a buyer or seller has to pay in closing a deal on a home. Settlement costs include personal insurance and property tax payments, special assessments for improvements to municipal facilities and sales commissions.

TAXES—Local real estate assessments which are levied on the individual units and not on the condominium Association.

TITLE—The evidence of a person's legal right to possession of property, normally in the form of a deed.

TITLE COMPANY—A company that specializes in insuring title to property.

TITLE INSURANCE—Special insurance which usually protects lenders against loss of their interest in property due to unforeseen occurrences that might be traced to legal flaws in previous ownerships. An owner can protect his interest by purchasing separate coverage. A mortgagee's policy, as distinguished from an owner's policy, usually protects only the lender in an amount equal to the outstanding balance of the mortgage loan.

TITLE SEARCH OR EXAMINATION—A check of the title records, generally at the local courthouse, to make sure you are buying the dwelling from the legal owner and that there are no liens, overdue special assessments, other claims, outstanding restrictive covenants, or other defects in title filed in the record.

UNDIVIDED INTEREST—In condominium law, the joint ownership of common areas in which the individual percentages are known but not applied to separate the areas physically. This situation is similar to the joint ownership of an automobile or home by husband and wife.

UNIT VALUE RATIO—A percentage developed by dividing the appraised value of a unit by the total value of all units. The percentage attaches to the dwelling unit and determines the percentage of value of the common estate attached to that unit, the percentage of votes the owner of the unit has in the government of the common estate, and the percentage of operating costs of the common area the respective unit owner must bear.

VA—Veterans Administration. A federal agency that in 1944 established a loan guarantee program to encourage private lending agencies to give liberal mortgages to honorably discharged veterans and their widows. Check your local Veterans Administration office for information.

ZONING—Classification of real property for varying uses. A municipality has a right to determine—and regulate—the use of property.

Senator BROOKE Our next witness is Mr. Terry.

STATEMENT OF GARY A. TERRY, AMERICAN LAND DEVELOPMENT ASSOCIATION, ACCOMPANIED BY WILLIAM INGERSOLL, LEGAL COUNSEL

Mr. TERRY. Thank you, Mr. Chairman.

I am Gary A. Terry, executive vice president of the American Land Development Association. Sitting behind me is Mr. William Ingersoll, legal counsel to the association.

ALDA is a national trade association representing real estate developers in the recreational, resort, and planned communities segments of the real estate industry. The majority of the member companies in our organization utilize condominium real estate ownership as the principal type of newly constructed housing.

Therefore, we are both interested in and concerned with this committee's consideration of S. 2273—Condominium Consumer Protection Act of 1975. I am appreciative of the opportunity of offering a few brief comments for your consideration.

The American Land Development Association testified before this committee last year when you were considering similar legislation. We also provided an in-depth analysis of our views on the subject of condominium regulation to staff members of this committee. In addition, we testified during the hearings on condominium and cooperative development conducted by the Department of Housing and Urban Development held in February of this year. Consequently, I believe we can assume that the detailed viewpoints of the American Land Development Association on this subject are well known. Therefore, in the interest of time, I'm going to summarize even my brief prepared statement with a couple of additional points and then attempt to answer any questions the committee members may want to ask.

While we still question the need for this Federal regulation, in our opinion, the most useful purpose to be served by S. 2273, if it were to be passed, would be to establish minimum disclosure standards for protection of the consumer in the purchase of condominium real estate. In this regard, I believe that the statement of Secretary Hills covering the views of HUD was an excellent assessment of the industry and consumer problems, level of required regulation, and suggested changes for S. 2273.

There are, in addition, some points that we didn't highlight in the written statement. First, section 18 of the bill, while philosophically very attractive to us, is probably not properly drafted. By way of explanation, I would like to read part of a letter to me from the chairman of our task force on Federal and State regulation of condominiums.

I think I'm going to get that same note.

First, it is technically inadequate for the supposed purpose. As long as a condominium is a security, section 18 merely does away with SEC registration under the 1933 act. It is still subject to all the provisions of the 1934 act, including civil liability under section 10(b), and Regulation 10(b)(5), and registration under section 12(g). To avoid

securities registration and regulations, the section must also be amended to exclude application of the 1934 act.

There are some drafting problems we see with some——

Senator BROOKE. Well, I'm going to have to ask you to put the rest of your statement in the record. It will be accepted for the record and you will have an opportunity during the question period to comment further.

Mr. TERRY. Thank you.

[The complete statement follows:]

TESTIMONY

of

GARY A. TERRY
EXECUTIVE VICE PRESIDENT
AMERICAN LAND DEVELOPMENT ASSOCIATION

Mr. Chairman, members of the Committee, I am Gary A. Terry, Executive Vice President of the American Land Development Association. ALDA is a national trade association representing real estate developers in the recreational, resort and planned communities segments of the real estate industry. The majority of the member companies in our organization utilize condominium real estate ownership as the principal type of newly constructed housing.

Therefore, we are both interested and concerned with this Committee's consideration of S.2273-Condominium Consumer Protection Act of 1975. I am appreciative for the opportunity to offer a few brief comments for your consideration.

The American Land Development Association testified before this Committee last year when you were considering similar legislation. We also provided an in-depth analysis of our views on the subject of condominium regulation to staff members of this Committee. In addition, we testified during the hearings on condominium and cooperative development conducted by the Department of Housing and Urban Development held in February of this year. Consequently, I believe we can assume that the detailed viewpoints of the American Land Development Association on this subject are well known.

This being the case my remarks this morning will be brief and can deal specifically with the current proposed legislation.

When we first reviewed S.2273 after it was introducted on August 1, we felt that significant and welcome changes from last year's bills were contained on S.2273. Especially the intent to minimize the penalty of economic impact on consumers and the lessening of Federal Government control and involvement. However, we noted the continued advocacy of adverse regulations to be imposed on developer-owners of condominium projects. In our opinion, the regulations would impose a serious financial hardship on condominium developers who are presently experiencing an unprecedented economic recession in this industry. In some instances the bill calls for regulations that could not possibly be complied with regardless of the investment of money and time.

In order to be brief this morning I will not address all of the elements of S.2273 with which we are concerned. However, should the Committee wish to have our views on those particular sections, I will be pleased to submit details by letter.

In our testimony before this Committee last year I indicated that we were not opposed to Federal legislation where corrective remedies for specific abuses were clearly called for, based on cost-benefit considerations, ineffective state controls or inability of the states to reach abuses, or non-availability of other Federal regulations for remedy. In light of this, it would seem to us that the most useful purpose to be served by S.2273 would be to establish minimum disclosure standards for protection of the consumer in the purchase of a condominium real estate unit. In this regard, I believe that the statement of Secretary Hills covering the views of HUD was an excellent assessment of the industry and consumer problems, level of required regulation, and suggested changes for S.2273.

For the most part we believe that if the changes to S.2273 that were recommended by the Department of Housing and Urban Development were adopted by this Committee we could support the proposed condominium legislation. However, we would most strongly urge one further consideration in addition to the HUD recommendations. This consideration is covered in Section 4, Prohibitions, paragraph b, generally described as the 15 day "cooling off" period. S.2273 would allow the purchaser to void a contract or agreement for the sale of a condominium unit for a period not less than fifteen days. I would urge the Committee to examine this section very carefully as it presents a serious restraint on the conduct of normal business by the condominium developer.

Briefly the fifteen day buyer rescission right could create several adverse situations for the developer. A major problem would be in the case of relatively small condominium developers where they would have to commit their available inventory of constructed units to a "hold" period for the fifteen days. This would impact

in construction debt service, sales costs and administrative costs. Another problem would develop because in new unit construction a developer schedules completion and sales of those units to his cash flow requirements. In other words he must construct, sell and take the contracts to his lender for additional incremental construction financing for the next phase. It is also possible that after a fifteen day period where recisions were initiated by certain buyers, the developer would end up with a surplus inventory of units requiring him unfairly to reduce his selling price in order to solve the problem. This may not be a problem in condominium conversion but I can assure you that it is critical in new construction. Again, I would urge you to consider this section either for elimination or for a waiver of the right of rescission in those cases where the condominium documents were put into the hands of the potential buyer at some period of time prior to signing a contract of sale. We think the inclusion of the "cooling off" period is unnecessary to the goal of giving the buyer sufficient time to review unit documents.

We appreciate this opportunity to appear here today. I sincerely hope that you will adopt the legislative changes recommended by Secretary Hills. We think it evident that her recommendations are soundly based on facts as revealed by the recently completed HUD national condominium study and by the experience of the Department of Housing and Urban Development in housing and construction matters. We could not support a bill which failed to include the Secretary's recommendations.

Thank you

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AMERICAN LAND DEVELOPMENT ASSOCIATION,
Washington, D.C., October 20, 1975.

Hon. WILLIAM PROXMIRE,
Chairman, Committee on Banking, Housing and Urban Affairs,
U.S. Senate, Washington, D.C.

DEAR MR. PROXMIRE: Time restrictions during the recent hearings on S. 2273, the Condominium Consumer Protection Act of 1975, prevented my mentioning two definitions which we feel warrant further consideration, but which we had not included in our prepared statement. Therefore, subject to your approval, I am submitting additional, brief comments for Committee consideration.

Thank you.

Sincerely yours,

GARY A. TERRY,
Executive Vice President.

ADDITIONAL COMMENTS SUBMITTED FOR COMMITTEE CONSIDERATION BY THE AMERICAN LAND DEVELOPMENT ASSOCIATION

While ALDA did not include mention in our statement filed at the time of the hearings, we do have considerable trouble with some of the definitions included in S. 2273. The following is not a complete list but is intended to demonstrate the kinds of definitions that trouble us:

Developer.—"Developer" is defined as "any person who, *directly* or *indirectly* (emphasis supplied) offers for sale condominium units in a condominium project." As drafted, this would include *resales by individuals.* Also, one wonders how one can sell "directly" or "indirectly." It seems clear that one is either the seller (or his "agent," which is defined) or one is not the seller. We wonder how one could "indirectly" develop or sell a project. The definition seems to be so drafted in an attempt to include every conceivable entity in a project. We think this is wrong.

Offer.—This term, as defined, would include all promotion and advertising, and conceivably, market research in the form of interviews and surveys. This would be a very unfortunate, wholly unnecessary definition, and would go completely contrary to essential and universally accepted trade usage of the term.

Senator BROOKE. Ms. Phyllis O'Connell.

STATEMENT OF PHYLLIS O'CONNELL, DIRECTOR, FLORIDA CONDOMINIUM DEVELOPERS ASSOCIATION

Ms. O'CONNELL. Thank you, Senator Brooke. I'd like to split my 5 minutes today with Anthony Battaglia, who is a very prominent developer in Florida.

I am the director of the Florida Condominium Developers Association and a member of the bar of the State of Michigan. Additionally, Senator Brooke, please take note I have, for the past 4 years, owned the condominium in which I reside and was the first president of the owner's association of that condominium, so I can face this picture from two angles. I am here today to speak in opposition to the pending bill and any scheme for Federal regulation of condominiums.

In Florida, we have not a first- or second-generation condominium consumer protection law, but a very sophisticated and comprehensive third-generation law. Among other requirements, it requires complete disclosure statements, abolishing escalating leases and contracts tied to any artificial index and, best of all, it now has an enforcement agency aided by an advisory arbitration panel composed of three developers and four owners.

Our State has shown it can draft strict and responsible condominium legislation. Florida legislation cannot be tailored to the specified needs of a particular State. Certainly the problems in Florida are different

than those in New York or Virginia. The condominium industry can best be served by our Federal Government if it strongly urges and assists the individual States to draft fair and equitable legislation.

Further, Federal regulation will only burden the consumer by increased costs of $500 to $1,000 for each unit. Obviously, this is not what President Ford has in mind when he called upon Congress and the executive branch "to eliminate Federal rules and regulations that would increase costs to the consumer, without good reasons."

I would like to yield now to Mr. Battaglia.

[Complete statement follows:]

PREPARED STATEMENT OF PHYLLIS O'CONNELL

BEFORE THE COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS

My name is Phyllis O'Connell. I am the Director of the Florida Condominium Developers Association, and a member of the Bar of the State of Michigan. Additionally, I have for the past 4 years owned the condominium in which I reside and was the first President of the Owner's Association of that Condominium, so I face this picture from 2 angles. I am here today to speak in opposition to the pending Bill and any scheme for Federal regulation of condominiums. Florida Condominium Developers Association was formally incorporated in 1974, and has been staffed since June 1975. It is a non-profit Association of Condominium Developers, Savings and Loan Associations, Bankers, REITS and others interested in establishing and/or operating condominium developments. Its primary purpose is to provide a voice for the industry and make the consumer public aware that we are not the boogie-men pictured in the press and TV. Our 22 point Code of Ethics is the concrete slab upon which our Association was built. I offer a copy of this as an exhibit. I am speaking today at the direction of and on behalf of the Board of Directors of the Florida Condominium Developers Association, and my comments reflect the views of that body. This is a fragmented industry, but when as now, its economic well being is challenged, it can get together and cooperate.

In Florida we have not a first or second generation condminium consumer protection law, but a very sophisticated and comprehensive third generation law. Among other requirements, it requires complete disclosure statements, abolishing escalating leases and contracts tied to any artifical index, and best of all it now has an enforcement

agency aided by an advisory arbitration panel composed of 3 developers and 4 owners.

Our State has shown it can draft strict and responsible condominium legislation. Federal legislation cannot be tailored to the specified needs of a particular state. Certainly the problems in Florida are different than those in New York or Virginia. The condominium industry can best be served by our Federal government if it strongly urges and assists the individual states to draft fair and equitable legislation.

Further. Federal regulation, attempting to wrap the consumer in swaddling clothes will only burden the consumer by increased costs of $500 to $1,000 for each unit. Obviously, this is NOT what President Ford has in mind when he called upon Congress and the Executive Branch "to eliminate Federal Rules and Regulations that would increase costs to the consumer, without good reasons . . ."

Instead of having the builder pack the unit with legal costs let him pack it with [illegible] and thus give the consumer more protection in bricks and mortar and design.

The real estate industry is in an extremely difficult period. Constricting and unbalanced legislation at this time would put an insurmountable stumbling block in its road to recovery. Unfortunately legislative wheels turn less slowly than the wheels of justice. It has been quick and easy to focus on the developer as the source of all problems but evidently that is where they become most apparent. He is the most visible dog to kick. In an attempt to remedy this, and also as a public service, Florida Condominium Developers Association recently advertised a 24 hour open "hot line", and invited calls from

condominium owners. I spoke personally to over 400 callers during the first week, and after tabulating the problems I heard, it was evident that the long term problem is the conflict between residents, especially those who have bought a condominium with not the first idea of the meaning of the condominium concept. Laymen are suddenly thrust into a position where they are responsible for service and maintenance of facilities which, if not carried out successfully, can spell disaster for the home owner, the lender, the Federal and private mortgage institutions and the local governments in which the projects are located.

Another problem, albeit a temporary one, is the gap between expectation and reality, that is, what they see in the sales office and what life is really like once they move into their home.

Problems relating to so called "abuses" were far in the minority. We do not deny they exist, but would draw your attention to the reality that unscrupulous individuals are a fact of life in every facet of our existence, and must be dealt with individually, for no amount of regulation, on any level will end their wily inventiveness.

What emerged finally from the emotional malestrom of calls from unhappy owners was the demonstration of a need for more information and education for the consumer, and this on a body to body level, not a lot of words in dusty volumes that will never be read by the consumer.

It is to this end that the Federal government should address itself if it would protect the consumer, instead of more shackling regulation aimed at the eventual but [illegible] of the small developer who constitutes 70% of the construction industry.

I thank you for this opportunity to be heard.

STATEMENT OF ANTHONY S. BATTAGLIA, DEVELOPER AND GENERAL COUNSEL, FLORIDA CONDOMINIUM DEVELOPERS ASSOCIATION

Mr. BATTAGLIA. Senator, I would like to state that I will waive my remarks. They are in the record.

I am chairman of the board of a public company on the American Stock Exchange. We have built probably close to 4,000 units in Pinellas County and other areas in Florida. I would like to point out several problems that I'm concerned with with the act.

I feel that the Federal bill, S. 2273, perhaps ought to be restricted to the interstate transactions similar to our "blue sky" laws that we have in each State. That is to say that in our securities field we have the SEC who takes care of our interstate transactions and our blue skies within the State. Florida, unlike several States, has a very adequate condominium act as you well know. It runs some 97 pages. It covers in depth some of the areas that you have and it goes further.

I'd also like to suggest that the act be restricted to those transactions of sales or matters that are going to take place outside of any given State and that if the State is not regulated in some form by State law that perhaps the Federal Government then under some very restricted provisions could come in and make some suggested changes to the local act and if they are not complied with then perhaps it should then go into effect.

Senator BROOKE. Would you agree that if the Federal law was more stringent than the State law that the State law would have to be brought into compliance with the Federal law?

Mr. BATTAGLIA. I think, Senator Brooke, that that is a hypothetical question which I don't believe I'm in a position to answer at this time because it's a question of interpretation and enforcement.

As an example, in your bill you have a criminal penalty provision which is not found in our act. I think it's harsh and I think that a developer who fails to technically comply—the words are "those matters which should have been filed are not filed would be subject to a serious criminal penalty." I feel that the civil penalties create enough hardship for any developer who's put out of business because he hasn't complied.

I think the provisions dealing with updating your requirements every 6 months is going to put the small developer out of business. He will have to have a staff of certified accountants who will constantly have to be updating the financial data.

Senator BROOKE. I have been told your time is up. I have used some of it, but you will have an opportunity later. Thank you very kindly.

[Complete statement follows:]

STATEMENT OF ANTHONY S. BATTAGLIA

BEFORE THE COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS

Mr. Chairman,

I want to thank you for allowing me to participate in these important and timely hearings. My name is Anthony S. Battaglia, and I am developer and general counsel for the Floirda Condominium Developers Association.

In light of the leaps and bounds growth of our industry in recent years, and in view of the growing trend toward condominium living, regulation is not only necessary, but healthy. However, over legislative regulation can be fatal. Over legislative regulation can depress a market which is already deflated and drive developers out of the industry. At a time when housing costs and needs are up, and construction starts down, efforts should be made to aid and protect BOTH the developer and the consumer.

Florida has led the nation in both condominium trends and regulations since 1967. After three generations of condominium legislation, Florida DOES NOT HAVE A PAPER TIGER Condominium Law. A careful analysis of the Florida Condominium Law as amended in 1975 will show that that law has more exacting requirements for prospectus disclosures than does the abstract called for in §6 of the Senate Bill. However, there are numerous disclosures required in the §6 abstract, but not in the Florida legislation. By no means does this make the Florida legislative effort defective or less protective for the consumer. On the contrary, there currently exists a multi-tier system of overseeing Florida condominium sales and practices. The Legislature has enacted laws requiring prospectus and disclosure materials be made available to every purchaser prior to every condominium sale.

The Florida Division of Land Sales and Condominiums requires filing by developers of key documents and advertising material. It reviews the material for deficiencies and non-disclosures, on much the same basis and with generally the same powers as are given to the Secretary under §12 of the Senate Bill. In addition, the industry has established self-regulating associations such as the Florida Condominium Developers Association, which effectively maintains a high degree of integrity and ethical standards in the industry.

All told, I feel the Florida effort surpasses contemporary attempts to protect the consumer. There reaches a point along the spectrum of consumer protection when the legislative attempt has a whiplash effect. I believe that maximum effectiveness in protection is currently being achieved in Florida today. Additional disclosures, statements and filings, only will mean additional cost. Costs which represent NO NEW PROTECTION, and only added expense for the developer. Added expense that will not be born by the developer, but passed on to the consumer. All the progress of the State to reach an equilibrium in protecting the consumer and providing a favorable atmosphere for nurturing such an economic and environmentally sound industry would be for naught, however, if this Bill were passed in its present form, or any form.

In an effort to comply with §7(2) of the proposed Bill, and achieve State authority and responsibility for its enforcement, the Florida Division of Land Sales would extend its regulation to extract those disclosures not presently required under the Florida Laws, such as §6(a) (6) and §6(a) (7). This means making additional disclosures, the costs of which would be borne by the consumer. It could also mean complying with

such unnecessary requirements as §5(a) (C) which would render an entire project non-profitable for the small developer who would be required to retain a permanent team of certified accountants to comply with the additional disclosures. The small developer, who constitutes 70% of the construction industry would be effectively eliminated. The result? Elimination of the small developer, added cost to the consumer and no greater protection than what existed before.

In conclusion, the industry and the State have done an effective job of self regulation. National legislation can provide no additional protection and only expose the consumer to greater expenses, and place undue burdens on an industry which is already struggling to stay alive.

Senator BROOKE. Mr. Wolcott.

STATEMENT OF HUNTER W. WOLCOTT, ON BEHALF OF THE FLORIDA HOME BUILDERS ASSOCIATION

Mr. WOLCOTT. Thank you, Senator Brooke.

I am Hunter Wolcott. I'm with the mortgage banking and realty companies of the KISLAK organization and I appear today on behalf of the Florida Home Builders Association. I appeared before this committee last year at this time and testified in strenuous opposition to the bills that you, Senator Biden, and Senator Proxmire offered, but I recognize that this bill has some significant and beneficial changes in it and I would say that our position is generally supportive of some concepts embodied in this legislation.

Specifically, we recognize, as you do, that condominium documents even to the most studious professional can be very difficult to understand. We therefore fully support the national standards for disclosure in S. 2273.

We feel that low-balling and the sweetheart contract, while they do exist, are nothing more than deceptive trade practices and we would hope that existing legislation, particularly through the Federal Trade Commission, could be enforced to stop these kinds of abusive practices.

There's also no doubt that recreation leases have been abused.

However, to ban recreation leases entirely, which includes those legitimate uses as a financing tool, means that the entire burden of financing improvements in planned unit developments and condominium communities will have to be borne up front by the purchaser.

We also support the provision of S. 2273 that any deposit or downpayment be held in trust or escrow.

We are astonished and pleased that the study recently by the Secretary of HUD reveals such a high level of satisfaction among condominium owners.

Like you, Senator Brooke, and Mrs. O'Connell who just spoke, I also live in a condominium. I live in a converted condominium and I lease from the owner of that converted condominium who can't sell his units so I think we can speak on both sides of that issue. I have to say I'm one of the 5 percent, also.

I think that your requirement in the bill that the affairs of the condominium association be turned over within the first year of its formation is an unworkable provision and I think in addition to the comments that Mr. Dowden made earlier that it would place a disproportionate burden upon the developer if he had to make full maintenance payments while the bulk of his condominium development was standing open.

Surprisingly, I find one of the major objections to condominium ownership has not been treated before this committee. That objection is the general weakness of the resale market. We are here to restore confidence in the condominium market and this is one of the major areas that I think has been ignored. The Federal Government has devoted enormous time, effort, and expense in providing for the uniformity of financing provisions for single family housing, but has done little or nothing for condominium financing.

Because of this failure on the part of Congress there's a growing tendency for condominium owners to become landlords because they can't sell their units. This was brought out in testimony last year, that the abuses of this uncontrolled group of landlords can't realistically be controlled by existing legislation because the number of units they own is below certain minimums.

I think that all of us realize that in order to restore confidence to the condominium industry, and confidence is the only answer to condominium depression, that some kind of uniformity of disclosure is going to be required throughout the Nation. We fully support that.

I am pleased to see that the high level of confidence throughout the country has been achieved without direct Federal intervention. I am displeased to find that my contention last year that the States have taken an eager and aggressive position in controlling condominium abuses has been in error. When I checked my statement, last year versus my statement this year, I find that there has been little or no progress on the part of States. Florida, certainly, the State that I reside in, has a stringent consumer protection statute. 45 States do not, and I think that that quite rightly is your concern.

Senator BROOKE. If you remember, I introduced this legislation last year and you opposed it and you came forth with that statement.

Mr. WOLCOTT. Yes, I did, sir, and that's why I would like to go on the record as saying I'm afraid I was in error.

Senator BROOKE. That's one of the reasons we're back this year.

Mr. WOLCOTT. Quite right, sir.

In summary, we would like to see the concepts of Senate 2273 embodied in the law of the land. We are not sure that Federal intervention is the proper route, but if it is the considered opinion of this committee that it is the only available alternative, it would be the position of the Florida Home Builders Association that we would support disclosure legislation.

Senator BROOKE. Thank you very much.

[Complete statement follows:]

STATEMENT OF HUNTER W. WOLCOTT

I am pleased to take this opportunity on behalf of the Florida Home Builders Association to make my statement to the Subcommittee on Housing and Urban Affairs of the United States Senate on Senate Bill 2273, The Condominium Consumer Protection Act of 1975.

INTRODUCTORY

I appeared before this Committee in October of 1974 and testified in opposition to Senate Bills 3658 and 4047, respectively the "Condominium Disclosure Act", and the "Condominium Act of 1974." The objections of our Association to these two pieces of legislation were strenuous and focused primarily upon the following areas:

1. We were concerned that the propriety, responsibility and necessity of federal government intervention in and regulation of essentially local trade practices had not been clearly demonstrated.

2. We felt that Senate Bills 3658 and 4047, as presented, would create a bureaucratic monstrosity, generate hastily conceived procedures, produce costs beyond immediate estimation, and would result in delays and confusion in the industry which could only have a deleterious effect contrary to the good intent of the bills.

We recognize that this new piece of legislation proposed by Senators Proxmire, Brooke and Biden contains some significant and beneficial changes, and it is to this revised legislative concept that we would like to direct our comments.

THE CONDOMINIUM APPEAL

I think all of us here realize that the trend toward condominium development is one which has not yet seen its crest, and which may not for some years to come.

The report released recently by the U. S. Department of Housing and Urban Development predicts that condominium living is likely to become even more popular in the future. Its contents reveal that the number of condominiums has increased twenty fold since 1970, and that almost a quarter of all newly constructed housing units this year are being sold as condominium units.

Senator Proxmire in his Statement of Introduction of this Bill to the Senate quite appropriately called attention to some of the economic factors which are fueling the condominium boom. The housing industry has been battered by disproportionate inflationary pressures resulting, in large part, from the lack of evolution in the traditional credit markets and the increasing scarcity of buildable land near urban employment centers. Compounding this problem, many urban areas are deliberately restricting the amount of land they make available for residential uses and are artificially limiting the growth of their communities, again increasing the cost of home ownership and driving more and more families into high density developments.

Condominiums, as a legal concept of home ownership and as a fact of economic life, are here to stay.

The good Senator from Wisconsin also brings to light another, often hidden, factor in the trend toward condominium development: Governmental shortsightedness is driving private capital away from the rental housing markets.

Although rent control is an area the federal government has quite prudently stayed away from, many local governmental bodies have chosen to take a more aggressive route and have turned landlords' profit margins into financial horror stories. In some areas utility costs have tripled and the costs of maintenance have risen more rapidly than the rental increases local politicians have found it prudent to permit. In addition, the Congress, in such areas as its drive to limit artificial accounting losses, and in its reluctance to support rental housing financing programs, seems to be discouraging long term investment in housing. The Congressional prediction that increasing numbers of American families will be driven toward condominium ownership as their last resort becomes, therefore, self-fulfilling.

CONDOMINIUM ABUSES

At this time last year, Senator Biden expressed his hopes that the one year period this Committee saw fit to invest in the study of the condominium situation would not be a year in which tens of thousands of home owners were "ripped off."

Fortunately, the Housing and Urban Development study referred to earlier indicates that the overwhelming majority of condominium owners surveyed claim to be either "satisfied" or"very satisfied" with their units. As a trade association we are naturally gratified to hear those results. That does not mean, however, that we are satisfied that consumer confidence in this type of ownership has been restored. I don't propose to be able to sit here and tell this Committee about the consumer problems in the industry. You hear them all the time and we do, too. So long as there is free enterprise and a public to be preyed upon there will be those rip-off

operators who make their living just doing that.

We recognize, as you do, that the condominium business is a little different from any other business. Condominium documents can run hundreds of pages long and the most studious professional sometimes finds it difficult to piece together their real meaning. We therefore fully support the "National Standards for Disclosure" in Senate Bill 2273.

"Low balling" and the so-called "sweetheart contract" are nothing more than deceptive trade practices, and existing legislation should be enforced to stop this abuse in this industry just as you would in any other industry. There is also no doubt that recreation leases have been abused to an unconscionable extent. I don't think we should overlook, however, the fact that a responsibly executed recreational lease can amount to developer financing of recreational facilities and, if offered properly, results in immediate benefits to the condominium purchaser by way of a lower sales price. It seems that there are ways to regulate the rate of return on recreation and maintenance leases just as you would regulate the rate of return on any other capital investment, i.e., by enforcement of usury laws. To ban recreation leases entirely, which includes all those legitimate uses of recreation leases means that the entire burden of financing improvements in planned unit developments and condominium communities will have to be borne, up front, by the purchaser. I am not sure that is really the intent of this Committee.

Like you, I have heard of the tragedy of the retired couples who put up sums, which sometimes amount to their life savings, as condominium purchase deposits only to lose them and be left without a home or savings because developers go broke. Because I see no other feasible way of

preventing this type of abuse, I also support the provision in S.B. 2273 that any deposit or down payment be held in trust or in escrow.

We also recognize that the condominium conversion has done great damage when utilized by unscrupulous developers, and we support the provisions of the National Standard for Consumer Protection, Section 5, paragraph 7, which you offer.

PLANNING THE FUTURE

The study released by the U. S. Department of Housing and Urban Development recognizes, as we all have, that the problems dealing with shoddy construction and deceptive sales practices are being brought under control, and that the quality of life within condominium communities is generally on the rise.

The economic pressures of the open market and increased public awareness of the problems and considerations attendant to condominium ownership, and sincere efforts on the part of the State, local and federal government agencies in barring unfair and deceptive trade practices have been major factors in this improvement.

The HUD study feels, however, that the "communal aspects of condominium living will surface as the most acute problem facing owners in the future." I think that it would be shortsighted of this Committee not to recognize this problem now. As with the problems presented the condominium owner by runaway maintenance costs, shoddy construction and mishandled management, these future abuses will be the result of the lack of competence . While I certainly recognize that you cannot legislate good business practices, you can encourage local bodies, as you have quite rightly done in this Bill in other areas,

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to promote, foster and encourage the development of governmental skills within condominium communities where they are so desperately needed. It may not be the appropriate measure, however, to thrust the full responsibility for this management upon what conceivably could be but a handful of owners within one year after the formation of the condominium association. These residents are likely to have no more, and probably much less, competence in the affairs of multi-million dollar apartment management than the builder. In addition, some associations will show a tendency toward "blackmailing" the developer, by threatened resistance, into providing amenities for which he had not bargained. Your requirement that the affairs of the association, including its budget, be turned over to the owners who are present at the end of the first year could also place a disproportionate financial burden upon the developer. It is conceivable that a project of, say, one hundred units, if they were not moving well could only have 10 or 20 per cent occupancy at the end of one year. If the developer had to bear all of the obligations of making the monthly maintenance payments to the condominium association, he would find himself at an unfair economic disadvantage. With only 10 to 20 per cent of unit owners in residence the maintenance cost would not be nearly so high as that which was budgeted and the developer by making full maintenance payments on vacant units will only be providing a windfall surplus to the association. Like any responsible business man he is going to attempt to recoup this unexpected loss with increases in sales prices to successive unit purchasers. I doubt that this was the intent of the Committee.

As a suggestion, I would like to see this Committee consider the type of schedule for turnover of tenant control that the State of Florida utilizes wherein certain minimum standards for transfer and control are

established with varying levels of occupancy and elapsed time from the formation of the association.

The developer should also be afforded the opportunity, within his documents, to be obligated to provide only deficit financing for the condominium association thus avoiding the potential problem of an unforeseen, and taxable, cash surplus in the association accounts.

Surprisingly, I find that one of the major objections to condominium ownership has rarely been treated in either the testimony or the legislative findings of this Committee. That major objection is the general weakness of the resale market for condominium units. The federal government has devoted an enormous amount of time, effort and expense in providing for uniformity of federal support for single family housing finance, but has given the area of condominium finance almost no attention whatsoever. The FHA 234 program is, at least in the eyes of the condominium developer a dismal failure. The VA was recently given the right to approve condominium developments on their own for no down payment financing. But as I sit here today, I am afraid that I must report that proof of their willingness to support the condominium market, either in new construction or in resales, have not been self-evident. In Florida for example, the VA has assigned just one man for review of 7,500 unit applications in 68 projects. I feel that the federal government, and this Committee in particular, should anticipate this major area of complaint which will be forthcoming in the future and press hard for legislation which will place the resale and initial financing of condominium units on an equal basis with that of other types of housing. Failure to do so will only invite additional, more innovative, forms of abuse which will be visited upon condominium owners attempting to resell. An obvious example of this kind of abuse, which cannot be effectively legislated against, is the growing tendency for condominium owners to become

landlords because there is no active resale market for their units. Where they own but one or two or so units these landlords fall through the cracks of most landlord/tenant laws. A large, uncontrollable group of unskilled lessors could, and probably will, abuse their rights and neglect their responsibilities as landlords. This point was brought out in testimony before the Committee last year, and unless we do something about it we all are going to be sitting here next year wondering why all these abuses exist. Stimulation of the resale market and establishment of uniformity in condominium financing is the surest way to provide for effective protection.

In this case, and hopefully in other cases like this in the future, I would like to see our industry work with you to head off problems before they arrive rather than dragging our feet on legislation when it is proposed.

THE CASE FOR FEDERAL REGULATION

I think that all the rational men in our industry recognize that it is essential that we curb the abuses that have plagued the condominium industry if we are to continue to provide for the changing housing needs of our Nation. Despite the abuses, the "ripoffs", the frauds and misunderstandings which have accompanied condominium sales in the past, the concept meets a need and the industry flourishes. I use the word "flourish" consciously because there are those who might contend that the condominium industry has, in fact, festered. An astonishing 96% of condominium owners are satisfied with their units according to the HUD study. This level of satisfaction was achieved without direct federal intervention in the industry, and I would risk the prediction that that level of confidence, if accurate, would compare favorably with that of any other industry.

Last year when I was here I said that many states had shown a

willingness and eagerness to enact consumer protection statutes in addition to their basic enabling statues to meet the problems of mushrooming condominium development. Sadly, I find that my contention may have been in error. I see that only five states have enacted statutes which could be considered strong consumer protection legislation.

The findings of this Committee and of its members that condominiums are a national phenomenon which can be expected to grow are not inconsistent with our observations, and there is no question that the differences in State laws do in fact, work a hardship on developer and purchaser alike.

We objected to last year's Bills on the grounds that a complex federal bureaucracy would be required to enforce its provisions. The Bill currently before you does not provide for this bureaucracy but does place a thin, hopefully resilient film of continuity at the federal level across the condominium industry. All too many times in the past, however, we have found that this resilient film can develop an incredible rigidity as it matures. You have recognized time and time again that our various state legislatures possess the requisite knowledge, skill, interest, and willingness to protect their residents from intra or interstate condominium abuses. Unfortunately for all of us, however, they have not done so.

In a move that probably will, (but should not), surprise you, I wholeheartedly endorse substantially all of the concepts contained in S.B. 2273. I say this not only individually but as the representative of the Florida Home Builders Association. I am somewhat disappointed, though, that the only means that this vast federal government has seen fit to consider to motivate our various state legislatures is the passage of a new federal law. The regulation of real estate transactions is an area to which our state legislatures are uniquely adapted.

We are deeply and unalterably opposed to the concept that two levels of legislation are better than one.

Federally supervised lenders are the lifeblood of most of the housing industry. State legislatures should have a deep, abiding concern for the welfare of their constituency. The National Conference of Commissioners on Uniform State Laws has as a project the drafting of a model condominium statute which would clear many of our current problems. And yet, with all of these legislative and regulatory resources at our disposal, can we come up with no better way of controlling highly visible abuses than by creating a new chapter in the federal law books?

An additional consideration is that the National Standards proposed in S.B. 2273 could be construed to be just minimum standards required for the protection of the public. You and I recognize that the standards set forth in this Bill are not minimal standards, but rather are quite comprehensive and even stringent standards for consumer protection. It should be clear that it would not be politically palatable for a locally elected official to deliver to his constituency only those minimum standards which he has to provide by federal law. It would seem much more appropriate to us to encourage local bodies to enact consumer protection statutes covering these abuses so that legislation could not only be tailored to meet individual regional requirements, but could also result in regulatory costs commensurate with the expected social benefit to the community.

The Office of Interstate Land Sales Registration currently supervises condominiums. The Federal Trade Commission has authority to control abuses which occur in sales practices in condominiums, and many states have so-called "little FTC" acts which guard against abuses. The free market has driven

many of the disreputable operators out of business and, unfortunately, many of the finest businessmen in our industry may follow. There is no doubt in my mind that S.B. 2273 is a good bill and will prove effective in controlling the type of abuses cited. We object to several of the provisions contained in this proposed legislation and I have attempted in this statement to explain the reasons for our opposition.

We would like to see the concepts embodied in S.B. 2273 become the law of the land. We are not convinced, however, that the enactment of federal legislation of this type is the only, or even indeed the best, way of treating the symptoms of condominium abuse.

SUMMARY

This Committee has made an exhaustive study of the types and frequency of abuses which have occurred in the condominium industry. It has attempted, and we think in a creative way, to treat some of the symptoms of this condominium abuse in S.B. 2273. With a few minor exceptions which are noted above, the Florida Home Builders Association wholeheartedly endorses the concepts embraced by this legislation. We feel that the eradication of the stigma that attaches to the condominium industry is essential if we are to meet America's growing and evolving housing needs.

If the Senate Committee on Banking, Housing, and Urban Affairs truly believes that it has exhausted all other available alternatives and sources to treat the condominium malaise which affects our industry, then the Florida Home Builders Association, in spite of our deep constitutional and philosophical objections to additional federal regulation of local transactions, would support the adoption of this Bill with the revisions that are indicated.

We thank you sincerely for your consideration of our point of view.

ARTICLE XVII: The condominium developer, as far as is practical and as far as is allowable by the laws of the State and the Nation, shall attempt to see that no unfair advantage over apartment owners shall be taken by other persons who may be dealing with apartment owners.

ARTICLE XVIII: The condominium developer should conduct his business in order to avoid controversies with other fellow condominium developers. In the event a controversy arises between the members of this Association, it shall be the duty of the condominium developer to attempt to resolve those difficulties within the Association.

ARTICLE XVIV: In the event a condominium developer is charged with any unethical practice, it shall be his duty to place all pertinent facts before the proper ethical standards committee of this Association and thereafter, it shall be his duty to fully abide by the decision of that committee.

ARTICLE XX: The condominium developer should not disparage the business practices of any of his fellow condominium developers who may be in competition with him.

ARTICLE XXI: The condominium developer shall not solicit the services of an employee or salesman in the organization of a fellow condominium developer without the knowledge of that developer.

ARTICLE XXII: The members of this Association pledge themselves to be loyal to this Association and to the condominium industry throughout the State and the Nation.

CONCLUSION

The condominium developer has created a way of life which, in most instances, far exceeds the expectations of the persons living in the condominium development. It is clear that the condominium developers' contribution to our society is immeasurable. It shall be the duty of the members of this Association to continue to uphold and to set the highest possible standards for our profession.

3333 Pasadena Avenue South
St. Petersburg, Florida 33707
(813) 360-2711

FLORIDA CONDOMINIUM DEVELOPERS ASSOCIATION

CODE OF ETHICS

The Florida Condominium Developers Association has as its sole purpose the enrichment of condominium living. Its members, through the Association, are dedicated to promoting the interests and benefits of condominium living for residents and developers, for both, in this way, have chosen it as their way of life. For the developer, there is a challenge and the satisfaction of providing a way of life superior in many respects to all others; for the resident, it is the pleasure and comfort and security of living within such an environment. Together, in sincerity and openess, the developer and resident can still further support and enhance condominium living; it is to this end, that the Florida Condominium Developers Association has been established and has pledged its members to observe this Code of Ethics:

FLORIDA CONDOMINIUM DEVELOPERS ASSOCIATION

CODE OF ETHICS

ARTICLE I: The condominium developer shall keep himself informed on all matters which affect or may affect the condominium industry in his condominium development, in his community, in his State and in the Nation, so that he may be able to contribute to the thinking of other members of the condominium industry and of persons owning condominium apartments on matters of taxation, legislation, land use, city planning and zoning and other matters affecting condominium interests.

ARTICLE II: The condominium developer shall remain well informed as to building costs and as to current market conditions in order to be able to offer to the public the fairest price possible for the condominium apartment.

ARTICLE III: The condominium developer shall remain informed as to current costs and current market conditions in order to be able to offer to his condominium development the most inexpensive and best possible management and maintenance fees consistent with offering effecient and effective service.

ARTICLE IV: The condominium developer shall in all his business dealings, both with the public and with other condominium developers and with all his employees, attempt to protect the public against fraud, misrepresentation and unethical practices in the condominium industry.

ARTICLE V: It shall be the duty of the condominium developer to eliminate in his community any practices which would damage the condominium developers' image in the eyes of the public or would damage the dignity and the integrity of the condominium industry. It shall be the duty of each and every member of this Association to assist the Association in regulating the practices of all condominium developers who are members of this Association.

ARTICLE VI: It is the intention of the members of this Association to comply with all existing laws, rules, regulations and statutes which affect the buying and selling of condominium units to prospective purchasers.

ARTICLE VII: It shall be the duty of the condominium developer to maintain his development in a manner that will instill a pride of ownership in every condominium apartment owner living in that development.

ARTICLE VIII: The condominium developer in his advertising shall be careful to present a true and correct picture of the nature of the condominium development and he should, at all times, refrain from any false and misleading statement.

ARTICLE IX: The condominium developer shall at all times protect and promote the interests of all of the owners of condominium apartments in his condominium development.

ARTICLE X: The condominium developer shall endeavor to sell condominium apartments to persons who will add harmony to the entire condominium development.

ARTICLE XI: The condominium developers should give heed to resident complaints, recommending prompt solutions as appropriate if those complaints are valid.

ARTICLE XII: The condominium developer shall expressly and impliedly warrant the fitness of each and every condominium apartment he sells.

ARTICLE XIII: The condominium developer shall endeavor to provide authorized maintenance and management services to the owners of condominium apartments at the lowest cost consistent with a fair and reasonable compensation for services rendered.

ARTICLE XIV: If a dispute arises between a condominium developer and an apartment owner, the developer shall attempt, as far as practical within the bounds of justice and fairness to all, to resolve and/or arbitrate the dispute without the necessity of any legal action.

ARTICLE XV: The condominium developer shall cooperate with the Condominium Association in order to promote the best interests of the Association and the apartment owners who are members of that Association.

ARTICLE XVI: The condominium developer or a duly authorized representative shall cooperate with the Florida Condominium Developers Association with respect to resolving any disputes that may arise between Association and the developer.

Senator BROOKE. Mr. Johnakin.

STATEMENT OF STEPHEN G. JOHNAKIN, LAWYERS TITLE INSURANCE CORP.

Mr. JOHNAKIN. Senator, the substantive provisions of this bill are based entirely on the Virginia Condominium Act of 1974, and I would like to supplement my written statement by giving you some background about how we got to where we are now in Virginia.

In 1962, Virginia became the second State in the country to adopt a condominium statute, right after Hawaii. All the States adopted condominium legislation between 1961 and 1968, and this first generation of condominium statutes was characterized by two very fundamental deficiencies. Virginia's act was no exception.

First, these early statutes imposed certain artificial and unreasonable restraints on the inherent flexibility of the condominium concept. The early statutes were really designed for single-structure high-rise residential condominiums, and this preconceived legislative stereotype of what a condominium ought to be made it difficult for developers to be really innovative in meeting the public demand for other types of condominium projects.

The second basic deficiency in the first generation of condominium statutes was the absence of adequate legislative safeguards to protect prospective purchasers of condominium units. I believe in a free market economy, but the free market works best only when consumers are able to make informed choices. With a new form of ownership like condominiums, I agree that it's necessary at a minimum to assure that prospective purchasers will have access to comprehensive information about what is entailed in their proposed purchase.

In 1973, the Virginia General Assembly decided to do something about those two basic problems. It directed the Virginia Real Estate Commission to appoint a condominium study committee comprising representatives of mortgage lenders, title insurers, builder-developers, and the public at large. I served as counsel to that study committee.

After a year of hard work, including public hearings throughout the State of Virginia, the study committee submitted a report to the general assembly recommending enactment of a wholly new condominium statute, the Virginia Condominium Act of 1974.

Not one single interest group in Virginia opposed that new legislation. The consumer groups applauded it because it vastly enhanced the protections afforded unit purchasers against the abuses that we are all familiar with. Tenant groups in northern Virginia endorsed it because it protected the rights of tenants in rental projects slated for conversion to condominiums. Developers liked it because it unleashed the inherent flexibility of the condominium concept providing a sound legal framework for any type of condominium the public might want. Mortgage lenders and title insurers supported it because it eliminated the legal pitfalls that arose when innovative developers proposed types of condominiums that did not conform to the stereotype on which those first-generation statutes were based.

The drafters of this Senate bill are, I am sure, thoroughly familiar with the Virginia Condominium Act of 1974, because they copied it. Every substantive protection in this bill, and the whole scheme of full disclosure to prospective purchasers, is based on one section or another of the Virginia Condominium Act. Nothing new has been added. The only thing that the drafters of this bill have done is make some of the restrictions even more restrictive.

The restrictions in the Virginia Condominium Act represented delicately negotiated compromises to which all affected interested groups were parties and to which all those interested groups concurred. The Virginia General Assembly ultimately formulated a statute that provided the maximum degree of purchaser protection compatible with fostering rather than chilling condominium development. The Virginia Condominium Act has been hailed as the model and forerunner of a second generation of new condominium legislation for the whole country. Other States have already begun to copy it. Georgia's act, based on Virginia's, went into effect this past October 1, just a few days ago.

The National Conference of Commissioners on Uniform State Laws has asked me and some of the other people who were instrumental in drafting the Virginia Act to develop a proposal for a uniform State Condominium Act on that basis.

Virginia, which certainly doesn't have the reputation for being the most progressive State in the Union, has shown that the States can do the job when the proponents of reform concentrate their efforts on the State level.

Here at the Federal level, I really think you're too far from both the people and the problems to have adequate input. Meanwhile, some of the States are imitating Virginia while others are trying their own approaches. Experimentation has just begun. More experimentation is needed in this novel realm. The genius of our Federal system is that the States can try different approaches to different problems, and the results are then susceptible to the kind of comparative analysis that simply isn't possible when a straitjacket of uniform Federal regulations is imposed on the whole country.

My technical objections are summarized in the sheet that I already gave you, together with my comments on this bill in general, and I look forward to questions.

Senator BROOKE. Thank you. I want to commend Virginia for what it has done in this area. We did consult with Virginia, but we also consulted with other States as well, and I don't think it's quite accurate—and I'd like the record to show—that we didn't copy verbatim the Virginia law. We drew from the best of many States. We looked at the Florida law as well as Virginia, but I do want to certainly pay respect to Virginia. It has been progressive in this field, and we are grateful for your testimony.

[Complete statement follows:]

COMMENTS ON S. 2273

by Stephen G. Johnakin

Lawyers Title Insurance Corporation

I appreciate this opportunity to speak in opposition to Senate Bill 2273 on behalf of Lawyers Title Insurance Corporation. I support the cause of purchaser protection in the condominium realm, and so do my colleagues in the land title industry. But we oppose any scheme for federal regulation of condominiums, because we think the states can do a better job.

In my own state, Virginia, we have already adopted and implemented a system of purchaser protection far more comprehensive and far more sophisticated than any proposal originating at the federal level. Indeed, the substantive protections in Senate Bill 2273 are based entirely on parallel provisions in the Virginia Condominium Act of 1974. Even our mistakes have been repeated! We tried to correct those mistakes in Virginia with a series of amendments enacted this past spring, but apparently the authors of this Senate Bill were working without the benefit of those amendments.

Virginia did not have to be prodded by federal legislation before acting to protect the condominium purchaser. On the contrary, it was the Virginia statute that the framers of this Senate Bill have drawn upon in formulating their proposals for a federal condominium act. But it was never intended by the drafters of the Virginia act that their plan for consumer protection should be

imposed by force on other states. Rather, it was our hope that we would have the opportunity to compare our experience under the Virginia plan with the experience of other states working under their own plans.

Now, in the guise of setting "minimum standards" for purchaser protection, the proponents of S. 2273 want to impose a straitjacket of federal controls on every state in the Union. Even Virginia will get a rap on the knuckles. In some areas our regulations are not as "strict" as those set forth in the Bill. As a result, the Secretary of Housing and Urban Development would have the power to "disapprove" the purchaser protection plan of our Condominium Act and to substitute the standards of this Bill in lieu thereof. It is certainly a slap in the face to those of us who worked so long and hard on the Virginia Condominium Act. Our standards represent delicately negotiated compromises worked out over a long period of time by people who had considerable expertise in the condominium realm and who actively solicited and sought out comments from all quarters even before drafting their own proposals. Now the draftsmen of this Bill are attempting to substitute their judgment of those who drafted the very act upon which this Bill is based. And Virginia, like every other state in the nation, would be forced to either meekly acquiesce in the new federal scheme or else see its own purchaser protection plan swept aside.

The justification that will no doubt be adduced for federal intervention is that the states--most states, anyhow--have not done

an adequate job. But other states could do just as effective a job as Virginia has done, if they chose to. Surely, it would be far better if each state set its own standards in the light of its own experience with its own problems. The federal government could surely perform a very useful function by providing a clearinghouse of information on different approaches used by different states and their experiences with those approaches. Reformers at the state level need that kind of information, and they would eagerly seek it out if the federal government were prepared to furnish it through the Department of Housing and Urban Development. But the federal government, while it might recommend "minimum standards" for purchaser protection, simply is not competent to prescribe such standards by law. At the federal level you are too far removed from both the problems and the people, and it is vitally important that lawmakers be close to both in a novel realm like this.

We in Virginia have shown how people at the state level can be more responsive to the problems and faster with the solutions. Virginia certainly does not have the reputation of being the most progressive state in the nation, yet Virginia is way out in front in the realm of condominium purchaser protection. If Virginia can do it, other states can do it. Many have already begun. If you want to kill the reform movement at the state level, there is no better way to do it than by passing a law like this in order to let the reformers know that in the final analysis Washington D. C. will be calling the shots, that federal bureaucrats will have to

review and approve state plans, and that anyone who disagrees with the minimum standards dreamed up by the proponents of this Bill will have to trek to Washington instead of their own state capitols if they want their views to be heard.

It is not the particular provisions of this Bill that I and my colleagues in the land title industry oppose. Ross Lloyd, the Virginia Condominium Administrator who testified here Monday, submitted to you a written list of the technical problems in the Bill arising from faulty draftsmanship, and I concur with his comments. But I think this whole enterprise is a mistake, and I would rather see the abandonment of this Bill than any attempt to repair it. I just do not think it makes any sense at this relatively early stage to take a statute drawn up by Virginians in the light of Virginia's experience and addressed to Virginia's problems, and to impose that statute by force on every state in the country. Give the other states time to come up with their own plans. Some of them already have. There has as yet been no study of the relative effectiveness of different purchaser protection plans. It is foolish to proceed as though we knew all the answers when there is still such a dearth of empirical data. We should avoid any restraint on the freedom of the states to experiment at a time when valuable experimentation has just begun and more is needed.

The genius of our federal system is that the states may undertake a variety of approaches and learn from one another's experience. Imposing strict minimum standards at the federal level would

render impossible the kind of comparative analysis than can only be undertaken when the states are free to explore alternative approaches. Even if some of the technical flaws in S. 2273 were cured, passage of the Bill would still leave the states with only the crumbs of federalism.

TECHNICAL DEFECTS IN S. 2273

by Stephen G. Johnakin

Lawyers Title Insurance Corporation

1. Section 2(12). The definition of developer is so broad as to include anyone who buys two or more units and then attempts to resell them. This is clearly unintentional.

2. Section 2(15) and (16). The definitions of purchaser and offer are so broad that it would be technically unlawful for a developer to advertise a condominium in a newspaper unless each newspaper was supplemented by an insert containing all the disclosures required by Section 6. A similar problem existed in the 1974 Virginia Condominium Act until eliminated by the 1975 amendments.

3. Section 4(b). If a right of rescission is to be provided, the statute should indicate how the purchaser may give notice of his election to exercise that right. Also, in an act merely laying down "minimum" standards for consumer protection, extending the right of rescission to fifteen days from the ten days allowed by the Virginia Condominium Act is unwarranted.

4. Section 5(2). This provision would prohibit the developer of a fee simple condominium from including a leasehold interest in recreational or other lands owned by him as a part of the common elements, even if the unit owners approved of such an arrangement. Why?

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5. Section 5(3). In a statute specifying "minimum" standards for purchaser protection, a one-year time limit on the period of developer control is absolutely unreasonable and unwarranted. There is no evidence whatsoever that longer periods of developer control cause any harm whatsoever so long as other safeguards are present. The Virginia Condominium Act imposes different limits depending upon how the project is structured, ranging from two years (in the case of a condominium fully complete at the time of the recordation of the condominium instruments) up to five years (in the case of an "expandable" condominium to which additional land and units might be added later on). A time limit as short as one year would effectively rule out development of any but the very smallest condominiums.

6. Section 5(4). In the case of bona fide agreements which are not self-dealing and which are commercially reasonable under the circumstances, the developer should be allowed to contract on behalf of the unit owners' association where it is necessary to do so to secure some benefit. A good example is a highrise residential condominium with commercial units on the first floor which are to be owned and leased out by the unit owners' association. No prospective commercial tenant would be willing to take a lease on such a unit knowing if the lease could be disavowed within a year or so by the unit owners' association. Other examples can easily be adduced.

7. Section 5(7). What empirical studies did the drafters

of this Bill consult before deciding that tenants in conversion condominiums need a minimum of 120 days advance notice to vacate? The only empirical study with which I am familiar indicated that 60 to 90 days is enough. In Virginia, a compromise was effected after lengthy negotiations providing for a minimum of 90 days notice.

8. Section 6(a)(7). No financially responsible engineer who has the benefit of competent legal counsel will expose himself to the danger of being sued (along with the developer) by any unit owner who might allege negligence in the preparation of the statement required by this subsection. The statement should come from the developer only, although the developer himself should base his statement on an engineer's report. An "independent" engineer should not be required unless there is some reason to believe that engineers who work for a salary are inclined to be less honest than those who work for a fee.

9. Section 7(b)(3). It is somewhat ironic that the Virginia Condominium Act, which the drafters of this Bill copied in preparing the proposed substantive regulations, would be "disapproved" by the Secretary of HUD under the so-called "minimum" standards of this Bill. Moreover, such disapproval would extend to <u>all</u> of the Virginia Condominium Act, since the Secretary is not given the power to confine disapproval to specific items. Thus, Virginia would go from having the <u>best</u> condominium statute in the country

to having no condominium statute at all until and unless the Virginia General Assembly agreed to kowtow toward Washington and conform its statute to the federal standards. That would be Virginia's thanks for formulating and enacting the statute upon which this Bill is based.

Senator BROOKE. Now, last but not least, from my own State of Massachusetts, which is a progressive State, Mr. Jackson Walter.

STATEMENT OF J. JACKSON WALTER, WALTER & SONNENSCHEIN, BOSTON, MASS.

Mr. WALTER. Thank you, Senator Brooke. I guess I'm one of the 5 percent, too. Today is a good day to make the line, "We're last in condominiums but first in the American League."

Senator BROOKE. After next week, we will be the World Series champions.

Mr. WALTER. Indeed. I am Jackson Walter, an attorney with offices in Boston and Amherst.

I have drafted a good many documents under the Northeast Statutes that Senator Biden spoke about earlier. My comments with respect to this bill stem from the work I have done on the subject matter of governance of condominium associations and in many ways support some of the remarks made earlier by the CAI group. My comments have just been published in the Real Estate Law Journal, and I don't particularly feel like going back over them. They appear in the record, and I think they are clear enough.

I would like, however, to emphasize one point that I have tried to make and, although it's not exactly subject to S. 2273, it seems as if it's a point worth thinking about as we begin to try to rationalize and standardize and buttress the statutes under the whole notion of condominium as real property; I refer expressly to the voting rights of owners of condominium units.

I'd like to argue that the entire voting scheme within a condominium association may be unconstitutional, citing a case called *Stewart* v. *Parish School Board* (Louisiana)—the notion here would be that the franchise within a condominium association is with a very few exceptions—I note Georgia and possibly Arizona—the franchise is distributed unequally among the units in proportion as the value of any one unit bears to the aggregate value of all of the units in the regime.

This is a scheme that weights voting directly proportional to the worth of a unit. The Federal district court in the eastern district of Louisiana considered exactly this same situation in a voting arrangement with respect to a school bond issue and, in a very thoughtful opinion by Judge Wisdom, struck down that voting arrangement on the basis of violation of the equal protection clause of the 14th amendment.

Since condominiums are a kind of property that exist solely by virtue of legislation and since with very few exceptions weighted voting is a mandatory feature of compliance with the statute and not a discretionary thing left to the developers, it would seem to me that even a simple sort of reading of the case law in State action cases would suggest that condominium is vested with a full measure of State action and if that follows, then it would seem to follow that *Stewart* is applicable to an analysis of the voting rights of unit owners and that those provisions of the statute presumably would fall.

Senator BROOKE. Do you have citations on that?

Mr. WALTER. I do. It's provided in my testimony, Senator.

I had other points to make but they are set forth in my testimony; for the moment I would simply like to emphasize that it seems to me that, as the HUD study shows, if the most vulnerable single portion of condominium regimes in the long run is going to be the efficiency of operation of the owners association and if we're now looking forward to a time at which perhaps condominiums is a kind of an ownership which could speak not only to upper middle class and very expensive units but, as has been argued in some of the literature that condominium is a way to open up some of the advantages for home ownership for lower-income people, then we really should look rather closely at the statutory form which in each case is the State enabling act.

If provisions of all or most of the State enabling acts are constitutionally unsound, then I think before we go a great deal further in creating these units we really should step back and realize that a great many—and I think this is the fundamental point that I make in my article—that a great many of the deficiencies and abuses that certainly are endemic and they have been cataloged here today in the condominium field flow not from greedy developers who rip off, or whatever phrase you want to use, but rather, from a problem of complying with the State law in the first place.

Thank you.

Senator BROOKE. Thank you very much.

[Complete statement follows:]

TESTIMONY WITH RESPECT TO

S.2273

"CONDOMINIUM CONSUMER PROTECTION ACT"

BEFORE THE

UNITED STATES SENATE

COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS

J. Jackson Walter
8 October 1975
Washington, D. C.

I am J. Jackson Walter, an attorney with offices in Boston and Amherst, Massachusetts, appearing here this morning on my own behalf. My comments with respect to S.2273 stem from my studies of condominium governance arrangements, that is, the processes of collective decision-making by which condominium unit owners govern themselves and the uses to which they devote their property. As I understand the positions taken relative to S.2273 by the major organizations in the housing industry, I will be discussing several items that have not been considered at length during these hearings. My work on condominium governance appears as a lead article in the Fall '75 issue of the Real Estate Law Journal, a copy of which article is attached to the text of my testimony.

As I read S.2273, the Condominium Consumer Protection Act, setting aside the inevitable and important quarrels over duration of warranties and timing of turnover-of-control clauses and enforcement techniques and so forth, I can find five bones that seem worth picking:

First, S.2273 rests upon the questionable assumption that a full disclosure law will cure abuses by condominium developers, when, in fact, the abuses are the all-but-necessary result of efforts by developers to comply with the various State condominium enabling acts.

> To a certain extent, Section 5 of S.2273 does address this topic -- but bear in mind that Section 5 is, in essence, a short-form national condominium act and not a full disclosure law at all. As discussed at Part II of my article, under the caption "Developer Paternalism", State condominium statutes require establishment of a condominium regime before units may be sold. S.2273 would in no way alter this system, by which a developer and his counsel must make countless decisions about the ways in which a new condominium regime will function long before any prospective unit owners appear on the scene, and even further in advance of when the new unit owners convene their first organizational meeting. There is no simple way to escape the fact that compliance with the State condominium statutes necessitates a decision-making process in which prospective unit owners go unrepresented. As discussed below, I believe the cure to this dilemma lies in the provisions by which the unit owners can amend the condominium documents once the developer has relinquished control over the owners association.

Second, S.2273 fails to capitalize on its best opportunity to assure full

and prompt control by unit owners over condominium regimes in that it treats the provisions for amending condominium documents as a disclosure issue under Section 6 and not as a consumer protection issue under Section 5.

The implication of Section 5-(3) of S.2273 is that once a developer loses control of an owners association, the unit owners will assume it and thereby gain the power to undo the stranglehold that the State condominium enabling acts authorize a developer to achieve over a condominium regime. I point out at Part I-(B) of my article, under the caption, "Developers at the Ballot Box", that this implication may be misleading. The general topic of transfers of control over condominium regimes becomes complicated by the fact that developers must be able to maintain enough control to complete a project in accordance with their governmental permits. Developers typically reserve effective power and control over condominium regimes to themselves in ways that would not be affected by Section 5-(3). S.2273 gives explicit recognition to the provisions for amending condominium documents only at Section 6-(a.8.F), which is a straightforward disclosure requirement. A better approach to this issue would revise Section 5 to provide that, once control over an owners association passes from a developer to the unit owners in accordance with Section 5-(3), condominium documents must enable a simple majority of the total voting power of the condominium to amend the condominium documents. Such a

change would reduce developer paternalism to a level more likely to result in a condominium regime run by and reflective of the needs and concerns of the unit owners who would, of course, be free to increase the percentage vote needed to amend the condominium documents thereafter.

Third, S.2273 does not lay to rest the possibility of long-term developer control in the context of a multi-phased condominium development program. The policy of Section 5-(3), which clearly favors a transfer of control over owners associations to unit owners as promptly as possible, could be thwarted by the ambiguities of the language of Section 5-(3) and section 6-(a,2). The former refers simply to the units in a condominium project, suggesting that the number of such units is fixed, while the latter considers possible expansions and mergers of condominium projects, thereby suggesting that the number of such units may be uncertain. Do the turnover-of-control provisions of Section 5-(3) refer to the units in an entire condominium project, in any one phase of a condominium project, in that portion of a condominium project for which occupancy permits have been issued, or is the phrase "condominium project" in Section 5-(3) to be read in some other way? Neither Section 5-(3) nor the disclosure requirement at Section 6-(a.2) nor the definition at Section 2-(2) offers a solution. As discussed at Part III of my article, under the caption "Setting Up Multiphase Projects", the multi-phase

condominium development project poses very thorny problems for the draftsman of condominium documents. Unless the timing of the turnover-of-control formula in Section 5-(3) can be made more precise, S.2273 will only increase the confusion.

Fourth, S.2273 remains silent with respect to other Federal full disclosure and consumer protection efforts more or less akin to this one, most especially the OILSR program regulating the sale of subdivided lands.

Senator Biden's remarks on S.2273, as they appear in the Congressional Record (S 14969, 1 August 1975), point clearly to two major and commendable points of departure by S.2273 from the OILSR program and from prior condominium consumer protection bills: enforcement by wronged purchasers, not by HUD, and regulation by the States, not by HUD. I would hope the OILSR program could be amended to incorporate these "new federalism" improvements. On the other hand, it is unclear to me why the scope of disclosure appropriate for a condominium project should be narrower than in the case of subdivided lands or why the number of units that triggers a condominium registration requirement should be fewer than the minimum number of lots for an OILSR filing. One of the major accomplishments of the OILSR program has been to curtail to some degree the multiple-filing burdens of the interstate seller of subdivided lands; the approach of S.2273 to this problem seems an excellent improvement, especially in light

of the $500 minimum recovery clause at Section 9-(b). Finally, I wonder whether approval by the Secretary of a State enforcement plan, pursuant to Section 7-(b.2), might not constitute a "major federal action" for the purposes of NEPA (National Environmental Policy Act of 1969, 42 USC § 4321 et seq.)?

Fifth, S.2273 does not recognize that the voting schemes required by State condominium enabling acts for all condominium regimes are susceptible to challenge on constitutional grounds.

I am contending that all present and future condominium regimes that comply with the present standards of State condominium statutes involve an unconstitutional voting arrangement. S.2273 does not seek to redress this situation, nor could it because the "one unit-one vote" scheme that should characterize voting by unit owners in a condominium regime would violate the mandatory weighted voting systems of the State laws. As discussed at Part I-(A) of my article, under the caption "The Question of Voting Rights", the basic statutory scheme for voting in a condominium regime distributes the franchise unequally among the units, in the same proportion as the fair value of a unit at the inception of the regime bears to the then aggregate value of all the units.

Stewart v. Parish School Board, 310 F. Supp 1172 (E.D.La., 1970), aff'd mem. 400 US 884(1970), concerned a Louisiana voting scheme for a local school bond referendum in which only property

taxpayers could vote and their votes were weighted in direct proportion to the amount of assessed property owned by each voter. This setup exactly parallels the statutory scheme for voting in condominium regimes. In finding that this arrangement "debases" the vote of small landowners and constitutes a violation of the Equal Protection Clause of the Fourteenth Amendment, the court -- in an opinion by Judge Wisdom -- concluded:

> "In terms of voting responsibly, there is no necessary correlation between the amount of an assessment and the degree of interest a taxpayer may have in a particular bond issue. ... The actual effect of gearing assessments to the vote is simply to dilute the participation of small landowners and to exaggerate the participation of large landowners, in violation of the one man, one vote canon."

Even the most mechanistic interpretation of the caselaw suggests that condominium, which is a kind of real property created by action of the State legislatures within the very recent past and recognized and protected by Federal law, is invested with a full measure of "state action". The choice to distribute the franchise unequally among the units was not left to developers' counsel but is required as a necessary condition of compliance with the enabling statutes. Stewart suggests that the condominium voting scheme, a system that weights votes according to value, must fail a challenge on

constitutional grounds. That S.2273 cannot remedy such an obvious defect in the underlying structure of all condominium regimes in no way diminishes the need to reform this system of housing on a sound and proper constitutional base.

S.2273 seems to be a useful first response to the findings of the HUD-commissioned Arthur D. Little, Inc., study on condominium housing, which study shows that the greatest potential problem related to the long-term viability of condominiums is the ability of the owners associations to function efficiently. I believe my testimony has several points that deserve serious review and that S.2273 should be revised accordingly. Thank you for the opportunity to submit this statement.

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PROFESSOR JEROME G. ROSE
Department of Urban Planning
Livingston College, Rutgers University
New Brunswick, New Jersey 08903

Condominium Government: How Should the Laws Be Changed?

J. JACKSON WALTER*

This article offers valuable insights to everyone involved with condominiums and interested in seeing that a balance between the interests of unit owners, title insurers, and host municipalities is achieved.

Condominium involves not only a statutory system of ownership but also a process of collective decision-making by unit owners concerning the uses they make of their property. The author here identifies deficiencies in the enabling statutes' treatment of the general issue of condominium governance. These deficiencies, he believes, are responsible for or conducive to most of the abuses presently singled out by consumer advocates for special federal protection. Several elements of a program of curative legislation are suggested.

How shall condominium unit owners govern themselves and the uses to which they devote their property? A rash of proposed consumer protection legislation suggests that whatever arrangements may exist, condominium regimes would work better and more equitably if prospective unit buyers were to receive some sort of full disclosure report prior to purchase.[1] But the premise of benign developer parternalism, which is fundamental to all condo-

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* J. Jackson Walter is a member of the Massachusetts Bar and author of "A Survey of Permits and Impact Statements Required for a PUD: A Memorandum," 3 Real Estate L.J. 215 (1975).

[1] Three major condominium consumer bills were introduced during the 93d Congress: H.R. 15071, the "National Condominium Act," introduced by Rep. Collins (D-Ill.); S. 3658, the "Condominium Disclosure Act," introduced by Sen. Biden (D-Del.); and S. 4047, the "Condominium Act of 1974," introduced by Sen. Proxmire (D-Wis.) and Sen. Brooke (R-Mass.).

Regular reports on consumer protection efforts in the condominium field have appeared in *The Condominium Report*, published monthly by Warren, Gorham & Lamont. Of particular interest: "Condominium associations join forces to lobby for consumer protection measures," 2 The Condominium Report No. 4, pp. 1-2 (May 1974).

The Federal Trade Commission presently is conducting an extensive

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minium enabling statutes,[2] itself leads to many of the abuses and ambiguities that are targets of consumer wrath.

The condominium form of ownership has been transformed into such an infinitely flexible and adaptable tool for development that the original criteria for an adequate statutory base may no longer suffice.[3] The framers of the Puerto Rico and FHA condominium laws[4] surely understood that they were establishing an ownership arrangement that had no architectural or design implications. But today's use of condominiums in industrial, medical, retail, and office facilities, as well as with clusters of detached single and low-rise multifamily housing, confounds initial expectations that condominium ownership would be an arrangement peculiarly appropriate to high-rise residential buildings.[5]

This critique of condominium legislation focuses on issues of governance and, especially, on three general statutory deficiencies that reflect the constantly increasing occasions of condominium ownership:

- ☐ The statutes incorporate a theory of voting by condominium unit owners that possesses at best marginal political or constitutional justification.
- ☐ The statutes require developers unilaterally to decide issues of utmost importance to future condominium unit owners.

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investigation of condominium abuses, 2 BNA Housing and Development Reporter 187 (July 29, 1974).

This article does not deal directly with the context of any of these or other consumer protection proposals and probes.

[2] This article intentionally blurs the distinctions between the condominium enabling acts of the several states in order to deal with the common ground. Though several minor inaccuracies doubtless will result, this approach permits an argument to be developed without undue qualifications and unnecessary footnotes.

[3] See Berger, "Condominium: Shelter on a Statutory Foundation," 63 Colum. L. Rev. 987 (1963).

[4] P.R. Laws Ann. Tit. 31, § 1291-1293K (Supp. 1972), "Horizontal Property Act," Housing Act of 1961, § 234, 12 U.S.C. § 1715Y.

[5] As indicated by its title, "Horizontal Property Act," the Puerto Rico statute envisaged high-rise structures divided horizontally into separate units, rather than into units separated by vertical planes. The Act specifies that it applies only to a project consisting of a "building" (in the singular) or "apartment house," and it repeatedly refers to each unit as an "apartment" occupying all or part of a floor.

- ☐ The statues remain silent, or are misleading, about the source of the thorniest legal drafting problem, namely, the multi-phase condominium project.

The Question of Voting Rights

A Sweeping Critique

The statutory scheme for voting in condominium regimes distributes the franchise unequally among the units, in the same proportion as the fair value of a unit at the creation of the regime bears to the then aggregate value of all the units.[6] This same percentage figure defines the portion of common charges to be assessed to a unit and the extent of a unit's ownership interest in the common elements of the condominium.[7] While an identity of interest between assessment and ownership is sound, no good and sufficient legal or political arguments exist to justify a statutory linkage between voting on the one hand and assessment and ownership on the other.

The condominium voting scheme would die a swift and certain death if ever subjected to the standards that control public elections.[8] Even two centuries ago, when courts were loath to intervene in such matters and when a man qualified himself to vote by owning property or paying state taxes,[9] all votes cast were counted equally. Quite recently, the courts have had occasion to affirm the concept of one man, one vote.

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[6] See Rohan & Reskin, *Condominium Law and Practice* § 7.02(1), n. 4 (1965) (cited hereafter as Rohan & Reskin). The mechanics of voting in a condominium regime have been the subject of recent litigation in New York, Fisher v. Board of Managers of Coachlight Square Condominium (Westchester County, N.Y., 1974).

[7] Rohan & Reskin, note 6 *supra.*

[8] No state currently has property qualifications for voting in general elections, XVIII Council of State Governments, *The Book of the States, 1968-69,* 30 (1968).

[9] As to the reluctance of courts to interfere in this matter, see Luther v. Borden, 7 How. 1 (1849). This is the fountainhead case on the "political question" issue, cited by Frankfurter, J., in his dissent to the opinion of the Supreme Court in Baker v. Carr, 369 U.S. 186, at 292 (1961).

Vermont, not one of the thirteen original states of the Union, was the first (in 1791) to have full manhood suffrage without any property test, although there was a requirement of one year's residence of "quiet and peaceable behavior." Porter, *A History of Suffrage in the U.S.* 3 (Univ. of Chicago, 1918).

Stewart v. Parish School Board[10] concerned a Louisiana voting scheme for a local school bond referendum in which only property taxpayers could vote and their votes were weighted in direct proportion to the amount of assessed property owned by each voter. This setup exactly parallels the statutory scheme for voting in condominium regimes. In finding that this arrangement "debases" the vote of small landowners and constitutes a violation of the Equal Protection Clause of the Fourteenth Amendment, the court—in an opinion by Judge Wisdom—concluded:

> "In terms of voting responsibly, there is no necessary correlation between the amount of an assessment and the degree of interest a taxpayer may have in a particular bond issue. . . . The actual effect of gearing assessments to the vote is simply to dilute the participation of small landowners and to exaggerate the participation of large landowners, in violation of the one man, one vote canon." [11]

What has *Stewart* to do with the voting rights of condominium unit owners? The obvious defense of the statutory scheme asserts that *Stewart* is irrelevant, that votes by unit owners are not cast at public elections, that the context is strictly one of private property, that the voting scheme itself is required by legislation, and that a link between voting and assessments and ownership is a just and equitable arrangement.

But is *Stewart*, in fact, irrelevant? Rather obviously, the case would be relevant in a situation subject to challenge and scrutiny on constitutional grounds. And such a situation could exist in the context of a discussion of condominium ownership. Let us look at the specific case of "condominium communities."

Advertisements for condominium communities boast of numerous attributes conventionally characterized as being "municipal"

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[10] Stewart v. Parish School Board, 310 F. Supp. 1172 (E.D. La. 1970), *aff'd mem.* 400 U.S. 884 (1970).

[11] A contrary opinion was reached by the Texas Supreme Court in the case of Montgomery Independent School District v. Martin, 464 S.W.2d 638 (1971), noted at 25 Sw. L.J. 633 (Oct. 1971). The Texas court held that although constitutional and statutory provisions in Texas restrict the right to vote in school board elections to real and personal property owners who have rendered their property for taxation, that class of persons is so all-inclusive as to constitute no violation of the equal protection guarantee. The Texas court in *Montgomery* distinguished *Stewart* on the grounds that *Stewart* was strictly a weighted voting case.

in nature: large tracts of land subject to private land-use covenants and restrictions (rather like private zoning); a variety of housing types, streets and sidewalks, water supply, sewage treatment and solid waste disposal services, security protection, parks and recreational facilities (all owned privately by the condominium owners association and financed by tax revenues or "common charges"); and elected governing bodies. They are just like any other town. The allusion, of course, is to *Marsh v. Alabama,*[12] where the Supreme Court, in an opinion by Justice Black, held that the company that owned the town of Chicksaw, Alabama, could not use a private property defense to wall out the First Amendment's guarantee of free speech.

The theory of *Marsh* was one of "functional equivalence":[13] The more "municipal" attributes a place has and the closer in function it resembles any other town, the more susceptible it should be to constitutional guarantees and standards. In the rather narrow case of condominium communities, which typically advertise that they come equipped with even more "municipal" amenities than most other towns, the functional equivalence test would seem easily to be met. On this reasoning and in this specific situation, *Stewart* does have direct relevance and the condominium voting arrangements should fail in a challenge to their constitutional validity.

In the more typical context of a single high-rise residential condominium, an argument against the statutory voting arrangement must veer to a different tack. The functional equivalence test of *Marsh* presumably could not be passed; a challenger must therefore direct his argument against the statutory voting arrangement itself. It seems important to state the matter simply: Every state legislature has enacted a scheme for voting by condominium unit owners that was found untenable in the context of a public election when challenged on constitutional grounds. Certainly, one may identify a full measure of state action in the process by which state legisla-

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[12] Marsh v. Alabama, 326 U.S. 501 (1946).

[13] Two recent First Amendment cases, involving suburban shopping centers, have reconsidered the *Marsh* test: Amalgamated Food Employees Union v. Logan Valley Plaza, 391 U.S. 308 (1968), and Lloyd Corp. v. Tanner, 407 U.S. 551 (1972). The cases seem to go in opposite directions and leave unresolved the future of a "functional equivalence" test. *Marsh,* however, has not been cast adrift.

tures created a new form of real property ownership.[14] Condominium is a creature of state laws.[15] The choice to distribute the franchise unequally among the units of a condominium regime has not been left to developers' counsel. It is required as a necessary condition of compliance with the enabling statutes. Once one has established that an action does constitute state action and does involve the kinds of special values that the Supreme Court has recognized as deserving of its protection, the question—in the instant situation—must be whether legislative approval of weighted voting is constitutional. *Stewart* settles this issue: It is not.

PROPOSAL: Enact, as a minimal legislative response, a "one unit, one vote" scheme while simultaneously permitting the identity of interest between assessment and ownership to remain intact.

Developers at the Ballot Box

Stopping short of a sweeping critique of the entire condominium voting scheme, one nonetheless may inquire into the voting rights of and reservations of power and control to developers following conveyance of the initial unit of a new condominium. The examples of condominium documents found in Rohan and Reskin[16] and other documents familiar to readers of this *Journal* contain such a wondrous assortment of turnover-of-control formulae and special voting setups for developers that one must quickly conclude that the statutes are ambiguous, presenting developers' counsel with but little pause or guidance. Consider only the following arrangements:

- ☐ Cumulative voting is allowed to a developer, who votes the unsold units, but not to unit purchasers.
- ☐ Purchasers vote once per unit as Class A members of the owners association, while a developer votes three times per unsold unit as Class B members of the same association.

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14 See Van Alstyne & Karst, "State Action," 14 Stan. L. Rev. 3 (Dec. 1961). The state action cases have involved chiefly desegregation situations, and the commentary on this case law is voluminous.

15 Rohan & Reskin, at Ch. 4, discusses "nonstatutory (common law) approaches to condominium" and finds them generally awkward but possible.

16 Rohan & Reskin, App. C.

- ☐ Although a developer loses voting control on a simple majority principle, he continues to designate all officers of an owners association until a much larger percentage of units has been sold.
- ☐ Variations on the above with staggered terms for officers of an owners association, so that even after control of voting has been relinquished, officers designated by a developer control for several more years.

Developers do need to protect themselves from attempts by initial unit owners to force changes in a development program that would cause violations of the terms and conditions of governmental permits and financing agreements.[17] The issue here, however, is not whether developer paternalism is a good thing nor how promptly control ought to be turned over to unit purchasers but, rather, whether the many favorable voting and control positions carved out for developers by their lawyers adequately comport with condominium enabling legislation.

A reasonably strict reading of the statutes suggests that they do not. The statutes do not authorize a special status for a developer following conveyance of the first unit and continuing until sellout. They do not sanction differences in voting power between unsold and sold units. Indeed, the statutes imply that a developer must lose control as soon as the voting power appurtenant to the unsold units, which he reasonably and properly may vote, equals less than one-half the total.

PROPOSAL: Amend the statutes to include explicit treatment of the voting power of unsold units, so that initial unit owners cannot be tyrannized by developers who resort to arcane and legally dubious techniques to protect their development programs.

Developer Paternalism

Condominium statutes require establishment of a condominium regime before units may be sold. Conventionally, this means that

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[17] With regard to one category of governmental permits that a developer of condominium communities will encounter, see this author's "Survey of Permits and Impact Statements Required For a PUD: A Memorandum," 3 Real Estate L.J. 215 (Winter 1975). But not all the reasons for which developers seek protection are proper. This article defers to the consumer protection proposals and probes, referred to above at note 1, for a catalog of excesses and abuses.

developer's counsel will draft documents and circulate them for review and comment to his client, to counsel for probable sources of end loans, and frequently to the host municipality—well before the units go on the market. Prospective purchasers subsequently receive a set of documents—including various declarations, deeds, bylaws, plans, rules, and regulations that will shape their future style of living—on a take-it-or-leave-it basis. There is no room for negotiated changes.

To appreciate the degree of developer paternalism that is required in order to comply with the statutes, even by the most benevolent and high-minded of developers, consider what a developer and his counsel must do. They determine the percentage vote required to amend the documents to elect officers of the owners association, and to decide most other matters that will be on agenda at meetings of unit owners and of officers. They choose the name of the condominium. They establish the finances of the owners association, including such things as provision for regular accumulation of reserves, procedures for approving special capital improvements to the common elements, procedures for adopting annual budgets, and the terms and conditions for management contracts. They decide on covenants and restrictions controlling use of the property, especially the issue of first refusal rights upon resale or lease of the units (generally with an exemption for sales and leases by the developer), private professional offices at home, age restrictions on owners and residents, rules about pets, and various controls over aesthetic and design matters. Finally, the developer and his counsel choose the organizational form of the owners association (thus determining the tax consequences), the committee structure, the accountant and attorney who will serve the association, indemnity protections for association officers, and turnover-of-control formulae.

The statutes obviously conceive of developer paternalism as a benign power likely to create well-run and efficient projects. Once a developer and his counsel have made a decision concerning one or another of the items listed above, the unit owners will be able to change it only by amending the particular condominium document that contains the questionable provision. In order to protect and virtually guarantee the immortality and inviolability of these initial decisions, developers typically fix the percentage vote necessary to amend at 75 percent or higher, as well as make it procedurally cumbersome to undertake the effort. It goes without saying

that prominent among the clauses thus protected are those that carve out favorable voting and control positions for developers.[18]

PROPOSAL: Amend the statutes to require that condominium documents, as originally recorded, permit a simple majority of the total voting power of the condominium—the unsold units being expressly disenfranchised in this situation—to amend. Such a change would reduce developer paternalism to a level more likely to result in a condominium regime run by and reflective of the needs and concerns of the unit owners themselves.

Setting Up Multiphase Projects

Framers of condominium statutes did not contemplate multiphase projects. First-generation condominium developments consisted of a fixed number of units in a single predetermined structural package. Not so today. Developers who build new kinds of condominium projects demand flexibility: No one can say for sure how many units a given market will absorb, nor can the acceptability to buyers of alternative architectural programs be forecast with much precision over the long period of construction and sellout, nor will the developers' institutional lenders consent to be locked into an inflexible scene. The solution favored by many developers has been to build out in several phases, so that the profits and buyer responses from one phase can fuel later ones.

But draftsmen of condominium documents suffer whenever their developer clients opt for maximum flexibility because the legislatures have devised a statutory straitjacket. Title lawyers will be apprehensive about dilution or reduction of a unit owner's interest in the common areas and facilities that may result when additional development phases join an initial one. Unit owners likely will object whenever a developer tries to change subsequent phases with regard to structural design, costs of maintenance, quality of hardware and other finish details, target markets, and so forth. Unit owners will be even more likely to object if a developer who

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[18] It is, of course, precisely these unassailable clauses that are the subjects of consumer protection proposals and probes. Additionally, some condominium documents exempt unsold units from liability for common charges.

lost control over an association of unit owners during sellout of a previous development phase regains control of an enlarged association. Counsel to construction lenders and unit mortgagees will be reluctant to approve loans if dilution may ensue and possibly jeopardize the security of a loan. Consumer advocates could have a litigious field day if subsequent development phases cause an increase in common charges or a cutback in the availability of common facilities, especially of such things as swimming pools and tennis courts.

Draftsmen of condominium documents have invented numerous sleights of hand to escape or avoid the statutory straitjacket. The outline for a recent and typical seminar on the legal aspects of condominiums[19] listed five such ways that practitioners have established multiphase condominium regimes:

(1) "Chinese-menu approach." Possible future programs for development and the consequences to unit owners under each are set forth in detail.

(2) "Annexation." With the consent of owners of earlier phases, or at least some portion of the owners, each new phase is simply added to the previous ones, without concern for dilution.

(3) "Annexation But Without Change in Percentage Interest." Rights of owners of units in one phase over the common elements of another are secured by easements and rights reserved by a developer.

(4) "Separate Condominiums With Single Recreational Association." [20] Each phase constitutes a separate condominium neighborhood and all recreational facilities are constructed on adjacent common land controlled by a special homeowners association in which all unit owners automatically become members upon acceptance of a unit deed.

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[19] "Legal Aspects of Condominium Development," 18-19 March 1974, an AMR Seminar, Ch. 1, pp. 19-21.

[20] See Schreiber, "The Lateral Housing Development: Condominium or Home Owners Association?" 117 Univ. Pa. L. Rev. 1104 (June 1969). See also Krasnowiecki, "Townhouse Condominiums Compared to Conventional Subdivision With Homes Association," 1 Real Estate L.J. 232 (Spring 1973).

(5) "Common Area and Recreation Committee." Similar to version 3, especially with regard to recreational facilities, this method offers a single recreation committee composed of representatives from each phase.

Each of these solutions gives elaborate testimony to the inventiveness of counsel to developers—and to the ambiguity of the statutes. On the other hand, none of the solutions is perfect and each has rather serious drawbacks, not the least of which is that in the absence of litigation on the subject no one can say with certainty which, if any, of the solutions conform to the statutes.

PROPOSAL: The two-tier approach, listed above as version 4, would appear most certainly to conform to the statutes, but the resulting plethora of owners organizations can become an administrative nightmare. What is called for, quite clearly, is a careful attempt to frame new legislation that will set ground rules for the expanding and contracting condominium situation and achieve a balance between the competing interests of unit owners, developers, lenders and title insurers, and host municipalities.[21]

Conclusion

A buyer of a condominium unit acquires a personal and private place for living and automatic membership in an organization of private government. Much has been written about the potential of condominiums to bring about reform in our current practices and institutions regarding property[22] but very little about the need to achieve an equitable distribution of power within the condominium itself.[23] Collective decision-making is an integral part of

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[21] For an account of efforts in Virginia to do just this, see "Virginia—The Condominium Act of 1974," 9 U. Richmond L. Rev. 135 (1974).

[22] See Quirk, Wein & Gamberg, "A Draft Program of Housing Reform —The Tenant Condominium." 53 Cornell L. Rev. 361 (1968). See also "Homeownership for Low-Income Families: The Condominium," 21 Hastings L.J. 243 (1970).

[23] In the context of "new towns" and neighborhood control of public facilities, more has been written on issues akin to this. See Hanson, *New Towns: Laboratories for Democracy* (The Twentieth Century Fund, New York, 1971). See also Foer, "Democracy in the New Towns: The Limits of Private Government." 36 U. Chi. L. Rev. 379 (1969).

condominium ownership. The organization of unit owners represents government close to home,[24] with jurisdiction over important issues of daily living and with power to tax and enforce its decisions. The statutes write off this element of internal self-rule as "management," thereby making light of the intense local politics characteristic of meetings of unit owners. As the percentage of housing in condominium owership continues to increase, amending the statutes to accord careful and fair treatment to the process of collective decision-making by the owners of condominium units should become a matter of highest legislative priority.

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[24] See Friedman, "The Future of the Urban Habitat," in *Environment: A New Focus for Land-Use Planning* 57 (Research Applied to National Needs, National Science Foundation, Washington, Oct. 1973). Especially, "Toward New Forms of Governance," *id.* at 78-82. See also Kotler, *Neighborhood Government: The Local Foundations of Political Life*. (Bobbs-Merrill 1969).

THE LAND GAME TODAY

The smart landbuyers of yesteryear find that the rules have changed. It used to be you bought raw land, figured on engineering, and got into the marketplace within nine months. Today, one large firm pays 5 percent down, 5 percent interest, and it is agreed with the seller that it will take five years to get any use out of it. The owner is a church and time is eternity to them anyway. When the builder buys for big cash plus big debt, what has he got but some accounting value in his latest press release to the "Street?" The new rules are you pay market price for the land, pay three years of interest before any flow (plus taxes), and finally get 50 percent of the density you originally figured.

—*The Goodkin Report*
Sanford R. Goodkin Research Corp.
Del Mar, California
March 1974

Senator BROOKE. I think the HUD study showed that as far as the future is concerned governing operations of these condominiums is really going to be an important factor and I quite agree. I'm sure that statement is accurate. I just wonder how much participation we get in condominium government now. As one of the 5-percent club I think maybe that's where we ought to start. We ought to participate more fully.

Now I have a question that I want to throw out and ask each of you to comment on. I'll ask you to be brief.

Secretary Hills stated on Monday—I don't know whether you were here or read her testimony—but she stated that a Federal law would be a major benefit to developers if it prescribed a minimum disclosure form and barred any State from requiring that out-of-State builders comply with its laws before marketing condominiums in that State. Under her proposal the developer would only have to comply with the law of the State in which the condominium is physically located. Other States can indicate that the condominium did not meet their requirements, but could not bar its sale within their boundaries.

HUD estimates that this would be a substantial help to developers and would save them at least $13.5 million a year.

Now do you agree with the Secretary's assessment of the burden placed on developers involved in interstate sale by differing and sometimes conflicting State laws? Is it a problem for your members to comply with five or six different laws in order to market their condominiums widely? Will this problem become greater if more and more States adopt their own law and there is no basic Federal law to establish some uniformity?

Why don't we start with you, Mr. Battaglia?

Mr. BATTAGLIA. I agree with that position, Senator. I think that the only difference I would have is that if we do go into interstate there perhaps should be some Federal legislation. Simply answering that the expense would be exorbitant if we had to comply with both State, Federal and also other States, the filing requirements, the constant updating of the financial data would be much similar to what is now required by SEC for public companies which is becoming almost exorbitant for people—private enterprise to stay in the public market as far as companies are concerned.

Senator BROOKE. Thank you.

Mr. KEEN. Senator, our association finds that the vast majority of condominium sales take place within the boundaries of a State, that the amount of interstate sales that take place are relatively insignificant related to the total volume produced.

Senator BROOKE. Do you have any figures on that?

Mr. KEEN. I don't have them handy, Senator, but we can get them to you.

Senator BROOKE. Would you send them in for the record? It would be very helpful.

Mr. KEEN. Yes, sir.

SUBMISSION FOR THE RECORD BY THE NATIONAL ASSOCIATION OF HOME BUILDERS

There are no readily available statistics as to the number of condominium units that have been sold on an intrastate basis primarily as principal residences, as opposed to the number which have been sold on an interstate basis primarily as second homes or for other recreational purposes. NAHB does not have such

numbers, nor does the Department of Housing and Urban Development, nor does the Community Associations Institute. These are the principal sources of data of this type. However, it is the belief of NAHB, from talking to and dealing with its members engaged in condominium construction, that the great majority of condominium units are sold as principal residences on an intrastate or metropolitan interstate basis. Additionally, a good number of the condominium units built for recreational or second home use are similarly sold on an intrastate basis, according to the information available to us from our membership.

Senator BROOKE. Thank you.

Mr. TERRY. Since we represent developers of resort condominiums, I would say it would be our people who would be aided most by a uniform statute. In theory, a uniform statute as promulgated by the Federal Government is an appealing thing. In fact, it will not work. For it to work, the Federal Government would have to demonstrate a clear intention to occupy the field of condominium regulation, that is, take it completely away from the States. I don't think there is willingness to do that.

Ms. O'CONNELL. I can't help but agree with the fact that multiple registration would drive the cost of condominium purchases up so high that the ordinary person couldn't afford them.

Mr. WOLCOTT. As a point of fact, I would tend to think that condominiums are not marketed in more than one State for the simple reason that the redundancy of registration requirements does impede their trade. The fact that they are not today marketed interstate is not an indication I wouldn't think that they can't be or shouldn't be, but rather that the current structure is such that the developers are not willing to hazard that type of marketing.

I would tend to agree with the Secretary.

Mr. WALTER. I join in Mr. Terry's remarks.

Mr. JOHNAKIN. I agree. They may be put under some burden if there are different disclosures. But States might be able to cope with that problem by providing that other States disclosure requirements will be deemed satisfactory for offerings in the State for purchasers of condominiums in the State where the condominium is located.

For example, Virginia provides that a prospectus approved by the SEC will be deemed sufficient in lieu of compliance with the disclosures required by the Virginia law. Furthermore, I think that the most useful role that HUD can serve is by promulgating guidelines for disclosure requirements that might be adopted by the States with uniformity. The National Conference of Commissioners on Uniform State Laws will, I believe, recommend disclosure requirements be adopted by the various States and I think that that sort of disclosure might prove most useful.

Senator BROOKE. Why do you feel that voluntary uniform State laws are more desirable than mandatory Federal?

Mr. JOHNAKIN. Because I would like for people in Wyoming, Montana, or Idaho to be able to make recommendations for changes of the law without having to trek off to Washington, D.C., every time they want to be heard. I'm not sure that all the answers lie in Washington, and I'm not sure that all the people who might have some expertise or something to contribute will find it convenient to come to Washington.

Senator BROOKE. Mr. Wolcott, I'm interested to hear you state that State enforcement of usuary laws should regulate the return on recreation leases just as on any other type of capital investment. Do you know of any suits which have been brought under State usuary laws which have resulted in bringing down recreation leases?

Mr. WOLCOTT. No, sir, I do not. I know of a couple of cases where the constitutionality of recreation leases per se has been challenged.

I preface my statement—I am not an attorney nor am I a student of the practice of law, but the substance of a properly executed recreation lease is that of a financing tool. If its legislative form could also be that of a financing tool, then I feel it should follow that usuary laws would be effective for enforcement. I do not mean to imply that usuary laws today would be effective.

Senator BROOKE. Mr. Walter, could you answer that question?

Mr. WALTER. No. I have no—in the northeast, the amount of work we do with recreation leases, comparable to Florida, is very insignificant.

Senator BROOKE. Mr. Battaglia, you said that 4,000 units were in Florida?

Mr. BATTAGLIA. Yes, sir.

Senator BROOKE. I think somebody else said that there would be more condominiums. I think we have only begun, frankly. I think we'll get to hopefully low and moderate income houses as well as middle income and upper income for condominiums throughout the country. It may well be our answer. I really enjoy living in one, despite the problems. I like the concept. I think it's an excellent concept and it offers many advantages to certain people who perhaps live alone or are in small families. So I think it's here with us and it's going to be with us for some time.

Now why should there be a Federal law regarding condominiums? Well, you get Federal law because you have abuses and sometimes States have not gone into the field and have not legislated. Also, some of you have not been policing your own industries.

I'd just like to know how much policing you do of your industry, the builders, for example?

Mr. BATTAGLIA. The policing of the industry in Florida right now is through the Florida Land Sales Board, Condominium Division, that is now specifically provided for in the 1975 amendment. It requires that we file our prospectuses, which are disclosure requirements, together with all documents and the advertising materials must be updated. That particular agency has the right if we do not comply and make our filings timely, which will be for the first time October 30 of this year—they have a right to enter a cease and desist order and if we don't comply with the cease and desist order they have a right to go in and get an injunction in circuit court to enjoin sales. In addition to that, the organization which is up here today also has its code of ethics which it requires the developer to or part of that organization to abide by. There are sanctions if the developer doesn't.

Senator BROOKE. Does anyone else want to add to that?

Mr. KEEN. Our national association has launched a homeowners warranty program which provides substantially more warranty protection to purchasers than is brought forth in the bill submitted. While it is a new program, only in effect for a year and a half, we are finding

that builders around the country are entering into the program and lenders are beginning to recognize that they want to go along with construction and permanent funding to those builders that are part of the warranty program.

Now the policing activity of the industry through this program is very effective. As the program takes hold and the public becomes more aware of its availability and its impact on their protection, then the builders that do not conform to the requirements of the warranty program will not be eligible to provide it and may well be deprived eventually of lending facilities. We feel that it's an effective tool and doing an excellent job in homeowner protection.

Senator BROOKE. Mr. Keen, has your association supported proposed State legislation?

Mr. KEEN. I didn't get the question, Senator.

Senator BROOKE. Did your association support or oppose condominium legislation at the State level?

Mr. KEEN. Our national association?

Senator BROOKE. In the States as condominium legislation was discussed? I'm going to ask all the builders associations and developers the same question. I'd like you to know that. I'd like to know whether you were behind legislation—were you supporting legislation within the States?

Mr. KEEN. Within the State of Virginia? Very much so. We participated in the formulation of the legislation and we are very happy that it's an excellent law within the State and provides all the necessary disclosures, warranties, and protections for the purchaser that any normal purchaser is entitled to.

Senator BROOKE. Has the national association concurred, and if so, I take it the NAHB encouraged their branches in the States to propose legislation within those States where we don't have such legislation?

Mr. KEEN. Yes, sir, they have.

Mr. BATTAGLIA. I was just going to say that the association that we are involved in not only assisted in legislation but implements it to the land sales board in Florida.

Senator BROOKE. Anyone else?

Ms. O'CONNELL. I'd like to say that we have cooperated completely with the Florida Land Sales Board. We have given them the benefit of our input and we helped write their rules and regulations.

Mr. WOLCOTT. Senator Brooke, I think we should all be as candid with you as we can. At the time the Florida legislation was introduced we were all reluctant to support that legislation. It was made pretty clear to us in the hearings that were held that the condominium industry had gotten itself into pretty sad shape. From that time forward to say that we have been active, honest participants in the legislative process is I believe a correct statement.

Senator BROOKE. Thank you for your candor.

Mr. JOHNAKIN. My company actively supported full disclosure in Virginia, but we would go further than that and say that each State should be free to require even stricter disclosure if it wants. I'm afraid if a Federal statute, if it preempted the field and prevented the States from requiring additional disclosures, might be unfortunate and, on the other hand, if you have a Federal minimum standard

for disclosure but permit the States to add on, then you're still going to have that problem of a multi-State offering having to comply with different disclosure standards in different States. So I don't think that having a Federal statute is the answer to the problem.

Mr. WALTER. I have in mind in the—I'm caught between the Department of State of the State of New York, the attorney general of the State of New York, and the builder exemption provision with respect to condominium filings. Certainly the appeal of any kind of one-stop shopping approach that you will come up with would be overwhelming but I think, as Mr. Terry said at the beginning, the problem is going to be, at least as I would see it, trying to get an expression from the Congress that it in fact supports one-stop shopping or a single filing, approach that cuts through a plethora of State laws which even the States don't know which of their agencies is going to regulate which aspect of an owners association versus a condominium filing or whatever. It's that complexity I think that befuddles the practitioners of this field.

Senator BROOKE. Anyone else?

Mr. TERRY. There's currently a lawsuit in the courts involving the Federal Government through HUD and the States of Florida and California over this issue of whether the States have the right to do their own thing, so to speak, in their States on real estate issues, and I think the States have shown very little inclination to give up their regulation of real estate to the Federal Government.

Senator BROOKE. Mr. Coan, do you want to add anything to what Mr. Keen has said as far as the national association is concerned?

Mr. COAN. Senator, I have my staff right now working on a draft bill which we plan to give to our local and State associations and urge them to consider. We have not to date made a major effort to urge them to seek State legislation. We have encouraged them through our normal advisory programs and our committee structure—that is, our membership—to be concerned about this and to participate in the development of State laws such as in Virginia and Florida and in other places.

I personally have served for the last 2 years as a member of the advisory committee for the Conference of Commissioners on Uniform State Laws on their Uniform Land Transactions Act. At my urging, and the urging of others, the condominium title was removed from that act by the Conference, in order to be expanded into a more consumer-oriented statute, rather than a technical statute. This they did last summer, and I'm hopeful that that will come forward in the next year as something which is then promulgated with the prestige of the Conference and then hopefully adopted at the State level. I must be candid to say it probably will not be adopted word for word. There are differences between the States and they have different concerns.

Senator BROOKE. Mr. Battaglia?

Mr. BATTAGLIA. I'd just like to point out, Senator, that there is an actual conflict taking place right now between State and Federal regulations in the State of Florida as it relates to the land sales boards. The State has been advised by HUD that they will not accept the filings that are filed with the State and approved as an exemption. They have to make a double filing. The attorney general went to court and

obtained a restraining order against the Federal Government precluding that requirement which is now still being tentatively resolved in the courts. It's just again another example of double expense where the average developer just cannot possibly make it. You're going to push the little guy out of business, Senator, and it's the big boys that's going to be sitting there building these condominiums if they have these multiple double tier filing requirements. They can't afford it.

Senator BROOKE. While you have the floor, have you seen any marked improvement as far as abuses are concerned, since your law has been in effect?

Mr. BATTAGLIA. I think that as a result of the Federal Government becoming interested in this field that there's no—I think we'd all have to admit that our State particularly has become more interested in the field and has become more conscious of the problem.

Since 1968 we have been making an effort in that direction in Florida to correct these abuses and there's no need for me to sit here and deny the fact, Senator, that there have been abuses, but I think now with the controls that are being imposed by these various agencies and the State that the abuses are on their way out and I think that we can operate in an intelligent manner to the satisfaction of all concerned.

Senator BROOKE. Mr. Coan, how long does it usually take for a uniform State law to become Federal law?

Mr. COAN. Senator, I don't have that answer.

Senator BROOKE. May I suggest 20 years?

Mr. COAN. To be adopted by all States? It may take that long. Some have not been.

Senator BROOKE. Can we wait that long?

Mr. COAN. Senator, if you have a few hundred units a year being built in a sparsely settled area should one resort to the Federal Government to try to deal with that?

Mr. KEEN. Senator Brooke, one of the items in the proposed law, section 13, which refers to the authority of the Secretary of Housing from time to time to amend, and issue, and modify, and make new regulations is one of the elements in this proposal that could drive condominium developers out of the condominium field. It's strictly a license to do anything that HUD decides is essential to override the State rules. I think that the intent is to provide consumer protection and to assure the minimum amount of abuses in the condominium field. In the condominium field today those initial abuses that took place in the early growth years have essentially been wiped clean by virtue of public disturbances over the abuses involved.

The States that now have condominium acts are effectively providing the consumer protection which is essential for purchasers and the other States that have no volume of condominium activity obviously have not reached the point where they want to develop these kinds of laws. If we have an overriding Federal Act that supersedes the authority of the State in governing its own local real estate transactions, we are encumbering a portion of the housing industry with more obstacles and more problems than we can afford to bear with.

I think this needs substantial amount of consideration in this concept of preservation of the consumers rights and interests. We are all

consumers. We are all interested in our purchasers as consumers. I think the thrust of the industry throughout the country has been improvement, self-policing, and doing those things which are proper and acceptable and in conformity with good business practices. I really do not feel that the abuses that have been brought forth in the initial years of condominium development have now reached any stage of crisis or panic where we need an overriding Federal rule that will put the authority in the hands of the Secretary of Housing to say we don't like what happened in 1975 so in 1976 we are seeking some new activities from you people in the business.

Senator BROOKE. Mr. Keen, you paint a beautiful picture. I just hope it's an accurate one. I hope that that's the state of the art.

Mr. KEEN. Senator, I'm on the firing line. I deliver units. I build them and I sell them and I worry with the purchasers and the coowners, and I can see what's happening within our State. I am well satisfied that the controls within our State and in our public authorities prohibit us, even if we wanted to, from doing something dishonorable.

Senator BROOKE. Well, I assure you that as a Republican I believe in the free enterprise system, and I'm not trying to find ways for Government to get into your business when it doesn't have to. We don't understand the condominium situation to be exactly as you have described. I'm sure there's been some improvement. There's much room for greater improvement. There still are abuses. We get mail from all over the country from people who are concerned about it. That's the only reason why we're concerned about it. Some States have adopted condominium laws. Some good laws, some not so good. We are not trying to inject the Federal Government into the business. We don't want to get in it if we don't have to. We generally don't get in unless we have to. It will depend on what the States do in the regulation of condominiums themselves.

It would also depend, as I said earlier, on what you do, what your associations and others in the business do to keep these abuses down and protect the consumer. It's a big business now. It's growing all the time. It's going to be much bigger and unless we have adequate protection for the consumer either applied by the State or by you, then the Federal Government is going to get into it. It's as simple as that. That's the history of Federal legislation.

Mr. JOHNAKIN. May I return for a moment to the question you raised about the inordinate length of time that is sometimes taken for a uniform State law to be adopted? All of the States in the Union adopted a condominium law between 1961 and 1968, and in that 7-year period they very largely copied from each other. I don't think the States are going to wait for a proposal for a uniform State condominium act before they act in the realm of consumer protection, because they have already begun to act; and just in the last 2 or 3 years we have seen so much progress, not just in my own State of Virginia, but in New York, in California, in Florida, in Georgia, and Utah now. Every year there seems to be substantial improvement in those States where the problems exist and where condominiums are most frequently encountered.

I think if we do come back next year we will find that many more States have adopted consumer protection measures.

Senator BROOKE. Thank you, Mr. Johnakin, and thank you, all of the members of the panel. We are going to review this testimony and, as I said earlier, I have an open mind. I'm sure my colleagues have open minds on this, even though three of us have proposed this legislation. We have had some good testimony both pro and con and we look forward to receiving the statistical data, Mr. Keen, from you, and anyone else. Your statements have been placed in the record. You have been very helpful, and we will just have to see where we go from here after giving it objective and very serious and very deep consideration. I want to thank every member of the panel. You have been very generous with your time and the committee thanks you.

The record will be kept open for 2 weeks.

[Whereupon, at 11:55 a.m., the hearing was adjourned.]

[Additional material received for the record follows:]

STATEMENT OF GEORGE W. DEFRANCEAUX

The National Housing Partnership was chartered under Title IX of the Housing and Urban Development Act of 1968 "to encourage the widest possible participation by private enterprise in the provision of housing for low and moderate income families." In response to this charter, the NHP has enlisted 270 private enterprise limited partners who invested $42 million for the construction of decent housing for such families. This investment has generated the organization, financing, construction and management of 155 "limited distribution" low and moderate income projects in 32 states that have or will provide decent housing for 25,000 American families.

One of the vehicles we are finding to be most efficient for such production is condominium development. Condominium development often provides for highly efficient and innovative use of land with a consequent reduction in the per-unit cost of development.

Though we have developed only 234 such units to date, we were so encouraged by the results that we have several hundred more units in the planning stage.

Of course, we are aware of some of the abuses that occurred recently in condominium development in its burgeoning growth in recent years. We share the concern of the sponsors of S. 2273 over these abuses.

It is to be noted, however, that condominium development thus far is concentrated heavily in a few states and those states have reacted to abuses with effective regulatory statutes. In addition the National Conference of Commissioners on Uniform State Laws is working on a model statute to be available to other states as condominium development spreads. We think this is encouraging and that regulation of such matter is more properly a state function, which the bill recognizes.

However, the proposed statute was born out of a quite legitimate concern for the people who invested their savings in what appeared to be a very attractive form of home ownership, but found that they had entered into onerous contractual relationships and had been misled as to the financial obligations they were undertaking. There is no question that public action should be taken to correct such abuses.

Our concern is that reaction to these abuses should not make it too difficult or costly for us to produce housing for the very people the bill seeks to protect.

In general, we think that any bill that may be reported should encourage sound state action with an overview role by the Federal Government and should provide standards for uniformity of disclosure to consumers which will enhance consumer confidence in the condominium field. We all wish to avoid a law which would permit and foster the kind of arbitrary over-regulation that grew out of the laudible intent of RESPA but which ended up with rigid requirements that deprived housing to the people it sought to aid.

We would hope for legislation that would encourage condominium development and do so along sound and efficient lines, with the federal government's role being that of a watchdog over the rights of consumers.

In general, that "watchdog" role is met by standards set out for disclosure contained in the bill, that is, those provisions which require that the developer provide certain information to all purchasers as to the future plans for development in the project, governance, voting rights, contractual information, etc.

Limiting the Federal role to a "watchdog" role would keep to a minimum additional demands upon HUD's scarce technical manpower, while at the same time having available Federal intervention in these rare situations where the states may fail in their responsibilities.

Our primary concern is the sweeping investigatory and regulatory powers which the bill would invest in HUD in Sections 12 and 13. The experience under the Real Estate Protection Act has indicated that the tendency is for HUD to go far beyond what seemed the statutory intent in implementation of such acts. We do no believe that it is the intent of the Committee to usurp state and local authority in what is by its very nature a highly localized activity. Yet the bill would in large measure permit or foster this.

In addition, certain specific requirements within Sections 5 and 6 we feel are excessively rigid, costly and possibly unworkable, and far beyond the watchdog role that we recommend for the Federal Government.

Under Section 5, there are two provisions that give us particular concern:

The rigid time provisions for transfer of common elements and termination of management contracts makes no allowance for special circumstances in various projects. There are many very competent developers who would be extremely wary of entering into a development—with his investments in it on the line—with the prospect that he might arbitrarily lose control of it because of market slowdown long before it was well sold out. We recommend eliminating the one year provision and leave the 80% sales provision as the triggering mechanism for turnover of management control.

The rigid warranty provisions put the government into a vast new area of enforcement. We think it would be best to provide for a private warranty program of the type now being provided by the National Association of Home Builders and the National Association of Realtors.

Under Section 6 we are concerned about the following:

The requirement of a two-year *certified* detailed budget projection. There is considerable doubt that such a certified projection could be obtained. And to what sanctions would a developer be subjecting himself if it proved faulty in these uncertain economic times? Guidelines should be provided for the type of budget projection the developer should give as his best estimate.

The requirement for a detailed engineers report on projects completed more than 12 months before offering could be very difficult and certainly very expensive to obtain. It is difficult to describe an alternative. Perhaps a statement by the developer should be required giving the age of the building and the status of repair and modernization of the mechanical systems therein.

The requirement of a statement of the potential effects of nonresidential development on the unit owners would seem to us to be a requirement most difficult to interpret or carry out with any real precision. It would have to be subjective at best and self-serving at worst. We recommend elimination of this requirement.

We should be pleased to render any additional assistance we can in achieving a bill that would cure abuses while permitting the continuance of a major housing production effort.

31 October 1975
2305 Blue Sage Lane
Arlington, Texas 76014

Senator William Proxmire, Chairman
Senate Banking Housing and Urban Affairs Committee Re: S.2273
5300 Dirksen Senate Office Building
Washington, D. C. 20510

Dear Senator Proxmire:

Please consider this letter for formal filing as part of the hearing report on Bill S. 2273.

As President of the Arlington Homeowners Townhome Association which is located in Arlington, Texas I have a vested interest in condominium type projects. I have reviewed your subject Bill and would like to see you add several items. The items I am requesting you add are ones which require the developer to pay his fair share of the operating cost of the development prior to sell out. Before attempting to determine a fair share portion I would like to discuss our development to give you the necessary insight into the problem.

Our development was one of four townhouse developments undertaken by Centennial Homes, Incorporated. Each development seems to have about the same problems so I will only discuss our development.

In March of 1973 I moved into our development which was slated to have a total of 153 units. By the end of 1973 there were 21 sold and 71 units built or 50 unoccupied units. The developer paid all the bills for yard maintenance, pool expense, etc. through December 31, 1973. On January 1, 1974 an Association was formed. The duties of the Association were to maintain the common areas (ie water and cut the grass, etc); maintain the pool and clubhouse facility; maintain the structural soundness and exteriors of all units (ie foundations, painting, roofs, etc); and collect the Association dues. Personal utilities are not included in the Association dues.

When we purchased these units we were told by the sales people that the monthly Association fee would be $17.50 per month and that 5% a year was the maximum amount the fee could be increased. The $17.50 a month was suppose to be adequate to cover all operating expenses plus establish a reserve fund for maintenance (ie replace roofs, siding, painting, etc.) In addition the project was to operate (by what means no one knows) with absolutely no input but financial from the members according to the sales people (the Covenants however did call for a Board of Directors).

By the end of 1974 we were informed by the developer that the Association was in debt to the developer for some $11,000.00 with zero dollars in reserve for maintenance and a $3,680.00 tax assessment due in January 1975.

In 1975 our assessment was raised to the maximum permitted by the Covenants which was $30.00/month, considerably more than 5% but with the legal By-Laws. As 1975 draws to a close we are still faced with a debt of approximately $11,000.00. A dire need for some maintenance amounting to thousands of dollars due to primarily inferior initial paint jobs and products. We still have a zero dollar maintenance fund and further we are under pressure

from the developer to take over the financial responsibility of the Association for certain concessions such as forgiveness of the debt (which is theirs by most anyones thinking) repair of a portion of the inferior construction and a token fund for reserve maintenance (in case you are wondering there are still only 71 of the proposed 153 units built and only 65 of the 71 units are sold. There is almost zero chance of development of the remaining units in the foreseeable future).

The problems with this and all the other Centennial developments in my opinion are as follows:

1. Their original assessments were unrealistically low - probably for the purpose of selling townhomes.

2. They had no budgets and no supervision.

3. They built a large expensive pool as well as a very unpractical clubhouse. The clubhouse was used as their sales office initially. Both the pool and clubhouse were built as and are still being used as sales promoting items but are being fully paid for through the Association.

4. The developer is only obligated to pay on a unit basis of 20% of the association dues paid by a private owner. The difference in cost to the association between a unit owned by the developer and one owned by an individual would not amount to 10%.

5. The developer pays zero dollars per month for the undeveloped lots but charged all the common area taxes to the Association (the developers assessments in 1974 did not pay their pro rata share of the 1974 property taxes).

The items which I want to see added to your bill are as follows:

1. The developer shall pay 90% of full homeowner assessments on developed units (perhaps 3 months grace would be acceptable to give the developer a reasonable selling time) and 25% of full homeowner assessments on vacant lots to help maintain expensive common area facilities. (If a project is developed in phases or panels such as projects with hundreds of units then the developer should not be subject to assessments on all vacant lots but rather those vacant lots which have facilities to maintain.)

2. When the developer turns the Association over to the private owners it should be debt free and capable of operating within its By-Laws.

3. This bill if put into law should become effective on all developments currently under construction.

Your consideration and concern in this matter is greatly appreciated as is the reminder of your badly needed bill.

Yours truly,

D. J. Hammerlindl

cc: Senator John G. Tower
Senator Lloyd M. Bentsen

Approved FHA Mortgagee

James F. Messinger & Co., Inc.
10800 South Halsted Street
Chicago, Illinois 60628

James F. Messinger
Carl A. Kinell
Ronald A. Noteboom
James F. Messinger, Jr.

Mortgage Appraisals Insurance Management

1975 AUG 15 PM 3 28

Room 5230

August 12, 1975

Honorable William Proxmire
Senate Office Building
Washington, D. C. 20005

Dear Senator:

We were very interested in your new Senate Bill #2273, which has been called "a buyer's bill of rights".

We were wondering if you could put a rider to this bill forbidding a conversion of existing apartment buildings into condominiums unless 50% of the existing tenants agreed to buy.

This provision would prevent a rip-off by some fast-talking promoters who are going around buying existing apartments that are now occupied by people who do not have the where-with-all to purchase a condominium, and need rental space.

We believe that throughout the country this is being done, and, of course, the people who live in the building already know what is wrong with them, and would not more buy them than the man in the moon.

We have already asked our state legislators,for the past two years, to pass such a bill, but, evidently these entrepreneurs have pretty good clout with them, and the bill has always died in Committee.

Since I am a mortgage banker, you may wonder why I am presenting this rider to you, since all mortgage bankers are supposed to be bad guys. We are known to the Chicago Area Department of HUD's John Waner, as his "knight in shining armor", who deals the cards from the top of the deck and has been doing so for 40 years.

We thank you for your interest.

Sincerely yours,

James F. Messinger

STATE OF NEW JERSEY
DEPARTMENT OF COMMUNITY AFFAIRS
363 WEST STATE STREET
TRENTON, N. J. 08625

PATRICIA Q. SHEEHAN
COMMISSIONER

October 27, 1975

The Honorable William W. Proxmire
5241 Dirksen Senate Office Building
Washington, D.C. 20510

Dear Senator Proxmire:

The New Jersey Department of Community Affairs strongly endorses the interest of the Senate Banking Committee with regard to the need for Federal legislation to curb the abuses that have come to be associated with condominiums and to restore consumer confidence in this type of housing.

While New Jersey has remained in the forefront in encouraging alternative housing formats, it has also begun to recognize that the complexities (i.e., covenants, deeds, restrictions, by-laws, etc.) and the needs of condominium type development are not being addressed by the public or private sector. This is partially reflected in the increased number of consumer complaints received by this Department, as well as by a study initiated within its housing and planning divisions which substantiates this public concern.

During the years 1970-1974, the number of occupied condominium units alone in New Jersey increased from 12,490 to 28,470, representing a 128 percent increase. Municipalities throughout the State are adopting one or more condominium types as growth takes place, and this trend will continue to mark an increase in such housing.

Our Department has carefully reviewed S. 2273, the "Condominium Consumer Protection Act," and is offering the following recommendations:

1. Definition of a "Condominium Project"

   S. 2273 is a comprehensive measure in that it recognizes the need for consumer protection and the registration and disclosure of information for those desiring or in need of alternative housing that requires the sharing of real property. This concept while generally known to a large segment of the public as "condominium(s)", in many cases comprises other housing formats which are not expressed in this bill. These formats may solely or in part include condominiums, cooperatives, retirement communities and planned unit developments, all of which require some form of undivided interest in common elements and represent the sharing of real property. The interrelationship of these formats within the context of the definition of a "condominium project" should be more clearly defined.

As a suggestion to the Committee in adopting a more flexible definition, a portion of New Jersey Senate Bill 3038 might be considered. A copy of this bill, which is presently in committee, has been attached to these recommendations.

From S-3038:

"Planned Real Estate Development" or "Development" means any real property situated within the state, whether contiguous or not, which consists of or will consist of, separately owned areas, irrespective of form, be it lots, parcels, units, or interest, and which are offered or disposed of pursuant to a common promotional plan, and providing for common or shared elements or interests among, or restrictions upon purchasers, creating among all or any number of such purchasers in mutual reliance, dependence, responsibility or relationship.

2. Documentation

Section 13 of the proposed bill prescribes that the Secretary will set forth "forms, instruments, and documents" used in the sale of condominium units.

It has been the experience of the Department's Division of State and Regional Planning that the process of document standardization, which already exists, has generally meant incomprehensible legal scripture for the prospective buyer. These are unnecessarily complex instruments which have, in many cases, led to general consumer dissatisfaction with the condominium purchaser often left in doubt as to exactly what he has bought and is responsible for.

It is the Department's opinion that such documentation should not be standardized but rather reflect each development's character consistent with existing or proposed laws. These documents should be set forth in a simple, straightforward fashion. The preparation of flexible guidelines would be an acceptable alternative to the standardization process.

It should be noted that of all existing Federal loan programs available for the construction of condominium type developments, there is no one single set of documents acceptable to all loan agencies. This has been a chronic complaint of builders and attorneys. While this appears to be consistent with the call for standardization of documents, the flexibility of those documents should be such that each community can determine its own character.

3. Condominium Conversion

With respect to condominium conversion, the Department suggests that the Committee consider New Jersey Assembly Bill 3570, which is more protective of tenants. Under this bill, a tenant receives a minimum of three years to vacate a building being converted into a condominium and in fact, a tenant already has six months under present state law. A copy of A-3570 has also been attached to these recommendations. The bill has been reported out of committee and may be voted on before the end of the year.

Our Department recommends that the proposed Federal legislation incorporate the provisions of A-3570 with respect to tenant protection.

4. State Funding

Between 1970 and 1974, the number of occupied condominium units in New Jersey increased by 128 percent. Alternative housing formats, as previously mentioned, contributed additional units to this proliferating market, comprising all income and age groupings.

As these units continue to comprise a greater segment of the housing market, there exists a continual need to assess the impact of such development as a component of New Jersey's total housing supply. However, in order to do so, it will be necessary to establish, as indicated under Section 8 of S. 2273, a state agency to administer a comprehensive program to assess this continual increase and its effect on the total housing supply. The 25 percent seed money that is provided in Section 8 for this purpose clearly does not meet the needs of New Jersey for the establishment of such an agency. A far better format for utilizing federal monies would be a phase program over a five year period at which time the state would ultimately control the designated agency:

	Federal	State
Year 1	75	25
2	66 2/3	33 1/3
3	50	50
4	33 1/3	66 2/3
5	25	75

This suggested format would give the designated agency time to establish a long-range program for implementation of a state condominium plan.
Thank you for giving these recommendations your consideration.

Very truly yours,

Patricia Q. Sheehan

1027 15th Street
Plano, Texas 75074
Tel (214) 423-1713

Management Division

rainwater & associates

31 October 1975

Senator William Proxmire, Chairman
Senate Banking Housing and Urban Affairs Committe
5300 Dirksen Senate Office Building
Washington, D. C. 20510

Re: S.2273

Dear Senator Proxmire:

This company is in the business of managing Townhome and Condominium properties in the Dallas/Fort Worth market. Our interest in the "Condominium Consumer Protection" bill is intense.

We have reviewed it with no less than 12 Townhome Association Presidents in our market. Other than some discussion on minor points, they are in unanamous agreement that the bill should be passed, intact.

My company's interest in the bill, is that we are the ones who have to come in after Association is in jeopardy and renovate it. In some cases, this is a matter of years, rather than months. We feel this is an unnecessary burden to be placed on the Homeowners, financially and emotionally.

To substantial our case, we are taking the liberty of submitting some documentation on various Associations we either manage or consult. We are not naming the Associations, but would be happy to do so if their Presidents agree.

Sincerely,

R. K. Rainwater

R. K. Rainwater
President

RKR:mm

Enclosure

1. Association MKS:

Townhomes, high $20,000 through mid $30,000's. Duplexes and quadraplexes, two story, brick veneer and frame. Amenities: swimming pool (small), 2 1/2 acre (approx.) greenbelt and creek (floodplain), playground, cabana with restroom (no clubhouse).

Problems: Low-balled. $13.00 per month assessment was quoted. $200.00 per homeowner maximum (according to Covenants) was selling point. "Carefree" living sales routine was employed. Landscaping nor amenities completed as of this date. Lawn and greenbelt sprinkler system inadequately designed and improperly installed, causing water leaks which cost the individual homeowner money on his own water bill. (Sprinklers are metered to individual house hold, rather than using common water.) Improper plumbing fittings used in sprinkler system which are now rusting out at the rate of approximately ten per month. Swimming pool installed improperly causing manifold leaks and loss of chemically treated water. Greenbelt not sodded causing serious erosion. Creek sluice (concrete liner) not filled properly causing erosion damage. Homeowners Association was saddled with bulk of expense of repair on all above items. Tree and bush installation never completed. Homeowner Association now funding completion. Due to low-balling, lack of maintenance performed at the outset, some Homeowners refuse to pay their assessments. Failure-to-pay assessments penalties were never fully explained to the prospective buyers. Some owners have abandoned their homes which have now been foreclosed. Developer is slow to respond to agreed upon items, although not the responsibility of the Association, have caused more members to refuse to pay assessments.

2. Association MTG:

Townhomes, mid-thirties to low forties in price. Duplexes and quadraplexes, two story, brick veneer, stucco and frame. Amenities: Swimming pools (two small ones) two story clubhouse, greenbelt and playground, tennis courts, living fences. All lawns and green areas sodded with tiff green grass, except one street of duplexes. Berms and hillocks landscaped in tiff areas. No sprinkler or irrigation facilities installed, even though tiff requires more irrigation than standard grasses for the area. Berms and hillocks most difficult to maintain because the tiff must be close cropped. Requires manual watering crew of at least three to five men, which shall be a perennial expense until an underground system is installed at a cost of $20,000 plus dollars. Developer bankrupted, subdivision foreclosed by prime lender who maintained it at no expense to homeowner for a period of almost two years. Assessments collected went into reserve fund. Little accounting, forecasting or budgeting done by any developers involved. Project has now been sold to a reputable builder in the market who is now becoming financially unable to keep up with the extremely high maintenance costs, due to the poor initial planning. Few delinquencies but list is mounting. Developer (new one) unwilling to invest capital in badly needed capital improvements. Homeowner morale low. Initial Association assessments low-balled.

3. Association MGW:

Townhomes, high twenties to mid thirties, quadraplexes, two story, brick veneer, frame and stucco. 2 1/2 acre greenbelt, swimming pool (adequate) creek and playground and picnic area, single story clubhouse (nice), sport court and putting green, concrete sluice lining creek bed, automatic sprinkler system, metered to Association, operational. Assessments low-balled. Developer picked up the deficit, then billed it back to Association. Some shoddy construction: carports not completely painted, leaving rust streaks down frame members, association will have to pay for renovation.

General condition of association is good to excellent. When townhome market plunged, developer forced de-annexation of several lots in order to build single family-detached on Association land. Little compromise made for use of land, and for loss of Homeowner Assessments.

Developer low-balled assessments, and set ceiling too low in order to make attractive sales package. First assessments were $19.50. Went to $30.00 a year and half later. Developer participation and capital contribution to Association minimal to non-existent. Association was converted to "on-going" status 1 November 1975. No money in bank, in debt, having to borrow money to operate on, and will be in continual debt until assessment ceiling is raised to pay for developer shortcomings. Is having to cut back on services in order to provide maintenance fund which was promised as part of original maintenance assessment (19.50). Some homes now in need of painting and there is no money to do it.

4. Association MNC:

Idential situation as aobve, except for lack of greenbelts or park. Has cabana instead of enclosed clubhouse. Swimming pool and playground are only amenities. Low-balled. Assessment is now up to $35.00 after having started at $19.50 two years ago. Hand picked member/owner Board members. Association left in debt, saddled with numerious heavy repairs. No reserve fund. Developer is charging back operational deficits to Homeowners ($9,000 plus) to be paid back in two years. Some Association members consider that debt was part of sales expense, but cannot get Board to respond. Same developer as MGW Association.

5. Association MSR:

Same developer as previous two. Large clubhouse, junior olympic size pool, courtyards, 1/2 acre greenbelt. Sprinkler system renovated at homeowners expense (partially), requires additional expansion to get water to homeowner's front flowerbeds. Developer attempted to recoup "deficits" from Homeowners but met with intense resistance from homeowner. Resident Board members are opposed to accepting any responsibilities for developer's problems. Assessments were low-balled. (19.50) two year's ago, now up to $30.00. No reserve for maintenance, even though promised by developer to be included in maintenance assessment. Building exteriors rough, need some paint; no money. Developer attempted to saddle association with $11,000 payback of debt. Association has thusfar resisted all attempts to pay the "sales" cost of developer. Members prepared to take up collection to take builder to court if necessary. Builder so far, remaining almost inflexible on matter. Many lots yet to be developed, control still in hands of developer.

6. Association MCW:

One of the most beautifully landscaped areas in the market. Lovely two story homes in high forties to low sixties. Creek and greenbelt, no problems, swimming pool, tennis courts, expansive clubhouse. Aesthetically perfect environment. Original developer bankrupt, turned over to reliable developer to finish sales and construction. Low-balled. Original assessment cited as being less than twenty dollars. (uncertainty as to exact amount, since original developer's salesmen quoted various amounts.) Current assessment is $30.00 while development was in hands of receivers, the Homeowners organized, starting to collect assessments and banking them into a reserve fund. New developer picking up costs of maintenance (severe until Association can get enough members to carry this load, and still set aside healthy reserves. Developer is doing this at no penalty nor payback to Homeowners.

Problems: Original developer "blue-skied" the subdivision. Built sub-standard private streets, which the Association cannot afford to maintain nor pay taxes on, attempts to dedicate streets to City have failed, but efforts are not yet terminated. Original plan was to have entry gates, security guards and a multitude of other unaffordable luxuries on a less than $20.00 assessment. Homeowner morale is high, however, even in the face of increased assessments, and previous misrepresentation of original developer.

General summary:

Virtually every Association in the market was low-balled on assessments. Shoddy construction of homes as well as amenities abounds. Numbers of developers were unable to compete when market was glutted, and attempted to lower overhead any way possible. May Associations are strapped with developer originated debt either direct disbursement, or construction faults. Salesman misrepresentation is uniform. Some Homeowners were not even aware of the existance of protective covenants and restrictions. Many more were not aware of assessments until receiving billings. Only one or two builders in market which could be called reputable. Thousands of disgruntled Homeowners, dozens of Homeowners Associations which are doomed to failure because of Homeowner disinterest due to misrepresentations, and other financial problems.

Most Homeowners who have read Bill S. 2273 are renewing their interest in hoping that something can be done to prevent future exploitation of this most vulnerable market.

SAMUEL SHECHET
CERTIFIED PUBLIC ACCOUNTANT
FLORIDA / NEW YORK

1301 N. E. 191st STREET • NORTH MIAMI BEACH, FLORIDA 33162
PHONE 940-1935

October 14, 1975.

Honorable William Proxmire,
Chairman of the Finance Committee
of Housing & Urban Development,
United States Senate,
Washington, D.C.20510.

Dear Senator:-

I have read in the October 7, 1975 Wall Street Journal that you will collaborate with Secretary Carla A. Hills about new legislation for the sale of condominiums.

In Florida State, Condominium Law 711 was passed in 1974, which applies strictly to condominiums purchased after the enactment of this new law. It had no retroactive provisions.

Most older and retired folks came down from the North and other areas to Florida in years 1967 through 1974.

The condominiums sold in these period years were as follows:-

A one Bed Room Apartment 900' of space for $ 18,000.00

A two Bed Room Apartment 1200' of space for $ 26,000.00

A two Bed Room Apartment De Luxe 1500' space for $30,000.00.

The Developers realized at least $3000.00 to $5000.00 in profit on each apartment from each sale.

The Developers also made each purchaser sign a Sales Contract coupled with a 99 year lease where each apartment purchaser was compelled to pay the developer a monthly charge of about $25.00 per month for 99 year. To rub it in they made the lease with an escalator clause based upon a cost of living increase every five years, resulting in an almost 100% increase of the original monthly rental.

This was to pay for the elevator, the pool area and other miscellaneous common element areas, which certainly belonged to the purchaser, otherwise he could not use the premises.

The purchaser received no warranties of construction and since construction was of very poor quality, each apartment owner pays considerably for repairs and huge maintenance bills daily.

The purchaser also has to keep, maintain and handle the finance of the entire complex without any cost to the developer.

The developer made this exorbitant lease with himself as a director of a corporate association formed for each building, and assigned this onerous lease to a newly elected board of this owner association. The board of this owner association consisted of older men - and retired ones, who knew nothing of this fraud perpetrated by the developers.

Now, what can happen to such a deal? Every owner will eventually be compelled to give up the premises. He will not be able to sell it with such contingencies of liability. It will be a big loss to each, and every retired person who came down for some sunshine to Florida. After such losses the owners will certainly not recommend to anyone to purchase such premises with such losses. This does not recommend such housing which the country's economy needs very badly.

All this must be remedied by Federal or State legislation. A law must be passed to eliminate these leases, since the developer made huge gains on the sale of these apartments, and have already collected enough booty in these rentals on the fraudulent leases.

These are facts which you must take into consideration for enactment of new legislation.

Very truly yours,

Samuel Shechet

Andrew C. Weiss

CLEMATIS BUILDING - SUITE 600
208 CLEMATIS STREET
WEST PALM BEACH, FLORIDA 33401

October 9, 1975

TO: SENATOR LAWTON CHILES

FROM: ROD TENNYSON

COMMENTS -- FEDERAL CONDOMINIUM CONSUMER PROTECTION ACT OF 1975.

In reviewing the provisions of this proposed act, it appears that the general philosophy of the bill is to provide minimum standards for the states to impose in regulating construction of condominium developments. This concept provides the best protection with as little bureaucracy as possible. It would also appear that the consumer protection provisions of the Act are designed to require the developer, after building a project, to sell units in an honest manner, turn over control of the association to unit owners, and then exclude himself entirely from the operation of the condominium. The Act also prohibits the developer from continuing to extract long-range profits from a condominium through sweetheart contracts he negotiated with the association or unit owners while he still controlled such associations. The goals of the Act are desirable and needed in the regulation of condominiums. However, to achieve these goals, several recommendations and changes are suggested to plug any potential loophole which the developer may use to frustrate these general purposes.

The first definition in Section 2 that may need some revision is the definition of "condominium project". It is unclear from reading the definition of this phrase as to whether or not "condominium project" includes cooperative developments. Cooperative developments are very similar to condominiums except

that title to the unit is retained in the homeowners' association and the individual unit owner simply holds a leasehold interest in his unit. Section 711.42(8) of the Florida Condominium Act defines a cooperative to be "that form of ownership of improved property under which units are subject to ownership by one or more owners, which ownership is evidenced by a lease or other muniment of title or possession granted by the association as owner of the cooperative property". The definition of "condominium project" should probably be further refined to make it clear that cooperative living also comes under the provisions of this Act.

In subsection (7) of the definitional section, the term "leasehold condominium project" is defined. It is not clear whether this definition was designed to include co-ops as it could be interpreted to mean a condominium project located on a ninety-nine year leased plot of land. It is quite common in Florida for the developer to retain title to the land under the condominium project. He then negotiates a long-term lease to the condominium association with a rental provision that escalates with the cost of living. Of course, as unit owners purchase their condominium unit, title to their unit is subject to the long-term lease which they must pay through their association and which escalates each year with the cost of living. The land lease concept differs from a cooperative because in a cooperative, title to the land is actually held by a homeowners' association whereas in the land lease condominium complex, title to the land is still held by the developer which gives him opportunity to

extract long-term profits from the property for ninety-nine years. In my opinion, condominiums or cooperatives should not be allowed to be built unless fee simple title is held either in the homeowners' association or in each individual unit owner's name. If condominiums are to be built on leased land, then the Congress should at least prohibit the escalating rental payment contract provisions in the lease.

Another important definitional phrase is "common elements". This phrase is defined to mean areas of the condominium development to which unit owners receive "a right of exclusive use, enjoyment and access". The problem here is the use of the term "exclusive". Many developers today are setting up country clubs adjacent to the condominium development and requiring unit owners to pay a fee to become a member of this club as a condition for sale of the unit. However, the club is not an "exclusive" club and other citizens outside the condominium complex may use it. Therefore, since the club does not give "exclusive use, enjoyment and access", it would not fall under the definition of common element and would leave a potential loophole for developers. I would suggest the term "exclusive" be stricken from that definitional term.

In Section 5, National Standards for Consumer Protection, several other loopholes need to be closed. Subsection (4) allows reaffirmance of a developer contract, recreational lease or management contract by a vote of the unit owners in accordance with the association by-laws. The by-laws to the homeowners' association are written by the developer and many

times include provisions which allow amendment only by concurrence of the developer. It is conceivable the by-laws could contain provisions making it procedurally impossible for the unit owners to conduct a vote to throw out the developer's sweetheart contracts. Therefore, the term "by-laws" should be substituted with the phrase "rules of the Secretary".

Section 6, dealing with national standards for disclosure, covers most of the major disclosure items relevant to condominiums. However, at the time these disclosure requirements and state disclosure requirements are fitted into book form, a rather thick document emerges. The document is quite complicated and the disclosure provisions are not readily undersood by the average unit purchaser. Therefore, there should be a provision either in the disclosure section or the standards for consumer protection section requiring the developer, upon a potential purchaser's request, to offer a copy of the disclosures and other documents for a fee not to exceed his actual printing cost for the disclosure items. The potential buyer should be able to purchase these disclosures and documents without obligating himself to a contract for sale for the unit. This way the buyer may shop several developments, obtain the documents for a reasonable cost, and arrange an appointment with his attorney to review the various documents to advise him on pros and cons of the various developments he has shopped. With this requirement, the unit owner is not under any time restraints, such as the fifteen day cancellation provision under Florida law, and is allowed much more time to retain

counsel and get an expert opinion on exactly what he is getting into.

There may be some constitutional problems with Section 13(c), Rules, Regulations and Orders, which gives the Secretary rule-making power without adequate standards. Perhaps this subsection should be re-written as follows:

> "(c) In addition to the standards contained in this Act, the Secretary may, after notice and opportunity for public comment, prescribe additional disclosures to further inform the condominium purchaser of all elements of the condominium sale."

State of Wisconsin \ GOVERNOR'S COUNCIL FOR CONSUMER AFFAIRS

1975 Patrick J. Lucey
Governor FM 2:34

Martin J. Schreiber, Lieutenant Governor
Chairman

MADISON, WISCONSIN 53703
PHONE (608) 266-3104
V29E, Capitol

November 20, 1975

The Honorable William Proxmire
Chairman
Senate Committee on Banking, Housing and Urban Affairs
Washington, D.C. 20510

Dear Senator Proxmire:

On behalf of the Governor's Council for Consumer Affairs, I appreciate this opportunity to express my feelings on the issues raised by Senate Bill 2273 regulating the sale of condominiums. I have reviewed the bill and I am pleased to express my support for it.

Condominium development has gotten off to a slow start in Wisconsin; however, I do not expect it will remain that way much longer. The value of real estate and the cost of all the things associated with home construction and ownership have increased so rapidly that the single family home may become available only for the rich.

An example from a recent report prepared by the Milwaukee Tax Commissioner's office serves to highlight that problem. The report refers specifically to a one-story frame home on the city's north side which sold for $17,500 in 1963. It changed hands several times and finally was sold again in July of 1973 for $34,900, an increase of 145% in only ten years.

In that same period, all the costs associated with maintaining that home also went up. Interest rates on home mortgages are about 50% higher than they were in 1963. Insurance rates have doubled. Taxes are up. Utility rates are up. Building costs are up. In short, everything costs more and, in many cases much more. People of limited means are facing the fact that they simply cannot afford the home they had planned on purchasing.

For an increasing number of people, condominiums are providing an alternative. The Milwaukee Tax Commissioner's report gives the example of a developer who turned a tract of three bedroom townhouses he owned into a condominium which he then offered for sale to his tenants. After figuring their income tax savings, the tenants were able to buy the same units they had rented for a total cost of $85 per month lower than they had been paying in rent. The same developer turned a 16-unit apartment building into a condominium which he again offered for sale to his tenants. Their total cost went from $185 per month to less than $140. Obviously, for

some, condominiums are an excellent opportunity.

But it would be foolish for us to sing the praises of condominiums without taking note, as well, of the widespread reports of problems and serious abuses. We who are involved in consumer protection are particularly concerned about those who might well bear the brunt of such problems. For condominiums appeal particularly to singles and young marrieds who are looking for their first home and to those who are at or near retirement age and looking for their last. It's tragic that those to whom condominiums are particularly appealing are also those who, because of limited financial resources, are least able to cope with the consequences of a financial mistake.

I find Senate Bill 2273 is thorough and direct in establishing minimum standards for condominium development while leaving states the option of refining its provisions to meet their own particular needs. I think it is a good bill which, if enacted into law, should benefit the developer as well as the consumer. For with the assurance that he will receive fair treatment, I am certain the consumer will be more likely to consider the condominium a sound investment. That perception will be good for all concerned.

Yours very truly,

Martin J. Schreiber

Martin J. Schreiber
Lieutenant Governor

MJS:hj

Florida Home Builders Association

P.O.BOX 1259 · TALLAHASSEE, FLORIDA 32302 · TELEPHONE (904) 224-4316

October 14, 1975

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President

United States Senate Committee
on Banking, Housing and Urban Affairs
Senate Office Building
Washington, DC 20001

Gentlemen:

We have in our possession a copy of testimony given your committee by Hunter W. Wolcott on October 8, 1975, relating to S. 2273, the Condominium Consumer Protection Act of 1975.

Please be advised that Florida Home Builders Association, a statewide organization of approximately 5,000 company members and representing well over 200,000 employees in the residential construction industry in Florida did not authorize Hunter W. Wolcott to represent us on this matter.

This association in a statewide meeting just concluded on Marco Island (in south Florida) adopted a resolution opposing S. 2273 for the reason that it is our belief that S. 2273 would be harmful in an area that is and should be a matter of state responsibility.

Florida has a good law regulating condominium and cooperative apartments. The legislature and the industry have worked cooperatively on perfecting this law over the past few years and we now feel that it is more than adequate to meet the needs. And with our annual legislative sessions and administrative regulatory body we can move to correct any situation much more rapidly than could the United States Congress.

Additionally, this association's Executive Director testified as to this association's opposition to the federal government becoming involved in the regulation of condominiums during the HUD hearings in south Florida earlier this year.

We thank you for allowing us to clarify our position in this matter.

Yours very truly,

John J. Koelemij

John J. Koelemij
Chairman, Governmental Affairs Committee
for the Board of Directors

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