Case No. 69399 c/w 70478

IN THE SUPREME COURT OF NEVADA

FREDERIC AND BARBARA ROSENBERG LIVING TRUST, Appellant/Cross-Respondent, vs. MACDONALD HIGHLANDS REALTY, LLC, a Nevada Limited Liability Company; MICHAEL DOIRON, an Individual; and FHP VENTURES, a Nevada Limited Partnership, Respondent/Cross-Appellants.	Electronically Filed Oct 12 2016 01:02 p.m. Elizabeth A. Brown Clerk of Supreme Court
FREDERIC AND BARBARA ROSENBERG LIVING TRUST, Appellant, vs. SHAHIN SHANE MALEK, Respondent.	

APPEAL

from the Eighth Judicial District Court, Clark County
The Honorable KENNETH CORY, District Judge
District Court Case No. District Court Case No. A-13-689113-C

JOINT APPENDIX VOLUME 11

Respectfully submitted by:

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project at the foreclosure sale solely for the purpose of subsequent resale. It permits a foreclosing lender to undertake such a transaction without incurring the full burden of declarant obligations and liabilities. At the same time, the provision recognizes the need for continuing operation of the association and, to that end, permits a foreclosing lender to assume control of the association for the purpose of ensuring a smooth transition.

Third, paragraph (3) of subsection (e) provides that a successor who has only the right to maintain model units, sales offices, and signs does not thereby become subject to any obligations or liabilities as a declarant, except for the obligation to provide a public offering statement and any liability resulting therefrom. This provision also is designed to protect mortgage lenders and contemplates the situation where a lender takes over a project and desires to sell out existing units without making any additional improvements to the project. This provision facilitates such a transaction by relieving the mortgage lender, in that instance, from the full burden of obligations and liabilities ordinarily imposed upon a declarant under the Act.

Under Section 2-110, a declarant may reserve the right to create additional units in portions of a common interest community which were originally designated as common elements, even though, in a condominium, rights of unit owners have otherwise attached to the common elements, and even though, in a planned community or cooperative, the common elements have been conveyed to the association. The declarant, upon creation, becomes the owner of any units created. The right to create the units is an interest in land which may be sold or in which a security interest may be granted. If the mortgagee of that interest forecloses, the purchaser at the foreclosure sale has the choices concerning development rights and resulting liability which are described in the preceding paragraph. That is, under subsections (c) and (d), the purchaser may limit his liability by agreeing to hold the developments only for the purpose of transfer as provided by paragraph (e)(4) or may buy the rights under paragraph (c).

SECTION 3-105. TERMINATION OF CONTRACTS AND LEASES.

(a) Within two years after the executive board elected by the unit owners pursuant to Section 3-103(f) takes office, the association may terminate without penalty, upon not less than [90] days' notice to the other party, any of the following if it was entered into before the executive board was elected:

(1) any management, maintenance, operations, or employment contract, or lease of recreational or parking areas or facilities; or

(2) any other contract or lease between the association and a declarant or an affiliate of a declarant;

(b) The association may terminate without penalty, at any time after the executive board

elected by the unit owners pursuant to Section 3-103(f) takes office upon not less than [90] days' notice to the other party, any contract or lease that is not bona fide or was unconscionable to the unit owners at the time entered into.

(c) This section does not apply to:

(1) any lease the termination of which would terminate the common interest community or reduce its size, unless the real estate subject to that lease was included in the common interest community for the purpose of avoiding the right of the association to terminate a lease under this section; or

(2) a proprietary lease.

Comment

1. This section deals with a common problem in the development of condominium, planned community, and cooperative projects: the temptation on the part of the developer, while in control of the association, to enter into, on behalf of the association, long-term contracts and leases with himself or with an affiliated entity.

The Act deals with this problem in two ways. First, Section 3-103(a) imposes upon all executive board members appointed by the declarant liability as fiduciaries of the unit owners for all of their acts or omissions as members of the board. Second, Section 3-105 provides for the termination of certain contracts and leases made during a period of declarant control.

2. In addition to contracts or leases made by a declarant with himself or with an affiliated entity, there are also certain contracts and leases so critical to the operation of the common interest community and to the unit owners' full enjoyment of their rights of ownership that they too should be voidable by the unit owners upon the expiration of any period of declarant control. At the same time, a statutorily-sanctioned right of cancellation should not be applicable to all contracts or leases which a declarant may enter into in the course of developing a project. For example, a commercial tenant would not be willing to invest substantial amounts in equipment and other improvements for the operation of his business if the lease could unilaterally be canceled by the association. Accordingly, this section provides that (subject to the exception set forth in the last sentence thereof), upon the expiration of any period of declarant control, the association may terminate without penalty, any "critical" contract (i.e., any management contract, employment contract, or lease of recreational or parking areas or facilities) entered into during a period of declarant control, any contract or lease to which the declarant or an affiliate of the declarant is a party, or any contract or lease previously entered into by the declarant which is not bona fide or which was unconscionable to the unit owners at the time entered into under the circumstances then prevailing.

3. The last sentence of the section addresses the usual leasehold common interest community situation where the underlying real estate is subject to a long-term ground lease.

Because termination of the ground lease would terminate the community, this sentence prevents cancellation. However, in order to avoid the possibility that recreation and other leases otherwise cancelable under subsection (a) will be restructured to come within the exception, a subjective test of "intent" is imposed. Under the test, if a declarant's principal purpose in subjecting the leased real estate to the common interest community was to prevent termination of the lease, the leave may nevertheless be terminated.

4. The 1994 amendment to this section tracks the greater flexibility given declarants of nonresidential common interest communities in Section 1-207.

5. The 2008 amendments contain two significant amendments in this section, one that limits the rights of unit owners to cancel declarant-imposed contracts to a two-year period, and a second that significantly expands the variety of contracts subject to cancellation during that two year period.

The first amendment limits the association's cancellation right to the 2 year period that begins when the unit owners assume control of the association. As drafted, contracts not cancelled during that 2 year period would become non-cancelable and presumably enforceable in accordance with their terms, subject to the rules of unconscionability in section 1-112 and in subsection (c) of this section. The drafters concluded that, on balance, associations are better served by the ability of third parties to rely on the enforceability of contracts between themselves and the associations if the association's right to unilaterally cancel those contracts was subject to a reasonable outer limit of two years after the time the independent directors assumed office.

The two year limit seems especially appropriate since the 2008 amendments considerably increase the types of enumerated contracts that are subject to cancellation, to include maintenance and operations contracts, regardless of whether those contracts were entered into with the declarant or an independent third party.

Finally, the two year limitation on the power to cancel contracts does not apply to contracts that were not "bona fide" at the time entered into, or were unconscionable. This preserves the rule as it existed in earlier versions of the Act, and is consistent with Section 1-112.

SECTION 3-106. BYLAWS.

(a) The bylaws of the association must:

(1) provide the number of members of the executive board and the titles of the officers of the association;

(2) provide for election by the executive board or, if the declaration requires, by the unit owners, of a president, treasurer, secretary, and any other officers of the association the bylaws specify;

(3) specify the qualifications, powers and duties, terms of office, and manner of electing and removing executive board members and officers and filling vacancies;

(4) specify the powers the executive board or officers may delegate to other persons or to a managing agent;

(5) specify the officers who may prepare, execute, certify, and record amendments to the declaration on behalf of the association;

(6) specify a method for the unit owners to amend the bylaws;

(7) contain any provision necessary to satisfy requirements in this [act] or the declaration concerning meetings, voting, quorums, and other activities of the association; and

(8) provide for any matter required by law of this state other than this [act] to appear in the bylaws of organizations of the same type as the association.

(b) Subject to the declaration and this [act], the bylaws may provide for any other necessary or appropriate matters, including matters that could be adopted as rules.

Comment

1. Because the Act does not require the recordation of bylaws, it is contemplated that unrecorded bylaws will set forth only matters relating to the internal operations of the association and various "housekeeping" matters with respect to the common interest community. The Act requires specific matters to be set forth in the recorded declaration and not in the bylaws, unless the bylaws are to be recorded as an exhibit to the declaration.

2. The requirement, set forth in subsection (a)(5), that the bylaws designate which of the officers of the association has the responsibility to prepare, execute, certify, and record amendments to the declaration reflects the obligation imposed upon the association by several provisions of this Act to record such amendments in certain circumstances. These provisions include Section 1-107 (Eminent Domain), Section 2-106 (expiration of certain leases), Section 2-112 (Relocation of Boundaries Between Adjoining Units), and Section 2-113 (subdivision or conversion of units). Section 2-117(e) provides that, if no officer is designated for this purpose, it shall be the duty of the president.

3. By deleting the words "if any," in sub-section (4) in 2008, the drafters did not intend a substantive change. As re-drafted, the Act does not require the Board to delegate any of its powers.

4. The Act does not prevent the bylaws from permitting the executive board to delegate all its powers to a manager or to another entity. Whether or not such a delegation were to take place, the law of principal and agent would apply to that relationship, and the executive board would remain responsible for fulfillment of its duties imposed under this Act.

5. As the definition of the term "bylaws" makes clear, the bylaws are intended to address procedural matters affecting the governance of the association. They are not intended to contain matters that might affect title to real property nor any of the covenants restricting the use of the units or the common property. That is one of the primary reasons why the Act requires that the declaration be recorded on the land records, while the bylaws need not be recorded.

6. The bylaws might include a broad range of qualifications for directors and officers. This Act neither imposes constraints on what these qualifications might be or mandates any such qualifications, other than the requirement that, after the period of declarant control ends, a majority of directors must be unit owners. Other law, of course, such as laws prohibiting various forms of discrimination, may independently impose limits on permissible qualifications.

7. The 2008 amendment to Section 3-106(a)(6) requires the bylaws to state a method by which the unit owners may amend the bylaws. This provision complements the new text in Section 3-102 (b) that precludes the executive board from amending the bylaws.

SECTION 3-107. UPKEEP OF COMMON INTEREST COMMUNITY.

(a) Except to the extent provided by the declaration, subsection (b), or Section 3-113(h), the association is responsible for maintenance, repair, and replacement of the common elements, and each unit owner is responsible for maintenance, repair, and replacement of his unit. Each unit owner shall afford to the association and the other unit owners, and to their agents or employees, access through his unit reasonably necessary for those purposes. If damage is inflicted on the common elements or on any unit through which access is taken, the unit owner responsible for the damage, or the association if it is responsible, is liable for the prompt repair thereof.

(b) In addition to the liability that a declarant as a unit owner has under this [act], the declarant alone is liable for all expenses in connection with real estate subject to development rights. No other unit owner and no other portion of the common interest community is subject to a claim for payment of those expenses. Unless the declaration provides otherwise, any income or proceeds from real estate subject to development rights inures to the declarant.

(c) In a planned community, if all development rights have expired with respect to any real estate, the declarant remains liable for all expenses of that real estate unless, upon expiration, the declaration provides that the real estate becomes common elements or units.

Comment

1. The Act permits the declaration to separate maintenance responsibility from ownership. This is commonly done in practice. In the absence of any provision in the declaration, maintenance responsibility follows ownership of the unit or rests with the association in the case of common elements. Under this Act, limited common elements (which might include, for example, patios, balconies, and parking spaces) are common elements. See Section 1-103(19). As a result, under subsection (a), unless the declaration provides that unit owners are responsible for the upkeep of such limited common elements, the association will be responsible for their maintenance. Under Section 3-115(c), the cost of maintenance, repair, and replacement for such limited common elements is assessed against all the units in the common interest community, unless the declaration provides for such expenses to be paid only by the units **benefitted**. See Comment 1 to Section 2-108.

2. Under Section 2-110, a declarant may reserve the right to create units in portions of the common interest community originally designated as common elements. However, under Section 3-107(b), the developer is obligated to pay all of the expenses of (including real estate taxes properly apportionable to) that real estate even though, in the case of a planned community or cooperative, it has been conveyed to the association. As to real estate taxes, see Section 1-105(c).

SECTION 3-108. MEETINGS.

(a) The following requirements apply to unit owner meetings:

(1) An association shall hold a meeting of unit owners annually at a time, date, and place stated in or fixed in accordance with the bylaws.

(2) An association shall hold a special meeting of unit owners to address any matter affecting the common interest community or the association if its president, a majority of the executive board, or unit owners having at least 20 percent, or any lower percentage specified in the bylaws, of the votes in the association request that the secretary call the meeting. If the association does not notify unit owners of a special meeting within 30 days after the requisite number or percentage of unit owners request the secretary to do so, the requesting members may directly

notify all the unit owners of the meeting. Only matters described in the meeting notice required by paragraph (3) may be considered at a special meeting.

(3) An association shall notify unit owners of the time, date, and place of each annual and special unit owners meeting not less than 10 days or more than 60 days before the meeting date. Notice may be by any means described in Section 3-121 The notice of any meeting must state the time, date and place of the meeting and the items on the agenda, including:

(A) a statement of the general nature of any proposed amendment to the declaration or bylaws;

(B) any budget changes; and

(C) any proposal to remove an officer or member of the executive board.

(4) The minimum time to give notice required by paragraph (3) may be reduced or waived for a meeting called to deal with an emergency.

(5) Unit owners must be given a reasonable opportunity at any meeting to comment regarding any matter affecting the common interest community or the association.

(6) The declaration or bylaws may allow for meetings of unit owners to be conducted by telephonic, video, or other conferencing process, if the alternative process is consistent with subsection (b)(7).

(7) Except as otherwise provided in the bylaws, meetings of the association must be conducted in accordance with the most recent edition of Roberts' Rules of Order Newly Revised.

(b) The following requirements apply to meetings of the executive board and committees of the association authorized to act for the association:

(1) Meetings must be open to the unit owners except during executive sessions. The executive board and those committees may hold an executive session only during a regular or special meeting of the board or a committee. No final vote or action may be taken during an

executive session. An executive session may be held only to:

(A) consult with the association's attorney concerning legal matters;

(B) discuss existing or potential litigation or mediation, arbitration, or administrative proceedings;

(C) discuss labor or personnel matters;

(D) discuss contracts, leases, and other commercial transactions to purchase or provide goods or services currently being negotiated, including the review of bids or proposals, if premature general knowledge of those matters would place the association at a disadvantage; or

(E) prevent public knowledge of the matter to be discussed if the executive board or committee determines that public knowledge would violate the privacy of any person.

(2) For purposes of this section, a gathering of board members at which the board members do not conduct association business is not a meeting of the executive board. The executive board and its members may not use incidental or social gatherings of board members or any other method to evade the open meeting requirements of this section.

(3) During the period of declarant control, the executive board shall meet at least four times a year. At least one of those meetings must be held at the common interest community or at a place convenient to the community. After termination of the period of declarant control, all executive board meetings must be at the common interest community or at a place convenient to the community unless the unit owners amend the bylaws to vary the location of those meetings.

(4) At each executive board meeting, the executive board shall provide a reasonable opportunity for unit owners to comment regarding any matter affecting the common interest community and the association.

(5) Unless the meeting is included in a schedule given to the unit owners or the meeting is called to deal with an emergency, the secretary or other officer specified in the bylaws

shall give notice of each executive board meeting to each board member and to the unit owners. The notice must be given at least 10 days before the meeting and must state the time, date, place, and agenda of the meeting.

(6) If any materials are distributed to the executive board before the meeting, the executive board at the same time shall make copies of those materials reasonably available to unit owners, except that the board need not make available copies of unapproved minutes or materials that are to be considered in executive session.

(7) Unless the declaration or bylaws otherwise provide, the executive board may meet by telephonic, video, or other conferencing process if:

(A) the meeting notice states the conferencing process to be used and provides information explaining how unit owners may participate in the conference directly or by meeting at a central location or conference connection; and

(B) the process provides all unit owners the opportunity to hear or perceive the discussion and to comment as provided in paragraph (4).

(8) After termination of the period of declarant control, unit owners may amend the bylaws to vary the procedures for meetings described in paragraph (7).

(9) Instead of meeting, the executive board may act by unanimous consent as documented in a record authenticated by all its members. The secretary promptly shall give notice to all unit owners of any action taken by unanimous consent. After termination of the period of declarant control, the executive board may act by unanimous consent only to undertake ministerial actions or to implement actions previously taken at a meeting of the executive board.

(10) Even if an action by the executive board is not in compliance with this section, it is valid unless set aside by a court. A challenge to the validity of an action of the executive board for failure to comply with this section may not be brought more than [60] days after the minutes of

the executive board of the meeting at which the action was taken are approved or the record of that action is distributed to unit owners, whichever is later.

Comment

1. Original Section 3-108 was significantly amended and reorganized in 2008. New subsection (a) imposes a variety of requirements dealing exclusively with unit owner meetings, while subsection (b) contains new "open meeting" requirements for executive board meetings and meetings of committees which are authorized to act for the Board. Importantly, this section will apply to all common interest communities in the adopting state, including "old" communities created before the effective date of the Act, by virtue of Section 1-204 (a)(13).

In addition to style changes in the previous 3-108, subsection (a) creates several new provisions designed to enhance unit owner participation in unit owner meetings. For example, paragraph (a)(5) requires that unit owners be provided the opportunity to address the executive board during each meeting of the unit owners. While this provision is an important part of the democratization process in community associations, it is implicit that the officers and executive board members have the inherent right to establish reasonable controls over the behavior of unit owners during the meetings. Thus, for example, the board could prevent unit owners from interrupting the regular conduct of business and the time of other speakers, and could, as well, set reasonable limits on the number of speakers at any one meeting, the repetitiveness of unit owner comments, and the aggregate time that unit owners may consume during the meeting.

2. Subsection (a)(2) provides that, with respect to special meetings of the unit owners, "only matters described in the meeting notice...may be considered at" that meeting The purpose of limiting the agenda of a special meeting to the subjects identified in the notice is to allow a member, who has no concern about the items listed in the notice, to decide not to attend the meeting, secure in the knowledge that other topics cannot be raised and voted on without his or her knowledge. A generic heading such as "New Business" would not be sufficient to permit items to be taken up if they were not otherwise described in the notice. In contrast, of course, at an annual meeting, unit owners are entitled to consider any matter, whether or not on an agenda.

3. Subsection (a)(3) continues to detail the procedures and minimum content of the notice sent to unit owners. Importantly, the notice must contain "a statement of the general nature of any proposed amendment to the declaration or bylaws," rather than containing the precise text of any proposed amendment. Thus, the unit owners are entitled to make germane amendments to whatever text is proposed at the meeting; they are not bound to a "yes" or "no" vote on text fixed in that notice.

4. The 2008 amendments acknowledge in several places that the "town meeting" model for unit owner meetings - where only those persons physically present at a meeting of unit owners may vote - is no longer suited to a considerable number of communities, particularly larger communities and communities made up largely of second homes. While the Act has always contemplated the possibility of proxy voting, see, e.g., Section 3-110 (c), this section greatly expands the available procedures for voting, to include absentee ballots and voting without a meeting by electronic means or paper ballots; see Section 3-110(a) and (d). In addition, Section 3-108(a)(6) contemplates that the

declaration or bylaw may provide for unit owners to "meet" "by telephonic, video or other conferencing method...."

5. Subsection (a)(7) provides that meetings of the association must be conducted in accordance with Robert's Rules of Order unless the bylaws otherwise provide. As a consequence of this default rule, it was not necessary for this Act to address a range of procedural issues and, in the normal situation, it will be unnecessary for the association to adopt detailed meeting procedures, either in the bylaws or in separate rules.

By way of example, we might assume that a regularly scheduled unit owners' meeting was properly noticed and held, but that a quorum was not present. In that case, the procedural issue is presented as to whether that meeting might be recessed in these circumstances to enable solicitation of more attendance, or proxies, in order to conduct business. The statute might be drafted to address the issue, either directly or by requiring the bylaws to address it. The default rule of relying on Robert's Rules, however, completely resolves the issue, by expressly permitting a recess in these circumstances. See Robert's Rules of Order Newly Revised (10th ed. 2000) at 336-37.

Of course, it may be that the board of an association may prefer a more simplified set of meeting procedures. The bylaws could be amended to adopt such procedure, and many models are available. See, e.g., Nagle, Meetings and Elections: How Community Associations Exercise Democracy (CAI Press, 2005).

6. Subsection (b) sets out an entirely new set of "open meeting" requirements for meetings of the executive board and committees to which the board has delegated authority. The provisions are generally consistent with several existing state statutes; see, e.g., Virginia Stat. Ann. § 55-510.1. The highlights of the section are these:

First, the section provides generally that all meetings of the executive committee (except executive sessions) must be open to unit owners. To make this right meaningful, the section requires that unit owners be given notice of those meetings, access to the same materials provided to members of the executive board, and the right to speak at executive board meetings.

Second, while the executive board may meet in executive session, the purposes for which such meetings may be held, and the permissible outcomes of those meetings are considerably limited. Such sessions may only be held in conjunction with a regular or special meeting of the executive board (and therefore noticed to unit owners); no final vote or action may be taken during an executive session; and the purposes for which an executive session may be held are considerably circumscribed.

Third, the Act provides that the board and its members "may not use incidental or social gatherings of board members or any other method to evade" the open meeting requirements of this section.

Fourth, the Act mandates that the executive board meet at least four times a year, and that those meetings "must be at" or "at a place convenient to" the common interest community.

Fifth, while the executive board may meet telephonically, by video or other conferencing method, it may only do so if unit owners have a means to participate in that conference and hear or perceive the proceedings.

Sixth, while the executive board may act without a meeting by unanimous written consent - a procedure uniformly allowed by all corporate statutes - they may do so after the period of declarant control "only to undertake ministerial actions or to implement actions previously taken at a meeting of the executive board."

7. Subsection (b)(5) does provide that the need for notice to unit owners of executive board meetings may be avoided in the event of an "emergency". While the Act does not define that term, the concept plainly includes the notion of "immediate irreparable harm" or other circumstances where the board must act promptly to either avoid an adverse outcome or avoid failing to take advantage of an opportunity. "Emergency" includes the further notion that there is insufficient time from the time the issue came to the attention of the directors to give complete notice to owners.

8. Subsection (b)(10) seeks to strike a balance between the open meeting requirements of subsection (b) and the legitimate expectations of third parties who may rely on the action of an executive board that, in hindsight, was taken without complying with the notice or other constraints imposed on executive board actions by this section. Under this section, a decision of the executive board will be insulated from challenge because of defective notice to unit owners or other failure if the challenge is not brought within 60 days after the minutes of the executive board at which the action is taken are distributed, or those minutes are approved, whichever is later.

SECTION 3-109. QUORUM.

(a) Unless the bylaws otherwise provide, a quorum is present throughout any meeting of the unit owners if persons entitled to cast [20] percent of the votes in the association:

(1) are present in person or by proxy at the beginning of the meeting;

(2) have cast absentee ballots solicited in accordance with Section 3-110 (c)(4) which have been delivered to the secretary in a timely manner; or

(3) are present by any combination of paragraphs (1) and (2).

(b) Unless the bylaws specify a larger number, a quorum of the executive board is present for purposes of determining the validity of any action taken at a meeting of the executive board only if individuals entitled to cast a majority of the votes on that board are present at the time a vote regarding that action is taken. If a quorum is present when a vote is taken, the affirmative vote of a

majority of the board members present is the act of the executive board unless a greater vote is required by the declaration or bylaws.

(c) Except as otherwise provided in the bylaws, meetings of the association must be conducted in accordance with the most recent edition of Roberts' Rules of Order Newly Revised.

Comment

Mandatory quorum requirements lower than 50 percent for meetings of the association are often justified because of the common difficulty of inducing unit owners to attend meetings. The problem is particularly acute in the case of resort common interest communities where many owners may reside elsewhere, often at considerable distances, for most of the year.

SECTION 3-110. VOTING; PROXIES; BALLOTS.

(a) Unless prohibited or limited by the declaration or bylaws, unit owners may vote at a meeting in person, by absentee ballot pursuant to subsection (b)(4), by a proxy pursuant to subsection (c) or, when a vote is conducted without a meeting, by electronic or paper ballot pursuant to subsection (d).

(b) At a meeting of unit owners the following requirements apply:

(1) Unit owners who are present in person may vote by voice vote, show of hands, standing, or any other method for determining the votes of unit owners, as designated by the person presiding at the meeting.

(2) If only one of several owners of a unit is present, that owner is entitled to cast all the votes allocated to that unit. If more than one of the owners are present, the votes allocated to that unit may be cast only in accordance with the agreement of a majority in interest of the owners, unless the declaration expressly provides otherwise. There is majority agreement if any one of the owners casts the votes allocated to the unit without protest being made promptly to the person presiding over the meeting by any of the other owners of the unit.

(3) Unless a greater number or fraction of the votes in the association is required by

this [act] or the declaration, a majority of the votes cast determines the outcome of any action of the association.

(4) Subject to subsection (a), a unit owner may vote by absentee ballot without being present at the meeting. The association promptly shall deliver an absentee ballot to an owner that requests it if the request is made at least [three] days before the scheduled meeting. Votes cast by absentee ballot must be included in the tally of a vote taken at that meeting.

(5) When a unit owner votes by absentee ballot, the association must be able to verify that the ballot is cast by the unit owner having the right to do so.

(c) Except as otherwise provided in the declaration or bylaws, the following requirements apply with respect to proxy voting:

(1) Votes allocated to a unit may be cast pursuant to a directed or undirected proxy duly executed by a unit owner.

(2) If a unit is owned by more than one person, each owner of the unit may vote or register protest to the casting of votes by the other owners of the unit through a duly executed proxy.

(3) A unit owner may revoke a proxy given pursuant to this section only by actual notice of revocation to the person presiding over a meeting of the association.

(4) A proxy is void if it is not dated or purports to be revocable without notice.

(5) A proxy is valid only for the meeting at which it is cast and any recessed session of that meeting.

(6) A person may not cast undirected proxies representing more than [15] percent of the votes in the association.

(d) Unless prohibited or limited by the declaration or bylaws, an association may conduct a vote without a meeting. In that event, the following requirements apply:

(1) The association shall notify the unit owners that the vote will be taken by ballot.

(2) The association shall deliver a paper or electronic ballot to every unit owner entitled to vote on the matter.

(3) The ballot must set forth each proposed action and provide an opportunity to vote for or against the action.

(4) When the association delivers the ballots, it shall also:

(A) indicate the number of responses needed to meet the quorum requirements;

(B) state the percent of votes necessary to approve each matter other than election of directors;

(C) specify the time and date by which a ballot must be delivered to the association to be counted, which time and date may not be fewer than [three] days after the date the association delivers the ballot; and

(D) describe the time, date, and manner by which unit owners wishing to deliver information to all unit owners regarding the subject of the vote may do so.

(5) Except as otherwise provided in the declaration or bylaws, a ballot is not revoked after delivery to the association by death or disability or attempted revocation by the person that cast that vote.

(6) Approval by ballot pursuant to this subsection is valid only if the number of votes cast by ballot equals or exceeds the quorum required to be present at a meeting authorizing the action.

(e) If the declaration requires that votes on specified matters affecting the common interest community be cast by lessees rather than unit owners of leased units:

(1) this section applies to lessees as if they were unit owners;

(2) unit owners that have leased their units to other persons may not cast votes on

those specified matters; and

(3) lessees are entitled to notice of meetings, access to records, and other rights respecting those matters as if they were unit owners.

(f) Unit owners must also be given notice of all meetings at which lessees are entitled to vote.

(g) Votes allocated to a unit owned by the association must be cast in any vote of the unit owners in the same proportion as the votes cast on the matter by unit owners other than the association.

Comment

1. Subsection (c) (e) addresses an increasingly important matter in the governance of common interest communities: the role of tenants occupying units owned by investors or other persons. Most present statutes require voting by owners in the association. However, it may be desirable to give lessees, rather than lessors, of units the right to vote on issues involving day-today operation both because the lessees may have a greater interest than the lessors and because it is desirable to have lessees feel they are an integral part of the common interest community.

2. The 1994 version of the Uniform Common Interest Ownership Act did not contain any provision by which unit owners may cast ballots except during a physical meeting of the unit owners. As discussed in the comments to Section 3-108, the 2008 amendments significantly alter that outcome, and offer a very broad range of voting options.

The current text incorporates both existing and proposed laws from a significant number of states' corporate and common interest community statutes, as well as existing provisions of the Model Non-Stock Corporation Act, and proposed amendments to that model act that were pending at the time this Act was promulgated.

3. In the case of new Section 3-110 (d), permitting voting by ballot without the need for a meeting, the Act borrows significantly from Florida statutes governing the election of directors of the unit owners association; see Fla. Gen. Stat. 718.112 (Bylaws) (2)(d)2, 3.

4. Proxy voting has been the subject of some controversy in the states, primarily as a consequence of some unit owners seeking to collect very large numbers of undirected proxies to be cast at meetings where contested matters are to be voted on. While the declaration and bylaws may impose further restrictions on proxy voting, the 2008 amendments impose only two: subsection (c)(5) limits the validity of proxy only to the meeting at which it is cast; and (c)(6) limits the proxies that any one person may cast to a percent set by statute.

5. New subsection (g) confirms that votes allocated to units owned by the association will be counted towards the quorum for any meeting, but will otherwise not affect the outcome of the voting by other unit owners.

SECTION 3-111. TORT AND CONTRACT LIABILITY; TOLLING OF LIMITATION PERIOD.

(a) A unit owner is not liable, solely by reason of being a unit owner, for an injury or damage arising out of the condition or use of the common elements. Neither the association nor any unit owner except the declarant is liable for that declarant's torts in connection with any part of the common interest community which that declarant has the responsibility to maintain.

(b) An action alleging a wrong done by the association, including an action arising out of the condition or use of the common elements, may be maintained only against the association and not against any unit owner. If the wrong occurred during any period of declarant control and the association gives the declarant reasonable notice of and an opportunity to defend against the action, the declarant who then controlled the association is liable to the association or to any unit owner for all tort losses not covered by insurance suffered by the association or that unit owner, and all costs that the association would not have incurred but for a breach of contract or other wrongful act or omission. Whenever the declarant is liable to the association under this section, the declarant is also liable for all expenses of litigation, including reasonable attorney's fees, incurred by the association.

(c) Except as provided in Section 4-116(d) with respect to warranty claims, any statute of limitation affecting the association's right of action against a declarant under this [act] is tolled until the period of declarant control terminates. A unit owner is not precluded from maintaining an action contemplated by this section because he is a unit owner or a member or officer of the association. Liens resulting from judgments against the association are governed by Section

3-117.

Comment

1. This section provides that any action in tort or contract arising out of acts or omissions of the association shall be brought against the association and not against the individual unit owners. This changes the law in States where plaintiffs are forced to name individual unit owners as the real parties in interest to any action brought against the association. The subsection also provides that a unit owner is not precluded from bringing an action in tort or contract against the association solely because he is a unit owner or a member or officer of the association.

2. In recognition of the practical control that can (and in most cases will) be exercised by a declarant over the affairs of the association during any period of declarant control permitted pursuant to Section 3-103, subsection (a) provides that the association or any unit owner has a right of action against the declarant for any losses (including both payment of damages and attorneys' fees) suffered by the association or any unit owner as a result of an action based upon a tort or breach of contract arising during any period of declarant control. To assure that the decision to bring such an action can be made by an executive board free from the influence of the declarant, the subsection also provides that any statute of limitations affecting such a right of action by the association shall be tolled until the expiration of any period of declarant control.

3. If a suit based on a claim which accrued during the period of developer control is brought against the association after control of the association has passed from the developer, reasonable notice to, and grant of an opportunity to the developer to defend, are conditions to developer liability. If, however, suit is brought against the association while the developer is still in control, obviously the developer cannot later resist a suit by the association for reimbursement on the grounds of failure to notify.

4. This draft makes clear what the drafters of the Uniform Condominium Act and the first version of this Act intended: that the form in which common elements are owned – whether in a condominium, planned community or cooperative – should not impose joint and several personal liability on condominium owners, when no such liability exists for owners in planned communities. Thus, the 1994 amendment to Section 3-111(a) rejects the decision in Ruoff v. Harbor Creek Community Association, 10 Cal.App.4th 1624, 13 Cal. Rptr 2d 755 (Cal.App. 1992). Rather, the result under both this section and Section 3-117 – which imposes liability on unit owners for unsatisfied judgments against the association in proportion to their common expense liabilities – is consistent with the decision in Dutcher v. Owens, 647 S.W.2d 948 (Texas 1983).

5. The 1994 amendment to new subsection (b) of this section makes clear that no period of limitation regarding an association's claim against the declarant, including a limit appearing in this or any other section of this Act, begins to run against the association until the period of declarant control terminates. This would include warranty claims for common elements arising under Section 4-116, unless a declarant elects to permit an independent unit owner review as described in that section. See Section 4-116(d) and Comments.

Thus, for example, the six-year – or two-year – limitation period within which a claim for breach of warranty must be brought under Section 4-116(a) would not commence until the earlier of

either: (a) the date on which the period of declarant control terminates by operation of law (see Sections 3-103(d) and 3-111(b)), or the date the declarant empowers an independent executive board committee to evaluate and enforce warranty claims. (See Section 4-116(d).)

SECTION 3-112. CONVEYANCE OR ENCUMBRANCE OF COMMON ELEMENTS.

(a) In a condominium or planned community, portions of the common elements may be conveyed or subjected to a security interest by the association if persons entitled to cast at least [80] percent of the votes in the association, including [80] percent of the votes allocated to units not owned by a declarant, or any larger percentage the declaration specifies, agree to that action; but all owners of units to which any limited common element is allocated must agree in order to convey that limited common element or subject it to a security interest. The declaration may specify a smaller percentage only if all of the units are restricted exclusively to non-residential uses. Proceeds of the sale are an asset of the association, but the proceeds of the sale of limited common elements must be distributed equitably among the owners of units to which the limited common elements were allocated.

(b) Part of a cooperative may be conveyed and all or part of a cooperative may be subjected to a security interest by the association if persons entitled to cast at least [80] percent of the votes in the association, including [80] percent of the votes allocated to units not owned by a declarant, or any larger percentage the declaration specifies, agree to that action; but, if fewer than all of the units or limited common elements are to be conveyed or subjected to a security interest, then all unit owners of those units, or the units to which those limited common elements are allocated, must agree in order to convey those units or limited common elements or subject them to a security interest. The declaration may specify a smaller percentage only if all of the units are restricted exclusively to nonresidential uses. Proceeds of the sale are an asset of the association.

Any purported conveyance or other voluntary transfer of an entire cooperative, unless made pursuant to Section 2-118, is void.

(c) An agreement to convey common elements in a condominium or planned community, or to subject them to a security interest, or in a cooperative, an agreement to convey any part of a cooperative or subject it to a security interest, must be evidenced by the execution of an agreement, or ratifications thereof, in the same manner as a deed, by the requisite number of unit owners. The agreement must specify a date after which the agreement will be void unless recorded before that date. The agreement and all ratifications thereof must be recorded in every [county] in which a portion of the common interest community is situated, and is effective only upon recordation.

(d) The association, on behalf of the unit owners, may contract to convey an interest in a common interest community pursuant to subsection (a), but the contract is not enforceable against the association until approved pursuant to subsections (a), (b), and (c). Thereafter, the association has all powers necessary and appropriate to effect the conveyance or encumbrance, including the power to execute deeds or other instruments.

(e) Unless made pursuant to this section, any purported conveyance, encumbrance, judicial sale, or other voluntary transfer of common elements or of any other part of a cooperative is void.

(f) A conveyance or encumbrance of common elements or of a cooperative pursuant to this section does not deprive any unit of its rights of access and support.

(g) Unless the declaration otherwise provides, if the holders of first security interests on 80 percent of the units that are subject to security interests on the day the unit owners' agreement under subsection (c) is recorded consent in writing:

(1) a conveyance of common elements pursuant to this section terminates both the undivided interests in those common elements allocated to the units and the security interests in

those undivided interests held by all persons holding security interests in the units; and

(2) an encumbrance of common elements pursuant to this section has priority over all preexisting encumbrances on the undivided interests in those common elements held by all persons holding security interests in the units.

(h) The consents by holders of first security interests on units described in subsection (g), or a certificate of the secretary affirming that those consents have been received by the association, may be recorded at any time before the date on which the agreement under subsection (c) becomes void. Consents or certificates so recorded are valid from the date they are recorded for purposes of calculating the percentage of consenting first security interest holders, regardless of later sales or encumbrances on those units. Even if the required percentage of first security interest holders so consent, a conveyance or encumbrance of common elements does not affect interests having priority over the declaration, or created by the association after the declaration was recorded.

(i) In a cooperative, the association may acquire, hold, encumber, or convey a proprietary lease without complying with this section.

Comment

1. Subsection (a) provides that a condominium or planned community association may sell or encumber portions of the common elements and subsection (b) provides that a cooperative association may sell part, or encumber all, of the cooperative. The difference in treatment of condominiums and planned communities, on the one hand, and cooperatives, on the other, arises out of the fact that in a cooperative title to the entire cooperative is in the association. Also, historically, cooperative associations have had greater control over the regime real estate, including the units, than has been the case in condominiums or planned communities.

The power given by subsections (a) and (b) can be exercised only on agreement of unit owners holding 80% of the votes in the association (80% is the percentage required for termination of a common interest community under Section 2-118). This power may be exercised during the period of declarant control, but, in order to be effective, 80% of nondeclarant unit owners must approve the action. The ability, without termination, to sell common elements in a condominium or planned community or to sell part of a cooperative gives common interest communities desirable flexibility. For example, the unit owners, some years after the initial creation of the common interest community may decide to convey away a portion of the open space which has been

reserved as a part of the common elements because they no longer find the area useful or because they wish to use sale proceeds to make other improvements.

Similarly, the ability to encumber real estate in the common interest community gives the association power to raise money for improvements through the device of mortgaging the improvements themselves. Of course, recreational improvements will frequently not be sufficient security for a loan for their construction. Nevertheless, the ability to take a security interest in such improvements may lead lenders to be more favorably disposed toward making a loan in larger amounts and at lower interest rates.

2. Subsection (c) requires that the agreement for sale or encumbrance be evidenced by the execution of an agreement in the same manner as a deed by the requisite majority of the unit owners. The agreement then must be recorded in the land records. The recorded agreement signed by the unit owners is not the conveyance itself, but is rather a supporting document which shows that the association has full power to execute a deed or mortgage. Under subsection (d) it is contemplated that the association will execute the actual instrument of conveyance. Under subsection (f), a conveyance or encumbrance under this section may not deprive a unit owner of rights of access and support.

3. As originally written, subsection (g) was intended to cut off the interests of unit lenders whose lien extended to the owner's undivided interest, in the case of a condominium, or beneficial interest, in the case of a cooperative or planned community, in the common elements. The 1994 revision simply clarifies this intent, and states precisely the procedure needed to accomplish the desired result.

To the extent that a lien on a unit (whether in the nature of a security interest, tax lien, attachment, or construction lien) also reaches the owner's interest in the common elements, this amendment makes clear that a proper vote of unit owners and first mortgage holders cuts off that lien.

This section does not affect the interests of persons who hold a direct lien on the common elements nor does it affect the priority or validity of any interest with respect to the unit itself.

4. The introductory clause, "unless the declaration otherwise provides," contemplates the possibility that the declarant or his construction lender may desire to completely prohibit the conveyance or encumbrance of common elements, may require unanimous consent of first mortgagees, or may require another outcome which varies the result of the default rule of this section. Nonetheless, the drafters believe that the default rule strikes an appropriate balance between the interests of security holders and the interests of the association. A rule which requires the consent of every holder of every interest in every unit in a common interest community imposes unreasonable transaction costs for an otherwise rational economic transaction.

On the other hand, the association ought not be able to dispose of its assets automatically and in all cases to the detriment of persons who have made loans to unit owners in reliance on the value of the common elements, without the consent of those persons. Thus, a default rule requiring the consent of a super-majority of first mortgagees should ensure that in the usual case, the interests of all lenders will be adequately protected without unduly restricting the needs of the association.

5. The effect of foreclosure of security interests granted pursuant to this section is governed by Section 2-118 (Termination).

SECTION 3-113. INSURANCE.

(a) Commencing not later than the time of the first conveyance of a unit to a person other than a declarant, the association shall maintain, to the extent reasonably available and subject to reasonable deductibles:

(1) property insurance on the common elements and, in a planned community, also on property that must become common elements, insuring against risks of direct physical loss commonly insured against, which insurance, after application of any deductibles, must be not less than 80 percent of the actual cash value of the insured property at the time the insurance is purchased and at each renewal date, exclusive of land, excavations, foundations, and other items normally excluded from property policies;

(2) commercial general liability insurance, including medical payments insurance, in an amount determined by the executive board but not less than any amount specified in the declaration, covering all occurrences commonly insured against for bodily injury and property damage arising out of or in connection with the use, ownership, or maintenance of the common elements and, in cooperatives, also of all units; and

(3) fidelity insurance.

(b) In the case of a building that contains units divided by horizontal boundaries described in the declaration, or vertical boundaries that comprise common walls between units, the insurance maintained under subsection (a)(1), to the extent reasonably available, must include the units, but need not include improvements and betterments installed by unit owners.

(c) If the insurance described in subsections (a) and (b) is not reasonably available, the association promptly shall cause notice of that fact to be given to all unit owners. The declaration

may require the association to carry any other insurance, and the association may carry any other insurance it considers appropriate to protect the association or the unit owners.

(d) Insurance policies carried pursuant to subsections (a) and (b) must provide that:

(1) each unit owner is an insured person under the policy with respect to liability arising out of the owner's interest in the common elements or membership in the association;

(2) the insurer waives its right to subrogation under the policy against any unit owner or member of the owner's household;

(3) no act or omission by a unit owner, unless acting within the owner's scope of authority on behalf of the association, voids the policy or is a condition to recovery under the policy; and

(4) if, at the time of a loss under the policy, there is other insurance in the name of a unit owner covering the same risk covered by the policy, the association's policy provides primary insurance.

(e) Any loss covered by the property policy under subsections (a)(1) and (b) must be adjusted with the association, but the insurance proceeds for that loss are payable to any insurance trustee designated for that purpose, or otherwise to the association, and not to any holder of a security interest. The insurance trustee or the association shall hold any insurance proceeds in trust for the association, unit owners, and lien holders as their interests may appear. Subject to subsection (h), the proceeds must be disbursed first for the repair or replacement of the damaged property, and the association, unit owners, and lien holders are not entitled to receive payment of any portion of the proceeds unless there is a surplus of proceeds after the property has been completely repaired or replaced, or the common interest community is terminated.

(f) An insurance policy issued to the association does not prevent a unit owner from obtaining insurance for the owner's own benefit.

(g) An insurer that has issued an insurance policy under this section shall issue certificates or memoranda of insurance to the association and, upon request made in a record, to any unit owner or holder of a security interest. The insurer issuing the policy may not cancel or refuse to renew it until [30] days after notice of the proposed cancellation or non-renewal has been mailed to the association, each unit owner, and each holder of a security interest to whom a certificate or memorandum of insurance has been issued at their respective last known addresses.

(h) Any portion of the common interest community for which insurance is required under this section which is damaged or destroyed must be repaired or replaced promptly by the association unless:

(1) the common interest community is terminated, in which case Section 2-118 applies;

(2) repair or replacement would be illegal; or

(3) [80] percent of the unit owners, including every owner of a unit or assigned limited common element that will not be rebuilt, vote not to rebuild.

(i) The cost of repair or replacement in excess of insurance proceeds, deductibles, and reserves is a common expense. If the entire common interest community is not repaired or replaced:

(1) the insurance proceeds attributable to the damaged common elements must be used to restore the damaged area to a condition compatible with the remainder of the common interest community; and

(2) except to the extent that other persons will be distributees:

(A) the insurance proceeds attributable to units and limited common elements that are not repaired or replaced must be distributed to the owners of those units and the owners of the units to which those limited common elements were allocated, or to lien holders, as

their interests may appear; and

(B) the remainder of the proceeds must be distributed to all the unit owners or lien holders, as their interests may appear, as follows:

(i) in a condominium, in proportion to the common element interests of all the units; and

(ii) in a cooperative or planned community, in proportion to the common expense liabilities of all the units.

(j) If the unit owners vote not to rebuild any unit, that unit's allocated interests are automatically reallocated upon the vote as if the unit had been condemned under Section 1-107(a), and the association promptly shall prepare, execute, and record an amendment to the declaration reflecting the reallocations.

(k) This section may be varied or waived in the case of a common interest community all of whose units are restricted to nonresidential use.

Comment

1. Subsections (a) and (b) provide that the required insurance must be maintained only to the extent reasonably available. This permits the association to comply with the insurance requirements even if certain coverages are unavailable or unreasonably expensive.

2. Subsection (a) has been amended in 2008 to permit only "reasonable deductibles" in the context of mandatory insurance that the association must carry. The subject is one of some controversy in the field, since large premium increases in parts of the country, coupled with dropping property values, have caused some associations to explore all means of reducing common expense assessments; self-insurance in the form of large deductibles is one possible and superficially attractive means.

The issue becomes more complex because of the theoretical alternatives that present themselves for dealing with the consequences of substantial deductibles when the association suffers an actual loss.

Indeed, a recurring issue under Section 3-113 has been whether and under what circumstances the association may charge the cost of repair for damage to a unit or common elements to an individual unit owner, whether or not the association has insurance covering that loss.

The theoretical possibilities are several, including: (i) charging only the deductible to the damaged unit(s) regardless of fault; (ii) charging the entire cost of repair of units and common elements against the damaged units, regardless of fault, rather than filing a claim against the association's policy; or (iii) doing either (i) or (ii) but only in circumstances evidencing "fault".

During the drafting process, the drafters learned of legislative proposals requiring, for example, that "the amount of any deductible on any property and liability insurance maintained by the association is a common expense." On the other hand, the drafters became aware of situations where association lawyers include in their declarations a provision that the amount of any deductible must be allocated among the units damaged, regardless of fault, or solely to the unit damaged if the owner was negligent.

The reasons most often advanced in support of this latter position is that the individual unit owner will most commonly carry a form of homeowners insurance for which the premiums are generally low and which, in any event, have already been paid. The argument is that by passing along the costs to the unit owner and thence to the individual carrier, the association will enjoy the benefits flowing from being able to carry larger deductibles, and from filing fewer claims with its primary insurance carrier.

Certain philosophical and practical consequences flow from the efforts to pass along risk to individual owners. One of the fundamental provisions of the Act from its inception was the concept, which remains in subsection (d)(2) , that property and commercial general liability insurance policies must waive the carriers' right of subrogation against any unit owner or member of the owner's household. Thus, to the extent the association files a claim under its policy, the individual unit owner would not be responsible to repay the insurance company.

This appears consistent with traditional insurance practice, since a homeowner that carries fire insurance on her own home and pays the premium for that policy, is not held liable for her own negligence when the house burns and the carrier is required to pay the cost of rebuilding. In the common interest ownership context, the insurance premiums are paid by the association, and the assessments to pay those premium dollars are typically raised by assessments against all the unit owners based on their relative shares of the common expenses.

Moreover, to the extent the association chooses to self-insure against so-called "first dollar" losses by purchasing a policy with a deductible, the benefit of the reduced premium paid by the association is typically shared by those same owners in the form of reduced common charges.

Thus, to the extent that any portion of the costs resulting from a casualty loss are passed through to the unit owners whose units are damaged, rather than paid by the association as a whole, the result is contrary to the policy underlying mandatory waiver of subrogation.

Nevertheless, the practical aspects of who pays, and under what circumstances, are difficult to ignore. Anecdotal evidence suggests that too-frequent claims against a carrier may result in dramatic premium increases, or in policy cancellation; careful directors of unit owner associations will surely seek to avoid those results. Moreover, unlike the individual home owner carrying an individual policy, the association suffers from the risk of the careless unit owner whose risky behavior incurs no consequences to himself, since the unit owner in a common interest community

is not at risk of having his individual policy cancelled. In the absence of the same incentives, it is difficult to assume that individuals in the common interest community will behave with the same care that a single home owner will behave.

A closely related circumstance that may arise is when the association would prefer not to file a claim against its policy for a small loss, but the owner of the damaged unit wishes to do so, especially if the consequence of the association's decision would be to force the damaged unit owner to pay.

The Act takes a middle position in all these regards; see the discussion of the 2008 amendments to § 3-115(e), which permit the association to pass along the cost of damage to the unit owner, in the circumstances described in that section.

3. Subsection (b) represents a significant departure from the present law as to condominiums and planned communities in virtually all States by requiring that the association obtain and maintain property insurance on **both** the common elements **and** the units within buildings with "stacked" units. See Comment 3. While it has been common practice in many parts of the country (either by custom or as mandated by statute) for associations to maintain property insurance on the common elements, it has generally not been the practice for the property insurance policy to cover individual units as well. However, given the great interdependence of the unit owners in the stacked unit situation, mandating property insurance for the entire building is the preferable approach. Moreover, such an approach will greatly simplify claims procedures, particularly where both common elements and portions of a unit have been destroyed. If common elements and units are insured separately, the insurers could be involved in disputes as to the coverage provided by each policy.

4. The 2008 amendments require the association to carry more insurance than under earlier versions of the Act.

First, subsection (a)(3) requires the association to carry "fidelity" insurance. Typically, fidelity insurance protects against loss of money or physical property as a result of criminal behavior. Common claims under fidelity policies involve employee dishonesty, embezzlement, forgery, robbery, computer fraud, wire transfer fraud, counterfeiting, and other criminal acts.

Second, subsection (b) significantly expands the mandatory property and casualty coverage that associations must carry on units. The original Act mandated that units be covered by the association's policy only if they were separated by "horizontal boundaries" - that is, where units in a building were "stacked" above or below one another, as in a high rise building. The 2008 amendment extends this mandatory coverage to townhouse projects or other units that share a common wall between units.

In a cooperative, the association must carry insurance on all units since legal title to all units is in the association.

5. The distinction between what is a common element and what is a unit with respect to the insurance coverage required by this section is complex. The definitions of common elements and a unit in Section 1-103(4) (6) and (31) (35) are not sufficient for this purpose. To determine the

distinction between the common elements and units, one must refer first to the declaration's section on unit boundaries. That section will define the unit boundaries. If the declaration fails to do so, and if ceilings, walls, or floors are boundaries, the provisions of Section 2-102 apply.

Section 2-102 provides that, if the declaration is silent, all non-loadbearing and non-structural portions of the walls, floors, and ceilings are part of the unit, while all loadbearing and structural portions of the walls, floors, and ceilings are common elements. Further, with respect to any structure partially within and partially outside of the boundaries of a unit, any portion thereof serving only that unit is a limited common element (see definition in Section 1-103(21)), and any portion thereof serving more than one unit or any portion of the common elements is a part of the common elements.

Under Section 2-102, all spaces, interior partitions, electrical, plumbing, and mechanical systems, and all other items within the boundaries of the unit which are attached to the unit boundaries, whether or not deemed fixtures under state law, are part of the unit.

Put simply, if any item is installed, constructed, repaired, or replaced by the declarant or his successor in connection with the original sale of a stacked unit, the item is insured by the association. Clearly, this does not include items of personal property easily movable within the unit or easily removable from the unit (whether or not deemed a fixture under state law), such as a vase, table, or other furnishings. If improvements or betterments are made to a unit by a unit owner, they will typically be covered under the owner's insurance policy, even if the unit itself is generally covered by the association's policy, since most policies exclude "improvements or betterments made by the owner," and the Act does not mandate improvements and betterments coverage. The subject is a complex one, and careful attention should be paid to it by the association's insurance advisor.

6. Although "all risk" coverage is not required as to conversion buildings, but merely fire and extended coverage, this is not intended to imply that such coverage is unnecessary. "All risk" coverage is not required because it may not be appropriate in the case of an unrenovated conversion where cost is a critical factor.

7. The minimum requirement as to the amount of insurance, which is 80% of the actual cash value, should not be viewed as a recommendation; rather, the 80% is a floor. Typically, many common interest community documents require insurance in an amount equal to **100% of the replacement cost** of the insured property. The Act permits greater flexibility, however, inasmuch as different types of construction and varieties of projects may not require such total coverage with its attendant higher premium cost.

8. Subsection (a)(2) covers only the liability of the association, and unit owners as members, but does not cover the unit owner's individual liability for his acts or omissions or liability for occurrences within his unit.

9. Clause (1) of subsection (h) would operate as follows: (1) if the common interest community consists of campsites, restoration after fire damage might consist of merely resodding the area damaged; (2) if the common interest community consists of separate garden-type buildings, restoration after fire damage might consist of demolishing the remaining structure and

paving or landscaping the area; and (3) if the common interest community consists of a single high-rise building, restoration may not be required (if the building is substantially destroyed) inasmuch as "a condition compatible with the remainder of the common interest community" would be damaged and unrestored.

10. The scheme of this section, as set forth in subsection (h), is that any damage or destruction to any portion of the common interest community must be repaired (if repairs can be made consistent with applicable safety and health laws) absent a decision to terminate the common interest community or a decision by 80% of the unit owners (including the owners of any damaged units) not to rebuild. Unless a decision is made not to rebuild, any available insurance proceeds must be used to effectuate such repairs. For this reason, subsection (e) provides that any loss covered by the association's property insurance policy shall be adjusted with the association and that the proceeds for any loss shall be payable to the association or to any insurance trustee that may be designated for such purpose. Significantly, such insurance proceeds may not be paid to any mortgagee or other outside party. This provision is necessary to insure that insurance proceeds are available to effectuate any repairs or restoration to the common interest community that may be required.

If units or limited common elements are not rebuilt, insurance proceeds are to be distributed to lienholders or owners of units unless the declaration provides that such payments are to go to some other person.

11. The words "damaged or destroyed" appear in subsection (h), as part of a general requirement that "[a]ny portion of the common interest community for which insurance is required under this section which is **damaged or destroyed must be repaired** or replaced promptly by the association unless, the project is terminated, repair would be illegal, or 80% of the owners vote not to rebuild."

These words may cause confusion among unit owners since the line between the rules for dealing with "damage and destruction" on one hand and "maintenance, repair and replacement" on the other are not clear.

Generally, in common insurance usage, "damage or destruction" deals with items commonly covered by insurance, while everything else is maintenance, repair or replacement. That is, a working distinction is that a portion of a common interest community is "damaged or destroyed" (or suffers damage or destruction) if it suffers physical damage that is of a type and is caused by an occurrence of a type commonly covered by the casualty insurance required by Section 3-113 of this Act or by the Declaration or for which insurance carried by the Association is in effect. Otherwise, to "maintain, repair and replace" (or to perform maintenance, repair and replacement) is the act of addressing and correcting deterioration, wear and tear, and obsolescence to the Property which is not covered by the casualty insurance required by Section 3-113.

SECTION 3-114. SURPLUS FUNDS. Unless otherwise provided in the declaration, any surplus funds of the association remaining after payment of or provision for common expenses

and any prepayment of reserves must be paid annually to the unit owners in proportion to their common expense liabilities or credited to them to reduce their future common expense assessments.

Comment

1. Surplus funds of the association are generally used first for the pre-payment of reserves, and remaining funds are thereafter credited to the account of unit owners or paid to them. In some cases, however, unit owners might prefer that surplus funds be used for other purposes (e.g., the purchase of recreational equipment). Accordingly, this section permits the declaration to specify any other use of surplus funds.

2. The requirements of this section track the requirements of the current Internal Revenue Code; see Rev. Rul. 70-607. The unit owners, of course, may vote to reverse this outcome. As a practical matter, in the everyday activities of the unit owners association, the matters addressed in this section will rarely arise.

SECTION 3-115. ASSESSMENTS.

(a) Until the association makes a common expense assessment, the declarant shall pay all common expenses. After an assessment has been made by the association, assessments must be made at least annually, based on a budget adopted at least annually by the association.

(b) Except for assessments under subsections (c), (d), and (e)**,** or as otherwise provided in this [act], all common expenses must be assessed against all the units in accordance with the allocations set forth in the declaration pursuant to Section 2-107(a) and (b). The association may charge interest on any past due assessment or portion thereof at the rate established by the association, not exceeding [18] percent per year.

(c) To the extent required by the declaration:

(1) a common expense associated with the maintenance, repair, or replacement of a limited common element must be assessed against the units to which that limited common element is assigned, equally, or in any other proportion the declaration provides;

(2) a common expense benefiting fewer than all of the units or their owners may be assessed exclusively against the units or unit owners benefitted; and

(3) the costs of insurance must be assessed in proportion to risk, and the costs of utilities must be assessed in proportion to usage.

(d) Assessments to pay a judgment against the association may be made only against the units in the common interest community at the time the judgment was entered, in proportion to their common expense liabilities.

(e) If damage to a unit or other part of the common interest community, or if any other common expense is caused by the willful misconduct or gross negligence of any unit owner or a guest or invitee of a unit owner, the association may assess that expense exclusively against that owner's unit, even if the association maintains insurance with respect to that damage or common expense.

(f) If common expense liabilities are reallocated, common expense assessments and any instalment thereof not yet due must be recalculated in accordance with the reallocated common expense liabilities.

Comment

1. This section contemplates that a declarant might find it advantageous, particularly in the early stages of project development, to pay all of the expenses of the common interest community himself rather than assessing each unit individually. Such a situation might arise, for example, where a declarant owns most of the units in the project and wishes to avoid building the costs of each unit separately and crediting payment to each unit. It might also arise in the case of a declarant who, although willing to assume all expenses of the common interest community, is unwilling to make payments for replacement reserves or for other expenses which he expects will ultimately be part of the association's budget. Subsection (a) grants the declarant such flexibility while at the same time providing that once an assessment is made against any unit, all units, including those owned by the declarant, must be assessed for their full portion of the common expense liability.

2. Under subsection (c), the declaration may provide for assessment on a basis other than the allocation made in Section 2-107 as to limited common elements, other expenses benefiting less than all units, insurance costs, and utility costs.

3. If additional units are added to a common interest community after a judgment has been entered against the association, the new units are not assessed any part of the judgment debt. Since unit owners will know the assessment, and since such unpaid judgment assessments would affect

the price paid by purchasers of units, it would be complicated and unnecessary to fairness to reallocate judgment assessments when new units are added.

4. Subsection (f) refers to those instances in which various provisions of this Act require that common expense liabilities be reallocated among the units of a common interest community by amendment to the declaration. These provisions include Section 1-107 (Eminent Domain), Section 2-106(d) (expiration of certain leases), Section 2-110 (Exercise of Development Rights), and Section 2-113(b) (subdivision of units).

5. Recall that the 2008 amendment to the definition of "Common interest community" in Section 1-103(9) expanded the definition to include those circumstances where the only unit owners' shared obligation was "to pay for a share of ... services ..related to common elements, other units, or other real estate described in the declaration." The amendment to subsection 3- 115 (c)(2) reflect this increasing practice where, for example, assisted living communities organized as common interest communities are in the business of providing food, janitorial, nursing and other services to residents of individual units as part of the common expense budget of the association. This may occur whether or not the occupants are the owners of those units.

Clearly, there are other means by which those charges might be paid. For example, rather than including meals in the annual budget of the association and then having those costs reflected in the periodic common charge assessment, a more direct means would be to charge the beneficiaries of those services directly on a "fee for service" basis.

The purpose of the amendment is simply to call to the drafter's attention the concern that if some forms of unusual or unique services are to be included in the common expense budget for the entire association, rather than being charged to individual service recipients, then the drafter might use the mechanism permitted under (c)(2) to insure that the non-benefitted owners should not be assessed, and possibly have a lien against their units, for services provided to other persons. As drafted, however, the default rule does not yield that result; instead, services included in the regular budget would be charged to all unit owners, whether or not benefitted.

6. Subsection (e) previously provided that "[i]f any common expense is caused by the misconduct of any unit owner, the association may assess that expense exclusively against his unit." As drafted, it did not directly address the concerns discussed in the commentary to Section 3-113, where the association may incur an insurable loss to a unit or common element as a result of a unit owner's actions.

The 2008 revised subsection (e) does address that issue. As noted, it strikes a middle position on the questions of whether and under what circumstances a unit owner may be charged with the costs of repair. First, the section makes clear that such a charge back may be appropriate, notwithstanding the policy underlying the mandated waiver of subrogation rights contained in 3-113(d)(2), even when the association does carry an insurance policy covering that loss. Thus, in an appropriate case, the association might choose not to submit a claim under its insurance policy, and instead proceed directly against the unit owner for the entire amount of the cost of repair, including any sum that would otherwise be paid from the deductible.

However, in contrast to the practice of some associations, the section does not permit a charge back in a "no fault" or in a "simple negligence" situation. Instead, the unit owner to be assessed, or the owner's guest or invitee, must be guilty either of "willful misconduct" or "gross negligence."

These comments are not intended to identify all those circumstances that might satisfy those standards, and those determinations will ultimately be left to the finder of fact. At the same time, some common situations are clear.

Example 1: Assume a fire were to occur in Unit A as a result of a frayed electrical cord hidden behind a wall. It is difficult to imagine a finder of fact concluding that the owner of Unit A was guilty either of "willful misconduct" or "gross negligence."

Example 2: Assume an association for a high rise building were to adopt a policy requiring periodic replacement of water heaters in all units. Thereafter, the property manager personally notified each unit owner, including the owner of Unit B, of the owner's obligation to replace that heater in a timely way. If the owner refused to do so after personal notice, and the heater thereafter failed and caused water damage to the owner's unit and the units below, a finder of fact would likely conclude that the refusal on the part of the owner of Unit B constituted willful misconduct.

Example 3: Assume the association for a common interest community at a western ski area has a history of frozen pipes bursting and causing water damage during the week, when unit owners are often absent. This history is well known to unit owners, who are repeatedly advised in the mail to maintain 189 a minimum heat in their units of 55 degrees. The teenage son of the Owner of Unit C turns off all the heat after his last run on Sunday, and on Monday night, the pipes in Unit C burst. A finder of fact might properly conclude that the son of the owner of Unit C was grossly negligent.

SECTION 3-116. LIEN FOR SUMS DUE ASSOCIATION; ENFORCEMENT.

(a) The association has a statutory lien on a unit for any assessment attributable to that unit or fines imposed against its unit owner. Any priority accorded to the association's lien under this section is a priority in right and not merely a priority in payment from the proceeds of the sale of the unit by a competing lienholder or encumbrancer. Unless the declaration provides otherwise , reasonable attorney's fees and costs, other fees, charges, late charges, fines, and interest charged

pursuant to Section 3-102(a)(10), (11), and (12), and any other sums due to the association under the declaration, this [act], or as a result of an administrative, arbitration, mediation, or judicial decision are enforceable in the same manner as unpaid assessments under this section. If an assessment is payable in installments, the lien is for the full amount of the assessment from the time the first installment thereof becomes due. [A lien under this section is not subject to [insert appropriate reference to state homestead, dower and curtesy, or other exemptions].]

(b) A lien under this section has priority over all other liens and encumbrances on a unit except:

(1) liens and encumbrances recorded before the recordation of the declaration and, in a cooperative, liens and encumbrances that the association creates, assumes, or takes subject to;

(2) except as otherwise provided in subsection (c), a first security interest on the unit recorded before the date on which the assessment sought to be enforced became delinquent or, in a cooperative, the first security interest encumbering only the unit owner's interest and perfected before the date on which the assessment sought to be enforced became delinquent;

(3) liens for real estate taxes and other governmental assessments or charges against the unit or cooperative; and

(4) mechanics' or materialmen's liens to the extent that law of this state other than this [act] gives priority to mechanics' or materialmen's liens.

(c) A lien under this section also has priority over a security interest described in subsection (b)(2), but only to the extent of:

(1) the unpaid amount of assessments for common expenses, not to exceed six months for each budget year of the association, as based on the periodic budget adopted by the association under Section 3-115(a) for the applicable year; and

(2) reasonable attorney's fees and costs incurred by the association in enforcing the

association's lien.

(d) Unless the declaration otherwise provides, if two or more associations have liens for assessments created at any time on the same property, those liens have equal priority.

(e) Recording of the declaration constitutes record notice and perfection of the lien. No further recordation of any claim of lien for assessment under this section is required.

(f) A lien for unpaid assessments is extinguished unless proceedings to enforce the lien are instituted within [three] years after the full amount of the assessments becomes due.

(g) This section does not prohibit an action by an association against a unit owner to recover past due sums for which subsection (a) creates a lien or prohibit an association from taking a deed in lieu of foreclosure.

(h) A judgment or decree in any action brought under this section must include costs and reasonable attorney's fees for the prevailing party.

(i) The association upon request made in a record shall furnish to a unit owner a statement setting forth the amount of unpaid assessments against the unit. If the unit owner's interest is real estate, the statement must be in recordable form. The statement must be furnished within [10] business days after receipt of the request and is binding on the association, the executive board, and every unit owner.

(j) On nonpayment of an assessment on a unit, the association is entitled to obtain possession of the unit under [insert reference to forcible entry and detainer act of this State].

(k) The association's lien may be foreclosed as provided in this subsection and subsection (p):

(1) in a condominium or planned community, the association's lien must be foreclosed in like manner as a mortgage on real estate [or by power of sale under [insert appropriate state statute]];

(2) in a cooperative whose unit owners' interests in the units are real estate, the association's lien must be foreclosed in like manner as a mortgage on real estate [or by power of sale under [insert appropriate state statute]] [or by power of sale under subsection (l)]; [and]

(3) in a cooperative whose unit owners' interests in the units are personal property, the association's lien must be foreclosed in like manner as a security interest under [insert reference to Article 9, Uniform Commercial Code][;and]

[(4) in a foreclosure under [insert reference to state power of sale statute], the association shall give the notice required by statute or, if there is no such requirement, reasonable notice of its action to all lien holders of the unit whose interest would be affected].

[(l) If the unit owner's interest in a unit in a cooperative is real estate, the following requirements apply:

(1) The association, upon nonpayment of assessments and compliance with this subsection, may sell that unit at a public sale or by private negotiation and at any time, date, and place. The association shall give to the unit owner and any lessee of the unit owner reasonable notice in a record of the time, date, and place of any public sale or, if a private sale is intended, of the intention of entering into a contract to sell and of the time and date after which a private disposition may be made. The same notice must also be sent to any other person that has a recorded interest in the unit which would be cut off by the sale, but only if the recorded interest was on record seven weeks before the date specified in the notice as the date of any public sale or seven weeks before the date specified in the notice as the date after which a private sale may be made. The notices required by this subsection may be sent to any address reasonable in the circumstances. A sale may not be held until five weeks after the sending of the notice. The association may buy at any public sale and, if the sale is conducted by a fiduciary or other person not related to the association, at a private sale.

(2) Unless otherwise agreed, the unit owner is liable for any deficiency in a foreclosure sale.

(3) The proceeds of a foreclosure sale must be applied in the following order:

(A) the reasonable expenses of sale;

(B) the reasonable expenses of securing possession before sale; the reasonable expenses of holding, maintaining, and preparing the unit for sale, including payment of taxes and other governmental charges and premiums on insurance; and, to the extent provided for by agreement between the association and the unit owner, reasonable attorney's fees, costs, and other legal expenses incurred by the association;

(C) satisfaction of the association's lien;

(D) satisfaction in the order of priority of any subordinate claim of record; and

(E) remittance of any excess to the unit owner.

(4) A good faith purchaser for value acquires the unit free of the association's debt that gave rise to the lien under which the foreclosure sale occurred and any subordinate interest, even though the association or other person conducting the sale failed to comply with this section. The person conducting the sale shall execute a conveyance to the purchaser sufficient to convey the unit and stating that it is executed by the person after a foreclosure of the association's lien by power of sale and that the person was empowered to make the sale. Signature and title or authority of the person signing the conveyance as grantor and a recital of the facts of nonpayment of the assessment and of the giving of the notices required by this subsection are sufficient proof of the facts recited and of the authority to sign. Further proof of authority is not required even though the association is named as grantee in the conveyance.

(5) At any time before the association has disposed of a unit in a cooperative or

entered into a contract for its disposition under the power of sale, the unit owners or the holder of any subordinate security interest may cure the unit owner's default and prevent sale or other disposition by tendering the performance due under the security agreement, including any amounts due because of exercise of a right to accelerate, plus the reasonable expenses of proceeding to foreclosure incurred to the time of tender, including reasonable attorney's fees and costs of the creditor.]

(m) In an action by an association to collect assessments or to foreclose a lien on a unit under this section, the court may appoint a receiver to collect all sums alleged to be due and owing to a unit owner before commencement or during pendency of the action. The receivership is governed by [insert state law generally applicable to receiverships]. The court may order the receiver to pay any sums held by the receiver to the association during pendency of the action to the extent of the association's common expense assessments based on a periodic budget adopted by the association pursuant to Section 3-115.

(n) An association may not commence an action to foreclose a lien on a unit under this section or to evict a unit owner under subsection (j) unless:

(1) the unit owner, at the time the action is commenced, owes a sum equal to at least [three] months of common expense assessments based on the periodic budget last adopted by the association pursuant to Section 3-115(a) and the unit owner has failed to accept or comply with a payment plan offered by the association; and

(2) the executive board votes to commence a foreclosure action specifically against that unit or to evict the unit owner.

(o) Unless the parties otherwise agree, the association shall apply any sums paid by unit owners that are delinquent in paying assessments in the following order:

(1) unpaid assessments;

(2) late charges;

(3) reasonable attorney's fees and costs and other reasonable collection charges; and

(4) all other unpaid fees, charges, fines, penalties, interest, and late charges.

(p) If the only sums due with respect to a unit are fines and related sums imposed against the unit, a foreclosure action may not be commenced against the unit unless the association has a judgment against the unit owner for the fines and related sums and has perfected a judgment lien against the unit under [insert reference to state statute on perfection of judgments].

(q) Every aspect of a foreclosure, sale, or other disposition under this section, including the method, advertising, time, date, place, and terms, must be commercially reasonable.

[(r) Foreclosure of a lien under this section does not terminate an interest that is subordinate to the lien to any extent unless the association provides notice of the foreclosure to the record holder of the subordinate interest.]

Legislative Note: *In a state that permits only judicial foreclosure of an association's lien,* subsection (r) should be omitted. In a state that permits nonjudicial foreclosure, but by statute provides that a foreclosure sale does not extinguish a subordinate lien unless the subordinate lienholder was provided notice of the sale, subsection (r) should be omitted.

Comment

1. Section 3-116(a) was amended in 1994 to delete the language "from the time the assessment or fine becomes due." The deleted clause was intended to make clear that the lien was enforceable at the time the assessment became due. Commentators have observed, however, that the language caused confusion with respect to priority issues. The intention of the statute, as demonstrated by the Comments, was that the inchoate statutory lien was the functional equivalent of real estate taxes except with respect to the special priorities identified in subsection (b) of the section. The deletion of the language as suggested makes clear that the lien arises immediately upon the effective date of the statute for old common interest communities and upon recording of the declaration for new common interest communities.

As a result of this deletion, it is clear that in the absence of an exception in a title insurance policy for common charges, a title insurer would be liable for post-insurance obligations which have a priority established prior to the time the policy was issued. This, however, is no different than in other inchoate liens such as real estate taxes and mechanics liens, all of which have become standard exceptions in the title industry.

2. To ensure prompt and efficient enforcement of the association's lien for unpaid assessments, such liens should enjoy statutory priority over most other liens. Accordingly, subsection (b) provides that the association's lien takes priority over all other liens and encumbrances except those recorded prior to the recordation of the declaration, those imposed for real estate taxes or other governmental assessments or charges against the unit, and first security interests recorded before the date the assessment became delinquent (except as provided in subsection (c), as described below).

As originally promulgated in 1982, subsection (c) provided that the association's lien did have priority to the extent of six months of unpaid common expense assessments, based on the association's periodic budget. In 2008, subsection (c) was amended to extend this limited priority to include the cost of the association's reasonable attorneys' fees and court costs.

The six-month limited priority for association liens constituted a significant departure from pre-existing practice, and was viewed as striking an equitable balance between the need to enforce collection of unpaid assessments and the need to protect the priority of the security interests of lenders in order to facilitate the availability of first mortgage credit to unit owners in common interest communities. This equitable balance was premised on the assumption that, if an association took action to enforce its lien and the unit owner failed to cure its assessment default, the first mortgage lender would promptly institute foreclosure proceedings and pay the unpaid assessments (up to six months' worth) to the association to satisfy the association's limited priority lien. This was expected to permit the mortgage lender to preserve its first lien and deliver clear title in its foreclosure sale — a sale that was expected to be completed within six months (in jurisdictions with nonjudicial foreclosure) or a reasonable period of time thereafter, thus minimizing the period during which unpaid assessments would accrue for which the association would not have first priority. Likewise, it was expected that in the typical situation, a unit would have a value sufficient to produce a sale price high enough for the foreclosing lender to recover both the unpaid mortgage balance and six months of assessments.

The real estate market facing common interest communities post-2007 is substantially different from the one contemplated by the drafters of the original UCIOA. Many units are "underwater," with values below the outstanding first mortgage balance. More significantly, long delays have developed in the completion of foreclosures. In states permitting only judicial foreclosures, these delays were often beyond lender control. In many situations, however, mortgage lenders strategically delayed the institution or completion of foreclosure proceedings on units affected by common interest assessments. When a lender acquires a unit at a foreclosure sale by way of a credit bid, it becomes legally obligated to pay assessments arising during the lender's period of ownership. Some lenders have chosen to delay scheduling or completing a foreclosure sale, fearful that they may be unable to resell the unit quickly for an appropriate return in a depressed market. During this period of delay, neither the unit owner nor the mortgage lender is paying the common expense assessments — the unit owner is often unable or unwilling to do so, and the mortgagee is not legally obligated to do so prior to acquiring title. In the meantime, the association (and the remaining unit owners) bear the full financial consequences of this situation, because the association must either force the remaining owners to bear increased assessments to meet budgeted expenses or reduce expenditures for (or the level of) community maintenance, insurance and services.

If other unit owners have to pay the burden of increased assessments to preserve community services or amenities, the delaying lender receives a benefit in that the value of its collateral is preserved while the lender waits to foreclose. Yet this preservation comes through the community's imposition of assessments that the lender does not have to pay or reimburse. This benefit constitutes unjust enrichment of the mortgage lender, particularly to the extent that the lender enjoys this benefit by virtue of a conscious decision to delay completing a foreclosure sale.

In addition to its inadequacy to protect the legitimate financial interests of community residents, the language used to create the limited priority lien in subsection (c) has also prompted a number of interpretive disputes. For example:

> First, there has been a developing split of judicial authority as to whether subsection (c) creates in the association a true lien priority or merely a payment priority. For example, suppose that a condominium association forecloses its lien and conducts a sale following a unit owner's default in assessment payments, and the first mortgage lender does not participate in the sale. As originally drafted, subsection (c) was intended to create a true lien priority, and thus the association's foreclosure properly should be viewed as extinguishing the lien of the first lienholder (to the same extent that foreclosure of a real estate tax lien would extinguish an otherwise-first mortgage lien). See, e.g., SFR Investments Pool 1, LLC v. U.S. Bank, N.A., ___ Nev. ___ (Nev. 2014); Chase Plaza Condominium Ass'n, Inc. v. JPMorgan Chase Bank, N.A., ___ A.3d ___, 2014 WL 4250949 (D.C. Ct. App. 2014); 7912 Limbwood Court Trust v. Wells Fargo Bank, N.A., ___ F.Supp.2d ___, 2013 WL 5780793 (D.Nev.2013); Summerhill Village Homeowners Ass'n v. Roughley, 270 P.3d 639 (Wash.Ct.App. 2012). Nevertheless, several trial court decisions have held that an association's nonjudicial foreclosure of its assessment lien does not extinguish the lien of the first mortgage lender. See, e.g., Weeping Hollow Ave. Trust v. Spencer, 2013 WL 2296313 (D.Nev. May 24, 2013); Diakonos Holdings, LLC v. Countrywide Home Loans, Inc., 2013 WL 531092 (D. Nev. Feb. 11, 2013).
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> Second, a split of authority has developed as to whether the association may extend its six-month lien priority by filing successive lien foreclosure actions at six month intervals. Compare Drummer Boy Homes Ass'n v. Britton, 2011 Mass. App. Div. 186 (2011) (UCIOA lien priority cannot be extended beyond six months through repetitive foreclosure actions by association) with Bank of America, N.A. v. Morganbesser, No. 675-10-10 (Vt. Super. Ct. Jan. 18, 2013) (recognizing continuation of association's priority for assessments accruing during pendency of association foreclosure, even beyond six months, because subsection (c) would allow repetitive actions every six months).

For the reasons discussed above, subsections (a), (b) and (c) are amended to clarify the scope of the association's limited lien priority, as follows:

> First, subsection (a) affirms the result in Summerhill Village Homeowners Ass'n v. Roughley, 270 P.3d 639 (Wash.Ct.App. 2012), and makes clear that the association's lien has true priority over the lien of an otherwise first mortgage lender to the extent of the amount specified in subsection (c). Thus, if the association conducts a foreclosure sale of its association lien and the otherwise first mortgagee does not act to redeem its interest by satisfying the association's limited priority lien, the mortgagee's lien would be

extinguished.

Second, subsection (c) makes clear that the association's lien is not capped at only six months of unpaid common expense assessments. Instead, the association's lien is entitled to priority under subsection (c) to the extent of six months of unpaid common expense assessments each year, based on each year's periodic budget as adopted by the association for the applicable year.

By allowing the association to extend its priority for six months per year throughout any period of delay by a foreclosing lender, subsection (c)(1) strikes a more appropriate and equitable sharing of the costs of preserving the value of the mortgagee's security. The following illustrations demonstrate the application of subsection (c):

Illustration 1. Owner owns a unit subject to a first mortgage held by Bank (but no other liens). Owner fails to pay any assessments during either 2012 or 2013. In December 2013, the association conducts a foreclosure sale (having given proper notice of the sale to both Owner and Bank). Based on the association's annual budgets, assessments were $100/month for 2012 and $125/month for 2013. The unpaid balance of Owner's assessments was thus $2,700, and the association incurred an additional $1,000 in reasonable attorney fees and costs in enforcing its lien. Under subsection (c), the association's lien would be entitled to priority over Bank's mortgage to the extent of $2,350, which represents (1) six months of unpaid 2012 assessments (a total of $600), (2) six months of unpaid 2013 assessments (a total of $750), and (3) $1,000 in attorney fees and costs. The association's foreclosure sale extinguishes Bank's mortgage lien. The association receives the first $2,350 in sale proceeds for application to Owner's unpaid assessments. The sale proceeds would next be applied to the balance secured by Bank's mortgage. If there remained any surplus sale proceeds following the satisfaction of Bank's mortgage, those proceeds would be applied to the remaining balance of the Owner's unpaid assessments.

Illustration 2. Owner owns a unit subject to a first mortgage held by Bank (but no other liens). In December 2013, the association conducts a foreclosure sale (having given proper notice of the sale to both Owner and Bank). Based on the association's annual budgets, assessments were $100/month for 2012 and $125/month for 2013. At the time of the sale, Owner had neither paid assessments for March and April of 2012 (a total of $200) nor for the period March-December 2013 (a total of $1,250). The unpaid balance of Owner's assessments was thus $1,450, and the association incurred an additional $1,000 in reasonable attorney fees and costs in enforcing its lien. Under subsection (c), the association's lien would be entitled to priority over Bank's mortgage only to the extent of $1,950, which represents (1) two months of unpaid 2012 assessments (a total of $200), (2) six months of unpaid 2013 assessments (a total of $750), and (3) $1,000 in attorney fees and costs. The association's foreclosure sale extinguishes Bank's mortgage lien. The association receives the first $1,950 in sale proceeds for application to Owner's unpaid assessments. The sale proceeds would next be applied to the balance secured by Bank's mortgage. If there remained any surplus sale proceeds following the satisfaction of Bank's mortgage, those proceeds would be applied to the remaining balance of the Owner's unpaid assessments.

Illustration 3. Owner owns a unit subject to a first mortgage held by Bank (but no other liens). In December 2013, the association schedules a foreclosure sale (having given proper notice of the sale to both Owner and Bank). Based on the association's annual budgets, assessments were $100/month for 2013, and Owner had not paid any assessments for 2013. The unpaid balance of Owner's assessments was thus $1,200, and the association incurred an additional $1,000 in reasonable attorney fees and costs in enforcing its lien. Just prior to the scheduled foreclosure sale, however, Bank paid the association a total of $1,600, which represents (1) six months of unpaid 2013 assessments (a total of $600) and (2) $1,000 in the association's attorney fees and costs. Bank's payment extinguishes the priority that the association's lien would otherwise have had pursuant to subsection (c); therefore, if the association proceeds with its foreclosure sale, the sale will not extinguish Bank's mortgage lien, and the buyer at the sale will take the unit subject to Bank's mortgage lien.

In cooperatives, the association has legal title to the units and depending on the election made in the declaration pursuant to Section 2-118(i) may have power to create, assume, or take subject to security interests in the units which have priority over the interest of unit owners. Obviously, the cooperative association's lien should not have priority over an interest which the association itself has given, assumed, or taken subject to and subsection (b) expressly so provides.

The special reference to cooperatives in subsection (b)(2) merely recognizes that in a cooperative both the association and the unit owner have an interest in a unit.

3. Units may be part of two common interest communities. For example, a large real estate development may consist of one or more condominiums which are also part of a larger planned community. In that case, the planned community association might assess the condominium units for the general maintenance expenses of the planned community and the condominium association would assess for the direct maintenance expenses of the building itself. In such a situation, subsection (d) provides that unpaid liens of the two associations have equal priority regardless of the relative time of creation of the two regimes and regardless of the time the assessments were made or became delinquent.

4. Subsection (g) makes clear that the association may have remedies short of foreclosure of its lien that can be used to collect unpaid assessments. The association, for example, might bring an action in debt or breach of contract against a recalcitrant unit owner rather than resorting to foreclosure.

5. Subsection (j) originally provided an additional remedy for cooperative associations dealing with defaulting or recalcitrant unit owners. In the typical cooperative the association will have a substantial underlying mortgage on all or a substantial portion of the real estate in the cooperative and a large part of each unit owner's periodic assessment will go toward payment of that particular unit's proportionate share of the mortgage. If the unit owner fails to pay his assessment on time, the association may be forced into default on its own mortgage payments with consequent possible foreclosure of the underlying mortgage and loss by all unit owners of their interests in the cooperative. Therefore, in the cooperative context it is essential that the cooperative association have a fast and effective remedy for failure of a unit owner to pay his assessment. For this reason, subsection (j) provided that upon nonpayment the cooperative unit owner could be evicted in the

same manner as an unlawfully holding over commercial tenant.

If the unit owner's interest is real estate, subsection (k)(2) then offers the State two alternatives as to nonjudicial foreclosure of a cooperative association's lien. The first alternative is power of sale under any existing state statute authorizing power of sale under mortgages. If there is no power of sale statute or if the legislature chooses to adopt a special power of sale provision for of the lien on cooperative units, the State can choose the 2d alternative: power of sale under subsection (l) of this section.

Subsection (l), which is patterned after the power of sale foreclosure provisions of the Uniform Land Transactions Act, is a modern power of sale provision which frees private power of sale foreclosure from many of the costly, time consuming, and inefficiency producing strictures of most existing private power of sale statutes. At the same time, it provides reasonable protection to the unit owner and junior interests.

If the unit owners' interest in a cooperative is personal property, the association's lien is foreclosed as if it were a security interest under Article 9 of the Uniform Commercial Code. Article 9 foreclosure is generally less expensive and faster than either judicial or power of sale real estate foreclosure. This difference in cost and speed of foreclosure, both for association liens and security interests, is one of the major factors to be considered in choosing whether, under Section 1-105, the unit owner's interest in a cooperative will be real property or personal property. Article 9 foreclosure is currently used in foreclosing security interests in mobile homes, and has been accepted in the various States as a permissible method of foreclosure in that housing area without serious challenge.

As originally promulgated, subsection (j) only authorized a possessory remedy prior to foreclosure for cooperatives. Subsection (j) did not extend such a possessory remedy to an association in a condominium or planned community, on the theory that a unit owner's failure to pay assessments on a timely basis would have less significant consequences and that the association's foreclosure remedy was sufficient.

By contrast, Illinois has adopted procedures that allow a condominium association to use forcible entry and detainer to obtain possession of a unit from a defaulting owner, and to lease the unit to a tenant and apply the rents toward the satisfaction of unpaid assessments. 735 ILCS 5/9-111. Upon recovering possession of the unit, the association has the power (though not the obligation) to lease the unit to a tenant for a period not to exceed 13 months; if the association so leases the property, the association must apply rents collected to unpaid assessments, fines, and ongoing assessments as they come due, with any surplus returned to the unit owner. 735 ILCS 5/9-111.1. Once the unit owner has paid off the unpaid assessments and becomes current on its obligations to the association, the unit owner may obtain an order vacating the judgment; if the premises are being leased by the association as described above, the judgment would be vacated effective at the end of the lease term. 735 ILCS 5/9-111.

The Illinois statute discourages strategic default by underwater unit owners in possession of their units (defaults which can place a serious financial burden on the association and other unit owners). The potential benefit of such a remedy is additionally magnified in jurisdictions (such as Illinois) that permit only judicial foreclosure. In those states in which a year or longer might

elapse before an association could complete a judicial foreclosure of its assessment lien, and there is a viable market for rental of such units, this possessory remedy would enhance the ability of the association to reduce the assessment delinquency (and thereby help meet its budgeted expenses) pending completion of the foreclosure of the association lien.

As a result, subsection (j) is amended to extend a comparable remedy to all associations. A state that adopts amended subsection (j) may need to consider conforming amendments in its forcible entry and detainer statute that are similar in character to the provisions in the Illinois statute, 735 ILCS 5/9-111 and 9-111.1.

6. Subsection (m) makes clear that the courts have authority to appoint receivers upon request by associations to aid in collection of common charges.

7. Few issues are more contentious in common interest communities than the prospect of unit owners losing their homes as a consequence of non-payment of common charges – and the loss of all or most of their equity – when the association forecloses. The reaction in state legislatures in recent years has been widespread.

At the same time, it is crucial that the association be able to secure timely payment of common charges in order to provide services to all the residents of the common interest community.

In an effort to balance these competing interests, the 2008 amendments provided additional safeguards governing foreclosure of liens for unpaid common charges. These procedures may be summarized as follows:

First, Section 3–116(n) bars foreclosure for sums that are less than 3 months of common charges. Likewise, subsection (n) also bars the association from pursuing a possessory remedy against a defaulting unit owner unless more than 3 months of common charges are unpaid.

Second, Section 3–116(n) also requires the association board, to first, offer the delinquent owner a payment plan which the owner rejects, and second, expressly approve each foreclosure action.

Third, Section 3–116(o) requires that payments of delinquent assessments be applied first to principal rather than to interest and fees, in order to avoid the usual practice of accruing additional interest and late charges as the monthly fees remain unsatisfied while the attorneys' fees and interest are paid first.

Fourth, Section 3–116(p) bars any foreclosure for fines alone unless the association first secures a personal judgment against the unit owner.

Finally, Section 3–116(q) requires that if a foreclosure does go forward, any sale of a unit must be commercially reasonable. In the first reported case of foreclosure arising in a state that has adopted this Act, the court required that the sale be reasonable. See Will v. Mill Condominium Owners Association et al, 176 VT 380, 848 A2d 336 [2004].

These special procedures would comprise an overlay on existing state foreclosure procedures, whether judicial or non-judicial. Taken together, they respond in a concise but responsible way to the widespread reports of abuses in this field. Hopefully, they will also be viewed by the various States as a responsible and balanced response to the issues confronting elected officials, defaulting unit owners and homeowners association directors with a fiduciary responsibility to maintain the property.

8. In states that permit an association to foreclose its association lien by nonjudicial foreclosure, questions may arise regarding the finality of a sale in which a person holding a subordinate lien did not receive notice of the nonjudicial sale. In some states, nonjudicial foreclosure procedures require notice to subordinate lienholders only when those lienholders have recorded a timely request for notice of sale on the real property records. There also is authority in some nonjudicial foreclosure states to the effect that a subordinate lien can be extinguished in favor of a bona fide purchaser at the sale even if the subordinate lienholder who had requested notice did not receive it. In other states, a subordinate lienholder that does not receive notice of a nonjudicial foreclosure sale does not have its lien extinguished by that sale. See, e.g., Wash. Rev. Code Ann. § 61.24.040(7).

The issue of notice to subordinate lienholders becomes more critical under this Act, given that subsection (c) gives the association a limited priority over the otherwise-first mortgage lender, thus rendering that lender a subordinate lienholder. It would be manifestly unfair for an association's foreclosure sale to extinguish the lien of the otherwise-first mortgage lender if the association did not in fact provide the lender with notice of that sale. For this reason, subsection (r) is added to make clear that the association's foreclosure does not terminate a subordinate lien unless the association provides notice of the foreclosure to the person that is the record holder of the subordinate interest.

Subsection (r) is not necessary in judicial foreclosure-only states, nor in states (such as Washington) that provide that a nonjudicial foreclosure can extinguish subordinate liens only if such lienholders were provided notice prior to the sale.

9. Section 3-116 rejects more extreme provisions favoring defaulting unit owners espoused in various forums. For example, extensive provisions were adopted by North Carolina regarding fines enforcement and collection which may pose significant impediments to the financial well-being of unit owner associations. See, e.g., 2205 North Carolina Session Act No. 422. Similarly, the section does not adopt the extensive borrower protections contained in the Uniform Non-Judicial Foreclosure Act. That act contains provisions dealing with repetitive and detailed default notices, mandated meetings before foreclosure, a period of limitation on foreclosures, mandated judicial supervision of foreclosures, extensive redemption rights after foreclosure, and the like. In those cases where foreclosure is supervised by a judge, those procedures are not likely to be of significant benefit to defaulting to unit owners, but will impose significant transaction costs on associations in non-judicial foreclosure states; there is no reason to distinguish common interest community foreclosures from every other procedure.

10. The issue of how the association protects itself from non-payment of assessments may be of concern in a state with a homestead exemption. Either direct foreclosure of the association's statutory lien for unpaid assessments, or foreclosure of a perfected judgment lien which the

association might have secured in lieu of foreclosure, may conflict with existing homestead statutes. Further consideration of this issue in those states, in order to reconcile conflicting statutes, would then be appropriate.

11. In requiring a delay for 3 months in commencement of a foreclosure proceeding, subsection 3-116(n)(1) imposes some risk on the association. Since the association's lien has only a limited priority over that of a first mortgage, anything which delays the commencement and completion of a foreclosure by the association, but does not result in the unit owner bringing his or her account current, may be seen as simply raising the cost to the association, and, therefore, to all of the other unit owners who are paying their common charges on time.

12. It may be that the reaction of some legislators to this Section will depend on the extent to which foreclosure actions in the respective states are subject to judicial supervision. In states where non-judicial foreclosure is either not available or not used in association lien foreclosures, the active role played by the court may minimize the need for certain of the borrower protections in this section.

SECTION 3-117. OTHER LIENS.

(a) In a condominium or planned community:

(1) Except as otherwise provided in paragraph (2), a judgment for money against the association [if recorded] [if docketed] [if [insert other procedures required under state law to perfect a lien on real estate as a result of a judgment]], is not a lien on the common elements, but is a lien in favor of the judgment lien holder against all of the other real estate of the association and all of the units in the common interest community at the time the judgment was entered. No other property of a unit owner is subject to the claims of creditors of the association.

(2) If the association has granted a security interest in the common elements to a creditor of the association pursuant to Section 3-112, the holder of that security interest shall exercise its right against the common elements before its judgment lien on any unit may be enforced.

(3) Whether perfected before or after the creation of the common interest community, if a lien, other than a deed of trust or mortgage, including a judgment lien or lien attributable to work performed or materials supplied before creation of the common interest

community, becomes effective against two or more units, the unit owner of an affected unit may pay to the lien holder the amount of the lien attributable to the unit, and the lien holder, upon receipt of payment, promptly shall deliver a release of the lien covering that unit. The amount of the payment must be proportionate to the ratio that the unit owner's common expense liability bears to the common expense liabilities of all unit owners the units of which are subject to the lien. After payment, the association may not assess or have a lien against that unit owner's unit for any portion of the common expenses incurred in connection with that lien.

(4) A judgment against the association must be indexed in the name of the common interest community and the association and, when so indexed, is notice of the lien against the units.

(b) In a cooperative:

(1) If the association receives notice of an impending foreclosure on all or any portion of the association's real estate, the association shall promptly transmit a copy of that notice to each unit owner of a unit located within the real estate to be foreclosed. Failure of the association to transmit the notice does not affect the validity of the foreclosure.

(2) Whether a unit owner's unit is subject to the claims of the association's creditors, no other property of a unit owner is subject to those claims.

Comment

1. This section deals with the effect on unit owners of judgments against the association. The issue is not free from difficulty. Presently, in most States, if the association is organized as a corporation, the unit owners are likely to receive the insulation from liability given shareholders of a corporation, so that the judgment lienholder can satisfy his judgment only against the property of the association. On the other hand, if the association is organized as an unincorporated association, under the law of most States each unit owner would have joint and several liability on the judgment. This Act strikes a balance between the two extremes.

2. In condominiums and planned communities, the Act makes the judgment lien a direct lien against each individual unit, but allows the individual unit owner to discharge the lien by payment of his pro-rata share of the judgment based on that unit's relative common expense liability. The judgment would also create a lien against any property owned by the association. In cooperatives, title to the units is in the cooperative so that it is not necessary for the Act to provide that a judgment

against the association creates a lien against units. The Act does provide, however, that no property of a cooperative unit owner other than the unit is subject to the claims of association creditors. The result is that the relationship between creditors of the association and unit owners is similar in all three forms of ownership.

There are, however, significant differences between cooperatives and condominiums or planned communities as to the position of unit owners as against association creditors. In one respect cooperative unit owners have greater liability than condominium or planned community unit owners and in another respect they have lesser liability.

They have greater liability in that, in a cooperative, if a judgment lien has priority over a unit owner's interest in a unit, the lien against the unit is not limited to the unit's common expense liability percentage. In contrast, in a condominium or planned community, the lien against a unit is only for the unit owner's pro rata share of the judgment.

Example: Suppose a four unit project in which there is a judgment against the association for $50,000. Further suppose that each of the units has a value of $100,000 and that there are outstanding mortgages as follows:

	Unit A	Unit B	Unit C	Unit D
Value	$100,000	$100,000	$100,000	$100,000
Mortgage	50,000	90,000	90,000	75,000
Equity	50,000	10,000	10,000	25,000

In a condominium or planned community, the judgment lien attaches to each unit in proportion to that unit's liability for common expense liability. If, in the above example, the common expense liability is equal, the lien would attach to each unit for $12,500. Therefore, the association judgment creditor could reach the full equity of Unit owners B and C in their units, but could reach only $12,500 of the interest of Unit owners A and D. Since the association cannot assess A and D for any additional amounts of the judgment, if B and C allow their interest to be foreclosed and foreclosure produces only $20,000, the association judgment creditor will collect only $45,000 of its $50,000 judgment. That is less than it would collect if all unit owners' interests in units were fully liable, but more than it would collect if only association assets were subject to attachment. (The judgment creditor may, however, satisfy his judgment in full by reaching the income stream of the association by appropriate creditor process.)

In a cooperative, on the other hand, the association creditor can reach the entire interest of any of the unit owners in their units and will have its judgment satisfied in full.

The liability of cooperative unit owners to association judgment creditors is less than that of unit owners in condominiums and planned communities in that there is no statutory provision giving the judgment creditor a direct lien against units. Since, in a cooperative, title to the units is in the cooperative, a judgment creditor of the association will have a lien on the units, but under ordinary recording and priority rules, that lien will be subordinate to unit owner interests in units if those interests were recorded prior to the attachment of the judgment lien. Therefore, in a cooperative, there is a possibility that the judgment lienor will have no rights as against the interests of the unit owners. However, the declaration may provide that association creditors have priority

over the interests of cooperative unit owners, and, if it does so, such a provision is effective (see Section 2-118), and even in the absence of Section 2-118 would be effective, as a general subordination of unit owner interests to creditors of the association. (The Act in Section 2-118 requires that all creditors of the association be treated in the same way as to priority against unit owners so that the declaration cannot provide, for example, that only contract creditors have priority over unit owners or, for another example, that only regulated financial institution debt has priority. However, the unit owners might subordinate their interest to the rights of individual creditors of the association by giving that individual creditor a subordination agreement.)

However, upon termination of the cooperative, liens against the cooperative which did not have priority over the cooperative interests do become proportional fractional liens against each individual cooperative interest (see Section 2-118(i) and the Comments thereto).

3. The provisions of Section 3-117 applicable to condominiums and planned communities were adopted after substantial consideration by the Committee and the National Conference and achieve what the drafters believe is appropriate unit owner liability for association debts. The somewhat different treatment given cooperatives arises out of the different history of cooperatives and out of the different tradition as to financing of cooperatives. The rules just stated in effect continue the existing law as to the relationship between cooperative unit owners (today commonly called proprietary lessees) and association creditors. The provisions also take account of a common way of financing cooperatives: in the typical cooperative, the cooperative association will take title to the real estate and will assume or take subject to existing mortgages on the real estate, or if there are no existing mortgages, will borrow a significant portion of the purchase price of the cooperative real estate and secure that price by a mortgage on the real estate. Thereafter, when individual units are conveyed (leased) to individual unit owners, the unit owner's interest will be subject to the prior recorded underlying mortgage. The unit owner also will commonly borrow money on the security of his lease interest to pay the purchase price of the unit owner's interest. Unless a subordination agreement has been taken from the unit owner or subordination of unit owner interest to subsequent association creditors is provided for in the declaration, the unit purchase financing lender who lends on the security of the unit owner's interest can assess his risk on the assumption that he will never be subject to a greater proportion of the underlying debt than he is at the time the loan is originally made. If there is a subordination agreement, the unit financing lender knows that his security interest is subject to being entirely defeated by subsequent transactions between the association and its creditors. In the cooperative context, that system has worked reasonably well, and many people with substantial experience with housing cooperatives wished to continue that system in the Model Real Estate Cooperative Act and in the Uniform Common Interest Ownership Act.

In the case of condominiums and planned communities, while the condominium or planned community judgment creditor has a direct lien against the units, the lien against a particular unit is limited to that unit's common interest percentage liability, and based on ordinary priority rules, the association judgment creditor's lien will be junior to any prior perfected liens or security interests in the unit owner's unit. Since the priority between association judgment creditors and holders of security interests or liens against individual units in condominiums or planned communities will be determined according to ordinary priority rules, as is the case of cooperatives in the absence of subordination agreements, the result as between association judgment creditors and holders of security interest or liens on individual units is essentially the same under all three acts. However, as pointed out above, as against the unit owner himself, the cooperative association lien creditor who

has priority over a unit owner's interest will have greater rights than does the association judgment creditor in the case of condominiums and planned communities.

4. It should be noted that, while the judgment lien runs directly against unit owners in condominiums and planned communities, the actual liability of the unit owner is almost identical with what it would be if the ordinary corporation rule insulating the unit owner from direct liability were applied. If the incorporated condominium or planned community association only is liable for a judgment, it will, of course, have no assets to satisfy the judgment except whatever personal property and real estate not a part of the common elements it owns. If a checking account or other cash funds of the association are attached or garnisheed by the creditor, the association, in order to maintain its operations and fulfill its other obligations, will be obliged to make an additional assessment against the unit owners to cover the judgment. The same result follows if the association is to prevent the sale of other assets at an execution sale. That additional assessment would be in precisely the amount for which this Act gives a direct lien against the individual unit owners. Further, if an association which is without sufficient assets to satisfy a judgment refuses to make assessments from which the creditor can have his claim satisfied, it is very likely that a court, in a supplemental proceeding on the judgment, would direct the association to make the necessary assessments against the unit owners. Unpaid assessments made by the association constitute liens against units just as do judgments.

Therefore, whether the lien of the judgment creditor runs against the units directly, or whether the lien is only against the association which finds it necessary to make additional assessments to satisfy the judgment, the unit owner who does not pay his proportionate share will end up with a lien against his unit.

The differences, therefore, between the lien system established by Section 3-117 for condominiums and planned communities and the system which would be applicable if ordinary corporation rules were applied are these:

(1) The unit owner can discharge his unit from the lien and free it from the possibility of being subsequently assessed by the association for the judgment by making a payment directly to the lien holder. This ability may be valuable to a unit owner who is in the process of selling or securing a mortgage on his unit during the period between the time the judgment is entered and the time the association makes a formal assessment against individual unit owners for the amount of the judgment lien.

(2) The judgment creditor through his ability to threaten to foreclose the lien on an individual unit if the judgment is not paid is given some leverage over individual unit owners to encourage them to see that the association pays the judgment. Procuring an assessment through pressure on individual unit owners may be quicker and cheaper for the judgment creditor than using supplemental proceedings and having a judge order that the board of directors make the necessary assessment.

5. In the rare case where, under corporation law an association could avoid payment of a judgment by dissolution of the association and vesting of title to the units or common elements the unit owners as tenants-in-common or otherwise, the National Conference of Commissioners on Uniform State Laws believes that that result is inappropriate, and that the unit in the condominium

or planned community itself should be viewed as equity property of the association capable of being reached by judgment creditors in satisfaction of the judgment. As a matter of social policy the condominium or planned community association is in quite a different position than the ordinary corporation. The corporation statutes provide shareholders immunity from liability for debts of the corporation to encourage investment in corporations whose entrepreneurial activities in the marketplace contribute to the general wealth and well-being of society. The condominium or planned community association, in managing the affairs of the homeowners, does not serve the same entrepreneurial function. It seems reasonable, as a matter of social policy, that an individual homeowner who would be fully liable for debts incurred in the renovation and maintenance of his home or for torts caused by his failure to adequately maintain the premises should not be able to entirely avoid that liability through the device of organizing with other homeowners into a condominium or planned community association. On the other hand, it is perhaps not fair to a unit owner in a condominium or planned community regime to have all of his assets at risk based on the contracts of the association over which he has little control and as to which he has only a fractional interest or benefit.

It should be noted that, except for situations in which the association has given a mortgage or deed of trust on common elements, the judgment creditor cannot assert a lien against common elements, but is rather left to a lien against the units. That is, the judgment creditor has no power to levy on the golf course or on the swimming pool or other open spaces and sell them independently of the units to satisfy the judgment.

SECTION 3-118. ASSOCIATION RECORDS.

(a) An association must retain the following:

(1) detailed records of receipts and expenditures affecting the operation and administration of the association and other appropriate accounting records;

(2) minutes of all meetings of its unit owners and executive board other than executive sessions, a record of all actions taken by the unit owners or executive board without a meeting, and a record of all actions taken by a committee in place of the executive board on behalf of the association;

(3) the names of unit owners in a form that permits preparation of a list of the names of all owners and the addresses at which the association communicates with them, in alphabetical order showing the number of votes each owner is entitled to cast;

(4) its original or restated organizational documents, if required by law other than

this [act], bylaws and all amendments to them, and all rules currently in effect;

(5) all financial statements and tax returns of the association for the past three years;

(6) a list of the names and addresses of its current executive board members and officers;

(7) its most recent annual report delivered to the [Secretary of State], if any;

(8) financial and other records sufficiently detailed to enable the association to comply with Section 4-109;

(9) copies of current contracts to which it is a party;

(10) records of executive board or committee actions to approve or deny any requests for design or architectural approval from unit owners; and

(11) ballots, proxies, and other records related to voting by unit owners for one year after the election, action, or vote to which they relate.

(b) Subject to subsections (c) and (d), all records retained by an association must be available for examination and copying by a unit owner or the owner's authorized agent:

(1) during reasonable business hours or at a mutually convenient time and location; and

(2) upon [five] days' notice in a record reasonably identifying the specific records of the association requested.

(c) Records retained by an association may be withheld from inspection and copying to the extent that they concern:

(1) personnel, salary, and medical records relating to specific individuals;

(2) contracts, leases, and other commercial transactions to purchase or provide goods or services, currently being negotiated;

(3) existing or potential litigation or mediation, arbitration, or administrative proceedings;

(4) existing or potential matters involving federal, state, or local administrative or other formal proceedings before a governmental tribunal for enforcement of the declaration, bylaws, or rules;

(5) communications with the association's attorney which are otherwise protected by the attorney-client privilege or the attorney work-product doctrine;

(6) information the disclosure of which would violate law other than this [act];

(7) records of an executive session of the executive board; or

(8) individual unit files other than those of the requesting owner.

(d) An association may charge a reasonable fee for providing copies of any records under this section and for supervising the unit owner's inspection.

(e) A right to copy records under this section includes the right to receive copies by photocopying or other means, including copies through an electronic transmission if available upon request by the unit owner.

(f) An association is not obligated to compile or synthesize information.

(g) Information provided pursuant to this section may not be used for commercial purposes.

Comment

1. There are two significant policy issues connected with the association's records: first, what records the association must retain, and second, who has access to those records. The 2008 amendments address both.

The original version of Section 3-118 dealt with these matters in a minimalist way. Regarding records maintenance, the first sentence of 3-118 required only that the association maintain those records needed to comply with Section 4-109 – that is , the obligation to provide a resale certificate. This minimum requirement was far less expansive than the provisions of, for

example, the Revised Model Non-Profit Corporation Act; it plainly did not address the significant issues of records maintenance that have arisen since UCIOA was first promulgated 25 years ago.

Section 3-118 was similarly superficial regarding issues of records access; it mandated simply that 'all' records of the association be 'reasonably available for examination by any unit owner or his authorized agent' – leaving questions as to whether the word reasonable" modified 'all …records' as well as "available", and leaving unanswered the large range of issues that courts and legislatures have struggled with in this field over the last quarter century.

2. The 2008 amendments replace the "minimalist" provisions of UCIOA Section 3-118 with provisions generally consistent with the cognate provisions of the Revised Model Nonprofit Corporation Act, supplemented by specific provisions from other more modern State enactments and proposals in the homes association field. In this latter regard, the amendments, for example, authorize a unit owner to have access to a mailing list of unit owners, although the association may retain the right to mail materials to unit owners at their last known addresses, in order to maintain the unit owners' privacy; and (ii) insure that minutes of all meetings must be kept.

3. Section 3-118(a) outlines the records that the Association must retain. The subsection generally avoids any substantive requirements as to how the Association's financial records are to be maintained, relying simply on the obligation to retain "detailed records of receipts" and "appropriate accounting records", "all financial statements and tax returns for the past 3 years" and, as in the original Act, "financial and other records sufficiently detailed to enable the association" to provide a resale certificate under Section 4-109." The Act rejects any proposal that it require records to be maintained in accordance with "generally accepted accounting principles"; there are simply too many associations for which that would be an unnecessary and burdensome requirement.

4. The rules of various Bar associations make it imprudent for this Act to characterize the files of an attorney representing the association as property of the association and thereafter to assert that those files are nevertheless exempt from disclosure. For that reason, the Act does not address the status of an attorney's records, but section 3-118(c)(5) does make clear that communications with the association's attorney will generally be exempt from disclosure.

5. Many associations, especially smaller ones, may not have a complete set of records going back to the first organization of the association. This may be attributable to many reasons, and often are not the fault of the association or its current leadership. For example, the original declarant may not keep adequate records or may have failed to turn them over at transition. Managers may fail to turn records over when their contracts expire or are terminated.

In either of these cases, the cost of suing to obtain the missing records is prohibitive, or certainly out of proportion to the loss or inconvenience caused by the missing documents. In many smaller communities, the minutes and other non-financial records are kept by a volunteer officer of the association. If someone dies, is taken ill or moves away, the records are often lost. While this reality may impede the practical realization of the requirements in this Act, a goal of the section would be that over time, those "ancient" records may become of less practical importance in older associations, while newer associations will be guided by the requirements of this Section to adopt sound record keeping practices from the outset.

6. Subsection 3-118(b)(i) permits the parties to agree on a mutually acceptable time and place for the inspection of the records. If they do not agree, the subsection provides that the inspection shall take place "during reasonable business hours or at a mutually convenient time and location." Another concern has to do with smaller self-managed associations where the records may be kept by a unit owner who works during the day. If the volunteer treasurer cannot easily leave his or her job during the day to meet with a unit owner, it may be unreasonable to insist that the unit owner, or the unit owner's attorney or accountant, have the power to make the treasurer take a day off from work.

SECTION 3-119. ASSOCIATION AS TRUSTEE. With respect to a third person dealing with the association in the association's capacity as a trustee, the existence of trust powers and their proper exercise by the association may be assumed without inquiry. A third person is not bound to inquire whether the association has power to act as trustee or is properly exercising trust powers. A third person, without actual knowledge that the association is exceeding or improperly exercising its powers, is fully protected in dealing with the association as if it possessed and properly exercised the powers it purports to exercise. A third person is not bound to assure the proper application of trust assets paid or delivered to the association in its capacity as trustee.

SECTION 3-120. RULES.

(a) Before adopting, amending, or repealing any rule, the executive board shall give all unit owners notice of:

(1) its intention to adopt, amend, or repeal a rule and provide the text of the rule or the proposed change; and

(2) a date on which the executive board will act on the proposed rule or amendment after considering comments from unit owners.

(b) Following adoption, amendment, or repeal of a rule, the association shall notify the unit owners of its action and provide a copy of any new or revised rule.

(c) An association may adopt rules to establish and enforce construction and design criteria

and aesthetic standards if the declaration so provides. If the declaration so provides, the association shall adopt procedures for enforcement of those standards and for approval of construction applications, including a reasonable time within which the association must act after an application is submitted and the consequences of its failure to act.

(d) A rule regulating display of the flag of the United States must be consistent with federal law. In addition, the association may not prohibit display on a unit or on a limited common element adjoining a unit of the flag of this state, or signs regarding candidates for public or association office or ballot questions, but the association may adopt rules governing the time, place, size, number, and manner of those displays.

(e) Unit owners may peacefully assemble on the common elements to consider matters related to the common interest community, but the association may adopt rules governing the time, place, and manner of those assemblies.

(f) An association may adopt rules that affect the use of or behavior in units that may be used for residential purposes, only to:

(1) implement a provision of the declaration;

(2) regulate any behavior in or occupancy of a unit which violates the declaration or adversely affects the use and enjoyment of other units or the common elements by other unit owners; or

(3) restrict the leasing of residential units to the extent those rules are reasonably designed to meet underwriting requirements of institutional lenders that regularly make loans secured by first mortgages on units in common interest communities or regularly purchase those mortgages.

(g) An association's internal business operating procedures need not be adopted as rules.

(h) Every rule must be reasonable.

Comment

1. This section, new in 2008, addresses in a single location many of the Act's provisions concerning rules, including procedures governing how rules are to be adopted, and several constraints on what rules may address. Thus, the section now includes - in new subsection (f) - text that previously appeared in Section 3-102 (c) addressing the ability of the association to adopt rules that affect use and behavior in units. The section also addresses several new constraints on the association's ability to regulate unit owner behavior, consistent with increasing sentiment to this effect in a number of states.

2. Subsections (a) and (b) enable unit owners to be aware of and involved in the rules adoption process. Under these procedures, the association must notify unit owners of its intention to engage in changing the rules, and provide owners the text of any proposed change. Unit owners are also entitled to submit comments on the proposed rules, and to know of the date before which those comments may be submitted for consideration. Finally, under subsection (b), after a rule has been changed, the association must notify unit owners of the change, and provide them a copy of any new or revised rule.

3. The 2008 amendments address in several ways the subject of how and when the unit owners may be subjected to constraints on the owner's ability to make changes on the exterior appearance of a unit, or engage in construction activity on a unit - including a lot - that would be visible from outside the unit.

It is increasingly common throughout the United States for associations to assume the power to establish and enforce design criteria and control the exterior appearance of units, whether those units are in high rise condominiums, townhouses or single family homes on individually-owned lots. It is often asserted that the power of the association to maintain a uniformly attractive and consistent appearance throughout a community adds considerably to the value and desirability of many of these communities.

At the same time, anecdotal evidence suggests that many of the decisions made during the design approval process have been controversial and, in some instances, are subject to abuse by those charged with enforcing the design criteria.

The original UCIOA was silent on this subject, relegating it simply to the general reserved powers of the association. However, because of the importance of the subject, the Act adopts significant amendments to the design approval process. Taken as a whole, these changes confirm the ability of the association to adopt such a process, but subject to significant constraints intended to protect the interests of individual unit owners.

This section first provides in subsection (c) that the ability of the association to regulate the design process must be affirmatively reserved in the declaration. This tracks Section 2-105(a)(14) requiring that "[t]he declaration must contain ...(14) any authorization pursuant to which the association may establish and enforce construction and design criteria and aesthetic standards...."

Note that the ability of the declarant to do so must similarly be reserved as a special declarant right pursuant to Section 2-105 (a)(8). However, if that special declarant right is reserved,

the association's power under this section would be subject to that reserved special declarant right to control the construction or design review process during the development process.

Second, assuming the authority exists in the declaration, the section requires that the rules of the design committee must be formally promulgated by the executive board, including a procedure for prompt consideration of an application. The rules must also describe the consequences flowing from the failure of the design committee or other group charged with enforcement of the criteria to act on an application within the time frame stated. This does not mean that the necessary effect of that failure is that the application will be deemed approved; the rules may state a different consequence, as they are permitted to do. As a practical matter, however, one might expect that in the usual case, the parties to an application pending before a design committee may choose to formally agree to extend the time within which the committee is otherwise required to act, in order to avoid the consequences of a failure to act, and nothing in this Act is intended to affect the parties' ability to do so.

4. The Act creates a significant interplay between the declaration and the association's rules when the subject is the possibility of a change in a permitted "use occupancy, or behavior", as that term is used in 3-120(d)(2).

First, Section 2-105(a)(12) makes clear that the declaration may contain any leasing restrictions in addition to those restrictions permitted under 3-120(d), and any other restrictions on alienation of the units. Section 2-105(b) permits the declaration to contain any other "restrictions on the uses of a unit or the number or other qualifications of persons who may occupy units." Section 2-117(f) then provides significant protection for those permitted uses; it imposes an 80% vote requirement in order to "prohibit or materially restrict" any permitted uses of or behavior in a unit, or in the number or other qualifications of persons who may occupy units," although the declaration may also state that the 80% vote may be limited to a specific group of affected units. In addition, under the last sentence of (f), any restrictions on uses "must provide reasonable protection for a use or occupancy permitted at the time of the amendment.

Then, under Section 3-120, the association's ability to adopt rules affecting use of or behavior in units is restricted to implementing provisions of the declaration, or regulating "any behavior in or occupancy of a unit which ...adversely affects the use and enjoyment of the units or the common elements by other unit owners." An obvious example of the latter would be noise regulations.

5. Subsections (d) and (e) expand existing federal law mandating that unit owners be allowed to display the flag of the United States, **see** the Freedom To Display the American Flag Act of 2005, Public Law 109-243 to provide greater freedom of action to unit owners. These sections increase the rights of unit owners to display flags of the enacting State, and political signs on their units. Like the federal law, the association is entitled to adopt regulations governing the time, place, size, number and manner of those displays." Similarly, the unit owners are entitled under subsection (e) to peacefully assemble on the common elements to consider matters related to the common interest community.

6. Subsection (f), formerly §3-102(c), imposes clear limits on the association's power to control the use, occupancy, and leasing of units in residential projects. Basically, these amendments

adopt the policy that unless the declaration otherwise provides, "use" restrictions must appear in the declaration in order to be enforceable by the association, and the association's regulatory power over "occupancy" activities is limited to those situations in which a unit owner's activities inside a unit affect other owners.

7. In perhaps the most significant change affecting rules, subsection (h) requires all rules to be "reasonable." The reasonableness standard, unlike the business judgment rule, is likely to lead to considerable controversy over the impact of particular rules; it may also lead to more constraint in the adoption of a variety of rules, which some unit owners may find onerous.

SECTION 3-121. NOTICE TO UNIT OWNERS.

(a) An association shall deliver any notice required to be given by the association under this [act] to any mailing or electronic mail address a unit owner designates. Otherwise, the association may deliver notices by:

(1) hand delivery to each unit owner;

(2) hand delivery, United States mail postage paid, or commercially reasonable delivery service to the mailing address of each unit;

(3) electronic means, if the unit owner has given the association an electronic address; or

(4) any other method reasonably calculated to provide notice to the unit owner.

(b) The ineffectiveness of a good faith effort to deliver notice by an authorized means does not invalidate action taken at or without a meeting.

Comment

1. This section was added in 2008. The alternatives listed in sub-section (a) include all the forms of notice previously authorized in UCIOA section 3-108, which required that unit owners be given notice of meetings. The new additional forms of notice are electronic transmissions and "(4) any other method reasonably calculated to provide notice to the unit owner." Depending on the circumstances, this might include posting notice on bulletin boards, placing large and legible "sandwich boards" at the entrances to the common interest community, or other methods. As a consequence, the Act no longer designates the method of giving notice in particular instances, which is a departure from the former Act. The basic concept reflected in the language permitting electronic notice is taken from a 2004 Maryland statute; **see** Maryland Stat. Ann. § 11B-113.1.

2. The Act no longer requires that notice be given in a particular manner, and it does not require that the bylaws must specify the method by which notice is to be given. However, there is no reason why either the declaration or the bylaws could not specify a particular form or method of giving notice to the unit owners, and such a requirement would be binding on the association. Whether or not the documents designate a specific form of notice, the declaration cannot override the statement in subsection (b) that protects actions taken at a meeting despite the failure of the notice to actually be delivered, so long as the notice was given in good faith.

3. Note that whatever form of notice may be used or required in a particular common interest community, subsection 3-108(b)(5) requires that the unit owners in that community receive the same notice of a meeting of the executive board that is given to the members of the board.

SECTION 3-122. REMOVAL OF OFFICERS AND DIRECTORS.

(a) Notwithstanding any provision of the declaration or bylaws to the contrary, unit owners present in person, by proxy, or by absentee ballot at any meeting of the unit owners at which a quorum is present, may remove any member of the executive board and any officer elected by the unit owners, with or without cause, if the number of votes cast in favor of removal exceeds the number of votes cast in opposition to removal, but:

(1) a member appointed by the declarant may not be removed by a unit owner vote during the period of declarant control;

(2) a member appointed under Section 3-103(g) may be removed only by the person that appointed that member; and

(3) the unit owners may not consider whether to remove a member of the executive board or an officer elected by the unit owners at a meeting of the unit owners unless that subject was listed in the notice of the meeting.

(b) At any meeting at which a vote to remove a member of the executive board or an officer is to be taken, the member or officer being considered for removal must have a reasonable opportunity to speak before the vote.

Comment

1. The 2008 amendments simplify the procedures available for removal of officers or directors, compared to the spare provisions contained in section 3-103(g) of the Act before these amendments. Thus, for example, while the section speaks in terms of a "meeting" of unit owners held for the purpose of removal, the section should be read in conjunction with Section 3-110 on voting. There, unless the declaration or bylaws prohibits or limits the various means by which voting may be conducted, the full panoply of decision making by vote would be available in the context of a "meeting" to consider removal. Accordingly, subject to any limitations contained in the community's documents, a removal vote could be taken by electronic or paper ballot.

2. For the same reasons discussed in comment 1, proxies will commonly be permitted in recall votes. The drafters recognize that generally, if both sides are soliciting proxies, the unit owners are likely to be given a realistic opportunity to choose between positions. In any event, there is no reason to distinguish those votes where proxies are permitted from others where they are prohibited.

3. While the amended Act simplifies the procedures for a removal vote, other provisions of the new section are designed to protect the reasonable expectations of other stakeholders in the process, and to reflect a basic sense of fairness. Thus, for example, the Act requires that any person who is subject to a removal vote must be given an opportunity to speak before the vote. Further, if the vote were to be taken by ballot without a meeting, then the procedures in the Act that allow informational materials to be distributed before the ballots are due would satisfy the policy underlying this provision.

Similarly, the Act provides that no one but the person who appoints or elects a director may remove that director, thus protecting the legitimate interests of parties who may be entitled under the provisions of a particular community to appoint "outside" directors.

SECTION 3-123. ADOPTION OF BUDGETS; SPECIAL ASSESSMENTS.

(a) The executive board, at least annually, shall adopt a proposed budget for the common interest community for consideration by the unit owners. Not later than [30] days after adoption of a proposed budget, the executive board shall provide to all the unit owners a summary of the budget, including any reserves, and a statement of the basis on which any reserves are calculated and funded. Simultaneously, the board shall set a date not less than 10 days or more than 60 days after providing the summary for a meeting of the unit owners to consider ratification of the budget. Unless at that meeting a majority of all unit owners or any larger number specified in the declaration reject the budget, the budget is ratified, whether or not a quorum is present. If a

proposed budget is rejected, the budget last ratified by the unit owners continues until unit owners ratify a subsequent budget.

(b) The executive board, at any time, may propose a special assessment. Except as otherwise provided in subsection (c), the assessment is effective only if the executive board follows the procedures for ratification of a budget described in subsection (a) and the unit owners do not reject the proposed assessment.

(c) If the executive board determines by a two-thirds vote that a special assessment is necessary to respond to an emergency:

(1) the special assessment becomes effective immediately in accordance with the terms of the vote;

(2) notice of the emergency assessment must be provided promptly to all unit owners; and

(3) the executive board may spend the funds paid on account of the emergency assessment only for the purposes described in the vote.

Comment

1. Subsection (a) of section 3-123, a new section introduced in 2008, closely follows the text of section 3-103(c) in the 1994 version of the Act, except that it requires each annual budget to expressly address the subject of reserves.

2. The provisions of paragraph (a) permit the unit owners to disapprove any proposed budget, but a rejection of the budget does not result in cessation of assessments until a budget is approved. Rather, assessments continue on the basis of the last approved periodic budget until the new budget is in effect.

3. In 2008, the drafters extensively considered the issue of whether state law should mandate that the declarations of all common interest community associations create a reserve fund for the replacement of common elements as replacement becomes necessary and, if so, the extent to which they should be mandated. This is a subject of considerable scholarly debate and widely varying statutory treatment in the States.

As drafted, Section 3-102 (a)(2) requires the unit owners association to adopt budgets and Section 3-123 (a) requires the association to provide a summary of the budget - including any

provisions for reserves and a statement of the basis on which the reserves are calculated. However, the Act does not require that the association maintain any reserves.

This is not the policy of all States. Some states either mandate that reserves be maintained or establish a default rule that such reserves be created in the absence of an affirmative vote by the association membership not to create reserves. Other states require that the association board undertake periodic studies of the association's need for reserves.

It is also true that the underwriting guidelines used by Fannie Mae when deciding whether to purchase mortgages in common interest communities, requires in condominiums – but not in planned communities – not only that the association maintain reserves but that those reserves be "adequate," without defining the meaning of that word.

Evidence suggests that the needs, practices and expectations of unit owners in common interest communities differ widely, depending on, for example, the size, age, location and design of the physical structures as well as the age, economic circumstances and other demographic characteristics of the unit owners.

For example, small, self-managed associations commonly will maintain minimal reserves and will typically self-assess for repairs as needed. Other larger common interest communities, particularly in high maintenance buildings, may choose to establish substantially higher reserves.

On the other hand, it appears that very few associations maintain reserves at a level which would be actuarially required by evaluating the useful life of each component of the building and then accumulating reserves through increases in the monthly common charges paid by each owner, based on a schedule reflecting each component's useful life.

Associations confront the same choices that a single family homeowner confronts in thinking about, for example, the future need to replace the roof on her house. That owner has at least three choices: (i) she can set aside a sum of money each month in a segregated fund – perhaps even calling it a 'reserve' fund – so that when the roof or other parts of her home need to be replaced, she will have the needed funds; (2) she can maintain savings which are not segregated and pay cash from those savings at the time the roof replacement occurs; or (3) she can borrow the needed funds, and pay that money back during the years when she is enjoying a dry home. She can also use a combination of these techniques. Today, encouraged by state laws such as UCIOA § 3-102(a)(8), which enables associations to pledge their future common charges as security for a loan, UCIOA § 3-112, which enables associations to mortgage the common elements as security for a loan, and UCIOA § 2-119, which confirms the rights of lenders to enforce conventional loan terms against associations, associations are increasingly borrowing as an alternative to self-funding of reserves by unit owners who may, in fact, be unable to realize the economic value of those reserve payments if the sell their units early in the life of the project.

The drafters were also mindful of the impact of a possible law mandating reserves on the needs of the elderly and those of limited economic means. In practice, older unit owners often resist reserves, while younger families may perceive a greater long term value in their creation. There are also special concerns for lower income owners in common interest communities, where poorer owners may default on their mortgages and abandon their units because of their inability to maintain mortgage payments and monthly common charges. If a statute were to mandate fully

funded reserve payments, policy maker should then be concerned with two possible unintended consequences: first, such a mandate might so raise the monthly common charges that many potential buyers might be disqualified from homeownership; and second, the increases in charges might accelerate the collapse of common interest communities housing marginal income existing owners, who might abandon their units in increased numbers. Neither of these outcomes would be desirable.

At the same time, the drafters understood the natural interest of elected officials, who may often be faced with constituent demands that government 'do something' about a common interest community that has not prudently managed its affairs, with the result that needed repairs have not been made and the needed funding is not readily identifiable.

For these reasons, this act is drafted on the assumption that the most appropriate statutory means of addressing this concern was to first, require the declarant to address the issue of reserves in the Public Offer Statement prepared pursuant to Section 4-103. The text in subsection 4-103(b) – relocated from former 4-103(a)(5) – requires in pertinent part that

> (b) The public offering statement must contain any current balance sheet and a projected budget for the association, **** The budget must include:
>
> > (A) a statement of the amount, or a statement that there is no amount, included in the budget as a reserve for repairs and replacement;
> > (B) a statement of any other reserves;
> > (C) the projected common expense assessment by category of expenditures for the association; and
> > (D) the projected monthly common expense assessment for each type of unit.

Besides mandatory disclosure of the status of reserves in the initial public offering statement, Section 4-109(5) of the Act confirms that the issue of reserves be fully disclosed in later resale documents.

Clearly, these sections simply require that the declarant affirmatively address the issue one way or the other, and that the association continue the practice for later purchasers. Presumably, once required to address the issue, the declarant and its professional advisors will draft a reasoned provision consistent with their best sense of the nature of the particular community and the likely financial circumstances of their purchasers.

Second, the Act addresses this concern by requiring the issue of reserves to be considered during the budget adoption process pursuant to Section 3-123(a). This provision does not require a particular outcome. But it does require that the budget must affirmatively address the issue one way or the other. Again, like the declarant, once the association is required to address the issue, the association will likely adopt a reasoned budget consistent with the financial needs and circumstances of its members.

These provisions do not in any way interfere with the flexibility of a declarant in addressing this and many other subjects of the budget process of associations. The provisions do not mandate fully funded reserves or "adequate" reserves and do not prevent future unit owners, after the end of the period of declarant control, from changing the initial result created by the declarant.

Thus, what this Act accomplishes is to make certain that the subject of reserves be consciously addressed by the party best suited at the time to understand the likely expectations and requirements of the unit owners. Over the long term, however, better education of declarants and unit owners alike, and the growth of 'best practices' in the common interest community field under the leadership of national and state interest groups, must provide the optimal outcome in each particular circumstance.

4. New subsection (b) addresses the issue of special assessments, a subject not addressed in the Act before 2008. The policy of the subsection assumes that, except in the case of an emergency, the executive board should follow the same procedures as apply in adoption of the regular periodic budget of the association.

On the other hand, it is not unusual for the executive board to be confronted with an emergency. In that event, as discussed in subsection (c), if 2/3s of the executive board determine that an emergency exists, the board may dispense with the unit owner vote and proceed directly to adopt a special assessment. The balance of subsection (c) describe various safeguards designed to avoid abusive use of the emergency special assessment.

Note that the term "special assessment" is not defined. However, as used in subsection (b), it refers to any assessment that is not part of the regular budget. Given the safeguards contained in (b), it is not likely that the procedure will be commonly abused.

5. The Act as drafted does not limit or prohibit the imposition of so-called "transfer fees." It does require their disclosure.

A transfer fee is, by definition, not assessed against all units in accordance with their percentages as required by Subsection 3-115(b) and it does not meet the description of a "common expense" in Section 3-115.

Some courts, in reviewing similar statutory provisions, have held that transfer fees are not permitted; see, e.g., Micheve, LLC vs. Wyndham Place at Freehold Condominium Association, 885 A.2d 35 (N.J. Super. Ct. App. Div. 2005.).

In any event, the Act takes no position on the validity or suitability of "transfer fees", whether imposed by the declarant, the association, or some third party. Plainly, there are abusive circumstances where some persons assert the right to be paid a fee on transfer of title; some states have sought to regulate such efforts. In other cases, advocates assert that transfer fees can measurably assist in the betterment of common interest communities, despite the fact that the fees are generally levied against persons who are departing from those communities and are therefore not likely to enjoy whatever theoretical benefits are to be realized as a consequence of these fees. The subject becomes more significant, of course, depending on the magnitude of the fees, and the extent to which the fees are paid at a time of rapidly increasing – rather than decreasing – property values.

Because of these variables, the drafters were unable to identify any obvious rule applicable to all such fees, other than to be clear that any such fees must be disclosed in the Public Offering Statement and in any resale certificate issued under Section 4-109. An amendment to Section 4-103(a)(7) requires disclosure of any fee due from either purchaser or seller at the time of sale.

SECTION 3-124. LITIGATION INVOLVING DECLARANT.

(a) The following requirements apply to an association's authority under Section 3-102 (a)(4) to institute and maintain a proceeding alleging a construction defect with respect to the common interest community, whether by litigation, mediation, arbitration, or administratively, against a declarant or an employee, independent contractor, or other person directly or indirectly providing labor or materials to a declarant:

(1) Subject to subsection (e), before the association institutes a proceeding described in this section, it shall provide notice in a record of its claims to the declarant and those persons that the association seeks to hold liable for the claimed defects. The text of the notice may be in any form reasonably calculated to give notice of the general nature of the association's claims, including a list of the claimed defects. The notice may be delivered by any method of service and may be addressed to any person if the method of service used:

(A) provides actual notice to the person named in the claim; or

(B) would be sufficient to give notice to the person in connection with commencement of an action by the association against the person.

(2) Subject to subsection (e), the association may not institute a proceeding against a person until [45] days after the association sends notice of its claim to that person.

(3) During the period described in paragraph (2), the declarant and any other person to which the association gave notice may present to the association a plan to repair or otherwise remedy the construction defects described in the notice. If the association does not receive a timely remediation plan from a person to which it gave notice, or if the association does not accept the terms of any plan submitted, the association may institute a proceeding against the person.

(4) If the association receives one or more timely remediation plans, the executive

board shall consider promptly those plans and notify the persons to which it directed notice whether the plan is acceptable as presented, acceptable with stated conditions, or not accepted.

(5) If the association accepts a remediation plan from a person the association seeks to hold liable for the claimed defect, or if a person agrees to stated conditions to an otherwise acceptable plan, the parties shall agree on a period for implementation of the plan. The association may not institute a proceeding against the person during the time the plan is being diligently implemented.

(6) Except as otherwise provided in Section 4-116(d) for warranty claims, any statute of limitation affecting the association's right of action against a declarant or other person is tolled during the period described in paragraph (2) and during any extension of that time because a person to which notice was directed has commenced and is diligently pursuing the remediation plan.

(b) After the time described in subsection (a)(2) expires, whether or not the association agrees to any remediation plan, a proceeding may be instituted by:

(1) the association against a person to which notice was directed which fails to submit a timely remediation plan, the plan of which is not acceptable, or which fails to pursue diligent implementation of that plan; or

(2) a unit owner with respect to the owner's unit and any limited common elements assigned to that unit, regardless of any action of the association.

(c) This section does not preclude the association from making repairs necessary to mitigate damages or to correct any defect that poses a significant and immediate health or safety risk.

(d) Subject to the other provisions of this section, the determination of whether and when the association may institute a proceeding described in this section may be made by the executive

board. The declaration may not require a vote by any number or percent of unit owners as a condition to institution of a proceeding.

(e) This section does not prevent an association from seeking equitable relief at any time without complying with subsection (a)(1) or (2).

Comment

1. This section, also new in 2008, responds to the concerns of the home building industry, and to many common interest community advocates, who believe that policies designed to resolve construction disputes without resort to litigation are preferable to the existing common pattern of litigation following turnover of control of the association. This new section recognizes the broad support that various groups have expressed for this approach to dispute resolution, as well as the extent to which similar statutes have been adopted in the States. At the same time, this section adopts controls and limitations on the use of the technique designed to avoid harm to associations in appropriate circumstances.

2. This section does not address issues that might arise under the warranty provisions of the Act, **see** Sec. 4-113 through 4-116, or the possibility of litigation against the declarant under other theories or in other circumstances. Consider, for example, the broad array of litigation that is commonly undertaken today involving land use hearings and appeals. If a declarant were to file an application for a zone change or site plan approval relating to a community, the community might choose to object to the application in part because it believes the declarant failed to construct the existing facilities properly. In such a circumstance, the declarant might argue that the intervention by the association "involved" a construction defect. The term "administrative proceedings", however, was not intended to apply to these kinds of proceedings, in that they do not involve "construction defects" arising in the instant proceeding.

Further, subsection (e) allows the association to seek injunctive or other equitable relief, without the delays imposed by this section.

The 2008 amendments to section 3-102(b) also make clear that the declaration may not impose any other limitations on the right of the association to commence litigation, except as provided in this section.

3. The possibility exists under this new section that there will be situations in which the association will send a notice to the declarant which the declarant will not consider to be sufficiently specific or where the declarant will respond to the association's notice with a plan that the association considers to be completely inadequate and rejects out of hand.

If the association then sues the declarant, arguments will perhaps arise over whether or not the association had satisfied the preconditions for suit. Even if the court were to dismiss the suit and if the statute of limitations on the claim has run in the meantime, the association will not be without remedy, because of the tolling provisions contained in subsection (a)(6).

[ARTICLE] 4

PROTECTION OF PURCHASERS

SECTION 4-101. APPLICABILITY; WAIVER.

(a) This [article] applies to all units subject to this [act], except as provided in subsection (b) or as modified or waived by agreement of purchasers of units in a common interest community in which all units are restricted to non-residential use.

(b) Neither a public offering statement nor a resale certificate need be prepared or delivered in the case of:

(1) a gratuitous disposition of a unit;

(2) a disposition pursuant to court order;

(3) a disposition by a government or governmental agency;

(4) a disposition by foreclosure or deed in lieu of foreclosure;

(5) a disposition to a dealer;

(6) a disposition that may be canceled at any time and for any reason by the purchase without penalty; or

(7) a disposition of a unit restricted to nonresidential purposes.

Comment

1. In the case of commercial and industrial common interest communities, the purchaser is often more sophisticated than the purchaser of residential units and thus better able to bargain for the protections he believes necessary. While this may not always be true, no objective test can be developed which easily distinguishes those commercial purchasers who are able to protect themselves from those who, in the ordinary course of business, have not developed such sophistication. At the same time, the cost of protection imposed by Article 4 may be substantial. Accordingly, subsection (a) permits waiver or modification of Article 4 protections in common interest communities where all units are restricted to non-residential use. However, except for certain waivers of implied warranties of quality (see Section 4-115) and certain exemptions from public offering statement and resale certificate requirements (see subsection (b)), no express waiver of the protections of this article with respect to the purchasers of residential units is permitted by this subsection. Accordingly, by operation of Section 1-104, the rights provided by this article may not be waived in the case of residential purchasers. Moreover, because of the interrelated rights of residential and commercial owners in mixed-use common interest communities, waiver or

modification of rights conferred by this article is restricted to purchasers in wholly non-residential common interest communities.

2. The 1994 amendment changed subsection (b)(7). The rationale for the change is contained in the revised Comment to Section 1-203.

SECTION 4-102. LIABILITY FOR PUBLIC OFFERING STATEMENT REQUIREMENTS.

(a) Except as otherwise provided in subsection (b), a declarant, before offering any interest in a unit to the public, shall prepare a public offering statement conforming to the requirements of Sections 4-103, 4-104, 4-105, and 4-106.

(b) A declarant may transfer responsibility for preparation of all or a part of the public offering statement to a successor declarant (Section 3-104) or to a dealer that intends to offer units in the common interest community. In the event of any such transfer, the transferor shall provide the transferee with any information necessary to enable the transferee to fulfill the requirements of subsection (a).

(c) Any declarant or dealer that offers a unit to a purchaser shall deliver a public offering statement in the manner prescribed in Section 4-108(a). The declarant or dealer that prepared all or a part of the public offering statement is liable under Sections 4-108 [and] [,] 4-117 [, 5-105, and 5-106] for any false or misleading statement set forth therein or for any omission of a material fact therefrom.

(d) If a unit is part of a common interest community and is part of any other real estate regime in connection with the sale of which the delivery of a public offering statement is required under the laws of this state, a single public offering statement conforming to the requirements of Sections 4-103, 4-104, 4-105, and 4-106 as those requirements relate to each regime in which the unit is located, and to any other requirements imposed under the laws of this state, may be prepared and delivered in lieu of providing two or more public offering statements.

Comment

This section permits declarants to transfer responsibility for preparation of a public offering statement to successor declarants or dealers, provided the declarant furnishes the information needed by the successor or dealer to complete the statement. The person who prepares the public offering statement is liable for his own misrepresentations and material omissions. A person who delivers a public offering statement prepared by others is responsible for any such deficiencies only to the extent he knows or reasonably should have known of them.

SECTION 4-103. PUBLIC OFFERING STATEMENT; GENERAL PROVISIONS.

(a) Except as otherwise provided in subsection (b), a public offering statement must contain or fully and accurately disclose:

(1) the name and principal address of the declarant and of the common interest community, and a statement that the common interest community is a condominium, cooperative, or planned community;

(2) a general description of the common interest community, including to the extent possible, the types, number, and declarant's schedule of commencement and completion of construction of buildings, and amenities that the declarant anticipates including in the common interest community;

(3) the number of units in the common interest community;

(4) copies and a brief narrative description of the significant features of the declaration, other than any plats and plans, and any other recorded covenants, conditions, restrictions, and reservations affecting the common interest community; the bylaws and any rules of the association; copies of any contracts and leases to be signed by purchasers at closing; and a brief narrative description of any contracts or leases that will or may be subject to cancellation by the association under Section 3-105;

(5) the financial information required by subsection (b);

(6) any services not reflected in the budget that the declarant provides, or expenses

that the declarant pays and which the declarant expects may become at any subsequent time a common expense of the association and the projected common expense assessment attributable to each of those services or expenses for the association and for each type of unit;

(7) any initial or special fee due from the purchaser or seller at the time of sale, together with a description of the purpose and method of calculating the fee;

(8) a description of any liens, defects, or encumbrances on or affecting the title to the common interest community;

(9) a description of any financing offered or arranged by the declarant;

(10) the terms and significant limitations of any warranties provided by the declarant, including statutory warranties and limitations on the enforcement thereof or on damages;

(11) a statement that:

(A) within 15 days after receipt of a public offering statement a purchaser, before conveyance, may cancel any contract for purchase of a unit from a declarant;

(B) if a declarant fails to provide a public offering statement to a purchaser before conveying a unit, that purchaser may recover from the declarant [10] percent of the sales price of the unit plus [10] percent of the share, proportionate to the purchaser's common expense liability, of any indebtedness of the association secured by security interests encumbering the common interest community; and

(C) if a purchaser receives the public offering statement more than 15 days before signing a contract, the purchaser may not cancel the contract;

(12) a statement of any unsatisfied judgment or pending action against the association, and the status of any pending action material to the common interest community of which a declarant has actual knowledge;

(13) a statement that any deposit made in connection with the purchase of a unit

will be held in an escrow account until closing and will be returned to the purchaser if the purchaser cancels the contract pursuant to Section 4-108, together with the name and address of the escrow agent;

(14) any restraints on alienation of any portion of the common interest community and any restrictions:

(A) on use, occupancy, and alienation of the units; and

(B) on the amount for which a unit may be sold or on the amount that may be received by a unit owner on sale, condemnation, or casualty loss to the unit or to the common interest community, or on termination of the common interest community;

(15) a description of the insurance coverage provided for the benefit of unit owners;

(16) any current or expected fees or charges to be paid by unit owners for the use of the common elements and other facilities related to the common interest community;

(17) the extent to which financial arrangements have been provided for completion of all improvements that the declarant is obligated to build pursuant to Section 4-119;

(18) a brief narrative description of any zoning and other land use requirements affecting the common interest community;

(19) any other unusual and material circumstances, features, and characteristics of the common interest community and the units;

(20) in a cooperative, a statement whether the unit owners will be entitled, for federal, state, and local income tax purposes, to a pass-through of deductions for payments made by the association for real estate taxes and interest paid the holder of a security interest encumbering the cooperative and a statement as to the effect on every unit owner if the association fails to pay real estate taxes or payments due the holder of a security interest encumbering the cooperative; and

(21) a description of any arrangement described in Section 1-209 binding the association.

(b) The public offering statement must contain any current balance sheet and a projected budget for the association, either within or as an exhibit to the public offering statement, for [one] year after the date of the first conveyance to a purchaser, and thereafter the current budget of the association, a statement of who prepared the budget, and a statement of the budget's assumptions concerning occupancy and inflation factors. The budget must include:

(A) a statement of the amount, or a statement that there is no amount, included in the budget as a reserve for repairs and replacement;

(B) a statement of any other reserves;

(C) the projected common expense assessment by category of expenditures for the association; and

(D) the projected monthly common expense assessment for each type of unit.

(c) If a common interest community composed of not more than 12 units is not subject to any development right and no power is reserved to a declarant to make the common interest community part of a larger common interest community, group of common interest communities, or other real estate, a public offering statement may include the information otherwise required by subsection (a) (9), (10), (15), (16), (17), (18), and (19) and the narrative descriptions of documents required by subsection (a)(4).

(d) A declarant promptly shall amend the public offering statement to report any material change in the information required by this section.

Comment

1. The best "consumer protection" that the law can provide to any purchaser is to insure that he has an opportunity to acquire an understanding of the nature of the products which he is purchasing. Such a result is difficult to achieve, however, in the case of the common interest community purchaser because of the complex nature of the bundle of rights and obligations which

each unit owner obtains. For this reason, the Act, adopting the approach of many so-called "second generation" condominium statutes, sets forth a lengthy list of information which must be provided to each purchaser before he contracts for a unit. This list includes a number of important matters not typically required in public offering statements under existing law. The requirement for providing the public offering statement appears in Section 4-102(c), and Section 4-108 provides purchasers with cancellation rights and imposes civil penalties upon declarants not complying with the public offering statement requirements of the Act.

2. Paragraph (a)(2) requires a general description of the common interest community and, to the extent possible, the declarant's schedule for commencement and completion of construction for all building amenities that will comprise portions of the common interest community.

Under Section 4-119 the declarant is obligated to complete all improvements shown on a site plan or other graphic representation in the public offering statement or other promotional materials unless they are labeled "NEED NOT BE BUILT." The estimated schedule of commencement and completion of construction dates provides a standard for judging whether a declarant has complied with those requirements.

3. Paragraph (4) requires the public offering statement to include copies of the declaration, bylaws, and any rules and regulations of the common interest community, as well as copies of any contracts or leases to be executed by the purchaser. In addition, the paragraph requires the public offering statement to include a brief narrative description of the significant features of those documents, as well as of any management contract, leases of recreational facilities, and other sorts of contracts which may be subject to cancellation by the association after the period of declarant control expires, as provided in Section 3-105. This latter requirement is intended to encourage the preparation of brief summaries of all common interest community documents in laymen's terms, i.e., the "brief narrative description" should be more than a simple explanation of what a declaration (or other document) is, but less than an extended legal analysis duplicating the contents of the documents themselves. The summary requirement is intended to alleviate the common problem of public offering statements being drafted in lawyers' terms and being no more comprehensible to laymen than the documents themselves.

4. The disclosure requirement of paragraph (6) is intended to eliminate the common deceptive sales practice known as "lowballing," a practice by which a declarant intentionally underestimates the budget for the association by providing many of the services himself during the initial sales period. In such a circumstance, the declarant commonly intends that, after a certain time, these services (which might include lawn maintenance, painting, security, bookkeeping, or other services) will become expenses of the association, thereby substantially increasing the periodic common expense assessments which association members must ultimately bear. By requiring the disclosure of these services (including the projected common expense assessment attributable to each) in paragraph (6), the Act seeks to minimize "lowballing."

5. Paragraph (9) requires disclosure of any financing "offered" by the declarant. The paragraph contemplates that a declarant disclose any arrangements for financing that may have been made, including arrangements with any unaffiliated lender to provide mortgages to qualified purchasers.

6. Under paragraph (10), the declarant is required to disclose the terms of all warranties provided by the declarant (including the statutory warranties set forth in Section 4-114) and to describe any significant limitations on such warranties, the enforcement thereof, or damages which may be collectible as a result of a breach thereof. This latter requirement would necessitate a description by the declarant of any exclusions or modifications of statutory warranties undertaken pursuant to Section 4-115. The statute of limitations for warranties set forth at Section 4-116, together with any separate written agreement (as required by Section 4-116) providing for reduction of the period of such statute of limitations, must also be disclosed.

7. Paragraph (14) requires that the declarant disclose the existence of any right of first refusal or other restrictions on the uses for which or classes of persons to whom units may be sold. It also requires disclosure of any provisions limiting the amount for which units may be sold or on the part of the sales price which may be retained by the selling unit owner. In some existing housing cooperatives for low income families the unit owner is required to sell at no more than a fixed sum; sometimes the amount which the unit owner paid; sometimes that plus a fixed appreciation. In addition to that practice, the section contemplates other possible limitations on the owner's right to receive sales proceeds such as a provision under which the developer shares in any appreciation in value.

8. Under paragraph (16), the declarant is obligated to disclose any current or expected fees or charges which unit owners may be required to pay for the use of the common elements and other facilities related to the common interest community. Such fees or charges might include swimming pool fees, golf course fees, or required membership fees for recreation associations. Such fees can represent a substantial addition to monthly assessments.

9. The "financial arrangements" required to be disclosed pursuant to paragraph (17) may vary substantially from one development to another. It is the intent of the paragraph to give purchasers as much information as possible with which to assess the declarant's ability to carry out his obligations to complete the improvements. For example, if a declarant has a commitment from a bank to provide construction financing for a swimming pool when 50% of the units in the common interest community are completed, that fact should be disclosed to potential purchasers.

10. In addition to the information required to be disclosed by paragraphs (1) through (18), paragraph (19) requires that the declarant disclose all other "unusual and material circumstances, features, and characteristics" of the common interest community and all units therein. This requires only information which is both "unusual **and** material." Thus, the provision does not require the disclosure of "material" factors which are commonly understood to be part of the common interest community, e.g., the fact that buildings have a roof, walls, doors, and windows. Similarly, the provision does not require the disclosure of "unusual" information about the common interest community which is not also "material," e.g., the fact that a common interest community is the first development of its type in a particular locality. Information which would normally be required to be disclosed pursuant to paragraph (19) might include, to the extent that they are unusual and material, environmental conditions affecting the use or enjoyment of the common interest community, features of the location of the common interest community, e.g., near the end of an airport runway or a planned rendering plant, and the like.

11. The cost of preparing a public offering statement can be substantial and may, particularly in the case of small common interest communities, represent a significant portion of the

cost of a unit. For that reason, subsection (b) permits a declarant to exclude from a public offering statement certain information in the case of a small common interest community (i.e., less than 12 units) which is not subject to development rights and which is not potentially part of a larger common interest community or group of common interest communities. Essentially, subsection (c) permits a declarant to exclude from a public offering statement those materials which, as a practical matter, require extended preparation effort by an attorney or engineer in addition of the normal effort which must be exerted to provide the declaration, bylaws, plats and plans, or other documents required by the Act.

12. For style purposes, subsection (b), new in 2008, now contains the mandated information previously required by 4-103(a)(5). In order to comply fully with the provision of subsection (b), the declarant must calculate the budget on the basis of his best estimate of the number of units which will be part of the common interest community during that budget year. This requirement as well operates to negate the effects of any attempted "lowballing."

SECTION 4-104. SAME; COMMON INTEREST COMMUNITIES SUBJECT TO DEVELOPMENT RIGHTS. If the declaration provides that a common interest community is subject to any development rights, the public offering statement must disclose, in addition to the information required by Section 4-103:

(1) the maximum number of units, and the maximum number of units per acre, that may be created;

(2) a statement of how many or what percentage of the units that may be created will be restricted exclusively to residential use, or a statement that no representations are made regarding use restrictions;

(3) if any of the units that may be built within real estate subject to development rights are not to be restricted exclusively to residential use, a statement, with respect to each portion of that real estate, of the maximum percentage of the real estate areas, and the maximum percentage of the floor areas of all units that may be created therein, that are not restricted exclusively to residential use;

(4) a brief narrative description of any development rights reserved by a declarant and of any conditions relating to or limitations upon the exercise of development rights;

(5) a statement of the maximum extent to which each unit's allocated interests may be changed by the exercise of any development right described in paragraph (3);

(6) a statement of the extent to which any buildings or other improvements that may be erected pursuant to any development right in any part of the common interest community will be compatible with existing buildings and improvements in the common interest community in terms of architectural style, quality of construction, and size, or a statement that no assurances are made in those regards;

(7) general descriptions of all other improvements that may be made and limited common elements that may be created within any part of the common interest community pursuant to any development right reserved by the declarant, or a statement that no assurances are made in that regard;

(8) a statement of any limitations as to the locations of any building or other improvement that may be made within any part of the common interest community pursuant to any development right reserved by the declarant, or a statement that no assurances are made in that regard;

(9) a statement that any limited common elements created pursuant to any development right reserved by the declarant will be of the same general types and sizes as the limited common elements within other parts of the common interest community, or a statement of the types and sizes planned, or a statement that no assurances are made in that regard;

(10) a statement that the proportion of limited common elements to units created pursuant to any development right reserved by the declarant will be approximately equal to the proportion existing within other parts of the common interest community, or a statement of any other assurances in that regard, or a statement that no assurances are made in that regard;

(11) a statement that all restrictions in the declaration affecting use, occupancy, and alienation of units will apply to any units created pursuant to any development right reserved by the

declarant, or a statement of any differentiations that may be made as to those units, or a statement that no assurances are made in that regard; and

(12) a statement of the extent to which any assurances made pursuant to this section apply or do not apply in the event that any development right is not exercised by the declarant.

Comment

This section requires disclosure in the public offering statement of the manner in which the declarant's exercise of development rights may affect purchasers who acquire units before those rights have been fully exercised. The purpose is to put the purchaser on notice of the extent to which the exercise of those rights may alter, sometimes quite dramatically, both the physical and the legal aspects of the project. For example, the prospective purchaser may be contemplating the acquisition of a particular unit because it enjoys a view of open, undeveloped land over which the declarant has, however, reserved development rights. It may be that the boundary of the parcel as to which development rights have been reserved actually coincides with, or runs quite close to, the outer wall of the unit in question. The disclosures or statements made pursuant to paragraphs (8) and (12) of this section will indicate to the prospective purchaser the extent (if any) to which he can rely on the declarant not to do anything which would radically alter the view from the unit.

SECTION 4-105. SAME; TIME SHARES. If the declaration provides that ownership or occupancy of any units, is or may be in time shares, the public offering statement shall disclose, in addition to the information required by Section 4-103:

(1) the number and identity of units in which time shares may be created;

(2) the total number of time shares that may be created;

(3) the minimum duration of any time shares that may be created; and

(4) the extent to which the creation of time shares will or may affect the enforceability of the association's lien for assessments provided in Section 3-116.

Comment

1. Time sharing has become increasingly important in recent years, particularly with respect to resort common interest communities. In recognition of this fact, this section requires the disclosure of certain information with respect to time sharing.

2. Virtually all existing state statutes dealing with condominiums, planned communities, or cooperatives are silent with respect to time-share ownership. The inclusion of disclosure provisions

for certain forms of time sharing in this Act, however, does not imply that other law regulating time sharing is affected in any way in a State merely because that State enacts this Act.

The Uniform Law Commissioners' Model Real Estate Time-Share Act specifies more extensive disclosures for time-share properties. A "time-share property" may include part or all of the common interest community, and Section 1-109 of the Model Act governs conflicts between this Act and time-share legislation.

SECTION 4-106. SAME; COMMON INTEREST COMMUNITIES CONTAINING CONVERSION BUILDINGS.

(a) The public offering statement of a common interest community containing any conversion building must contain, in addition to the information required by Section 4-103:

(1) a statement by the declarant, based on a report prepared by an independent [registered] architect or engineer, describing the present condition of all structural components and mechanical and electrical installations material to the use and enjoyment of the building;

(2) a statement by the declarant of the expected useful life of each item reported on in paragraph (1) or a statement that no representations are made in that regard; and

(3) a list of any outstanding notices of uncured violations of building code or other municipal regulations, together with the estimated cost of curing those violations.

(b) This section applies only to buildings containing units that may be occupied for residential use.

Comment

1. In the case of a common interest community containing one or more conversion buildings, the disclosure of additional information relating to the condition of those buildings is required in the public offering statement because of the difficulty inherent in a single purchaser attempting to determine the condition of what is likely to be an older building being renovated for the purpose of common interest community sales.

2. Paragraph (a)(1) requires the person who gives the public offering statement to retain an independent architect or engineer to report on the present condition of all structural components and fixed mechanical and electrical installations in the conversion building. Such information is as useful to declarant as to the purchaser since, under the implied warranty provisions of Section 4-114, a declarant impliedly warrants all improvements made by any person to the building "before

creation of the common interest community" unless such improvements are specifically excluded from the implied warranty of quality pursuant to Section 4-115(b).

3. See Comment 6 to Section 2-101 concerning the meaning of "structural components" as used in paragraph (a)(1). Any material changes in the "present condition" of these systems must be reported by an amendment to the public offering statement.

4. Under paragraph (a)(3), the person required to give the public offering statement is required to provide purchasers with a list of all outstanding notices of uncured violations of building codes or other municipal regulations. The literal wording of this provision does not require disclosure of known violations of such building codes or municipal regulations (at least violations having no effect upon the structural components or fixed mechanical and electrical installations of the planned community) unless actual "notices" of such violations have been received. To the extent that outstanding notices of uncured violations do exist, the cost of curing such violations would become a liability of the unit owners or the association following transfer of the unit to a purchaser. For that reason, the estimated cost of curing any outstanding violations must also be disclosed.

5. For the reasons set forth in the Comment to Section 4-101(a), this section does not apply to units which are restricted exclusively to non-residential use.

SECTION 4-107. SAME; COMMON INTEREST COMMUNITY SECURITIES.

If an interest in a common interest community is currently registered with the Securities and Exchange Commission of the United States, a declarant satisfies all requirements relating to the preparation of a public offering statement of this [act] if the declarant delivers to the purchaser [and files with the agency] a copy of the public offering statement filed with the Securities and Exchange Commission. [An interest in a common interest community is not a security under the provisions of [insert appropriate state securities regulation statutes].]

Comment

1. Some common interest communities will be regarded as "investment contracts" or other "securities" under federal law because they exhibit certain investment features such as mandatory rental pools. See SEC Securities Act Release No. 5347 (January 1973). The purpose of this section is to permit the declarant to file or deliver, in lieu of a public offering statement specifically prepared to comply with the provisions of this Act, the prospectus filed with and distributed pursuant to the regulations of the United States Securities and Exchange Commission. Absent this provision, prospective purchasers of common interest communities classified by the SEC as "securities" would have to be given two public offering statements, one prepared pursuant to this Act and the other prepared pursuant to the Securities Act of 1933. Not only would this result

increase the declarant's costs (and thus the price) of units, it might also reduce the likelihood of either public offering statement actually being read by prospective purchasers.

2. The bracketed language in the first sentence of this section should be inserted by States which choose to adopt the agency provisions of Article 5 of the Act. The second sentence should also be inserted by States opting to incorporate Article 5 of the Act to avoid duplicative regulation of common interest communities by the agency administering the State's securities regulation statutes.

SECTION 4-108. PURCHASER'S RIGHT TO CANCEL.

(a) A person required to deliver a public offering statement pursuant to Section 4-102(c) shall provide a purchaser with a copy of the public offering statement and all amendments thereto before conveyance of the unit, and not later than the date of any contract of sale. Unless a purchaser is given the public offering statement more than 15 days before execution of a contract for the purchase of a unit, the purchaser, before conveyance, may cancel the contract within 15 days after first receiving the public offering statement.

(b) If a purchaser elects to cancel a contract pursuant to subsection (a), he may do so by hand delivering notice thereof to the offeror or by mailing notice thereof by prepaid United States mail to the offeror or to his agent for service of process. Cancellation is without penalty, and all payments made by the purchaser before cancellation must be refunded promptly.

(c) If a person required to deliver a public offering statement pursuant to Section 4-102(c) fails to provide a purchaser to whom a unit is conveyed with that public offering statement and all amendments thereto as required by subsection (a), the purchaser, in addition to any rights to damages or other relief, is entitled to receive from that person an amount equal to [10] percent of the sale price of the unit, plus [10] percent of the share, proportionate to his common expense liability, of any indebtedness of the association secured by security interests encumbering the common interest community.

Comment

1. The "cooling off" period provided to a purchaser in this section is similar to provisions in many current state condominium statutes.

2. Subsection (a) requires that each purchaser be provided with both the public offering statement and all amendments thereto prior to the time that the unit is conveyed. If there is a contract for the sale of the unit, these documents must be provided not later than the date of the contract. The section makes clear that any amendments to the public offering statement prepared between the date of any contract and the date of conveyance must also be provided to the purchaser.

3. This section does not require the delivery of a public offering statement prior to the execution by the purchaser of an agreement pursuant to which the purchaser reserves the right to buy a unit but is not contractually bound to do so. Because such agreements (frequently referred to as "non-binding reservation agreements") may be unilaterally canceled at any time by a prospective purchaser without penalty, they do not constitute "contract[s] of sale" within the meaning of the section.

4. The requirement set forth in subsection (a) that a purchaser be provided with subsequent amendments to the public offering statement during the period between execution of the contract for purchase and conveyance of the unit does not, in itself, extend the "cooling off" period. Indeed, the delivery of such amendments is required even if the "cooling off" period has expired. The purpose of this requirement is to assure that purchasers of units are advised of any material change in the common interest community which may affect their sales contracts under general law. While many such amendments will be merely technical and will not affect the bargain that the purchaser and declarant entered into, each purchaser should be permitted to judge for himself the materiality of any change in the nature of the common interest community.

5. Under the scheme set forth in this section, it is at least theoretically possible that there will be a contract for sale of the unit, and that a public offering statement will be given to the purchaser at closing just prior to conveyance. However, the available evidence suggests that such practice would be rare, and that the provision of a public offering statement moments prior to conveyance would, in itself, tend to dampen the enthusiasm of the purchaser for immediate closing. In such circumstances, under subsection (a), the purchaser would, as a matter of right, be able to extend the date of closing for 15 days from the time the public offering statement is provided. This fact, together with the generally unsatisfactory experience with mandatory "cooling off" periods such as that imposed under the federal Real Estate Settlement Procedures Act, supports the conclusion that it is inappropriate to require a minimum period of delay between delivery of a public offering statement and conveyance.

6. Under subsection (a), the failure to deliver a public offering statement before conveyance does not result in a statutory right by the purchaser to cancel the conveyance or to reconvey the unit once conveyance has occurred. Any such cancellation or reconveyance following an actual conveyance could create serious mechanical and title problems that could not be easily resolved. The failure of the Act to provide for such cancellation or reconveyance is not, however, intended to diminish any right which a purchaser may otherwise have under general state law. For example, where it appears that a seller, by deliberately failing to disclose certain material information with respect to a transaction, substantially changed the bargain which he and the purchaser entered into,

it is possible that under the common law in some States reconveyance would be an available remedy.

Even absent such resort to general law, however, the penalty provisions of subsection (c) are designed to provide a sufficient incentive to the seller to insure that the public offering statement is provided in the timely fashion required by the Act. The penalty so specified in the subsection is in addition to any right a prevailing purchaser may have under Section 4-117 to collect punitive damages and attorney's fees in connection with his action against the declarant.

SECTION 4-109. RESALES OF UNITS.

(a) Except in the case of a sale in which delivery of a public offering statement is required, or unless exempt under Section 4-101(b), a unit owner shall furnish to a purchaser before the earlier of conveyance or transfer of the right to possession of a unit, a copy of the declaration, other than any plats and plans, the bylaws, the rules or regulations of the association, and a certificate containing:

(1) a statement disclosing the effect on the proposed disposition of any right of first refusal or other restraint on the free alienability of the unit held by the association;

(2) a statement setting forth the amount of the periodic common expense assessment and any unpaid common expense or special assessment currently due and payable from the selling unit owner;

(3) a statement of any other fees payable by the owner of the unit being sold;

(4) a statement of any capital expenditures approved by the association for the current and succeeding fiscal years;

(5) a statement of the amount of any reserves for capital expenditures and of any portions of those reserves designated by the association for any specified projects;

(6) the most recent regularly prepared balance sheet and income and expense statement, if any, of the association;

(7) the current operating budget of the association;

(8) a statement of any unsatisfied judgments against the association and the status of any pending suits in which the association is a defendant;

(9) a statement describing any insurance coverage provided for the benefit of unit owners;

(10) a statement as to whether the executive board has given or received notice in a record that any existing uses, occupancies, alterations, or improvements in or to the unit or to the limited common elements assigned thereto violate any provision of the declaration;

(11) a statement as to whether the executive board has received notice in a record from a governmental agency of any violation of environmental, health, or building codes with respect to the unit, the limited common elements assigned thereto, or any other portion of the common interest community which has not been cured;

(12) a statement of the remaining term of any leasehold estate affecting the common interest community and the provisions governing any extension or renewal thereof;

(13) a statement of any restrictions in the declaration affecting the amount that may be received by a unit owner upon sale, condemnation, casualty loss to the unit or the common interest community, or termination of the common interest community;

(14) in a cooperative, an accountant's statement, if any was prepared, as to the deductibility for federal income tax purposes by the unit owner of real estate taxes and interest paid by the association;

(15) a statement describing any pending sale or encumbrance of common elements; and

(16) a statement disclosing the effect on the unit to be conveyed of any restrictions on the owner's right to use or occupy the unit or to lease the unit to another person.

(b) The association, within 10 days after a request by a unit owner, shall furnish a

certificate containing the information necessary to enable the unit owner to comply with this section. A unit owner providing a certificate pursuant to subsection (a) is not liable to the purchaser for any erroneous information provided by the association and included in the certificate.

(c) A purchaser is not liable for any unpaid assessment or fee greater than the amount set forth in the certificate prepared by the association. A unit owner is not liable to a purchaser for the failure or delay of the association to provide the certificate in a timely manner, but the purchase contract is voidable by the purchaser until the certificate has been provided and for [five] days thereafter or until conveyance, whichever first occurs.

Comment

1. In the case of the resale of a unit by a private unit owner who is not a declarant or a person in the business of selling real estate for his own account, a public offering statement need not be provided. See Section 4-102(c). Nevertheless, there are important facts which a purchaser should have in order to make a rational judgment about the advisability of purchasing the particular unit. Accordingly, each unit owner not required to furnish a public offering statement under Section 4-102(c) and not exempt under Section 4-101(b) is required to furnish to a resale purchaser, before the execution of any contract of sale, a copy of the declaration, bylaws, and rules and regulations of the association and a variety of fiscal, insurance, and other information concerning the common interest community and the unit.

2. While the obligation to provide the information required by this section rests upon each unit owner (since the purchaser is in privity only with that unit owner), the association has an obligation to provide the information to the unit owner within 10 days after a request for such information. Under Section 3-102(a)(12), the association is entitled to charge the unit owner a reasonable fee for the preparation of the certificate. Should the association fail to provide the certificate as required, the unit owner would have a right to action against the association pursuant to Section 4-117.

3. Under subsection (c), if a purchaser receives a resale certificate which fails to state the proper amount of the unpaid assessments due from the purchased unit, the purchaser is not liable for any amount greater than that disclosed in the resale certificate. Because a resale purchaser is dependent upon the association for information with respect to the outstanding assessments against the unit which he contemplates buying, it is altogether appropriate that the association should be prohibited from later collecting greater assessments than those disclosed prior to the time of the resale purchase.

4. The 1994 revisions to this section track amendments in adopting States which simplified the contents of the resale certificate.

SECTION 4-110. ESCROW OF DEPOSITS. Any deposit made in connection with the purchase or reservation of a unit from a person required to deliver a public offering statement pursuant to Section 4-102(c) must be placed in escrow and held either in this state or in the state where the unit is located in an account designated solely for that purpose by [a licensed title insurance company] [an attorney] [a licensed real estate broker] [an independent bonded escrow company or] an institution whose accounts are insured by a governmental agency or instrumentality until (i) delivered to the declarant at closing; (ii) delivered to the declarant because of the purchaser's default under a contract to purchase the unit; or (iii) refunded to the purchaser.

Comment

1. This section applies to the sale by persons required to furnish public offering statements of residential units and of non-residential units unless waived pursuant to the provisions of Section 4-101. It does not apply, however, to resales of units between private parties.

2. This section provides declarant a number of choices as to the appropriate escrow agent. Whether the escrow agent must deposit the funds in an insured institutional depository, or in a particular type of account, depends on state law or the agreement of the parties. To minimize record keeping, of course, the institutional depository could itself be the escrow agent. The section does not require a separate account for each unit, so that mingling of funds in a single escrow account would be permitted. The account may be held either in the State where the unit is located, or in the enacting State, in recognition that buyers are often from outside the State where the unit is located.

3. The escrow requirements of this section apply in connection with **any** deposit made by a purchaser, whether such deposit is made pursuant to a binding contract or pursuant to a nonbinding reservation agreement (with respect to which no public offering statement is required under Section 4-101(b)(6)).

4. In some States current practice permits escrows to be held by certain title insurance or escrow companies, attorneys, or real estate brokers. Accordingly, the bracketed language should be included or deleted in accordance with local practice.

5. Under this section, any interest earned on an escrow deposit may, but need not, be credited to the purchaser at closing, added to any deposit forfeited to the seller, or added to any deposit refunded to the purchaser. In short, disposition of any interest is left to agreement of the parties.

6. In some States, such as New York, the substitution of a bond in place of a deposit escrow is permitted. The evidence indicates, however, that in many instances the use of the bonding device has forced purchasers to incur substantial costs and delay prior to obtaining refunds to which they

are entitled. For this reason, this Act does not include bonding as an alternative to the required escrow of deposits.

SECTION 4-111. RELEASE OF LIENS.

(a) In the case of a sale of a unit where delivery of a public offering statement is required pursuant to Section 4-102(c), a seller:

(1) before conveying a unit, shall record or furnish to the purchaser releases of all liens, except liens on real estate that a declarant has the right to withdraw from the common interest community, that the purchaser does not expressly agree to take subject to or assume and that encumber:

(A) in a condominium, that unit and its common element interest; and

(B) in a cooperative or planned community, that unit and any limited common elements assigned thereto; or

(2) shall provide a surety bond or substitute collateral for or insurance against the lien as provided for liens on real estate in [insert appropriate references to general state law or Sections 5-211 and 5-212 of the State Uniform Simplification of Land Transfers Act].

(b) Before conveying real estate to the association, the declarant shall have that real estate released from:

(1) all liens the foreclosure of which would deprive unit owners of any right of access to or easement of support of their units; and

(2) all other liens on that real estate unless the public offering statement describes certain real estate that may be conveyed subject to liens in specified amounts.

Comment

1. The exemption for withdrawable real estate set forth in subsection (a) is designed to preserve flexibility for the declarant in terms of financing arrangements. It deals with the unusual case in which a unit has been assigned a limited common element (for example, a parking space) on real estate which the developer has the right to withdraw from the common interest community. In

that case, the limited common element can be assigned to the unit without release of liens or assumption of them by the unit owner. Theoretically, a developer might partially avoid the lien release requirement of subsection (a) by placing part of the limited common element improvements such as a parking garage on withdrawable real estate. By doing so, it could separately mortgage that part of the limited common elements without being obligated to discharge the mortgage or secure partial releases when individual units to which the limited common elements are assigned are sold.

If a mortgage or other lien created by or arising against the developer attaches to withdrawable real estate after the declaration has been recorded, a lapse of the developer's right to withdraw the real estate would also terminate the rights of the lienors, since the lien would attach only to the developer's interest (the right to withdraw). However, an alert lienor would not permit the right to withdraw to lapse without taking steps to see that the right to withdraw is exercised. If the mortgage or other lien attached to the real estate and was perfected before the planned community declaration was recorded, lapse of the right to withdraw would not affect the lienor's rights and it could foreclose on the real estate whether or not the developer had lost the right to withdraw. As a practical matter, whether the mortgage or other lien against withdrawable real estate arises before or after the declaration is recorded, unit owners may find that, if the association does not release liens on withdrawable real estate containing limited common elements, the lienor will be able to withdraw the land and deprive the unit owners of its use. Therefore, unit purchasers and their counsel should be alert to that possibility.

2. Subsection (b) will most commonly apply in the case of a planned community, where all of the common elements, whatever they may be in a particular project, must be owned by the association, see Section 1-103(4), or in a cooperative, where Section 2-101 requires that all the real estate comprising the cooperative must be conveyed to the association at the time the cooperative is created. The section would also apply, however, in the event other real estate, such as units or other real property not subject to the declaration, is conveyed to the association.

SECTION 4-112. CONVERSION BUILDINGS.

(a) A declarant of a common interest community containing conversion buildings, and any dealer who intends to offer units in such a common interest community, shall give each of the residential tenants and any residential subtenant in possession of a portion of a conversion building notice of the conversion and provide those persons with the public offering statement no later than 120 days before the tenants and any subtenant in possession are required to vacate. The notice must set forth generally the rights of tenants and subtenants under this section and must be hand delivered to the unit or mailed by prepaid United States mail to the tenant and subtenant at the address of the unit or any other mailing address provided by a tenant. No tenant or subtenant may be required to vacate upon less than 120 days' notice, except by reason of nonpayment of rent,

waste, or conduct that disturbs other tenants' peaceful enjoyment of the premises, and the terms of the tenancy may not be altered during that period. Failure to give notice as required by this section is a defense to an action for possession.

(b) For [60] days after delivery or mailing of the notice described in subsection (a), the person required to give the notice shall offer to convey each unit or proposed unit occupied for residential use to the tenant who leases that unit. If a tenant fails to purchase the unit during that [60]-day period, the offeror may not offer to dispose of an interest in that unit during the following [180] days at a price or on terms more favorable to the offeree than the price or terms offered to the tenant. This subsection does not apply to any unit in a conversion building if that unit will be restricted exclusively to non-residential use or the boundaries of the converted unit do not substantially conform to the dimensions of the residential unit before conversion.

(c) If a seller, in violation of subsection (b), conveys a unit to a purchaser for value who has no knowledge of the violation, the recordation of the deed conveying the unit or, in a cooperative, the conveyance of the unit, extinguishes any right a tenant may have under subsection (b) to purchase that unit if the deed states that the seller has complied with subsection (b), but the conveyance does not affect the right of a tenant to recover damages from the seller for a violation of subsection (b).

(d) If a notice of conversion specifies a date by which a unit or proposed unit must be vacated and otherwise complies with the provisions of [insert appropriate state summary process statute], the notice also constitutes a notice to vacate specified by that statute.

(e) Nothing in this section permits termination of a lease by a declarant in violation of its terms.

Comment

1. One of the most controversial issues in the field of common interest community development relates to conversion of rental buildings to a common interest community. Opponents

of conversions point out that the frequent result of conversions, which occur principally in large urban areas, is to displace low- and moderate-income tenants and provide homes for more affluent persons able to afford the higher prices which the converted apartments command. Indeed, studies indicate that the burden of conversion displacement falls most frequently on low- and moderate-income and elderly persons. At the same time, the conversion of a building to common interest community ownership can lead to a substantial increase in property value, a result which proponents believe can be an important factor in curtailing the problem of declining urban tax bases. Proponents also point out that the conversion of rental units in inner-city areas to individual ownership frequently results in the stabilization of the buildings concerned, thus providing an important technique for use in neighborhood preservation and revitalization. This section, which seeks to balance these competing interests, is based principally on similar provisions set forth in the condominium statutes of Virginia and the District of Columbia.

2. In an attempt to strike a fair balance between the competing interests of rental tenants and prospective owners, subsection (b) provides the tenant a right for 60 days to purchase the unit which he leases at a price and on terms offered by the declarant. The subsection discourages unreasonable offers by declarants by providing that, if the tenant fails to accept the terms offered, the declarant may not thereafter sell the unit at a lower price or upon more favorable terms to a third person for at least 180 days. However, the declarant is not required to offer residential tenants the right to purchase commercial units or to offer to sell to tenants if the dimensions of their previous apartments have been substantially altered. The reason for this exception is that, if an apartment is subdivided or if two apartments are merged into a single planned community unit, compliance with the requirements of subsection (b) would be impossible.

3. Jurisdictions with rent control statutes should consider whether amendments to this section are necessary to conform to the procedures or substantive requirements set out in the rent control laws or whether modifications to the rent control laws may be required as a result of the enactment of this section.

4. Except for the restrictions on permissible evictions stated in subsection (a), this Act does not change the law of summary process in a State. As a result, if a tenant refuses to vacate the premises following the 120-day notice, the usual provisions of the State's summary process statutes would apply, while any defenses available to a tenant would also be available.

SECTION 4-113. EXPRESS WARRANTIES OF QUALITY.

(a) Express warranties made by a declarant to a purchaser of a unit, if relied upon by the purchaser, are created as follows:

(1) any affirmation of fact or promise which relates to the unit, its use, or rights appurtenant thereto, area improvements to the common interest community that would directly benefit the unit, or the right to use or have the benefit of facilities not located in the common interest community, creates an express warranty that the unit and related rights and uses will conform to the

affirmation or promise;

(2) any model or description of the physical characteristics of the common interest community, including plans and specifications of or for improvements, creates an express warranty that the common interest community will conform to the model or description unless the model or description clearly discloses that it is only proposed or is subject to change;

(3) any description of the quantity or extent of the real estate comprising the common interest community, including plats or surveys, creates an express warranty that the common interest community will conform to the description, subject to customary tolerances; and

(4) a provision that a purchaser may put a unit only to a specified use is an express warranty that the specified use is lawful.

(b) Neither formal words, such as "warranty" or "guarantee", nor a specific intention to make a warranty, are necessary to create an express warranty of quality, but a statement purporting to be merely an opinion or commendation of the real estate or its value does not create a warranty.

(c) Any conveyance of a unit transfers to the purchaser all express warranties of quality made by the declarant.

Comment

1. This section, together with Sections 4-114, 4-115, and 4-116, are adapted from the real estate warranty provisions contained in the Uniform Land Transactions Act (ULTA).

2. This section, which parallels Section 2-308 of ULTA, deals with express warranties, that is, with the expectations of the purchaser created by particular conduct of the declarant in connection with inducement of the sale. It is based on the principle that, once it is established that the declarant has acted so as to create particular expectations in the purchaser, warranty should be found unless it is clear that, prior to the time of final agreement, the declarant has negated the conduct which created the expectation.

3. Subsection (b) makes it clear that no specific intention to make a warranty is necessary if any of the factors mentioned in subsection (a) are made part of the basis of the bargain between the parties. In actual practice, representations made by a declarant concerning common interest community property during the bargaining process are typically regarded as a part of the description. Therefore, no particular reliance on the representations need be shown in order to weave them into the fabric of the agreement. Rather, the burden is on the declarant to show that

representations made in the bargaining process were not relied upon by the purchaser at the time of contracting.

4. Subsection (a)(1) provides that representations as to improvements and facilities not located in the common interest community may create express warranties. Declarants often assert that recreational facilities, such as swimming pools, golf courses, tennis courts, etc., will be constructed in the future and that unit owners will have the right to utilize such facilities once constructed. Such assertions are intended to be included within the language "have the benefit of facilities not located in the planned community." If, under the circumstances, such improvements would benefit the unit being sold, then the declarant may be liable for breach of express warranty if they are not completed. Such liability is distinct from the declarant's obligations, under Section 4-119, to complete all improvements labeled "MUST BE BUILT" on plats and plans.

5. Under subsection (a)(4), a contract provision permitting the purchaser to use a common interest community unit only for a specified use or uses creates an express warranty that the unit may lawfully be used for that purpose. Therefore, if there is a limitation on use, the resulting express warranty could not be disclaimed by a disclaimer of implied warranties under Section 4-115.

6. The precise time when representations set forth in subsection (a) are made is not material. The sole question is whether the language or other representations of the declarant are fairly to be regarded as part of the contract between the parties.

7. Subsection (b) makes clear that it is not necessary to the existence of a warranty that the declarant have intended to assume a warranty obligation. On the other hand, mere statements of opinion or commendations by the declarant do not necessarily create warranties. Whether a particular statement purports to be merely opinion or commendation is basically a question of whether the purchaser could reasonably rely upon the statement as a meaningful representation or promise with respect to the planned community. That determination depends, in turn, not merely upon the words used but also upon the relative characteristics and skills of the parties. Thus, a representation by a declarant to a novice purchaser that a particular planned community unit is in "good condition" may be more than mere opinion or commendation, while the same statement by a novice seller to a professional buyer would likely be only opinion or commendation, and thus not a warranty.

8. The provision of subsection (c) that the conveyance of a unit transfers to the purchaser all express warranties made by prior declarants is intended, in part, to avoid the possibility that a declarant could negate his warranty obligations through the device of transferring a unit through a shell entity to the ultimate purchaser.

SECTION 4-114. IMPLIED WARRANTIES OF QUALITY.

(a) A declarant and any dealer warrants that a unit will be in at least as good condition at the earlier of the time of the conveyance or delivery of possession as it was at the time of contracting, reasonable wear and tear excepted.

(b) A declarant and any dealer impliedly warrants that a unit and the common elements in the common interest community are suitable for the ordinary uses of real estate of its type and that any improvements made or contracted for by the declarant or dealer or made by any person before the creation of the common interest community, will be:

(1) free from defective materials; and

(2) constructed in accordance with applicable law, according to sound engineering and construction standards, and in a workmanlike manner.

(c) A declarant and any dealer warrants to a purchaser of a unit that may be used for residential use that an existing use, continuation of which is contemplated by the parties, does not violate applicable law at the earlier of the time of conveyance or delivery of possession.

(d) Warranties imposed by this section may be excluded or modified as specified in Section 4-115.

(e) For purposes of this section, improvements made or contracted for by an affiliate of a declarant are made or contracted for by the declarant.

(f) Any conveyance of a unit transfers to the purchaser all of the declarant's implied warranties of quality.

Comment

1. This section, which is based upon Section 2-309 of ULTA, overturns the rule still applied in many States that a professional seller of real estate makes no implied warranties of quality (the rule of "caveat emptor"). In recent years, that rule has been increasingly recognized as a relic of an earlier age whose continued existence defeats reasonable expectations of purchasers. Since the 1930's, more and more courts have completely or partially abolished the caveat emptor rule, and it is clear that the judicial tide is now running in favor of seller liability.

2. The principal warranty imposed under this section is that of suitability of both the unit and common elements for ordinary uses of real estate of similar type, and of quality of construction. Both of these warranties, which arise under subsection (b), are imposed only against declarants and dealers and not against unit owners selling their units to others.

3. Many recent cases have held that a seller of new housing impliedly warrants that the houses sold are habitable. The warranty of suitability under this Act is similar to the warranty of

habitability. However, under the Act, the warranty of suitability applies to both units and common elements in both commercial and residential common interest communities. If, for example, a commercial unit is sold for commercial use and is not suitable for the ordinary uses of common interest community units of that type, the warranty of suitability has been breached. Moreover, this warranty of suitability arises in the case of used, as well as new, buildings or other improvements in the common interest community.

4. The warranty of suitability and of quality of construction arises only against a declarant and dealers. As in the case of sales of goods, a non-professional seller is liable, if at all, only the any express warranties made by him. However, if a non-professional seller fails to disclose defects of which he is aware, he may be liable to the purchaser for fraud or misrepresentation under the common law of the State where the transaction occurred. Also, the warranties imposed by this section may be used to give content to a general "guarantee" by a non-professional seller.

5. The warranty as to quality of construction for improvements made or contracted for by the declarant or made by any person before the creation of the common interest community is broader than the warranty of suitability. Particularly, it imposes liability for defects which may not be so serious as to render the units or common elements unsuitable for ordinary purposes of real estate of similar type. Moreover, subsection (e) prevents a declarant from avoiding liability with respect to the quality of construction warranty by having an affiliated entity make the desired improvements.

6. Under subsection (c), a declarant also warrants to a residential purchaser that an existing use contemplated by the parties does not violate applicable law. The declarant, therefore, is liable for any violation of housing codes or other laws which renders any existing use of the unit or common elements unlawful.

7. The issue of declarant liability for warranties is an important one in cases where a transfer of the declarant's rights occurs, either as an arm's length transaction, as a transfer to an affiliate, or as a transfer by foreclosure or a deed in lieu of foreclosure. Subsection (f) makes clear that a conveyance of a unit transfers to the purchaser all warranties of quality made by any declarant, and Section 3-104(b)(1) makes clear that the original declarant remains liable for all warranties of quality with respect to improvements made by him, even after he transfers all declarant rights, regardless of whether the unit is purchased from the declarant who made the improvements. If the successor declarant is an affiliate of the original declarant, it is clear, under both Sections 3-104(b)(2) and 4-114(f), that the original declarant remains liable for warranties of quality or improvements made by his successor even after the declarant himself ceases to have any special declarant rights.

8. As to the liabilities of successor declarants for warranties of quality, a successor who is an affiliate of a declarant is liable, pursuant to Section 3-104(e)(1), for warranties or improvements made by his predecessor. However, any non-affiliated successor of the original declarant is liable only for warranties of quality for improvements made or contracted for by him, and is not liable for warranties which may lie against the original declarant even if the successor sells units completed by the original declarant to a purchaser. See Section 3-104(e)(2). In the case of a foreclosing lender, this is the same result as that reached under Section 2-309(f) of ULTA. The same result is also reached under ULTA in the case of a successor who, under ULTA Section 3-309(b), would be a

dealer since under that subsection the seller is liable only for warranties for improvements made or contracted for by him.

SECTION 4-115. EXCLUSION OR MODIFICATION OF IMPLIED WARRANTIES OF QUALITY.

(a) Except as limited by subsection (b) with respect to a purchaser of a unit that may be used for residential use, implied warranties of quality:

(1) may be excluded or modified by agreement of the parties; and

(2) are excluded by expression of disclaimer, such as "as is," "with all faults," or other language that in common understanding calls the purchaser's attention to the exclusion of warranties.

(b) With respect to a purchaser of a unit that may be occupied for residential use, no general disclaimer of implied warranties of quality is effective, but a declarant and any dealer may disclaim liability in an instrument signed by the purchaser for a specified defect or specified failure to comply with applicable law, if the defect or failure entered into and became a part of the basis of the bargain.

Comment

1. This section parallels Section 2-311(b) and (c) of ULTA.

2. Under this section, implied warranties of quality may be disclaimed. However, a warranty disclaimer clause, like any other contract clause, is subject to a possible court holding of unconscionability. Although the section imposes no requirement that a disclaimer be in writing, except in the case of residential units, an oral disclaimer might be ineffective under the law of parole and extrinsic evidence.

3. Except as against purchasers of residential units, there are no formal standards for the effectiveness of a disclaimer clause. All that is necessary under this section is that the disclaimer be calculated to effectively notify the purchaser of the nature of the disclaimer.

4. Under subsection (b), general disclaimers of implied warranties are not permitted with respect to purchasers of residential units. However, a declarant may disclaim liability for a specified defect or a specified failure to comply with applicable law in an instrument signed by such a purchaser. The requirement that the disclaimer as to each defect or failure be in a signed instrument

is designed to insure that the declarant sufficiently calls each defect or failure to the purchaser's attention and that the purchaser has the opportunity to consider the effect of the particular defect or failure upon the bargain of the parties. Consequently, this section imposes a special burden upon the declarant who desires to make a "laundry list" of defects or failures by requiring him to emphasize each item on such a list and make its import clear to prospective purchasers. For example, the declarant of a conversion common interest community might, consistent with this subsection, disclaim certain warranties for "all electrical wiring and fixtures in the building, the furnace, all materials comprising or supporting the roof, and all components of the air conditioning system."

5. This section is not intended to be inconsistent with, or to prevent, the use of insured warranty programs offered by some home builders. However, under the Act, the implied warranty that a new unit will be suitable for ordinary uses (i.e., habitable) and will be constructed in a sound, workmanlike manner, and free of defective materials, cannot be disclaimed by general language.

SECTION 4-116. STATUTE OF LIMITATIONS FOR WARRANTIES.

(a) Unless a period of limitation is tolled under Section 3-111 or affected by subsection (d), a judicial proceeding for breach of any obligation arising under Section 4-113 or 4-114 must be commenced within six years after the [claim for relief][cause of action] accrues, but the parties may agree to reduce the period of limitation to not less than two years. With respect to a unit that may be occupied for residential use, an agreement to reduce the period of limitation must be evidenced by a separate instrument executed by the purchaser.

(b) Subject to subsection (c), a [claim for relief] [cause of action] for breach of warranty of quality, regardless of the purchaser's lack of knowledge of the breach, accrues:

(1) as to a unit, at the time the purchaser to whom the warranty is first made enters into possession if a possessory interest was conveyed or at the time of acceptance of the instrument of conveyance if a nonpossessory interest was conveyed; and

(2) as to each common element, at the time the common element is completed or, if later, as to:

(A) a common element that is added to the common interest community by exercise of development rights, at the time the first unit which was added to the condominium by the same exercise of development rights is conveyed to a bona fide purchaser; or

(B) a common element within any other portion of the common interest community, at the time the first unit is conveyed to a bona fide purchaser.

(c) If a warranty of quality explicitly extends to future performance or duration of any improvement or component of the common interest community, the [claim for relief] [cause of action] accrues at the time the breach is discovered or at the end of the period for which the warranty explicitly extends, whichever is earlier.

(d) During the period of declarant control, the association may authorize an independent committee of the executive board to evaluate and enforce any warranty claims involving the common elements, and to compromise those claims. Only members of the executive board elected by unit owners other than the declarant and other persons appointed by those independent members may serve on the committee, and the committee's decision must be free of any control by the declarant or any member of the executive board or officer appointed by the declarant. All costs reasonably incurred by the committee, including attorney's fees, are common expenses, and must be added to the budget annually adopted by the association under Section 3-115. If the committee is so created, the period of limitation for a warranty claim considered by the committee begins to run from the date of the first meeting of the committee.

Comment

1. Under subsection (a), the parties may agree that the statute of limitations be reduced to as little as two years. However, such a contract provision (which, in the case of residential units, must be reflected in a separate written instrument executed by the purchaser) could, like other contract provisions, be subject to attack on grounds of unconscionability in particular cases.

2. Except for warranties of quality which explicitly refer to future performance or duration, a cause of action for breach of a warranty of quality would normally arise when the purchaser to whom it is first made enters into possession. Suit on such a warranty would thus have to be brought within six years thereafter. Even an inability to discover the breach would not delay the running of the statute of limitations in this regard.

3. Real estate sales frequently include warranties that certain components (e.g., furnaces, hot water heaters, air conditioning systems, and roofs) will last for a particular period of time. In the

case of such warranties, the statute of limitations would not start running until the breach is discovered, or, if not discovered before the end of the warranty term, until the end of the term.

4. The common elements typically have many components. While always dependent on the particular unit boundaries of the particular project, typical common elements include retaining walls, a swimming pool, water lines, sidewalks, party walls, etc. A phase for this purpose consists of the units, common elements and limited common elements created upon each occasion of the exercise by the declarant of development rights reserved by such declarant.

5. Under subsection (b)(2)(ii), if the declarant has not reserved development rights to expand the community by adding units and common elements or limited common elements, the claim for relief or cause of action for a common element accrues at the later of the time of the first unit sale or the time that common element is completed. However, under amended Section 3-111, that period does not begin to run until declarant control terminates.

On the other hand, if the declarant has retained development rights to expand the community, the cause of action accrues upon the first conveyance of a unit within the phase which includes that particular common element.

6. New subsection (d) creates an alternative mechanism by which a declarant may create an independent board committee to evaluate and enforce warranty claims. The committee is analogous to an independent audit committee composed of outside directors in a publicly held corporation. This section strikes a balance between the legitimate interest of a declarant in not having to provide warranties on the common elements for an unreasonable time, and the equally legitimate interest of unit owners in having an independent analysis of warranty claims before those claims expire.

SECTION 4-117. EFFECT OF VIOLATIONS ON RIGHTS OF ACTION; ATTORNEY'S FEES.

(a) A declarant, association, unit owner, or any other person subject to this [act] may bring an action to enforce a right granted or obligation imposed by this [act], the declaration, or the bylaws. [Punitive damages may be awarded for a willful failure to comply with this [act].] The court may award reasonable attorney's fees and costs.

(b) Parties to a dispute arising under this [act], the declaration, or the bylaws may agree to resolve the dispute by any form of binding or nonbinding alternative dispute resolution, but:

(1) a declarant may agree with the association to do so only after the period of declarant control has expired unless the agreement is made with an independent committee of the executive board elected pursuant to Section 4-116(d); and

(2) an agreement to submit to any form of binding alternative dispute resolution

must be in a record authenticated by the parties.

Comment

1. This section provides a general cause of action or claim for relief for failure to comply with the Act by either a declarant or any other person subject to the Act's provisions. Such persons might include unit owners, persons exercising a declarant's rights of appointment pursuant to Section 3-103(d), or the association itself. A claim for appropriate relief might include damages, injunctive relief, specific performance, rescission, or reconveyance if appropriate under the law of the State, or any other remedy normally available under state law. The section specifically refers to "any person or class of persons" to indicate that any relief available under the state class action statute would be available in circumstances where a failure to comply with this Act has occurred. This section specifically permits punitive damages to be awarded in the case of willful failure to comply with the Act and also permits court costs and attorney's fees to be awarded in the discretion of the court to any party that prevails in an action.

2. The 1994 amendments reflect the Conference's judgment that resolving disputes by non-judicial means is a desirable outcome, subject to the limitations contained in this section.

3. The language of subsection (a) is intentionally broad, and emphasizes the traditional authority of a court in equity to fashion a remedy suited to the circumstances of the case. Importantly, the provisions of this section would apply with equal force to a violation of either this Act or the declaration or by-laws by "any person" besides the declarant – including, for example, the association in its dealings with unit owners, a property manager or unit owners whose own behavior violates those same laws or instruments.

In appropriate cases involving association or executive board activities, the court might grant relief in the form of requiring new elections, removal of officers from office, and orders requiring offending parties to make the association whole for improperly expended funds. A civil action may lie, in an appropriate case, for failure of the executive board to comply with the "open meeting" requirement of §3-108. These examples are not intended to exhaust the traditional authority of a judge to grant "appropriate relief", and that authority is emphasized by the specific grant of discretion to authorize punitive damages or attorneys fees, as the circumstances warrant. The brackets around the punitive damages provisions in subsection (a), added in 2008, reflect the drafters' awareness of differing policies on that subject among the states.

4. Nothing in this section prohibits a unit owner from seeking independently to enforce any provision of the declaration, bylaws or rules. However, limitations in those instruments may require that the unit owner participate in some form of alternative dispute resolution before commencing suit; **see** Section 3-102(a)(18).

SECTION 4-118. LABELING OF PROMOTIONAL MATERIAL. No promotional material may be displayed or delivered to prospective purchasers which describes or portrays an improvement that is not in existence unless the description or portrayal of the improvement in the promotional material is conspicuously labeled or identified either as "MUST BE BUILT" or as "NEED NOT BE BUILT."

Comment

This section requiring the labeling of improvements depicted on promotional material is necessary to assure that purchasers are not deceived with respect to improvements the declarant indicates he intends to make in a common interest community.

SECTION 4-119. DECLARANT'S OBLIGATION TO COMPLETE AND RESTORE.

(a) Except for improvements labeled "NEED NOT BE BUILT," the declarant shall complete all improvements depicted on any site plan or other graphic representation, including any plats or plans prepared pursuant to Section 2-109, whether or not that site plan or other graphic representation is contained in the public offering statement or in any promotional material distributed by or for the declarant.

(b) The declarant is subject to liability for the prompt repair and restoration, to a condition compatible with the remainder of the common interest community, of any portion of the common interest community affected by the exercise of rights reserved pursuant to or created by Section 2-110, 2-111, 2-112, 2-113, 2-115, or 2-116.

Comment

1. The duty imposed by subsection (a) is a fundamental obligation of the declarant and is one with which a successor declarant is obligated to comply under Section 3-104.

2. Section 4-119(b) requires the declarant to repair and restore the common interest community following the exercise of any rights reserved or created to exercise a development right (Section 2-110), to alter units (Section 2-112), relocate the boundaries between adjoining units (Section 2-112), subdivide units (Section 2-113), use units or common elements for sales purposes

(Section 2-115), or exercise of easement rights (Section 2-116). Plainly, this obligation on the declarant exists only if the declarant, in his capacity as a unit owner, exercises these rights. If any right to, for example, alter units, is exercised by another unit owner, that unit owner and not the declarant, would be responsible for the consequences of those acts.

SECTION 4-120. SUBSTANTIAL COMPLETION OF UNITS. In the case of a sale of a unit in which delivery of a public offering statement is required, a contract of sale may be executed, but no interest in that unit may be conveyed, until the declaration is recorded and is substantially completed, as evidenced by a recorded certificate of substantial completion executed by an independent [registered] architect, surveyor, or engineer, or by issuance of a certificate of occupancy authorized by law.

Comment

The purpose of this section, complemented by Section 4-110, is to assure that the declarant is not able to obtain use of the purchaser's money until the purchaser is able to get a completed unit.

[OPTIONAL]

[ARTICLE] 5

ADMINISTRATION AND REGISTRATION

OF COMMON INTEREST COMMUNITIES

SECTION 5-101. ADMINISTRATIVE AGENCY. As used in this [Act], "agency" means [insert appropriate administrative agency], which is an agency within the meaning of [insert appropriate reference to state administrative procedure act]. [Insert any related provisions on creation, selection, and remuneration of personnel, budget, annual reports, fees, and other administrative provisions appropriate to the particular State.]

Comment

1. Each State should insert in lieu of the bracketed language in the first sentence that agency, whether it be the Real Estate Commission, the Attorney General's Office, or any other existing or new agency, which the State deems appropriate for regulation of common interest communities.

2. The 1961 Revised Model State Administrative Procedure Act (the "Model Act") had been adopted in 20 States and the District of Columbia by 1981. The appropriate reference in those States to the definition of "Agency" would be the statute adopting Section 1(1) of the Model Act. In those States which have not adopted the Model Act, reference to a similar statute should be made to insure that the procedures of the agency regulating planned communities are undertaken in accordance with the principles of procedural due process which underlie the Model Act. In those States which do not have an administrative procedure act, appropriate administrative procedures should be included, either in this section or elsewhere in this article, to provide for hearings, appellate review, regulations, and other administrative matters.

3. As indicated, Article 5 was not designed to solve all procedural matters which are appropriate for an agency. Rather, the Act relies on the cross reference to a state administrative procedure act. Even in such States, however, it may be appropriate to include other provisions, either in Section 5-101 or elsewhere in this article, which are necessary under state practice to insure the proper functioning of a state agency. This might include budget authority, salary levels, civil service requirements, and the like. This may be particularly important when a new state agency is created.

SECTION 5-102. REGISTRATION REQUIRED. A declarant may not offer or dispose of a unit intended for residential use unless the common interest community and the unit are registered with the agency, but a common interest community consisting of no more than 12 units

and which is not subject to development rights is exempt from the requirements of this section and Section 5-103(a).

Comment

1. Registration of a common interest community is only required in the case of a common interest community or unit intended for residential use. Commercial and industrial common interest communities, accordingly, are exempt from registration under this Act. Also exempt from the requirement of registration is a small common interest community containing 12 or fewer units, so long as the common interest community is not subject to development rights. However, the small common interest community and the industrial or commercial common interest community are still subject to scrutiny by the agency under its general powers, despite the fact that registration is not required.

2. If Article 5 were adopted in a particular State, a declarant could not offer or dispose of a residential unit unless that unit were registered with the agency. However, he could offer and dispose of the unit after registration was approved but before the common interest community was created, subject to the requirements of Sections 2-101 and 5-103.

SECTION 5-103. APPLICATION FOR REGISTRATION; APPROVAL OF UNCOMPLETED UNITS.

(a) An application for registration must contain the information and be accompanied by any reasonable fees required by the agency's [rules] [regulations]. A declarant promptly shall file amendments to report any actual or expected material change in any document or information contained in the application.

(b) If a declarant files with the agency a declaration or proposed declaration, or an amendment or proposed amendment to a declaration, creating units that he proposes to convey before they are substantially completed in the manner required by Section 4-120 and, in a condominium, by Section 2-101(b), the declarant shall also file with the agency:

(1) a verified statement showing all costs involved in completing the buildings containing those units;

(2) a verified estimate of the time of completion of construction of the buildings containing those units;

(3) satisfactory evidence of sufficient funds to cover all costs to complete the buildings containing those units;

(4) a copy of the executed construction contract and any other contracts for the completion of the buildings containing those units;

(5) a 100 percent payment and performance bond covering the entire cost of construction of the buildings containing those units;

(6) plans for the units which, in the case of a condominium or planned community, shall conform to the requirements of Section 2-109(c);

(7) if purchasers' funds are to be utilized for the construction of the common interest community, an executed copy of the escrow agreement with an escrow company or financial institution authorized to do business within the State which provides that:

(i) disbursements of purchasers' funds may be made from time to time to pay for construction of the common interest community, architectural, engineering, finance, and legal fees, and other costs for the completion of the common interest community in proportion to the value of the work completed by the contractor as certified by an independent [registered] architect or engineer, on bills submitted and approved by the lender of construction funds or the escrow agent;

(ii) disbursement of the balance of purchasers' funds remaining after completion of the common interest community must be made only when the escrow agent or lender receives satisfactory evidence that (A) the period for filing mechanic's and materialman's liens has expired, (B) the right to claim those liens has been waived, or (C) adequate provision has been made for satisfaction of any claimed mechanic's or materialman's lien; and

(iii) any other restriction relative to the retention and disbursement of purchasers' funds required by the agency; and

(8) any other materials or information the agency may require by its [rules] [regulations].

(c) The agency may not register the units described in the declaration or the amendment unless the agency determines, on the basis of the material submitted by the declarant and any other information available to the agency, that there is a reasonable basis to expect that the units to be conveyed will be completed by the declarant following conveyance.

Comment

1. Subsection (a) is a general provision empowering the agency by regulation to develop requirements for information to be submitted to the agency, and for the imposition of reasonable fees by the agency. Such rules or regulations, under the Model Act, could be adopted only after providing notice to interested persons and an opportunity to be heard. See Section 3 of the Model Act. The article encourages, but does not require, development of uniform regulations between States adopting Article 5. See Section 5-107(e).

2. Under Section 2-101(b) a condominium declaration may not be recorded until all structural and mechanical systems for units which will be created by the recording are substantially completed. While there is no similar requirement for planned communities and cooperatives, Section 4-120, which is applicable to all types of common interest communities, prohibits conveyance of units before they are substantially completed.

In addition, under Section 4-110, any deposit made in connection with the purchase or reservation of a unit must be held in escrow until closing. The combined effect of Sections 2-101(b), 4-120, and 4-110 is to insure that any funds of a purchaser are held in escrow until his unit is substantially completed and the purchaser has title.

Subsection (b) is a departure from the requirements of Sections 2-106(b) and 4-120. The need for consumer protection suggests that substantial completion of a residential unit should be a prerequisite for conveying the unit to a purchaser in the absence of an agency to control and review planned community projects. Under subsection (b), however, a declarant may file a declaration or proposed declaration, or an amendment to a declaration, for the purpose of creating a common interest community in which the units are not substantially completed.

Subsection (b) contemplates that the agency might nevertheless register the units described in the declaration or amendment, if the agency were satisfied that the units would be completed. Registration would then permit the declarant to offer to sell and convey the uncompleted units.

In addition, paragraph (7) of Section 5-103(b) contemplates that purchaser's funds might be used, despite the language of Section 4-110 for construction of the planned community. Controls are imposed, however, to insure that disbursements are made in accordance with the value of work completed and approved by an escrow agent.

Note that the common elements in the common interest community under the Act need not be completed at the time of the sale, even in the absence of an agency. Completion of common elements, however, is governed by Section 4-119 (Obligation to Complete and Restore).

3. The agency, by regulation, should determine the parties whom the payment and performance bond required under paragraph (b)(5) indemnifies.

SECTION 5-104. RECEIPT OF APPLICATION; ORDER OF REGISTRATION.

(a) The agency shall acknowledge receipt of an application for registration within [five] business days after receiving it. Within [60] days after receiving the application, the agency shall determine whether:

(1) the application and the proposed public offering statement satisfy the requirements of this [Act] and the agency's [rules] [regulations];

(2) the declaration and bylaws comply with this [Act]; and

(3) it is likely that the improvements the declarant has undertaken to make can be completed as represented.

(b) If the agency makes a favorable determination, it shall issue promptly an order registering the common interest community. Otherwise, unless the declarant has consented in writing to a delay, the agency shall issue promptly an order rejecting registration.

Comment

1. This section provides reasonable deadlines for agency review of an application for registration, and describes the standards by which the application should be measured. The agency is directed to review the documents provided to the purchaser, and is given a great deal of discretion in mandating the form and content of the public offering statement; see Section 5-110.

2. The agency is also charged with reviewing those common element improvements which a declarant has promised to make, and which would be labeled under Section 4-118 as "MUST BE BUILT," to determine whether the declarant has the financial capacity to build them.

3. In the event the agency were to issue an order rejecting registration under subsection (b), an important issue concerning judicial review of that order may arise in some States.

The order would appear to be a rejection of an application for a license, as defined in

Section 1(3) of the Model Act; it would be a "contested case," however, within the meaning of Section 1(2) of the Model Act, only if "an opportunity for hearing" is provided. No right to a hearing, or right of appeal, is provided in the Act.

The order rejecting registration thus might not be appealable under Section 15 of the Model Act, because judicial review is provided under Section 15 only for "contested cases." While that section does not limit utilization of, or the scope of judicial review available under, other means of review, some courts have held that, in the absence of specific statutory authority to hear an appeal from an administrative decision, courts have no jurisdiction to entertain such an appeal. See, e.g., *Rybinski v. State Employees' Retirement Comm.*, 173 Conn. 462 (1977).

Accordingly, the law of each State should be carefully reviewed. In cases where the state administrative procedure act provides for appeals from decisions on licensing matters made by state agencies regardless of the availability of a hearing, no amendment would be required

SECTION 5-105. CEASE AND DESIST ORDERS. If the agency determines, after notice and hearing, that any person has disseminated or caused to be disseminated orally or in writing any false or misleading promotional materials in connection with a common interest community or that any person has otherwise violated any provision of this [Act] or the agency's [rules] [regulations] or orders, the agency may issue an order to cease and desist from that conduct, to comply with the provisions of this [Act] and the agency's [rules] [regulations] and orders, or to take affirmative action to correct conditions resulting from that conduct or failure to comply.

SECTION 5-106. REVOCATION OF REGISTRATION.

(a) The agency, after notice and hearing, may issue an order revoking the registration of a common interest community upon determination that a declarant or any officer or principal of a declarant has:

(1) failed to comply with a cease and desist order issued by the agency affecting that common interest community;

(2) concealed, diverted, or disposed of any funds or assets of any person in a manner impairing rights of purchasers of units in that common interest community;

(3) failed to perform any stipulation or agreement made to induce the agency to issue

an order relating to that common interest community;

(4) misrepresented or failed to disclose a material fact in the application for registration; or

(5) failed to meet any of the conditions described in Sections 5-103 and 5-104 necessary to qualify for registration.

(b) A declarant may not convey, cause to be conveyed, or contract for the conveyance of any interest in a unit while an order revoking the registration of the common interest community is in effect, without the consent of the agency.

(c) In appropriate cases the agency, in its discretion, may issue a cease and desist order in lieu of an order of revocation.

Comment

1. This section permits the agency, after notice and hearing, to revoke a prior registration of a common interest community. Under Section 15 of the Model Act, the revocation would not be effective until the last day for seeking review of the agency order. While the filing of the appeal would not stay the agency's decision, the agency or reviewing court could grant a stay of the revocation. Naturally, this result may vary in a particular State.

2. A declarant is prohibited from disposing of any interest in a unit when registration has been revoked, without consent of the agency.

SECTION 5-107. GENERAL POWERS AND DUTIES OF AGENCY.

(a) The agency may adopt, amend, and repeal [rules] [regulations] and issue orders consistent with and in furtherance of the objectives of this [Act], but the agency may not intervene in the internal activities of an association except to the extent necessary to prevent or cure violations of this [Act]. The agency may prescribe forms and procedures for submitting information to the agency.

(b) If it appears that any person has engaged, is engaging, or is about to engage in any act or practice in violation of this [Act] or any of the agency's rules or orders, the agency without prior

administrative proceedings may maintain an action in the [appropriate court] to enjoin that act or practice or for other appropriate relief. The agency is not required to post a bond or prove that no adequate remedy at law exists.

(c) The agency may intervene in any action involving the powers or responsibilities of a declarant in connection with any common interest community for which an application for registration is on file.

(d) The agency may accept grants in aid from any governmental source and may contract with agencies charged with similar functions in this or other jurisdictions, in furtherance of the objectives of this [Act].

(e) The agency may cooperate with agencies performing similar functions in this and other jurisdictions to develop uniform filing procedures and forms, uniform disclosure standards, and uniform administrative practices, and may develop information that may be useful in the discharge of the agency's duties.

(f) In issuing any cease and desist order or order rejecting or revoking registration of a common interest community, the agency shall state the basis for the adverse determination and the underlying facts.

(g) The agency, in its sound discretion, may require bonding, escrow of portions of sales proceeds, or other safeguards it may prescribe by its [rules] [regulations] to guarantee completion of all improvements which a declarant is obligated to complete pursuant to Section 4-119 (Declarant's Obligation to Complete and Restore).

Comment

1. Under subsection (a), the agency is empowered to adopt regulations and issue orders in furtherance of the objectives of this Act. Those objectives are the same as the underlying purposes of the Act. The agency, however, is prohibited from intervening in the internal activities of the association except to the extent necessary to prevent or cure violations of this Act. The principal purpose of the agency is to regulate the behavior of the declarant, not the behavior of individual unit

owners. If, however, the declarant is misusing the association by virtue of his power to control its activities, and thereby violating the Act, the agency may act to prevent the violation.

2. Subsection (g) empowers the agency to require bonding, escrow, or other safeguards to guarantee completion of improvements labeled "MUST BE BUILT" (Section 4-118).

A substantive requirement for bonding is not included under Article 4 for all common interest communities, in all circumstances. While some States have adopted bonding and escrow requirements for completion of the common elements in condominiums (see, e.g., Section 47-74d, Conn. Gen. Stat.), the available economic evidence indicates that a universal bonding requirement would increase the cost of units, and that the cost of such provisions may not always be justified. The principal concern for consumer protection in this regard has been resolved in the Act by requiring substantial completion of all units prior to conveyance (Section 4-120) and by requiring labeling of common elements as either "MUST BE BUILT" or "NEED NOT BE BUILT."

At the same time, particularly in the case of common interest communities registered under Section 5-103(b), there may be individual cases where the agency, in its discretion, may find escrowing or bonding to be in the public interest. For that reason, this power is included only as a permissible power for the agency under Article 5.

SECTION 5-108. INVESTIGATIVE POWERS OF AGENCY.

(a) The agency may initiate public or private investigations within or outside this State to determine whether any representation in any document or information filed with the agency is false or misleading or whether any person has engaged, is engaging, or is about to engage in any unlawful act or practice.

(b) In the course of any investigation or hearing, the agency may subpoena witnesses and documents, administer oaths and affirmations, and adduce evidence. If a person fails to comply with a subpoena or to answer questions propounded during the investigation or hearing, the agency may apply to the [appropriate court] for a contempt order or injunctive or other appropriate relief to secure compliance.

Comment

The powers enumerated in Sections 5-107 and 5-108 are specifically granted to the agency because of judicial determinations in various States that, in the absence of such statutory powers, agencies have no authority to act.

SECTION 5-109. ANNUAL REPORT AND AMENDMENTS.

(a) A declarant, within 30 days after the anniversary date of the order of registration, annually shall file a report to bring up-to-date the material contained in the application for registration and the public offering statement. This provision does not relieve the declarant of the obligation to file amendments pursuant to subsection (b).

(b) A declarant promptly shall file amendments to the public offering statement with the agency.

(c) If an annual report reveals that a declarant owns or controls units representing less than [25] percent of the voting power in the association and that a declarant has no power to increase the number of units in the common interest community, or to cause a merger or confederation of the common interest community with other common interest communities, the agency shall issue an order relieving the declarant of any further obligation to file annual reports. Thereafter, so long as the declarant is offering any units for sale, the agency has jurisdiction over the declarant's activities, but has no other authority to regulate the common interest community.

Comment

1. This section requires annual reports from a declarant to the agency in order to keep the information filed with the agency current. This requirement parallels the declarant's obligation to provide a current public offering statement to unit owners. See Section 4-103(c).

2. Under subsection (c), if the period of declarant control has passed, the declarant is relieved of the obligation to continue to file an annual report. However, the obligation to continue to provide public offering statements is imposed on a declarant under Section 4-103(c) so long as he is offering any unit for sale. The agency would thus continue to have jurisdiction over the declarant's activities, but would have no other authority to regulate the common interest community.

SECTION 5-110. AGENCY REGULATION OF PUBLIC OFFERING STATEMENT.

(a) The agency at any time may require a declarant to alter or supplement the form or substance of a public offering statement to assure adequate and accurate disclosure to prospective

purchasers.

(b) The public offering statement may not be used for any promotional purpose before registration and afterwards only if it is used in its entirety. No person may advertise or represent that the agency has approved or recommended the common interest community, the disclosure statement, or any of the documents contained in the application for registration.

(c) In the case of a common interest community situated wholly outside this State, an application for registration or proposed public offering statement filed with the agency which has been approved by an agency in the State where the common interest community is located and substantially complies with the requirements of this [Act] may not be rejected by the agency on the grounds of non-compliance with any different or additional requirements imposed by this [Act] or by the agency's [rules] [regulations]. However, the agency may require additional documents or information in particular cases to assure adequate and accurate disclosure to prospective purchasers.

Comment

1. Subsection (c) attempts to facilitate interstate sales of units by requiring the agency in the enacting State to accept an agency-approved public offering statement from the State where the common interest community is located. This avoids the need for a different public offering statement in several States for the same project. If no agency exists in the State where the common interest community is located, however, a public offering statement must be prepared and approved before offering an out-of-state unit in an enacting State.

2. Because of the bracketed language contained in Section 1-208, which should be inserted in the Act if Article 5 is enacted, a foreign common interest community must only be registered under this article in an enacting State if a declarant is "offering" units in that common interest community in the enacting State. Thus, general advertising which did not meet the definition of "offering" could be circulated in the enacting State without registration. If an "offering" is once made, however, then all of Article 5 applies to the foreign common interest community. Any "disposition" of a foreign residential common interest community in an enacting State, of course, would require delivery of a public offering statement even in the absence of an agency; see Section 1-208. If an agency exists in the enacting State, any disposition in that State would be illegal if the common interest community were not registered in the enacting State; see Section 1-208.