

HOUSE OF REPRESENTATIVES STAFF ANALYSIS

BILL #: HB 407 Condominiums
SPONSOR(S): Schwartz
TIED BILLS: None **IDEN./SIM. BILLS:** SB 314

REFERENCE	ACTION	ANALYST	STAFF DIRECTOR
1) <u>Committee on Courts</u>	<u>5 Y, 0 N</u>	<u>Blalock</u>	<u>Bond</u>
2) <u>Safety & Security Council</u>	<u></u>	<u></u>	<u></u>
3) <u>Policy & Budget Council</u>	<u></u>	<u></u>	<u></u>
4) <u></u>	<u></u>	<u></u>	<u></u>
5) <u></u>	<u></u>	<u></u>	<u></u>

SUMMARY ANALYSIS

Recent catastrophic destructions of condominium buildings have highlighted the difficulties related to termination under current law. Unless otherwise provided for in the covenants of a condominium association, current law requires the consent of all the unit owners and all the holders of the recorded liens affecting any of the condominium units for termination of the condominium association; and requires distribution of the proceeds of the insurance and the sale of the land on a basis that may not be equitable.

This bill amends the law regarding condominium termination to:

- Provide for approval by less than 100% of owners and lienholders;
- Provide alternative methods for determining the allocation of proceeds from the sale of condominium property;
- Set forth procedures for management of the association and for distribution of the proceeds; and
- Provide for dissent and court review of a plan of termination.

The provisions of this bill apply to condominium associations currently in existence.

This bill does not appear to have a fiscal impact on state or local governments.

FULL ANALYSIS

I. SUBSTANTIVE ANALYSIS

A. HOUSE PRINCIPLES ANALYSIS:

Safeguard individual liberty -- This bill appears to increase the options that individuals have regarding termination of their condominium association.

B. EFFECT OF PROPOSED CHANGES:

Background

Condominiums are creatures of statute, and are thereby subject to the control and regulation of the legislature, which has broad discretion in its regulatory efforts, especially in fashioning remedies necessary to protect the interests of those persons involved.

Chapter 718, F.S., the "Condominium Act," governs condominium associations. Section 718.117, F.S., provides for termination of a condominium. The declaration of condominium may have different requirements for termination than those provided for in statute, although it is common for associations to not have any provision for termination. Condominium termination is somewhat analogous to the law of partition found in the common law and codified in ch. 64, F.S. The law of partition provides that where there are multiple people who own a single parcel of real property as joint tenants or tenants in common, one or more of the owners may petition a court of equity to force the division of the property into individually owned interests. If the property cannot be equitably divided by the court because the property includes a house or other improvement, then the court may force, sale of the property, and divide the proceeds in an equitable manner. Under the law of partition, one single owner may have the property divided into individually owned interests or sold, regardless of how many other people also own the property.

Unless the declaration provides otherwise, termination of a condominium requires the consent of all the unit owners and all the holders of the recorded liens affecting any of the condo parcels.¹ Achieving such consent is difficult under normal circumstances. Recent catastrophic events have revealed that achieving this unanimous consent can be exceedingly difficult. Some of the reasons for this difficulty include:

- Poorly drafted covenants, including covenants that have no provision for termination.
- Where the building is damaged to the point that it is not habitable, the occupants scatter and owners can be difficult to find.
- Working with the estates of owners killed in the catastrophe.
- Holdout or difficult owners.
- Absentee owners who live in other states or countries.
- Disputes with insurance companies that lead to uncertainty in the amount of proceeds available for distribution to owners.
- Unresponsive lenders.
- Members of the board are often as unavailable as the owners they represent, sometimes leading to a failure of leadership.
- The default statutory distribution formula does not take into account the sometimes substantial differences in fair market values of units based upon their condition or location in the structure.

¹ Section 718.117(1), F.S.

Effect of the Bill

The bill substantially amends and re-writes s. 718.117, F.S., regarding the method and process for termination of a condominium. Many provisions are simply moved within the section with grammatical and editorial changes. The substantive changes are summarized here:

Legislative Findings

The bill makes the following legislative findings:

The Legislature finds that condominiums are created as authorized by statute. In circumstances that may create economic waste, areas of disrepair, or obsolescence of a condominium property for its intended use and thereby lower property tax values, the Legislature further finds that it is the public policy of this state to provide by statute a method to preserve the value of the property interests and the rights of alienation thereof that owners have in the condominium property before and after termination. The Legislature further finds that it is contrary to the public policy of this state to require the continued operation of a condominium when to do so constitutes economic waste or when the ability to do so is made impossible by law or regulation. This section applies to all condominiums in this state in existence on or after July 1, 2007.

Termination of Condominium - Vote Required

Section 718.117(1), F.S., requires unanimous consent of all owners and lienholders to terminate the condominium, unless a lower threshold is provided for in the declaration. This applies regardless of the circumstances that lead to a decision to terminate the condominium.

This bill provides that, where the continued operation of the condominium would constitute economic waste or would be impossible, the necessary vote for termination is the vote required for amendment of the declaration. In general, amendment of a declaration of condominium requires a two-thirds vote of the membership, unless otherwise provided for in the declaration.² The criteria for economic waste or impossibility are:

- The total estimated cost of repairs necessary to restore the improvements to their former condition or bring them into compliance with applicable laws or regulations exceeds the combined fair market value of all units in the condominium after completion of the repairs; or
- It becomes impossible to operate or reconstruct a condominium in its prior physical configuration because of land-use laws or regulations.

The bill further provides that, regardless of whether continued operation would constitute economic waste or would be impossible, the condominium may be terminated if approved by at least 80 percent of the total voting interests of the condominium, unless the declaration provides for a lower threshold.

However, if 75% or more of the condominium units are timeshare units, the condominium may only be terminated by a plan of termination that is approved by 80% of the total voting interests of the association and the holders of 80% of the original principal amount of outstanding recorded mortgage liens of timeshare estates in the condominium, unless the declaration provides for a lower voting percentage.

² Section 718.110(1)(a), F.S. The bill also provides that a plan of termination is not an amendment subject to s. 718.110(4), F.S., which section relates to amendments that may change the configuration or size of any unit in any material fashion, materially alter or modify the appurtenances to the unit, or change the proportion or percentage by which the unit owner shares the common expenses of the condominium and owns the common surplus of the condominium. Such amendments essentially require, like a termination under current law, a 100% vote of owners and lienholders.

Mortgage Lienholders

Current law requires approval of all mortgage lienholders to terminate a condominium. This bill provides that approval is not required if the mortgage lienholder is to be paid in full from the termination proceeds. If the mortgage holder will not be paid in full and does not approve of the plan of termination, the mortgage holder has 90 days to contest plan (see contest provisions below).

Receivership

Current law provides a mechanism whereby the condominium can be placed into receivership after a natural disaster.³ Receivership is a form of court supervision over the ongoing management and affairs of the association with the end result being termination of the condominium and distribution of the net proceeds to the parties entitled to such proceeds. In relation to receivership, this bill adds a requirement for quarterly financial reporting, specifies that members of a termination board are subject to recall, and provides that lenders representing 50% of the outstanding mortgage balances on the condominium units may petition the court for appointment of a termination trustee.

Plan of Termination

Current law does not require a written plan of termination, although it is likely that owners would not vote to approve termination of the condominium without there being a plan of how to sell the condominium property and distribute the proceeds of the sale to lienholders and owners. This bill specifies what must be in a plan of termination.

A plan of termination must be a written document executed by owners and by the termination trustee. A copy of a proposed plan must be given to all unit owners.⁴ Approval of the plan may either be at an owner's meeting or by written consent of owners.⁵ If approved by the required number of owners and lienholders, the plan must be recorded in the public records. The plan is effective only upon recordation or at a later date specified in the plan.

A plan must specify:

- The name, address, and powers of the termination trustee;
- A date after which the plan of termination is void if it has not been recorded;
- The interests of the respective unit owners in the association property, common surplus, and other assets of the association, which will be the same as the respective interests of the unit owners in the common elements immediately before the termination, unless otherwise provided;
- The interests of the respective unit owners in any proceeds from any sale of the condominium property. The plan of termination may apportion those proceeds pursuant to any of the methods prescribed in s. 718.117(12) (see the discussion below regarding the allocation of property). If, condominium property or real property owned by the association is to be sold following termination, the plan must provide for the sale and may establish any minimum sale terms; and
- Any interests of the respective unit owners in any insurance proceeds or condemnation proceeds that are not used for repair or reconstruction. Unless the declaration expressly addresses the distribution of insurance proceeds or condemnation proceeds, the plan of

³ Section 718.117(4), F.S.

⁴ The notice must be given either in the same manner as for notice of an annual meeting and at least 14 days prior to the meeting during which the plan is to be voted upon, or must be sent together with a consent document.

⁵ Any written consent must be signed with the formality of a deed; i.e., two witnesses and a notary.

termination may apportion those proceeds pursuant to any of the methods prescribed in s. 718.117(12) (see the discussion below regarding the allocation of property).

The plan may additionally provide that each unit owner retains the exclusive right of possession to the portion of the real estate that formerly constituted the unit, in which case the plan must specify the conditions of possession.

In the case of a conditional termination, the plan must specify the conditions for termination. A conditional plan will not vest title in the termination trustee until the plan and a certificate executed by the association with the formalities of a deed, confirming that the conditions in the conditional plan have been satisfied or waived by the requisite percentage of the voting interests, have been recorded.

Allocation of Proceeds of Sale of Condominium Property

Current law provides that, upon termination, unless otherwise provided for in the declaration, each owner will receive a proportionate share in the net proceeds from sale of the condominium in proportion to each owner's share of the common elements.⁶

This bill substantially changes the provisions regarding distribution of the proceeds. Unless the declaration expressly provides for the allocation of the proceeds of sale of condominium property, the plan must first apportion the proceeds between the aggregate value of all units and the value of the common elements, based on their respective fair-market values immediately before the termination. The market values are to be determined by one or more independent appraisers selected by the association or termination trustee. The value of the common elements is to be paid to the owners according to their proportionate share in the common elements, as in current law.

The portion of proceeds allocated to the units is apportioned among the individual units. Any one of the following methods of apportionment are allowed:

- The respective values of the units based on the fair-market values of the units immediately before the termination, as determined by one or more independent appraisers selected by the association or termination trustee.
- The respective values of the units based on the most recent market value of the units before the termination, as provided in the county property appraiser's records.
- The respective interests of the units in the common elements specified in the declaration immediately before the termination.
- Any other method of apportionment in the plan of termination that achieves the necessary approval.

Liens that encumber a unit are transferred to the proceeds of the sale of the condominium property and the proceeds of sale or other distribution of association property, common surplus, or other association assets attributable to such unit in their same priority. The proceeds of any sale of condominium property pursuant to a plan of termination may not be deemed to be common surplus or association property.

Termination Trustee

Current law does not specify who is to carry out the termination, manage the property during the process, and distribute the proceeds. This bill provides that the existing association will serve as termination trustee unless another person is appointed in the plan of termination. This bill also provides that, if the association is unable, unwilling, or fails to act as trustee, any unit owner may petition the court to appoint a trustee. Upon approval of the plan of termination, the termination trustee takes title to the association assets.

⁶ Section 718.117(7), F.S.

Notice

Current law does not require notice of the termination. This bill requires the termination trustee to give notice to every owner and lienor of the termination within 30 days after a plan has been recorded, and requires that the division⁷ be notified within 90 days.

Right to Contest

Current law does not provide a means or time for contesting the termination of a condominium. This bill provides that a unit owner or lienor may contest a plan within 90 days after the date the plan is recorded. A unit owner or lienor who fails to contest the plan within that period is barred from asserting or prosecuting a claim against the association, the termination trustee, any unit owner, or any successor in interest to the condominium property. In an action contesting a plan, the person contesting the plan has the burden of pleading and proving that the apportionment of the proceeds from the sale among the unit owners was not fair and reasonable. However, the apportionment of sale proceeds is presumed fair and reasonable if it was determined pursuant to the methods prescribed above regarding the allocation of property.

The court may void the plan or modify the plan of termination to provide for a fair and reasonable apportionment of the proceeds. The prevailing party may recover reasonable attorney's fees and costs.

Distribution

Current law does not specify the procedures for distribution of the proceeds to owners and lienholders. This bill provides a termination trustee acts as trustee for unit owners and holders of liens on the units, in their order of priority.

Not less than 30 days prior to the first distribution, the termination trustee must deliver by certified mail, return receipt requested, a notice of the estimated distribution to all unit owners, lienors of the condominium property, and lienors of each unit at their last known addresses stating a good-faith estimate of the amount of the distributions to each class and the procedures and deadline for notifying the termination trustee of any objections to the amount. The deadline must be at least 15 days after the date the notice was mailed.

If a unit owner or lienor files a timely objection with the termination trustee, the trustee does not have to distribute the funds and property allocated to the respective unit owner or lienor until the trustee has had a reasonable time to determine the validity of the adverse claim. In the alternative, the trustee may interplead⁸ the unit owner, lienor, and any other person claiming an interest in the unit and deposit the funds allocated to the unit in the court registry, at which time the condominium property, association property, common surplus, and other assets of the association are free of all claims and liens of the parties to the suit. In an interpleader action, the trustee and prevailing party may recover reasonable attorney's fees and costs and court costs.

The proceeds of any sale of condominium property or association property and any remaining condominium property or association property, common surplus, and other assets must be distributed in the following priority:

1. To pay the reasonable termination trustee's fees and costs and accounting fees and costs;

⁷ Division refers to the Division of Florida Land Sales, Condominiums, and Mobile Homes of the Department of Business and Professional Regulation. Section 718.103(17), F.S.

⁸ "interplead" means to assert one's claim regarding property. In an interpleader action, a stakeholder deposits disputed property into a court's registry to abide the court's decision about who is entitled to the property.

2. To lienholders of liens recorded prior to the recording of the declaration;
3. To purchase money lienholders on units to the extent necessary to satisfy their liens.
4. To lienholders of liens of the association which have been consented to;⁹
5. To creditors of the association, as their interests appear;
6. To unit owners, the proceeds of any sale of condominium property subject to satisfaction of liens on each unit in their order of priority, in shares specified in the plan of termination, unless objected to by a unit owner or lienor;
7. To unit owners, the remaining condominium property, subject to satisfaction of liens on each unit in their order of priority, in shares specified in the plan of termination, unless objected to by a unit owner or a lienor;
8. To unit owners, the proceeds of any sale of association property, the remaining association property, common surplus, and other assets of the association, subject to satisfaction of liens on each unit in their order of priority, in shares specified in the plan of termination, unless objected to by a unit owner or a lienor.

After determining that all known debts and liabilities of an association in the process of termination have been paid or adequately provided for, the termination trustee will distribute the remaining assets pursuant to the plan. If the termination is by court proceeding, the distribution may not be made until any period for the presentation of claims ordered by the court has elapsed.

Assets held by an association upon a valid condition requiring return, transfer, or conveyance, which condition has occurred or will occur, will be returned, transferred, or conveyed in accordance with the condition. The remaining association assets shall be distributed pursuant to the priority order above.

C. SECTION DIRECTORY:

Section 1 amends s. 718.117, F.S., relating to termination of a condominium association.

Section 2 provides an effective date of July 1, 2007.

II. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT

A. FISCAL IMPACT ON STATE GOVERNMENT:

1. Revenues:

None.

2. Expenditures:

None.

B. FISCAL IMPACT ON LOCAL GOVERNMENTS:

1. Revenues:

None.

⁹ Section 718.121(1), F.S., requires the unanimous consent of the unit owners before a lien is valid against the condominium as a whole.

2. Expenditures:

None.

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

None.

D. FISCAL COMMENTS:

This bill provides increased opportunity for condominium owners who are a part of an uneconomic condominium to terminate that condominium; thereby allowing for greater flexibility in the investment or reinvestment of capital.

III. COMMENTS

A. CONSTITUTIONAL ISSUES:

1. Applicability of Municipality/County Mandates Provision:

This bill does not appear to require counties or municipalities to take an action requiring the expenditure of funds, reduce the authority that counties or municipalities have to raise revenue in the aggregate, nor reduce the percentage of state tax shared with counties or municipalities.

2. Other:

This bill may implicate the Contract Clause of the Florida Constitution, since some of the changes in this bill apply to existing associations. Article I, Section 10 of the Florida Constitution provides: "[n]o bill of attainder, ex post facto law or law impairing the obligation of contracts shall be passed."¹⁰

"A statute contravenes the constitutional prohibition against impairment of contracts when it has the effect of rewriting antecedent contracts, that is, of changing the substantive rights of the parties to existing contracts."¹¹ The Supreme Court of Florida held that laws impairing contracts can be unconstitutional if they unreasonably and unnecessarily impair the contractual rights of citizens.¹² The Court indicated that the "well-accepted" principle in this state is that virtually no degree of contract impairment is tolerable.¹³ When seeking to determine what level of impairment is constitutionally permissible, a court "must weigh the degree to which a party's contract rights are statutorily impaired against both the source of authority under which the state purports to alter the contractual relationship and the evil which it seeks to remedy."¹⁴

This bill may possibly modify existing contractual relationships between the owners a condominium unit and condominium association or a lending institution, and thus it may perhaps give rise to a constitutional concern that the bill impairs the obligation of contracts. However, in evaluating modifications of contractual rights in the relationship between condominium owners and their association or lending institution, the Florida Supreme Court has stated that "It may be assumed that the parties made their contract with knowledge of the power of the State to change the remedy or method of enforcing the contract, which may be done by a State without impairing contract

¹⁰ Article 1, Section 10(1) of the U.S. Constitution provides: "No State shall . . . pass any Bill of Attainder, ex post facto Law, or Law impairing the Obligation of Contracts"

¹¹ 10a Fla. Jur. s. 414, Constitutional Law. The term impair is defined as "to make worse; to diminish in quantity, value, excellence, or strength; or to lessen in power or weaken." 10a Fla. Jur. s. 414, Constitutional Law.

¹² *Pomponio v. Claridge of Pompano Condominium, Inc.*, 378 So. 2d 774 (Fla. 1979). The Florida Supreme Court has adopted the method of analysis from the United States Supreme Court in cases involving the contract clause. *Pomponio*, 378 So. 2d at 780.

¹³ *Pomponio*, 378 So. 2d at 780.

¹⁴ *Id.*

obligations.” *Palm Beach Mobile Homes, Inc. v. Strong*, 300 So.2d 881, 887 (Fla. 1974), quoting from *Mahood v. Bessemer Properties, Inc.*, 18 So.2d 775 (Fla. 1944). Because condominiums are highly regulated by current law, condominium owners and associations enter into contracts with the knowledge that new laws may be passed which could change some aspect of current contractual obligations. The courts have held that in these types of situations the State may pass certain laws affecting current contracts without violating the United States or Florida Constitution.

B. RULE-MAKING AUTHORITY:

None.

C. DRAFTING ISSUES OR OTHER COMMENTS:

None.

D. STATEMENT OF THE SPONSOR

This is the same bill that was unanimously approved last year without the provisions objected to in the Governor's veto message.

IV. AMENDMENTS/COUNCIL SUBSTITUTE CHANGES

None.