



## ***Due Diligence for Planned Community Acquisitions***

Now that sales of homes and condominium units are picking back up, developers are once again looking for development opportunities. Sometimes a better deal can be made by buying a partially completed development rather than starting from scratch and assembling raw land. However, buying into an existing development can bring risks and obligations as well. A prudent buyer always conducts research and analysis of a proposed real estate acquisition, but purchasing unsold inventory in a planned community or condominium project may require additional research beyond what is normally done when acquiring raw land for future development. This is particularly true where the seller is a lender who acquired the property through foreclosure. This article outlines a few of the issues to be examined.

*Examine Land Records.* A title examination should be conducted to determine whether any declaration of covenants, conditions and restrictions ("declaration") burdens the property being acquired. The analysis, however, can not end there. When a declaration exists for a planned community, many people assume that the declaration covers the entire community. That is not always the case. Some developments may have left off a portion of the community on purpose for flexibility or other purposes. Even when a portion of the property was subsequently subjected to the declaration, there are a number of ways in which such submission of land to a declaration can be defective. One of

the more common problems is that the party submitting the land does not actually own the land. A thorough examination should include an analysis as to which lots or tracts of land were submitted to the declaration and whether the party submitting such land owned the land or had the written consent of the land owner to do so.

*Identify any Community Association.* Where the declaration provides for an association, the actual existence of the association should be confirmed. Was the association incorporated? Is the corporate registration still valid, or has the association been dissolved by the state for failure to file annual registrations?

*Identify Community Governing Documents.* All documents that purportedly apply to the community should be identified. A title report should identify all documents recorded in the land records which affect the property, but there may be other documents which are not part of the public record that could bind a purchaser, such as association bylaws, articles of incorporation, design guidelines, and rules and regulations. The seller should be asked to identify and provide copies of all known community documents.

*Evaluate Effect of Any Foreclosure.* Often, the seller of the remaining lots in a planned community is a lender who acquired the property through foreclosure of the original developer. It is important to understand whether the lender's interest was subordinated to the declaration or had priority over the declaration. If the lender's interest has priority over the declaration, the lender could take title to the property through foreclosure of the mortgage without being subject to the declaration. If some lots had already been sold before the foreclosure, the community could be left with some lots being subject to the declaration and some not if the lender does nothing to consent to or otherwise adopt the declaration.

*(Continued on page 2)*

### **In this Issue...**

- **Due Diligence for Planned Community Acquisitions**
- **Georgia Imposes Restrictions on Transfer Fee Covenants**
- **Inside News**

*Volume XXVII Summer Edition 2013*

This newsletter addresses current issues and developments in the law relating to development and operation of planned communities. It is published periodically for distribution to clients and friends of Hyatt & Stubblefield, P.C., Attorneys and Counselors. The information presented is not intended as specific legal advice to any person. Principles of law expressed in this newsletter are subject to change from time to time.

*Examine Status of Declarant Rights.* If the buyer desires to have any control over the community or special rights or status beyond that of a general property owner, the buyer must acquire the rights reserved to the original developer or "declarant" in the declaration or other governing documents. Declarant rights do not automatically stay with the land, so the buyer will need to obtain an assignment of any declarant rights. The purchase contract should grant the buyer the option of obtaining an assignment of some or all declarant rights from the seller at closing.

Before determining whether to acquire declarant rights, the actual rights should be examined along with any obligations of the declarant. Many of the rights may have expired and the declarant obligations may outweigh the benefits of being the declarant. A developer buying the remaining inventory in a planned community cannot assume that it will be able to wield total control over the community. The governing documents will need to be examined to determine what control a new declarant may hold over the land and the association.

In addition, declarant rights may only be acquired from one who currently holds those rights. It is important to determine whether the seller obtained a valid assignment from the original declarant. A lender who acquired the property through foreclosure may not have acquired the declarant rights from the original declarant. If the seller does not hold the declarant rights, is the original declarant still in existence? Can the seller cause the original declarant to make an assignment to the buyer?



*Examine Rights Under Governing Documents.* There are a number of actions that a developer typically wants to take or wants to protect against. A thorough examination of all of the community governing documents is necessary to fully understand the scope of control that the developer will hold, whether as a special declarant right or by virtue of holding a certain number of units in the community.

- Does the homeowners association sell memberships to persons who are not lot owners within the community?
- If the buyer acquires land that has not yet been submitted to the declaration, will the declarant have the power and option to submit such land to the declaration?

- Is there any land that should be withdrawn from the declaration, and will the declarant hold the power to do so?
- Does the declarant hold architectural review/control rights? Does the declarant have the power to amend or adopt any design standards?
- Does the declarant have the power to unilaterally amend the governing documents?
- Does the declarant have the power to block other unit owners from amending the governing documents?
- Does declarant control the composition of the association's board of directors or will declarant hold at least a majority of the seats on the board?

*Evaluate Obligations Under Governing Documents.* In addition to rights that will accrue to the buyer, the community documents need to be examined to determine the obligations on the property being acquired and when any future obligations will become due. What is the nature of the land being acquired?

- Do the units being acquired presently owe assessments to the association? When will the assessment obligation be triggered?
- Is there an obligation to construct a home within a certain period of time?
- Will the buyer be acquiring land that is designated as common area? If so, should the property be transferred to the association by the seller prior to closing?

*Investigate Association Funding.* Regardless of whether the developer will take over control of the association, the association's financial state should be reviewed since it could impact sales. Have owners been assessed? What is the delinquency rate? If the declarant owes assessments on its property, have those assessments been paid? Have reserves been adequately funded or could future assessment increases be needed to fund repairs?

Thorough community association due diligence can be beyond the scope of experience of some acquisition teams and what they are prepared to conduct. We are happy to help analyze a community prior to acquisition and can efficiently synthesize the issues based on our over 40 years of experience in the development of planned communities.



## Georgia Imposes Restrictions on Transfer Fee Covenants

Georgia recently adopted a statute which prohibits the imposition of a non-exempt restriction or covenant running with the land on real property which obligates the seller or purchaser of the real property, or their heirs, successors, or assigns, to pay a fee in connection with the transfer of such property to the person establishing the restriction or covenant or to a third-party (often called a "transfer fee covenant"). A transfer fee covenant, however, may be imposed under limited circumstances. The statute makes only new non-exempt transfer fee covenants created on or after July 1, 2013 void and unenforceable and does not affect existing transfer fee covenants.

The prohibition does not apply to a restriction or covenant running with the land that requires the fee to be paid in connection with the conveyance of property to:

- a condominium association;
- a property owners' association that has elected to be subject to the Georgia Property Owners' Association Act;
- a property owners' association that has not elected to be subject to the Georgia Property Owners' Association Act, but only if the association complies with the provisions of such Act requiring an association to give an owner a statement of amounts due upon request (O.C.G.A. § 44-3-232(d));
- a "community land trust" or "community development corporation" that is tax-exempt under Section 501(c)(3) or 501(c)(4) of the Internal Revenue Code, provided the transfer fee funds collected are applied to expenses incurred in the administration of ongoing community program services or rights provided to "shared equity property interests" within the land subject to the community land trust or the geographic area served by the community development corporation; or
- a licensed real estate broker for brokerage services rendered in connection with the property transfer.

The terms "community land trust" and "community development corporation" are not defined in either the Georgia statutes or the Internal Revenue Code, so it is unclear how the exception for those type organizations is to be applied. Various federal statutes define those terms for purposes of the

particular federal statute at issue, but, in every context, the term involves affordable housing for low-income individuals.

If the community development corporation and community land trust exception is interpreted as involving only affordable housing organizations, then the uses for which transfer fees may be used in the future will be limited. For example, no longer may new transfer fee covenants be created for the purpose of funding environmental, conservation, educational, or community building activities, unless these activities are conducted by a property owners' association that satisfies the Property Owners' Association Act.

In addition, a new restriction or covenant on the land may not require the property owner to buy a membership in, make an equity contribution to, or pay some type of initiation fee to a recreational or social club that is separate from the property owners' association. New restrictions or covenants may still require that a property owner acquire a membership in a club, but the transfer of the property cannot trigger a payment. In other words, the property owner can be required to pay periodic dues or assessments during the term of membership, but they cannot be required to "buy" into the club.

While the statute does not abolish transfer fee covenants already in existence, it will substantially limit (in future applications) the purposes for which transfer fee covenants have traditionally been used. New mechanisms will need to be developed to fund many of the future environmental, conservation, and social programs that have customarily been funded through transfer fee covenants.





HYATT & STUBBLEFIELD, P.C.

ATTORNEYS AND COUNSELORS

Peachtree Center South Tower

225 Peachtree St., N.E., Suite 1200

Atlanta, Georgia 30303



## Inside News: Wayne Hyatt Receives National Recognition

The American College of Real Estate Lawyers (ACREL) awarded its prestigious Frederick S. Lane Award to Wayne Hyatt at its Mid-Year Meeting in Florida this past spring. Jonathan R. Shils, President of ACREL, stated: "The Frederick Lane Award is the highest honor the College can bestow. The Lane Award has previously been given only seven times since the College was founded in 1978 to honor the career contributions of distinguished real estate lawyers who have selflessly served the profession, the College and their community. In honoring Wayne Hyatt with the Lane Award, the College affirms these values by recognizing such a worthy recipient with this accolade from his peers."

Wayne served as President of ACREL in 2004. His prior service to the organization included terms as President-Elect, Vice President, Secretary, and member of the Board of Governors; Chair of the Bylaws, Common Interest Ownership and Affordable Housing com-

mittees; and membership and leadership participation in over a dozen committees. He was the driving force behind establishing ACREL Cares, a community service program.

ACREL was founded in 1978 as a non-profit organization of lawyers who have gained distinction in the practice of real estate law. The group devotes its efforts to improving the practice of real estate law around the country, and its membership consists of lawyers from 50 states, the District of Columbia, and the U.S. Virgin Islands. It has become the nation's most prestigious peer selected organization for practicing real estate lawyers.

Admission to ACREL is by invitation only. This national legal real estate organization elects to its membership lawyers distinguished for their skill, experience and high standards of professional and ethical conduct in the practice of real estate law.