

IN ASSOCIATION

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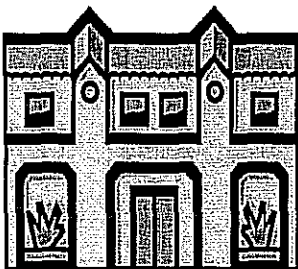
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NEWS ABOUT OUR FIRM

We are pleased to announce that Scott J. Sandler has become a principal of our firm. The name of our firm has changed to Perlstein & Sandler, LLC.

Under our new name, we will continue to provide legal services to condominium and homeowner associations throughout Connecticut.

PRACTICAL STEPS TO FACILITATE TRANSITION OF THE ASSOCIATION FROM THE DECLARANT TO THE UNIT OWNERS

The transition of control of a condominium or homeowners association from the declarant to the unit owners is not a one step event. It is a process.

Under the Section 47-245 of the Connecticut Common Interest Ownership Act ("Act"), the transition process begins, or should begin, when the declarant has sold one-third of the units that may be created. At that point, the unit owners are entitled to elect at least one-third of the board members. This allows the unit owners to participate in the activities of the association and to become familiar with its operations and procedures. Once sixty percent of the units have been sold, the unit owners are entitled to elect all of the board members.

As a practical matter, however, the process often does not begin when it is supposed to. Declarants frequently fail or refuse to let unit owners elect one-third of the board members after one-third of the units have been sold. Even after the unit owners take full control, many issues between the association and the declarant often remain open and unresolved. Disputes over uncompleted "punch lists," construction warranties, declarant mismanagement of association funds, and undelivered association records, property, documents and audits can go on for years. Though eager to get on with the business of managing the association, new boards can find

their energies and funds stressed by addressing such issues with the declarant.

The following are some practical suggestions to assist a new board in dealing with transition issues, to facilitate a timely and ultimate resolution:

1. Establish a Transition Committee. The new board should establish a transition committee, made up of board members and volunteer unit owners. This committee should conduct a thorough review of the declarant's activities while the association was under its control. Among the specific tasks of the committee are the following:

- a. Review the requirements of Section 47-245 and other relevant provisions of the Act, to ascertain which documents, records, contracts, leases, property and audits the declarant must provide to the association.
- b. Collect and inventory all items produced by the developer.
- c. Review all of the books and records of the association to ensure they were properly kept and that the affairs of the association were properly managed.

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2. **Seek Expert Advice.** The association should seek expert advice from professionals familiar with the structure and practices of common interest communities, and who possess experience in addressing transition issues. These experts should include at least the following:

- a. **An Attorney.** An attorney can review the association's governing documents for completeness, assist in obtaining the declarant's compliance with the requirements of the Act, and review the existing contracts and leases between the declarant and third-party service providers such as contractors, landscapers, snow plowers, and even managers. The latter is extremely important because under Section 47-247 of the Act, the new board can terminate many of these contracts, without penalty, following transition.
- b. **An Accountant.** An accountant is indispensable in assisting the association in reviewing the association's financial records that were kept by the declarant. This is particularly important when, as frequently happens, the declarant fails or refuses to provide the certified audit of the financial records as required by Subsection 47-245(h) of the Act. The accountant is also needed to identify financial claims against the declarant for the mismanagement of the association while it was under declarant control. The association may also uncover mismanagement by the individual board members appointed by the declarant.
- c. **An Engineer.** An engineer can inspect the buildings and infrastructure to determine whether the declarant has met its obligations under the statutory warranties and the governing documents. The engineer can also prepare a "punch list" of unfinished work or remedial work that may be required.
- d. **A Property Manager.** A property manager can give the association professional assistance in setting up records, collecting assessments,

assessing fines, enforcing the rules and in maintaining the common elements. If the declarant employed a manager, the association may wish to evaluate how well it works with this manager and whether it would be better suited hiring a different manager.

3. **Make Demands On the Declarant.** Once the initial review of the declarant's activities while in control of the association has been completed, the association should make a written demand on the declarant for any missing records, property and audits. The demand may also include any claims the association may have for mismanagement, incomplete construction work or violations of statutory warranties. The declarant may respond favorably to these demands. Unfortunately, however, many associations find that such demands are ignored. In some cases, the declarant never even kept the documents and records that must be turned over to the association.

4. **Review Litigation Options.** The association should seek the advice of its attorney concerning the costs and benefits of litigating unresolved issues with the declarant. Often times, associations conclude that litigation is not in their best interests. Litigation is time consuming and expensive. The costs and fees incurred in litigation may exceed the financial claims themselves. While the Act permits the court to award attorney fees, such an award is within the discretion of the court. The court may award far less than the actual fees and costs incurred by the association. Moreover, many declarants are limited liability entities, created for the sole purpose of forming a particular community and designed to be insolvent after completing the project. There may be nothing to collect even if the association obtains a judgment.

5. **Moving Forward.** If there are unresolved issues and litigation is not worth the cost and effort, the best option available to the association may be to cut its losses and get on with the business of running the affairs and activities of the community. While having the declarant address all of the unresolved issues may be the most desirable outcome, it frequently does not happen. Fortunately, the association has the power and ability to proceed with the operation

The association has the power and ability to proceed with the operation of the community, even if the declarant refuses to cooperate.

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of the community, even if the declarant refuses to cooperate.

In conclusion, the transition process is often difficult. An association going through transition should attempt to get all of its books, records and property from the declarant. Ultimately, however, time and expense may require the association to set aside unresolved issues with the declarant. After all, the association already has the power to collect assessments, manage its affairs and proceed with the governance of the community. In the long run, what matters is not getting even with the declarant, but rather making the community a good place in which to live and own.



EDUCATIONAL SEMINARS: THE IN'S AND OUT'S OF COMMUNITY ASSOCIATION OPERATIONS AND GOVERNANCE

Times change. Needs and expectations change. Board members and unit owners change. Our seminars are designed to assist your association in continuing its operations while meeting the changing needs of the community.

The rules of the game of operating a successful community association have changed over the years. Associations now find themselves facing issues that were previously unheard of. For example, many associations now borrow money to fund capital improvement projects. Fifteen or twenty years ago, such loans were rare, if they happened at all. Ten years ago, the deductible under a master insurance policy might have been \$1,000 or less. Associations are now forced to accept deductibles as high as \$10,000. This is frequently coupled with higher insurance premiums.

Not only have the rules changed, but frequently so have the players. Units are bought and sold, changing the association's membership. Board members come and go. When a board member

leaves, they often take their knowledge and experience with them.

The association must continually compensate for the changing rules and changing players. Perhaps the most important step is education. The association must learn of the changes, and what can be done to adapt.

We can help. We offer the following education seminars that are designed to assist you in adapting to changes in the environment of the association:

- New owner and new board member orientations. We introduce the new unit owners and new board members to the world of association operations. We provide an overview of the structure of the governing documents together with a discussion of the impact of many of the operating provisions. We also discuss the rights and responsibilities of the association and the unit owners. By exploring these issues with new owners and board members, the association reduces the likelihood of a later conflict.
- Dealing with higher insurance premiums and deductibles. We suggest methods for reducing the likelihood of increases in the insurance premium and shifting the cost of deductibles to other sources of insurance. Taking such measures may save the association thousands of dollars over time.
- Borrowing requirements. We review the governing documents of the association and outline the hypertechnical requirements of what is required to secure a loan. We also discuss the potential pitfalls that the association may face, such as resistance from the unit owners and dealing with banks that are still gaining experience in association lending.
- Conducting effective meetings through parliamentary procedures. We provide a survey of the use of the parliamentary procedures contained in Robert's Rules of Order (10th Edition), including the making of motions, conducting debate and proceeding with voting. We further illustrate the effectiveness of parliamentary procedures through a mock meeting of the association. We also discuss what you should include in the minutes of

The association must continually compensate for the changing rules and changing players.

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meetings and the proper use of executive sessions by the board. The use of parliamentary procedures will enable the association to conduct more effective and orderly meetings.

- Adoption and enforcement of rules and regulations. We review the process for adopting rules and regulations. We also distinguish between restrictions that may be adopted as rules and restrictions that belong in the declaration or bylaws of the community. We discuss issues such as parking, pets and satellite dishes, which many associations faced with mixed results. We further examine the benefits of providing unit owners with notice and an opportunity to comment or be heard. This assists the association in adopting rules and regulations that benefit the community and are legally enforceable.

- Reasonable accommodations for disabled persons. We provide an overview of the federal laws concerning the obligation of the association to make reasonable accommodations for persons with disabilities. We discuss how the association can verify whether an accommodation is required, and how to administer the accommodation. This enables the association to meet the special needs of certain unit owners while complying with federal law.

We are available to provide these seminars at a time convenient to the association. Please contact us if you would like to schedule a seminar or if you have questions concerning the content or cost of a seminar.



WHAT TO LOOK FOR IN A LOAN

Associations make good borrowers. More and more banks are offering loans to community associations in Connecticut. If your association is considering a loan, it can choose among more lenders and more diverse loan terms than ever before.

Not all banks offer the same terms and not all terms are equally attractive to all associations. Here are some items to consider:

- Interest Rates. All things being equal, and they often are not, the most attractive loan is the one with the lowest interest rate. Most banks offer fixed rate loans for terms of at least five years. Some banks fix the interest rate at the time the association applies for the loan. Other banks use a formula, tied to a national or regional index, to determine the rate at the time of the loan closing or when the loan begins to amortize. Some banks offer loans for a longer term with one or more rate adjustments partway through the term. Since the association is borrowing money that must be repaid by many unit owners who have different financial needs and circumstances, it may be best to take a conservative approach, opting for the plan that exposes unit owners to the least risk.

- Application Fees. Many banks charge a fee at the time the association applies for a loan. Some banks charge only a few hundred dollars, others charge thousands. The application fee is sometimes non-refundable. Other times it is refundable only if the bank rejects the application. There are a number of reasons why an association might apply for a loan but then not go forward with it. It may find better terms at another bank or the unit owners may not vote to approve the borrowing. For these reasons, the association should avoid large, non-refundable application fees.

- Prepayment Penalties. Some banks charge a prepayment penalty if the association repays the loan ahead of schedule. This penalty is usually expressed in terms of a percentage of the amount prepaid. Some prepayment penalties apply only if the association pays off the loan with money borrowed from another financial institution. Other prepayment penalties apply regardless of where the money comes from. Since many associations prepay all or part of their loans, prepayment penalties should be avoided unless the lender is offering a very favorable interest rate on the loan itself.

- Collateral. When an association borrows money, its principal collateral is a pledge of its right to collect future common charges. Under

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the Connecticut Common Interest Ownership Act, an association can pledge its right to collect future common charges if its declaration contains a provision permitting it to do so. Almost all communities created since 1984 have such a provision in their declarations. If your community was created before 1984, you will most likely have to amend your declaration to permit your association to pledge common charges. In most situations, a pledge of the association's right to collect common charges plus its power to set and levy assessments, is all the collateral the lender needs.

Occasionally, a lender will require other collateral, either in addition to or instead of a pledge of common charges. This collateral may include an assignment of other income such as payments from rooftop leases for cellular antennas or other telecommunications equipment. If the association owns a unit, the lender may ask for a mortgage on the unit. In most communities, it is inappropriate for the lender to ask for a mortgage on the common elements.

- **Primary Banking Relationship.** Some lenders will require the association to keep all or most of its bank accounts with the lender. This is good banking business and, ordinarily, not objectionable. There are a few exceptions. If the association is collecting common charges by means of a lockbox system operated by a bank that understands the particular needs of community associations, it may not want to change banks. In addition, since banks can buy and sell their loans, the association's obligation to maintain bank accounts should apply only to the bank from which it originally borrows the money.

- **Insurance Requirements.** Most lenders will specify the types and minimum amounts of insurance that an association must carry. Often these requirements are the same or similar to the requirements contained in the association's documents. Sometimes, however, the lender will require the association to carry significantly more insurance. Review the insurance provisions carefully to determine whether the association will be required to carry additional insurance in order to comply with the terms of a proposed loan.

The lender cannot ask for the right to be paid any of the insurance proceeds if there is a loss. Under the terms of almost all documents, these proceeds must be used to rebuild the damaged portion of the community.

- **Draw Down Period.** Most associations borrow money to pay for repairs or renovations. If the renovations will take a number of months, the association may prefer to receive the loan proceeds in several advances, so that it is not paying interest on money it does not yet need. Most lenders will offer the association a choice of receiving all of the loan proceeds at once or of drawing the loan proceeds down in installments. If the association chooses to receive the money in installments, it pays interest only on the amount it has actually borrowed until a specified date or until it has drawn down the entire loan. After that, the association makes monthly payments of principal and interest. Review your renovation plans and the payment terms of your renovation contract carefully before deciding what terms best meet the needs of the association.

- **Not a Construction Loan.** Even if the association uses the proceeds of the loan to pay for construction, the loan is not a "construction loan" as the term is ordinarily used. A typical construction loan is a mortgage on real estate where the value of the real estate increases as the loan increases. This is because the proceeds of the construction loan are used to build or repair something on the real estate, increasing the total value of the property. In a construction loan, the bank ordinarily reserves the right to make advances only after work has been done on the real estate, and the bank has inspected the work.

The collateral for an association loan is not the real estate. Rather, it is the association's income stream. It is ordinarily not necessary for the lender to keep inspecting the construction work,

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and charging inspection fees, before it makes advances. Some banks, particularly those that are not experienced in lending to associations, will include construction terms in their loan documents. Unless the association is a poor credit risk or the loan is unusually large, these terms are unnecessary and should be avoided.

- The Bank's Attorney. The bank's attorney will prepare the loan documents, review the opinions and certifications furnished by the association and its attorneys, and supervise the closing of the loan. As with most loans, the borrower is required to pay the attorney's fees incurred by the lender. While it is impossible to predict all of the issues that may come up in preparing for the loan closing, it is helpful to ask the bank for an estimate of its attorney's fees.

- Opinion of Borrower's Counsel. Before the bank can close the loan and begin advancing money to the association, it needs to verify that the association's documents enable it to enter into the transaction and that the association has followed all of the procedures required to approve the loan transaction. The bank does this in part by asking for documents and certifications from the association. It also asks the association's attorney for an opinion that the association has complied with applicable law and with its documents, and that the loan transaction will be binding. In order to give this opinion, we, as the attorneys for the association, must conduct a title examination of the land records of the town in which the community is located, review the records of the Secretary of the State, review the association's documents and review all of the board and unit owner resolutions and approvals concerning the loan as they appear in the association's minutes. If the votes the association has taken are not in full compliance with the relevant statutes and the documents, we cannot give the necessary opinion. For this reason, we strongly recommend that any association that is considering a loan consult with us before calling any meetings or preparing or adopting any resolutions. By drafting the resolutions for the association and outlining the procedures by which the resolutions are adopted, we can ensure that the association complies with all of the necessary requirements. If the association starts without

legal assistance, it is possible that it will have to go back and hold some of its meetings or adopt some of its resolutions again before it can close the loan.

- Level of Approval. Most documents prepared since 1984 permit associations to borrow money, and pledge their right to collect future common charges as collateral, with the approval of 51% of all of the voting power in the association. If an association must amend its documents to acquire the power to pledge common charges, the amendment may require the approval of two-thirds to three-quarters of the voting power in the community. Some lenders may require additional approvals, as high as 80% of the unit owners, before they will close a loan. Others may require unit owner approval of additional actions, such as an increase in the association's reserves or the annual budget, before they will close. If a lender requests such additional approvals, review them carefully to determine how difficult they will be to obtain.

- Does the Bank Know What It's Doing? Not every bank that is lending to associations knows what it is doing. If the bank has not taken the time to understand how associations operate, and to develop loan terms and documents that reflect the needs of associations, your association may find it difficult to do business with the bank even though it is offering competitive rates. We recommend that whenever the association talks to a bank, it ask the bank about its experience. The association should also talk to other associations that have done business with the bank. Additionally, the association should review the terms that the bank offers with the association's manager, its accountant and its lawyer before signing a loan commitment or taking any other steps.

If you have any questions, or would like to talk with us about a loan your association is contemplating, please don't hesitate to contact us.



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TELEPHONE SYSTEM EXTENSIONS

If you should call our office and the automated answering system answers, you may use the following extensions to reach us if we are in the office or to leave a message in our individual voice mailboxes:

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Scott J. Sandler:	Extension 15
Lawrence C. Malick:	Extension 16
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