

What happens to HOA when developer folds?

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Q. We live in a condo subdivision planned for 56 units. The developer has fallen into financial difficulty and has only sold six units. There are now 16 completed units. The developer is renting the remaining 10 units. Even though the six homeowners are paying \$155 monthly as association dues, the developer is not providing home maintenance. What legal recourse do we have? What would happen to our property if the developer declares bankruptcy or if all of the unsold property goes into foreclosure? Would the HOA, which only consists of six owners, be responsible for paying the mortgage on the clubhouse? Would we be responsible for paying property taxes on the unsold homes?

We are seeing situations like this a lot today in our practice. In a condominium, the developer typically pays all the expenses of the HOA until a sufficient number of units have been sold to allow the HOA to stand on its own financial feet.

At that point, the developer begins assessing each unit for its share of common area expenses. When that occurs, the developer is responsible for paying the same assessments on its unsold units that would be owed if the units were owned by homeowners. The fact that the developer still controls the HOA's board doesn't give him the right to withhold the payment of assessments on units he owns, once assessments have begun.

If the developer's lender forecloses on the unsold units, someone is going to buy that property at the foreclosure sale. More often than not, the lender is the only bidder at the foreclosure sale, and it takes title to the properties.

When it does, the law views the lender as it would any other owner: It will have to pay assessments on the homes that it owns in accordance with the Declaration of Condominium. The HOA should continue to function as normal.

The board should not vary from its policy for handling delinquent accounts just because a financial institution owns a number of the homes. If the HOA board is not fulfilling its duty to collect assessments and provide maintenance for the common areas, then the owners should consider filing a lawsuit against the board.

In a condominium, each homeowner owns a fractional percentage of the common elements. Keep in mind that if a lender forecloses on the unsold units, the HOA will not have to assume the mortgage payments because there will no longer be any mortgage debt owed on those

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units or the associated interest in the common areas.

A completed foreclosure "wipes out" the debt on the property. If there are unpaid property taxes on the units, those taxes would be the responsibility of the owner of the units, not the HOA. There should not be any taxes owed separately on the clubhouse, since it is jointly owned by the owners of all units, and taxed as part of the value of those individual units.

If the developer files bankruptcy before its lender completes a foreclosure sale, there are several possible outcomes. The lender could agree to reduce the amount of debt owed on the property and allow additional time for the project to be completed and homes sold.

Or, the lender could insist that the property be sold "as is" either by a broker or at a court-ordered sale. Whoever bought the property would become the new owner and be responsible for payment of assessments on the vacant units.

Or, the court could allow an investor willing and able to put additional cash into the project to complete the development.

E-mail questions to home@charlotteobserver.com

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