

Are Condominium Boards Acting More Like Co-op Boards? Is This Permissible And What Are The Risks?

By Pierre E. Debbas, Esq., Romer Debbas, LLP



Historically in New York City, the two most common forms of residential real estate are cooperative and condominium apartments. Co-ops are very specific to the New York area and these structures are rarely utilized outside of New York.

The main reason is that a co-op functions as a corporation in which you own shares and not an actual apartment. Co-ops are governed by Business Corporation Law (BCL). BCL gives co-op boards a very broad discretion in exercising its authority with the most prevalent being an approval process on the transfer of shares and the ability to impose conditions on same. Condominiums were developed for those who wanted the flexibility of freely transferring their property without the restrictions that can come with a co-op.

Generally, the only requirement in a condominium is the board waiving its right of first refusal. One of the main reasons a right of first refusal exists in a condominium is that if the board found issue with a prospective buyer, their financials, the purchase price, etc. then it would have the ability to purchase the unit for the condominium association at the exact same terms as the seller and buyer are under contract for.

The Condominium Act or for the most part a condominium's declaration, does not give a condo board any other rights on the transferability of an apartment except for exercising their right of first refusal.

The issue that is coming up is that condo boards are acting more like co-op boards in placing restrictions or holding the issuance of the waiver hostage until a buyer or seller concedes to the board's conditions. The condition that is most frequently seen is the requirement for a foreign national investor to place a common charge escrow (of 1-5 years of common charges) with the board for their entire duration of ownership.

The answer as to whether a condo board has this right is one which is highly debated these days. There is case law which states that a condo board has the fiduciary duty to act in the best interest of the condominium and has to its avail a concept such as the business judgment rule.

The business judgment rule is part of BCL and one of the main elements which allow for a co-op to make several decisions without having to provide an explanation (i.e. board turndowns).

One can make the argument that a condo board can impose re-

strictions on the issuance of the waiver in these scenarios if it believes it is acting in the best interest of the condominium. However, this now negates the entire purpose of a condominium. The reason that almost all new construction over the past decade has been condominiums is due to the consumers' desire to purchase real property without being subject to the blanket authority of a co-op board.

In imposing such restrictions, a condo board is exposing itself to liability in the sense that it is potentially acting outside of its legal scope of authority and jeopardizing the transferability of apartments in its building.

Furthermore, if a condo board does in fact want to enact policies of this nature, it should ensure that it does so in accordance with the voting requirements outlined in their governing documents. Any such conditions should be passed through a formal vote and shall also be disclosed in the condominium's application.

If a condo board neglects to do this, it risks the possibility of a discrimination claim by a foreign national who is being singled out in such a request or a claim by the seller whose transaction may potentially fail due to this. The condominium also risks devaluing property values by negating the aspect of the units being freely transferable.

The position that boards take that do impose this requirement has been that of might versus right. In my experience, not one counsel for a condominium board has provided a legal basis for being able to impose this right and essentially states that it is a requirement by board, banking on the fact that it will not be financially advantageous to buyer or seller to litigate the matter.

At some point, a transaction will fail due to this requirement and the parties will likely seek legal action against the board. If a condominium board does elect to impose requirements on the issuance of the waiver of right of first refusal, it should consult with its counsel to ensure it is taking the necessary steps to properly impose such requirements and it should carefully consider the pros/cons of doing so without solely relying upon its leverage in these situations.

*Pierre E. Debbas, Esq.
Romer Debbas, LLP
183 Madison Avenue – Suite 904
New York, NY 10016
Tel: 212-888-3100
PDebbas@romerdebbas.com
www.romerdebbas.com*