A 13 Point Plan for Successful Transition

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Point No. 1: ***Transfer common property before control of the Board passes to Unit Owners in large or slow selling projects.*** It is a mistake for both the developer and the unit owners to postpone the transfer and/or acceptance of the common property by the association until after seventy-five percent of the units have been sold and the unit owners assume control of the governing board, especially where there is a significant time lapse due either to the size of the project or the slow rate of sales. I would much rather see the Sponsor controlled board under these circumstances permit the minority unit owner members to select an independent engineer at the expense of the Association to inspect the completed portions of the common property and to negotiate the extent of the remedial work with the Sponsor, subject to an express written agreement that there is no waiver of any legal rights by either the Association or the Sponsor pending turnover of control of the Board to the unit owners. Although this approach may not be feasible in every circumstance, it encourages the separation of construction defects from maintenance problems and helps to isolate the responsibility for each type of problem. It also eases problems of proof for both sides should formal proceedings ultimately be instituted and encourages cooperative rather than adversarial solutions with respect to the physical problems which may exist. Most importantly, the developer can look to its subcontractors to remedy defects while they are still on the job and monies have been retained under their contracts. Some developers of large projects have included similar "early transition" provisions in their governing documents and the current version of NJ/ UCIOA also includes a mechanism for transition.

Point No. 2: ***Independent association counsel should be appointed shortly after the first transition election when 25% of the units have been conveyed.*** It is usually beneficial to both the developer and the unit owners to appoint independent counsel for the association soon after the first transition election, especially where the transition period is contemplated to be an extended one. Independent counsel's presence will significantly increase the comfort level of the unit owner members of the Board and help build communication between the Sponsor and the unit owners. Selection should be by the unit owner members of the Board so as to maximize trust and confidence between the unit owners and the attorney, which will hopefully result in a continuing relationship throughout transition, even after the unit owners take over control of the Board.

Point No. 3: ***Managing agents who are actively involved can be very helpful in achieving a successful transition.*** Managing agents can play an extremely constructive role in transition by giving the unit owner Board members perspective as to the dynamics of transition, the importance of communications, and the pitfalls of litigation. I sense that too often the manager takes a passive approach and is not concerned beyond the politics of what is best for himself when it comes to contract renewal time and by referring professionals to the Association whose primary qualification is whether they refer business to the manager, rather than whether they are best qualified for the job.

Point No. 4: ***Engineering inspection reports are not intended to be primarily for litigation purposes.*** The primary purpose of an engineering report commissioned by an Association at the outset of transition is to obtain professional assurance for the Board that the physical condition of the property is satisfactory and to identify deficiencies which need to be addressed. Its main object is to discharge the Board's fiduciary duty to ascertain the physical condition of the property before it is accepted for maintenance and not to serve as a spring board of settlement negotiation or litigation against the developer. Therefore, given this perspective, a clean report by a qualified engineer is the best result for both sides. Naturally, where there are construction problems, these reports should serve as a vehicle for promoting constructive dialogue with the developer regarding the remedial work that may be appropriate.

Point No. 5: ***Canned engineering reports may do more harm than good in transition negotiations.*** Canned engineering reports, as well as those which are overly judgmental, tend to raise questions about their technical credibility. A report which is more individually tailored and factual is normally better because the other side will address it more seriously. Also, the separation of maintenance problems from construction problems is important. To homogenize them in the same report can foster the notion that most of the problems are maintenance related and therefore not the responsibility of the developer which is clearly not always the case. Also, the engineering report should not contain either absurd or peripheral items for they only detract from the importance of the significant ones and impact negatively upon the credibility of the entire report. Also, this type of report tends to result in both parties getting hung up in the detail. Try to cull out these items before submitting a report to the other side and focus on the important items. The others usually disappear anyway if and when the primary issues are resolved.

Point No. 6: ***Don't be too quick to give a formal engineering report to the other side.*** Engineering reports can be trouble for either side if they are not judiciously prepared and reviewed by counsel before being finalized. Nothing can destroy the credibility of a report more completely than obvious mistakes engendered by carelessness, boiler plate, stretching of the facts, or inadequate homework. In addition, a report which is too candid or says too much can prejudice one's client in the absence of any litigation. Consideration should be given to having the engineers for each side prepare summary reports which may cover the major defects, although notes can be made and maintained by the engineer. The summary report can be used as a basis for initial discussions to see if a basic agreement can be reached on the major issues between the clients and their technical consultants. Otherwise, too many details stand in the way of reaching agreement on the important issues.

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Point No. 7: ***Experience in Transition and in court is an absolute must when choosing a law firm and experts for transition.*** In choosing a professional consultant in connection with a transition negotiation, try to obtain assurance from your attorney that the consultant's report and individual testimony will stand up in court. An experienced adversary will know or quickly learn about the weaknesses of each and exploit them during the settlement negotiations, as well as the time of trial, just as he will in the case of a law firm which does not have experience in construction defect or community association transition and litigation. Be on guard against being penny wise and pound foolish in this area for it is clearly more expensive to have to hire a second professional if the first turns out to be inadequate, not to mention the prejudice that may have occurred to your case as a result of the wrong initial choice.

Point No. 8: ***Informal communications between professional consultants can be effective and economical.*** Consider having the engineers and the accountants for both sides talk to each other early in the transition process. If they are professional in their approach, it should enhance communications, eliminate spurious claims and minimize professional fees for both sides. Attorneys by nature tend to be adversarial and therefore communications through attorneys do not necessarily promote constructive dialog. It is a good idea, however, to have a written understanding between the attorneys as to the ground rules and the fact that none of the discussions between the other professionals can be utilized in subsequent litigation.

Point No. 9: ***Punch lists from unit owners impede successful transition negotiations.*** The compilation of a unit owner punch list, especially with respect to individual units, can be a deterrent to a successful transition negotiation because it unduly raises the expectation level of the individual unit owners. Therefore, it is more difficult politically for the governing Board to reach a fair and reasonable settlement with the developer. Furthermore, an Association may not be empowered to settle unit claims and the unit owners should not be led to believe otherwise when it is clear that any knowledgeable developer will reject unit claims that are not pervasive as a matter of course. As for an alternative to a punch list, a questionnaire prepared by the engineer related to specific physical aspects of the common elements may be a useful tool in helping the engineer identify the construction problems

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which may exist, but care should be exercised to make certain that its purpose is not misunderstood.

Point No. 10: ***Transitions for conversion projects differ substantially from new construction projects.*** There is a significant difference between a conversion and a new construction project with respect to the Sponsor's obligations as to the common property. In the former case, the Sponsor's warranties are relatively limited and generally the property is sold in an "as is" condition. In addition, deficiencies in the engineering report required for conversions do not necessarily rise to a claim by the Association, as the Planned Real Estate Development Full Disclosure Act expressly limits the standing to assert damage remedies to purchasers who have placed reliance upon the disclosure information . In new construction, there are warranties that run not only to the original purchasers as in the case of conversions, but also to the Association under the Homeowner's Warranty Act and related warranty plans, as well as those required by the Department of Community Affairs in connection with PREDFDA registration.

Point No. 11: ***Don't indiscriminately sue developers personally.*** Combative instincts of attorneys tend to encourage the inclusion of principals and/or the officers and directors of the developers as a defendant in community association litigation even when their potential liability appears to be highly speculative or nonexistent. Suing them personally should not be a reflex action, however, because if there is either the hope or potential for future settlement dialogue, nothing can cause a developer to stonewall an association more quickly than to make the developer an individual defendant. Accordingly, the potential for settlement may be diminished significantly, if not extinguished altogether and instead, the association may be faced with the aggravation and expense of years of litigation.

Point No. 12: ***Community Association insurance is unique and changes should be approached cautiously.*** Changing insurance agents or carriers when control of the Board vests in the unit owners is not necessarily appropriate although a review of insurance coverage is encouraged. The review of coverage, rates and quality of service should be a periodic and ongoing process especially in an uncertain market place. Insurance should not be treated as political patronage, especially if the existing agent is providing good service and is knowledgeable.

Point No. 13: ***Consider enlisting the aid of the Department of Community Affairs in the transition process where there are substantial problems which the developer persists in ignoring.*** The Department of Community Affairs is playing an ever increasing role in the enforcement process and can sometimes be helpful to an Association when sales are still going on by requiring the developer to meet its obligations under its public offering statement or the transition provisions of the Condominium Act or PREDFDA regulations. The Department is especially responsive to delinquencies by the Sponsor in its common expense payments or reserves, as well as construction defects which have the potential to seriously threaten the health, safety or welfare of the unit owners. By no means, however, is their involvement automatic and their response has a lot to do with the nature of the complaint.

In conclusion, I have attempted to raise a number of issues which concern me about the transition process in New Jersey today. I should add that not for one second do I expect that anyone is going to agree with everything I've said, if indeed anyone agrees with me about anything at all. What I hope to do is to provoke some thoughts about the transition process which could be vitally important to future transitions, as well as to the community associations in general.

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