

**The Florida Senate**  
**PROFESSIONAL STAFF ANALYSIS AND ECONOMIC IMPACT STATEMENT**

(This document is based on the provisions contained in the legislation as of the latest date listed below.)

Prepared By: Judiciary Committee

BILL: CS/SB 314

INTRODUCER: Judiciary Committee and Senator Geller

SUBJECT: Condominiums

DATE: March 29, 2007                      REVISED: \_\_\_\_\_

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	<u>Sumner</u>	<u>Imhof</u>	<u>RI</u>	<b>Favorable</b>
2.	<u>Daniell</u>	<u>Maclure</u>	<u>JU</u>	<b>Fav/CS</b>
3.	_____	_____	_____	_____
4.	_____	_____	_____	_____
5.	_____	_____	_____	_____
6.	_____	_____	_____	_____

**I. Summary:**

This bill substantially revises the provisions of Florida law governing the method and process of termination of a condominium. Many provisions are simply moved within the section with grammatical and editorial changes. Substantively, the bill amends s. 718.117, F.S., to:

- Provide legislative findings related to condominium terminations;
- Provide for approval of termination by less than 100 percent of owners and lienholders;
- Provide for a written plan of termination with written notice provided to all unit owners prior to being voted upon;
- Provide for quarterly reports prepared by the receiver, as well as procedures to replace the receiver;
- Provide alternative methods for determining the allocation of proceeds from the sale of condominium property;
- Set forth procedures for management of the association during termination and for distribution of the proceeds; and
- Provide for a right to contest the plan of termination and court review of the plan.

The provisions of this bill will apply to all condominium associations in existence as of July 1, 2007.

This bill substantially amends section 718.117, Florida Statutes.

## II. Present Situation:

Condominiums are creatures of statute, and are thereby subject to the control and regulation of the Legislature, which has broad discretion in its regulatory efforts, especially in fashioning remedies necessary to protect the interests of those persons involved.

Condominiums are established pursuant to the provisions of ch. 718, F.S., the “Condominium Act.” The basic instrument that creates a condominium is the declaration of condominium,<sup>1</sup> which must be recorded in the public records “of the county where the land is located, executed and acknowledged with the requirements for a deed.”<sup>2</sup> Condominiums are governed by boards of administration that adopt bylaws for administration of the association.<sup>3</sup>

### Termination of a Condominium Property

Unless the declaration provides otherwise, termination of a condominium requires the consent of all the unit owners and all the holders of the recorded liens affecting any of the condominium parcels.<sup>4</sup> Achieving such consent can be difficult. The board of directors must notify the Division of Land Sales, Condominiums, and Mobile Homes within the Department of Business and Professional Regulation (division) before taking any action to terminate or merge the condominium or the association.

Section 718.117(2), F.S., provides the duties and powers of the board of directors or court-appointed persons after the commencement of the termination. They have the power to:

- Employ directors, agents, and attorneys to liquidate or wind up its affairs;
- Continue the conduct of the affairs of the association insofar as necessary for the disposal or winding up thereof;
- Carry out contracts and collect, pay, compromise, and settle debts and claims for and against the association;
- Defend suits brought against the association;
- Sue in the name of the association, for all sums due or owing to the association or to recover any of its property;
- Perform any act necessary to maintain, repair, or demolish unsafe and uninhabitable structures, or other condominium property in compliance with applicable codes;
- Sell at public or private sale, exchange, convey, or otherwise dispose of all or any part of the assets of the association for an amount deemed in the best interest of the association, and to execute bills of sale and deeds of conveyance in the name of the association;
- Collect and receive any and all rents, profits, accounts receivable, income, maintenance fees, special assessments, and insurance proceeds for the association; and

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<sup>1</sup> Section 718.103(15), F.S., defines declaration of condominium to mean “the instrument or instruments by which a condominium is created, as they are from time to time amended.” A condominium is created upon the recording of the declaration in the public records. *See* s. 718.104(2), F.S.

<sup>2</sup> Section 718.104(2), F.S.

<sup>3</sup> *See* s. 718.103(4) and (6), F.S.

<sup>4</sup> Section 718.117(1), F.S.

- Make contracts and to do any and all things in the name of the association which may be proper or convenient for the purposes of winding up, selling, and liquidating the affairs of the association.<sup>5</sup>

Unless the declaration or bylaws provide otherwise, a vacancy on the board during the winding up proceeding shall be filled by a majority vote of the unit owners.<sup>6</sup>

In cases of natural disaster, s. 718.117(4), F.S., provides that if the identity of the directors or their right to hold office is in doubt, or if they are dead or unable to act, or refuse or fail to act, or their whereabouts cannot be ascertained, any interested person may petition the circuit court to determine the identity of the directors or appoint a receiver.

Section 718.117(5), F.S., provides that after determining that all known debts and liabilities of an association in the process of winding up have been paid or adequately provided for, the board, or other person or persons appointed by the court, shall distribute all the remaining assets.

Assets that are held under a valid condition must be disposed of pursuant to that condition. The remaining assets are to be distributed through the provisions in the declaration or bylaws.<sup>7</sup> If the declaration or bylaws do not provide for distribution, then the property “is owned by the unit owners in the same shares as each owner previously owned in the common elements. All liens shall be transferred to the share in the condominium property attributable to the unit originally encumbered by the lien in its same priority.”<sup>8</sup>

Section 718.117(8), F.S., provides that the distribution “may be made either in money or in property or securities and either in installments from time to time or as a whole, if this can be done fairly and ratably and in conformity with the declaration and shall be made as soon as reasonably consistent with the beneficial liquidation of the assets.”

An association that has been terminated nevertheless continues to exist for the purpose of winding up its affairs, prosecuting and defending actions by or against it, collecting and discharging its obligations, disposing of and conveying its property, and collecting and dividing its assets.<sup>9</sup>

### **Challenges to Condominium Termination**

According to the Condominium and Planned Development Committee of the Real Property, Probate, and Trust Law Section of the Florida Bar (RPPTL), obtaining 100-percent agreement of all unit owners in order to terminate a condominium has proven to be an impossibility in many cases. A representative of the section stated that, as condominiums have aged, become obsolete, or suffered serious hurricane or other casualty damage, it has become apparent that the current statute is an impediment to terminating a condominium. Missing or intransigent owners or unresponsive mortgagees can veto termination through inaction.

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<sup>5</sup> Section 718.117(2)(a)-(i), F.S.

<sup>6</sup> Section 718.117(3), F.S.

<sup>7</sup> Section 718.117(6), F.S.

<sup>8</sup> Section 718.117(7), F.S.

<sup>9</sup> Section 718.117(9), F.S.

A subcommittee of the Condominium and Planned Development Committee began working on revising the provisions of s. 718.117, F.S., in February 2003. Its recommendations were reviewed by the Condominium and Planned Development Committee and then the full Executive Council of the RPPTL Section in November 2004. In November 2005 the initiative was approved by the section as a legislative position pursuant to the Rules Regulating the Florida Bar.<sup>10</sup> The Advisory Council on Condominiums<sup>11</sup> approved the bill, which was passed as SB 1556 in the 2006 session but was vetoed by the Governor.

The Governor stated that SB 1556 may cause unintended consequences by possibly denying condominium unit owners of their rights to remain in their units without adequate procedural safeguards.<sup>12</sup> While the Governor agreed that there is a need to modify the law on condominium terminations due to natural disasters, he stated that the bill, as proposed, may be too overreaching.<sup>13</sup>

The Governor enumerated the following concerns with SB 1556:

- (1) The ability for optional termination on any basis, “if 80 percent of the total voting interests fail to approve the plan of termination but fewer than 20 percent of the total voting interests vote to disapprove.” This may allow for optional termination by a small fraction of the total voting interests.
- (2) The possibility of allowing one owner (such as a developer) to purchase 80 percent of the units in a condominium and seek termination, with the ultimate goal of redevelopment, in the absence of economic waste or impossibility. The Governor suggested that a possible remedy would be to require one vote per person, regardless of the number of units owned.
- (3) There are minimal procedural safeguards for the objecting unit owners, limiting the right to contest to apportionment of the proceeds and creating a presumption that the valuation and apportionment are fair and reasonable.
- (4) The bill allows a termination plan to be modified by a judge after the fact, which could prejudice the majority owners by permitting the court to apportion a greater amount of the proceeds to the holdouts. The Governor stated that, moreover, there is no provision in the bill for the majority to retract its votes if the court-modified termination plan is unacceptable.
- (5) Service of process by publication limits the ability of absentee owners who live in other states or countries to receive notice. The Governor stated that the bill should

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<sup>10</sup> R. REGULATING FLA. BAR 2-7.5.

<sup>11</sup> In 2004, the Advisory Council on Condominiums was created, in part, to receive public input regarding issues of concern with respect to condominiums and recommendations for changes in the condominium law. See s. 718.50151, F.S., which provides for the composition and functions of the council.

<sup>12</sup> Correspondence from Governor Jeb Bush to Secretary of State Sue Cobb, June 7, 2006 (on file with the Senate Committee on Judiciary).

<sup>13</sup> *Id.*

provide for actual notice or, at a minimum, impose a requirement for due diligence in contacting title owners before noticing by publication.

- (6) The bill shifts the cost of contesting the apportionment to the objecting owner, who may have to hire appraisers and who will be required to pay the attorney's fees of the prevailing party if the contest is denied. The Governor stated that many residents of older condominiums that are likely to be terminated under the new law are persons on fixed incomes who can ill-afford the cost of challenging the termination or finding a new place to live.
- (7) The retroactive application of the bill to all existing condominiums will have a diminishing effect on the owners' existing rights. The Governor stated that retroactive application should only apply to condominium terminations that relate to hurricane-damaged facilities.<sup>14</sup>

The Governor directed the Division of Land Sales, Condominiums, and Mobile Homes within the Department of Business and Professional Regulation (division) to conduct a series of town hall meetings in areas throughout the state that are heavily populated with condominium owners to discuss the bill, including the concerns expressed in the veto message. The division's findings were to be provided to the State's Condominium Ombudsman for review and comment. The division was also required to provide a report to the Governor, the President of the Senate, and the Speaker of the House, including the comments of the Ombudsman, no later than October 1, 2006.<sup>15</sup>

The division conducted eight public meetings and issued its report.<sup>16</sup> The report included the following recommendations:

- The Legislature should not permit optional termination under the terms of SB 1556.<sup>17</sup> Moreover, optional insurance, if applied at all, should not apply retroactively.
- The presumption of reasonableness should be removed from the proposed legislation, and the unit owners should be given the right to contest *any* aspect of a plan of termination;
- Personal service or service via certified mail to the last known address or emergency contact address should be included in the proposed legislation;
- The proposed legislation should be revised to require the judge to apportion costs and fees in an equitable manner, taking into account the merits of the case, the financial status of the parties, the outcome of the case, and other factors deemed relevant;
- The Legislature should amend the Condominium Act to allow termination-for-cause based on changes in land use regulation or substantial destruction of the property as provided in the bill.

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<sup>14</sup> *Id.*

<sup>15</sup> *Id.*

<sup>16</sup> See [http://www.myflorida.com/dbpr/lsc/condominiums/information/sb1556\\_report.pdf](http://www.myflorida.com/dbpr/lsc/condominiums/information/sb1556_report.pdf).

<sup>17</sup> The terms provided in SB 1556 were (a) when 80 percent of the voting interests approve the termination or (b) when less than 20 percent of the total voting interests vote against it. See [http://www.myflorida.com/dbpr/lsc/condominiums/information/sb1556\\_report.pdf](http://www.myflorida.com/dbpr/lsc/condominiums/information/sb1556_report.pdf).

This bill has attempted to incorporate some of the division's recommendations.

### **III. Effect of Proposed Changes:**

This bill substantially revises s. 718.117, F.S., the statute governing the termination of the condominium form of ownership of a property.

According to the Legislative Counsel for the Real Property, Probate, and Trust Law Section of the Florida Bar (RPPTL), the bill has two primary purposes:

1. The first objective is to provide an equitable method of termination following a natural disaster or in other circumstances that fully values the interests of each unit, as well as the common elements. (Currently, the law does not contemplate valuation of the units, and places unit owners in a position of not being able to receive the market value of their investments).
2. The second objective is to eliminate the ability of an owner or a small minority of owners from extracting an excessive portion of the termination proceeds at the expense of the other unit owners in the community. (Currently, the law allows one or more owners to withhold approval to obtain additional money and does not provide a remedy for other owners to challenge the conduct).

### **Legislative Findings**

This bill provides that it is the public policy of the state to provide a method to preserve the value of condominium owners' property interests, and that it goes against public policy to require continued operation of a condominium when to do so would constitute economic waste or the ability to do so is made impossible by law.

The bill provides that s. 718.117, F.S., applies all condominiums in this state in existence on or after July 1, 2007.

### **Termination of a Condominium**

The bill provides that where the continued operation of the condominium would constitute economic waste or would be impossible, the necessary vote for termination is the lesser of the lowest percentage of voting interests needed to amend the declaration. In general, amendment of a declaration of condominium requires a two-thirds vote of the membership, unless otherwise provided for in the declaration.<sup>18</sup> The criteria for economic waste or impossibility are:

- The total estimated cost of repairs necessary to restore the improvements to their former condition or bring them into compliance with applicable laws or regulations exceeds the combined fair market value of all units in the condominium after completion of the repairs; or
- It becomes impossible to operate or reconstruct a condominium in its prior physical configuration because of land-use laws or regulations.

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<sup>18</sup> Section 718.110(1)(a), F.S.

The bill further provides that, regardless of whether continued operation would constitute economic waste or would be impossible, the condominium may be terminated if approved by at least 80 percent of the total voting interests of the condominium, provided that not more than 10 percent of the total voting interests of the condominium have rejected the plan of termination by negative vote or by providing written objections thereto. The declaration can provide for a lower threshold.<sup>19</sup>

However, if 75 percent or more of the condominium units are timeshare units, the condominium may only be terminated by a plan of termination that is approved by 80 percent of the total voting interests of the association and the holders of 80 percent of the original principal amount of outstanding recorded mortgage liens of timeshare estates in the condominium, unless the declaration provides for a lower voting percentage.

The bill also provides that a plan of termination is not an amendment subject to s. 718.110(4), F.S., which relates to amendments that may change the configuration or size of any unit in any material fashion, materially alter or modify the appurtenances to the unit, or change the proportion or percentage by which the unit owner shares the common expenses of the condominium and owns the common surplus of the condominium. Such amendments essentially require, like a termination under current law, unanimous approval of the owners and lienholders.

### **Mortgage Lienholders**

The bill provides that, notwithstanding any provision to the contrary in the declaration or chapter 718, F.S., approval of a plan of termination is not required by the mortgage lienholder, if the lienholder is to be paid in full from the termination proceeds. If the mortgage lienholder will not be paid in full and, accordingly, does not approve the plan of termination, the lienholder has 90 days to contest the plan.

At the time of sale, the lien shall be transferred to the proportionate share of the proceeds assigned to the condominium parcel in the plan of termination or as subsequently modified by the court.

### **Powers in Connection with Termination**

The bill provides that the association shall continue in existence following approval of the plan of termination, with all powers it had before approval of the plan. Notwithstanding any contrary provision in the declaration or bylaws, after approval of the plan, the board has certain powers in connection with termination, which powers are necessary to continue with the business and operation of the association.<sup>20</sup>

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<sup>19</sup> This optional termination procedure is prescribed in proposed s. 718.117(3), F.S.

<sup>20</sup> These powers are similar to the powers currently granted in s. 718.117(2), F.S.

## Natural Disasters and Receiverships

The bill provides a mechanism whereby the condominium can be placed into a receivership after a natural disaster.<sup>21</sup> Receivership<sup>22</sup> is basically a form of court supervision over the ongoing management and affairs of the association with the end result being termination of the condominium and distribution of the net proceeds to the parties entitled to such proceeds. Specifically, the bill provides that if, after a natural disaster, where the board of directors cannot be located, identified, or refuses to act, any interested person may petition the court to determine the identity of the directors or, if found to be in the best interests of the unit owners, to appoint a receiver to conclude the affairs of the association following notice to persons as directed by the court. Lienholders shall be given notice of the petition and shall have the right to propose persons for the consideration by the court as receiver.

The receiver shall have all the powers enumerated in s. 718.117(6), F.S., as provided for in this bill, as well as those powers given to the board by the condominium documents and any other powers that are necessary to conclude the affairs of the association and are set forth in the order of appointment.

This bill also adds a requirement for quarterly financial reporting following the approval of the plan of termination,<sup>23</sup> specifies that members of a termination board are subject to recall,<sup>24</sup> and provides that lenders representing 50 percent of the outstanding mortgage balances on the condominium units may petition the court for appointment of a termination trustee.

## Plan of Termination

The plan must be a written document executed by unit owners having the requisite percentage of voting interests to approve the plan and by the termination trustee. A copy of the proposed plan must be given to all unit owners.<sup>25</sup> A unit owner may agree to the plan by executing the plan or by consent to or joinder in the plan.<sup>26</sup> If approved by the required number of owners and lienholders, if required, the plan must be recorded in the public records. The plan is effective only upon recordation or at a later date specified in the plan.

A plan of termination must specify:

- The name, address, and powers of the termination trustee;
- A date after which the plan of termination is void if it has not been recorded;

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<sup>21</sup> Currently, s. 718.117(4), F.S., provides a similar mechanism.

<sup>22</sup> A receivership is defined as “[t]he position or function of being a receiver appointed by a court or under a statute.” A receiver is a “disinterested person appointed by a court, or by a corporation or other person, for the protection or collection of property that is the subject of diverse claims.” BLACK’S LAW DICTIONARY 1275 (7th ed. 1999).

<sup>23</sup> These reports shall provide the status and progress of the termination, costs and fees incurred, the date the termination is expected to be completed, and the current financial condition of the association, receivership, or trusteeship. Copies must be provided by regular mail to the unit owners and lienholders.

<sup>24</sup> Members may be removed with or without cause as provided in s. 718.112(2)(j), F.S.

<sup>25</sup> The plan must be given in the same manner as for notice of an annual meeting and at least 14 days prior to the meeting during which the plan will be voted upon, or it must be sent together with a consent document.

<sup>26</sup> Any written consent must be signed with the formality of a deed, i.e., two witnesses and a notary.

- The interests of the respective unit owners in the association property, common surplus, and other assets of the association, which will be the same as the respective interests of the unit owners in the common elements immediately before the termination, unless otherwise provided;
- The interests of the respective unit owners in any proceeds from the sale of the condominium property. The plan of termination may apportion those proceeds pursuant to any method prescribed in the Allocation of Proceeds section as described below. If the condominium property or real property owned by the association is to be sold following termination, the plan must provide for the sale and may establish any minimum sale terms; and
- Any interests of the respective unit owners in any insurance proceeds or condemnation proceeds that are not used for repair or reconstruction. Unless the declaration expressly addresses the distribution of insurance proceeds or condemnation proceeds, the plan of termination may apportion those proceeds pursuant to any of the methods prescribed in the Allocation of Proceeds section as described below.

The plan may provide that each unit owner retains the exclusive right of possession to the portion of the real estate that formerly constituted the unit, in which case the plan must specify the conditions of possession.

In the case of a conditional termination, the plan must specify the conditions for termination. A conditional plan will not vest title in the termination trustee until the plan and a certificate executed by the association with the formalities of a deed have been recorded that confirm the conditions in the conditional plan have been satisfied or waived by the requisite percentage of the voting interests.

### **Allocation of Proceeds of Sale of Condominium Property**

This bill substantially changes the provisions regarding distribution of the proceeds of sale. Unless the declaration expressly provides for the allocation of the proceeds of sale of condominium property, the plan must first apportion the proceeds between the aggregate value of all units and the value of the common elements, based on their respective fair-market values immediately before the termination. The market values are to be determined by one or more independent appraisers selected by the association or termination trustee. The value of the common elements is to be paid to the owners according to their proportionate share in the common elements, as in current law.

The portion of proceeds allocated to the units is apportioned among the individual units. The apportionment is deemed fair and reasonable if it is determined by any of the following methods:

- The respective values of the units based on the fair-market values of the units immediately before the termination;
- The respective values of the units based on the most recent market value of the units before the termination;
- The respective interests of the units in the common elements specified in the declaration immediately before the termination; or

- Any other method of apportionment agreed upon in the plan of termination.

Liens that encumber a unit are transferred to the proceeds of the sale of the condominium property and the proceeds of sale or other distribution of association property, common surplus, or other association assets attributable to such unit in their same priority.

### **Termination Trustee**

The association will serve as termination trustee unless another person is appointed in the plan of termination. If the association is unable, unwilling, or fails to act as trustee, any unit owner may petition the court to appoint a trustee. Upon the effective date of the termination plan, title to the condominium property vests in the trustee. Generally, the termination trustee will be vested with the powers given to the board.

If the association does not serve as the termination trustee, the trustee's powers are usually coextensive with those of the association. If the association is dissolved, the trustee will also have the powers necessary to conclude the affairs of the association.

If termination is optional or pursuant to economic waste or impossibility, the unit owners' rights and title vest in the termination trustee when the plan becomes effective (upon recordation or a later date specified in the plan). The unit owners then become the beneficiaries of the proceeds realized from the plan of termination.

The termination trustee may deal with the condominium property or any interest therein if the plan confers on the trustee the authority to protect, conserve, manage, sell, or dispose of the condominium property. The trustee may contract for the sale of real property.<sup>27</sup>

### **Notice**

The termination trustee must provide notice by certified mail, return receipt requested, to all unit owners and lienholders within 30 days of a plan being recorded. The notice tells the owner or lienor where to find the plan in the public records and informs the unit owner or lienor of the right to contest the fairness of the plan.

Within 90 days after the effective date of the plan, the trustee must provide to the Division of Florida Land Sales, Condominiums, and Mobile Homes of the Department of Business and Professional Regulation a certified copy of the recorded plan as well as certain recording information.

### **Right to Contest**

A unit owner or lienor may contest a plan by initiating a summary procedure, pursuant to s. 51.011, F.S.,<sup>28</sup> within 90 days after the date the plan is recorded. The right to contest is deemed waived if not done in this time period, thereby, barring a unit owner or lienor from asserting or

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<sup>27</sup> The contract is not binding, however, until the plan is approved by the unit owners and lienholders.

<sup>28</sup> This section provides for expedited trial procedures

prosecuting a claim against the association, termination trustee, any other unit owner, or any successor in interest to the condominium property.

In an action contesting a plan, the person contesting the plan has the burden of pleading and proving that the apportionment of the proceeds from the sale among the unit owners was not fair and reasonable. The apportionment of sale proceeds is presumed fair and reasonable if it was determined pursuant to the methods prescribed in this bill (see the discussion above regarding the allocation of property).

The plan is to be implemented if the judge finds it to be fair and reasonable. However, if the court determines that the plan is not fair and reasonable, the court may (i) void the plan or (ii) modify and approve the plan based on findings during the court proceedings. In such an action, the prevailing party may recover reasonable attorney's fees and costs.

### **Distribution**

Following termination, the condominium property, association property, common surplus, and other assets of the association are held by the termination trustee.

Not less than 30 days prior to the first distribution, the termination trustee must deliver by certified mail, return receipt requested, a notice of the estimated distribution to all unit owners, lienors of the condominium property, and lienors of each unit stating a good-faith estimate of the amount of the distributions to each class and the procedures and deadline for notifying the termination trustee of any objections to the amount. The deadline for objections must be at least 15 days after the date the notice was mailed.

If a unit owner or lienor files a timely objection with the termination trustee, the trustee does not have to distribute the funds and property allocated to the respective unit owner or lienor until the trustee has had a reasonable time to determine the validity of the adverse claim. In the alternative, the bill provides for an interpleader action.<sup>29</sup>

The proceeds of any sale of condominium property or association property and any remaining condominium or association property, common surplus, and other assets must be distributed in the following priority:

1. To pay the reasonable termination trustee's fees and costs and accounting fees and costs;
2. To lienholders of liens recorded prior to the recording of the declaration;
3. To purchase money lienholders on units to the extent necessary to satisfy their liens;
4. To lienholders of liens of the association which have been consented to;<sup>30</sup>
5. To creditors of the association, as their interests appear;

<sup>29</sup> An interpleader action is a "suit to determine a right to property held by a usu. disinterested third party (called a *stakeholder*) who is in doubt about ownership and who therefore deposits the property with the court to permit interested parties to litigate ownership. • Typically, a stakeholder initiates an interpleader both to determine who should receive the property and to avoid multiple liability." BLACK'S LAW DICTIONARY 823 (7th ed. 1999).

<sup>30</sup> Section 718.121(1), F.S., requires the unanimous consent of the unit owners before a lien is valid against the condominium as a whole.

6. To unit owners, the proceeds of any sale of condominium property subject to satisfaction of liens on each unit in their order of priority, in shares specified in the plan of termination, unless objected to by a unit owner or lienor;
7. To unit owners, the remaining condominium property, subject to satisfaction of liens on each unit in their order of priority, in shares specified in the plan of termination, unless objected to by a unit owner or lienor;
8. To unit owners, the proceeds of any sale of association property, the remaining association property, common surplus, and other assets of the association, subject to satisfaction of liens on each unit in their order of priority, in shares specified in the plan of termination, unless objected to by a unit owner or a lienor.

After determining that all known debts and liabilities of an association in the process of termination have been paid or adequately provided for, the termination trustee will distribute the remaining assets pursuant to the plan. If the termination is by court proceeding, any court-ordered time period for the presentation of claims shall be enforced.

Assets held by an association upon a valid condition, which has occurred or will occur, shall be distributed according to that condition. The remaining association assets will be distributed pursuant to the priority order above.

Distribution may be made in money, property, or securities and in installments or as a lump sum, if it can be done fairly and ratably and in conformity with the plan of termination. Distribution shall be made as soon as is reasonably consistent with the beneficial liquidation of the assets.

#### **Association Status and Creation of Another Condominium**

The termination of a condominium does not change the corporate status of the association that operated the condominium property, nor does it bar the creation of another condominium.

#### **Exclusion**

The provisions of this bill do not apply to the termination of a condominium incident to a merger of that condominium with one or more other condominiums.

#### **Effective date**

The act shall take effect July 1, 2007.

#### **IV. Constitutional Issues:**

##### **A. Municipality/County Mandates Restrictions:**

None.

##### **B. Public Records/Open Meetings Issues:**

None.

C. Trust Funds Restrictions:

None.

D. Other Constitutional Issues:

Condominium declarations are contracts. Because this bill will apply to all condominium associations in existence as of July 1, 2007, it has the effect of re-writing previously recorded declarations that have termination provisions or that implement the protections provided by s. 718.110(4), F.S., and therefore may be an unconstitutional impairment of obligation of contract, under Art. I, s. 10, Fla. Const. The constitution provides in relevant part, “No... law impairing the obligation of contracts shall be passed.” Article I, s. 10 of the United States Constitution provides in relevant part, “No state shall . . . pass any . . . law impairing the obligation of contracts.” These provisions empower the courts to strike laws that retroactively burden or alter contractual relations. “A statute contravenes the constitutional prohibition against impairment of contracts when it has the effect of rewriting antecedent contracts, that is, of changing the substantive rights of the parties to existing contracts.”<sup>31</sup>

In *Pomponio v. Claridge of Pompano Condominium, Inc.*, 378 So. 2d 774, 776 (Fla. 1979), the court stated that some degree of flexibility has developed over the last century in interpreting the contract clause in order to improve the harshness of the original rigid application used by the United States Supreme Court. The court set forth several factors in balancing whether a state law has in fact operated as a substantial impairment of a contractual relationship. The severity of the impairment measures the height of the hurdle the state legislation must clear.<sup>32</sup> The court stated that if there is minimal alteration of contractual obligations the inquiry can end at its first stage, while severe impairment will force a careful examination of the nature and purpose of the state legislation.<sup>33</sup> The factors to be considered are:

1. Whether the law was enacted to deal with a broad, generalized economic or social problem;
2. Whether the law operates in an area that was already subject to state regulation at the time the contract was entered into; and
3. Whether the effect on the contractual relationships is temporary or whether it is severe, permanent, immediate, and retroactive.<sup>34</sup>

The Florida Supreme Court in *United States Fidelity & Guaranty Co. v. Department of Insurance*, 453 So. 2d 1355 (Fla. 1984), also adopted the method used in *Pomponio*, which requires a “balancing of a person’s interest not to have his contracts impaired with the state’s interest in exercising its legitimate police power.”<sup>35</sup>

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<sup>31</sup> 10A Fla. Jur. 2d *Constitutional Law* s. 414 (2007). The term “impair” is defined as “to make worse; to diminish in quantity, value, excellence, or strength; or to lessen in power or weaken.” *Id.*

<sup>32</sup> *Pomponio*, 378 So. 2d at 779.

<sup>33</sup> *Id.*

<sup>34</sup> *Id.*

<sup>35</sup> *United States Fidelity & Guaranty Co.*, 453 So. 2d at 1360.

Adopting the method of analysis used by the U.S. Supreme Court, the court outlined the main factors to be considered in applying this balancing test:

- The threshold inquiry is “whether the state law has, in fact, operated as a substantial impairment of a contractual relationship.”<sup>36</sup> The severity of the impairment increases the level of scrutiny.
- In determining the extent of the impairment, the court should consider whether the industry the complaining party entered has been regulated in the past. This is a consideration because if the party was already subject to regulation at the time the contract was entered, then it is understood that it would be subject to further legislation upon the same topic.<sup>37</sup>
- If the state regulation constitutes a substantial impairment, the state needs a significant and legitimate public purpose behind the regulation.<sup>38</sup>
- Once the legitimate public purpose is identified, the next inquiry is whether the adjustment of the rights and responsibilities of the contracting parties are appropriate to the public purpose justifying the legislation.<sup>39</sup>

This bill addresses termination of a condominium and is therefore permanent and possibly retroactive in nature since it may modify existing contractual relationships between the owners of a condominium unit and the condominium association originally entered into in the declaration.<sup>40</sup> Thus, as to the threshold inquiry, at least on an as-applied-basis, the bill seems to operate as a substantial impairment of a contractual relationship.

Condominiums were created by statute and therefore the law operates in an area that is already subject to extensive regulation. In evaluating modifications of contractual rights in the relationship between condominium owners and their association, the Florida Supreme Court has stated, “It may be assumed that the parties made their contract with knowledge of the power of the State to change the remedy or method of enforcing the contract, which may be done by a State without impairing contract obligations.”<sup>41</sup> Because condominiums are highly regulated by current law, condominium owners and associations enter into contracts with the knowledge that new laws may be passed which could change some aspect of current contractual obligations.

The legislative purpose of the statute seems to indicate that the law was enacted to deal with broad economic problems by stating that the Legislature finds that it is contrary to the public policy of the state to require the continued operation of a condominium when

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<sup>36</sup> *Id.* (quoting *Allied Structural Steel Co., v. Spannaus*, 438 U.S. 234, 244 (1978)).

<sup>37</sup> *Id.* (internal citations omitted).

<sup>38</sup> *Id.*

<sup>39</sup> *Id.* at 1361.

<sup>40</sup> *See generally, Coastal Petroleum Co. v. Chiles*, 672 So. 2d 571, 572 (Fla. 1st DCA 1996) (the court found that a retroactive application of a statute to a preexisting lease impaired the obligations under the preexisting lease and, therefore, contravened article I, section 10 of the state constitution).

<sup>41</sup> *Palm Beach Mobile Homes, Inc. v. Strong*, 300 So. 2d 881, 887 (Fla. 1974) (quoting *Mahood v. Bessemer Properties, Inc.*, 18 So. 2d 775, 779-80 (Fla. 1944)).

to do so would constitute economic waste or when the ability to do so is made impossible by law or regulation. Moreover, the bill serves the public policy of the state by providing an equitable method of termination that fully values the interests of each unit, as well as the common elements. The bill also eliminates the ability of an owner, or a small minority of owners, from extracting an excessive portion of the termination proceeds at the expense of the other unit owners in the community, which is against public policy.

The last inquiry, whether the adjustment of the rights and responsibilities of the contracting parties are appropriate to the public purpose justifying the legislation, could be true for the “economic waste or impossibility” method of approving a plan of termination. Where there are situations involving economic waste or impossibility, the adjustments of the rights of condominium owners concerning approval of termination of the condominium form of ownership may seem reasonably related to the Legislature’s findings for this bill. However, the other methods for approving a plan of termination<sup>42</sup> may be considered unreasonable because in some circumstances they could be used for any reason to override the provisions of the declaration. Nevertheless, the adjustment of the rights and responsibilities of the contracting parties may be reasonable and appropriate because these other methods address deficiencies in the current law. As previously discussed, the current law, s. 718.117(7), F.S., places unit holders in the position of not being able to receive the market value of their investments and allowing one or more owners to withhold approval for the sale of the property<sup>43</sup> (after termination of the condominium) to obtain a disproportionate share of the proceeds.

## **V. Economic Impact and Fiscal Note:**

### **A. Tax/Fee Issues:**

None.

### **B. Private Sector Impact:**

According to the Department of Business and Professional Regulation (department), the bill allows for termination of a condominium with less than 100 percent of the voting interests’ approval. This would be most helpful in those situations where the condominium is uninhabitable, or laws and regulations prohibit reconstruction, and not all of the unit owners will agree to the termination.

The department also indicated that the bill may expand commercial freedom by permitting the termination of condominiums because of economic waste or impossibility that would not otherwise be terminated under the condominium’s declaration. This, in turn, allows for redevelopment of the land.

<sup>42</sup> For example, an optional termination plan or a plan for timeshare units.

<sup>43</sup> After termination of the condominium form of ownership, the current law, s. 718.117(7), F.S., provides that the property is owned by the unit owners in the same shares as each owner previously owned in the common elements, which is typically based on the square footage of the unit, not the market value. Because all of the property is owned as tenants in common after the termination of the condominium form of ownership, one or more owners could withhold approval for the sale of the property to extract a disproportionate share of the proceeds.

**C. Government Sector Impact:**

The bill appears to leave the termination procedures within the jurisdiction of the Division of Land Sales, Condominiums, and Mobile Homes (division) in compliance and arbitration cases. If the division receives complaints regarding the new termination procedures, it may be required to expend investigative resources for these purposes; however, the department has indicated that any fiscal impact should be accommodated within current resources.

**VI. Technical Deficiencies:**

None.

**VII. Related Issues:**

As mentioned earlier in the analysis, this bill is substantially the same as SB 1556, enacted during the Regular Session of 2006. The public voiced concerns with certain sections of the bill and the division's report to the Governor, President of the Senate, and Speaker of the House proposed recommendations.<sup>44</sup> The department noted its concern that some of the perceived problems from SB 1556 have not been addressed in this bill.

According to the department, the lack of a definition of "natural disaster" and "interested person" in s. 718.117(7), F.S., may cause some uncertainty in the operation of the provision. With respect to interested persons, the department states that if an association refuses to pay a contested bill after an unrelated hurricane affected the county, it is possible that the creditor will have standing to petition for termination. The department suggested that it may be that interested persons should be more closely tied to owners and mortgagees. The department also felt that there was a possible lack of clarity on when to apply the act because of a lack of a definition of "natural disaster."

The department also provides that s. 718.117(10)(e), F.S., of the bill, which addresses distribution of insurance proceeds, does not address the allocation of the insurance deductible. The department states that this will result in uncertainty in how associations should allocate the insurance proceeds where, for example, termination occurs after a natural disaster has caused damage exceeding the deductible. The bill requires that the insurance proceeds for the common elements be paid to the unit owners in the percentage of ownership in the common elements. However, the insurance proceeds for the units may be distributed based on the fair market value of the units. Therefore, the distribution to each unit owner would be different depending on how the deductible is allocated to the proceeds. The department states that this problem could be fixed by requiring that the deductible be allocated in some designated manner.

However, a representative of the Condominium and Planned Development Committee of the Real Property, Probate, and Trust Law Section of the Florida Bar did not express these concerns.

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This Senate Professional Staff Analysis does not reflect the intent or official position of the bill's introducer or the Florida Senate.

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<sup>44</sup> See "Present Situation" section of this analysis.

## **VIII. Summary of Amendments:**

None.

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