

**COOPERATIVES
AND
CONDOMINIUMS**

by Patrick E. Kehoe

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INTRODUCTION

Anyone who takes the time to look through the real estate section of a newspaper will quickly see that a rather significant number of the homes being offered for sale are not the traditional type of individually owned, free-standing dwellings surrounded by their own yards. Rather, he will see that many of the advertisements are for homes in condominium or cooperative developments. He will also find a wealth of articles about these two nontraditional types of home ownership. A careful examination of both the advertisements and the articles will show that condominiums and cooperatives involve the use of many types of housing construction such as traditional free-standing homes, town houses, and units in high-rise apartment buildings.

Real estate statistics point out that in the United States more than 50 percent of the newly constructed dwelling units that were sold during 1973 were condominiums. This increase in popularity is most surprising when one realizes that until a very few years ago most of us had not even heard the word "condominium," let alone had any concept of what it meant. Also, until recently most of us tended to think of a "cooperative" as being an infrequently used method of apartment ownership which was reserved either for the wealthy or for low-cost, government sponsored urban housing for the poor. Why then are condominiums and cooperatives so popular today?

Condominiums and cooperatives appeal primarily to two groups of potential home purchasers, which together make up more than 55 percent of our total population: the newly married or young home-buyers, and the so-called senior citizens who no longer have young children living with them. The former group is primarily attracted to the condominium because of its usual ease of financing and relative low cost in comparison to other comparable types of owner-occupied housing. The latter group appears attracted to both condominiums and cooperatives because of their resulting relaxed life style, which is relatively free of the time-consuming maintenance duties normally associated with home ownership. Either a condominium or a cooperative provides a situation having most of the advantages of living that one enjoys

in a rented apartment, while still retaining the psychological and financial attractions of real home ownership.

However, home ownership in any form, including condominiums and cooperatives, is not without certain legal consequences. The purpose of this Legal Almanac, therefore, will be to explain the meaning of these two concepts of ownership, and relate them to some of their legal advantages and disadvantages. The reader must, however, be aware from the beginning that the laws relating to both condominiums and cooperatives are still undergoing development and change in our country, and are by no means the same in every jurisdiction. Thus the author's discussion, which is based on general principles, should not serve as a substitute for competent legal counsel whenever one is seriously contemplating the purchase of either a condominium or a cooperative home.

Chapter 1

HOME OWNERSHIP - FEE SIMPLE, CONDOMINIUM, COOPERATIVE DISTINGUISHED

In order to understand home ownership, it is necessary first to understand the concept of land ownership. The basic system of land ownership, or title to real property, that we have in the United States originated in England about a thousand years ago. Under this system, the most secure form of land ownership that a private person can acquire is known as a fee simple or fee simple absolute title. When someone owns land in fee simple, his ownership is protected against the claims of all others except the state, which represents society acting as a whole. The process by which the state can take away an individual's fee simple ownership of land is referred to as "condemnation." Condemnation, or as it is sometimes called, the state's power of eminent domain, is based on the premise that all land started out as belonging to society as a whole, and was never fully given to individual owners. Thus, when society as a whole has a need for a particular piece of land, then that land must be surrendered to society by its owner. In the United States, as a part of the condemnation process, the state is required by the Constitution to compensate an ousted landowner for his loss.

Whenever one holds a fee simple title to land, he may create titles in or rights to the use of that land in others, either by conveying (transferring) the fee title or a portion of the fee title, as in the creation of an easement, or by the granting of a contractual right to another, such as is done when land is leased or mortgaged. The enforcement of a lease or the foreclosure of a mortgage, then is not the taking away of the fee title itself, but rather the enforcement of a contractual right against the owner of the fee title.

When a man rents a house or apartment from another he is in reality leasing the right to use or occupy that dwelling and the land upon which it stands from the individual or entity that owns the fee title to the land. Sometimes, the actual owner of the dwelling is himself merely a lessee of the owner of the fee title to the land and is, in reality, subletting his right to occupy that land to the person who rents and occupies the dwelling

unit. When the lease or leases expire, the right to use and occupy the land will automatically revert to the owner of the fee title.

In the traditional case of home ownership, the owner of a house is really the fee simple owner of the land upon which it stands, and his ownership and use of the structure is merely a part of the way in which he enjoys the use of his land. He has all the rights of any fee simple land owner. What rights then does the owner of a condominium or cooperative living unit have, and how do these rights differ from those of an ordinary homeowner?

The owner of a living unit in a condominium is in fact a fee simple owner of land, but one whose fee simple ownership is interrelated to fee simple ownerships of the other owners of units in the same condominium complex. This interrelationship involves contractual rights and obligations, which are established both by the law and by agreement among the various owners of the units, and which govern their use and enjoyment of their respective fee titles. This interrelated fee simple method of ownership, which typifies the condominium, perhaps can most clearly be explained by making reference to its use in a high-rise structure that houses a number of families. In such a structure, the use of a condominium format offers each owner an outright individual ownership of his own dwelling within the structure. It also offers him an undivided simultaneous ownership in common with all the other owners of dwellings in the condominium. This undivided ownership is of the land under the structure and all those parts of the structure that are necessary to support more than one unit, or are otherwise specifically designated as being for use by more than one owner. This usually means that the halls, elevators, stairways, roofs, basements, foundations, supporting walls, subfloors, and the like are owned in common by all the owners, as are the grounds around the structure and the land beneath it. The fee simple ownership is thus attached to the land, and the ownership of the individual living units and commonly owned portions of the structure are tied to the right of each fee owner to occupy and enjoy the use of his land. As does the fee simple owner of any piece of real estate, each unit owner in a condominium receives a deed certifying his land ownership.

Even when a condominium form of ownership involves low-rise structures, such as town houses and free-standing houses, the land upon which everything is built is owned jointly by all the unit owners. *Without this tie of common fee simple*

ownership of all the underlying land, there cannot be a condominium.

Unlike the traditional home owner or the owner of a condominium living unit, the occupant of a living unit in a cooperative, who is known as a "cooperator," does not have a fee simple ownership of land. In reality his unit is owned by the cooperative organization and the cooperator occupies it under a lease from the cooperative. What the cooperator actually does own is a portion of the cooperative organization itself. The cooperative organization also is ordinarily the fee simple owner of the land upon which its building stands, although in some situations the cooperative may lease the land and own the building, or even lease both the land and building. When the cooperative is itself a lessee, each cooperator is in effect a sublessee.

How then does the individual cooperator, along with his fellow cooperators, own the cooperative organization? This is usually accomplished by setting up the cooperative as a nonprofit corporation, in which case each cooperator is a shareholder. In a few situations, trusts or other forms of co-ownership are employed as the cooperative vehicle, but since their use is rare, no further discussion of them will be made herein.

In the corporate cooperative, each cooperator, solely by virtue of his ownership of stock, is automatically entitled to obtain a lease, called a proprietary lease, to a designated apartment or other dwelling, and to occupy and use that specified unit in return for the payment of a monthly or periodic payment, which is called a "maintenance charge." In many ways a cooperator is very much like any tenant instead of like an owner.

To recapitulate then, the owner of a unit in a condominium is very much like a traditional home owner, since each has a fee simple title to the land upon which his dwelling stands. On the other hand, the "owner" of a unit in a cooperative does not have a fee simple title to land or a resulting title to his individual dwelling. Rather he acquires his right to occupy his dwelling under a lease. He is, however, one of several owners of his "landlord," the cooperative organization, which may in turn be the fee simple owner of the land upon which the dwelling stands or the lessee of such land.

Chapter 2

HISTORICAL BACKGROUND OF CONDOMINIUM AND COOPERATIVE METHODS OF HOME OWNERSHIP

A system of ownership of parts of buildings by different persons, somewhat similar in basic concept to that of a modern condominium or cooperative, is thought by some experts to have existed in ancient Rome. There it is believed to have been used by wealthy home owners for several of the same purposes for which its modern counterparts are used today, such as providing, through the pooling of the financial resources of all the owners, certain luxuries that otherwise they would not have been able to afford.

During the Middle Ages, multiple ownership of buildings, in the form of ownership of floors or parts of houses by different persons, was common in some of the more crowded cities and towns in Europe. It is presumed that this multiple ownership came about due to an acute shortage of housing, with a resulting need to make very efficient use of that which was available. Later, however, the practice was discontinued and, in some countries, was even prohibited by law. The practice of multiple ownership of buildings is believed to have been abandoned in the late Middle Ages because of many disputes between owners, which arose due to a lack of clear-cut rules governing such routine matters as everyday maintenance and repair.

In modern times, provisions specifically authorizing the ownership of parts of single buildings by several individual owners have again been incorporated into the laws of many European countries. However, in order to prevent a repeat of the problems that led to the disputes of the Middle Ages, many of these laws are written so as to include very detailed instructions as to just how multiple ownership is to be achieved and carried out. Most current laws limit co-ownership to those portions of the complex that are used by the occupants of more than one unit, such as the underlying land, stairs, lobbies, hallways, and similar areas. Concurrently, these laws provide for individual ownership only of the respective living units themselves. In order to better insure that joint ownership ventures will be successful, European laws ordinarily also

provide that the individual owners' rights and obligations with respect to the other owners are to be spelled out and clearly regulated by agreements made at the time the multiple ownership first begins. Furthermore, the everyday running of all the common parts of the building and premises is to be done by a representative of all the individual co-owners. In these regards, our own condominium laws are similar to the modern European laws.

In England, from which we have taken our common law system, separate ownership of parts of a building has long been recognized as lawful. As early as 1508 for example, English court cases dealt with what they described as one house on top of another. In fact, multiple ownership of housing structures was fairly well established both in England and Scotland by the early eighteenth century, at which time the practice appears to have been based on the common law theory that several types of subordinate estates or interests in land could exist in the same fee simple title. Since the end of the Second World War, the use of various methods of multiple ownership, primarily condominiums, has grown greatly in England.

Surprisingly, the concept of individual ownership of parts of buildings did not really exist in the United States until a few years ago, probably because of the traditional abundance of land that was available here for individual homes. In those few instances where there was a need for the benefits afforded by multiple ownership of single buildings, such as during the period of the housing shortage which followed the First World War in some large cities, alternatives to individual ownership, such as the cooperative, were employed. During and following the 1930s however, even these schemes fell into disuse. The reason for this was the depression era failure of the vast majority of these projects, which was caused by the financial interdependence of their individual owners. As a result, since that time and until quite recently, ownership of the few cooperatives that did exist was limited either to the very wealthy who could afford to take the financial risks involved, or to the very poor whose interests were protected by government guarantees and assistance.

In the mid-1950s the need to provide for more efficient use of land in the United States, especially in the more crowded cities, became apparent. Experts determined that what was needed here was a method to permit individual ownership of portions of buildings, perhaps similar to those methods being

used in England and Europe. However, it was felt that in order to make this method of ownership attractive to potential owners, it would have to provide the same advantage of high-density housing that the cooperative provides without also providing the cooperative's inherent disadvantage of the financial interdependence of its owners.

Puerto Rico was the first American legal jurisdiction to provide the answer to this need when it enacted the Horizontal Property Act of 1958 and thereby specifically authorized the condominium.

Congress, in 1961, also recognized the need for more efficient use of urban land when it specifically authorized the Federal Housing Administration to insure mortgages on condominium living units, when their existence was lawful, and thereby greatly enhanced the attractiveness of this method of home ownership, not only for potential purchasers of homes, but also for those financial institutions that make home mortgage loans. This action on the part of Congress helped to open the floodgates, so to speak, to the enactment of condominium authorizing legislation in other American legal jurisdictions. By the end of 1963, thirty-nine states had passed such laws and in 1969, when Vermont finally did so, condominiums were legal in every jurisdiction.

Today, just a few short years after the condominium was first authorized as a means to permit the more efficient use of crowded urban land, its use has become widespread, not only for that purpose, but also as a means of providing housing in the uncrowded suburbs and even in some truly rural settings. At the same time, the popularity of the condominium has somehow brought about a rebirth in the use of the more traditional cooperative, which today appeals to a much wider group of potential home owners than it ever did in the past.

Chapter 3

METHODS OF HOME OWNERSHIP OR OCCUPANCY COMPARED

TRADITIONAL HOME OWNERSHIP

As has already been explained, legally speaking, what the individual or family has when it owns its own home in the traditional sense is a fee simple title to the land and a resulting ownership of everything on the land. This title is certified in a deed of ownership that is kept on file in the appropriate county land records office and, as such, is considered to be protected against the claims of any others who might come along.

When someone has a traditional title to his home he is pretty much free to do whatever he wishes with the home so as to maximize his enjoyment of it. Thus, even though he cannot violate local zoning, health, or safety laws, a traditional home owner is normally free to add a porch, garage, or room to the structure if he wishes or to erect a television antenna. He also is free to paint the house any color he pleases and to landscape his yard in whatever fashion he wishes. In other words, a traditional home owner can fix up his home to suit himself.

In some situations, such as in the so-called planned communities, traditional home owners may relinquish some of their freedoms, either by accepting deeds that contain certain restrictions in them or by entering into restrictive contracts with their neighbors. In return for accepting these restrictions, the home owner acquires the satisfaction and safety of knowing that, because there are similar restrictions on the actions of his neighbors, the value of his own property will be protected.

A traditional home owner also is in a position to take advantage of certain provisions in our various laws that are intended to promote home ownership. Often, for example, when the home owner first purchases his house he will need to borrow a portion of its purchase price. Since he is acquiring a fee simple title to his land and the resulting ownership of the house that is on it, he is in a position to use both the land and the house as security for the repayment of the loan. Taking advantage of this position is what is referred to as the "granting of a mortgage" on a home and, because of the high value of the security, the prospective

home owner is very likely to obtain his loan at a lower interest cost than otherwise would have been possible. In fact, if it were not for the security having been available in the first place, he might not even have been able to get the loan at all. This relative ease of obtaining mortgages on homes is possible because of special provisions in certain laws that govern mortgages.

Under our federal and state income tax laws, there are additional benefits for the home owner that are related to his mortgage. These laws provide that so long as the home owner is personally liable for the repayment of his mortgage loan, the amount of interest paid on it can be used as a deduction from his gross taxable income.

The traditional owner of a house has another potential advantage at income tax payment time: since he is also personally liable for any property or related taxes that might have been levied on his house and land, he can deduct these too from his gross taxable income.

One additional benefit of ownership that the traditional home owner has available to him should be mentioned. He can sell his property whenever and to whomever he pleases. Thus, before he sells, he need not first obtain the permission of anyone to do so, and should the house have increased in market value during the time that he owned it, he will, in all likelihood, realize a net profit from its sale.

RENTAL - THE LANDLORD - TENANT RELATIONSHIP

Of course not every American owns the housing unit in which he lives. Rather, many rent their living quarters from another who is the actual fee simple owner of the premises. In the ordinary rental situation the owner, who is called a landlord, receives payment of money, called rent, from the actual occupant of the premises, who is called the tenant. In return the landlord allocates a portion of his rights as fee simple owner to the tenant. In the ordinary rental agreement, a tenant will receive the right to occupy and quietly enjoy the use of the rented premises and the landlord will retain the other traditional owner's freedoms and duties. These include the right to choose whether to make any improvements to property, as well as the financial responsibility for its maintenance. The landlord also remains personally responsible for the payment of any property taxes that might be assessed against the premises. Therefore he and not the tenant, a portion of whose rent actually is used to pay these taxes,

is eligible for the special income tax deductions that were mentioned above. Similarly, though a portion of the tenant's rent goes to pay off any mortgage that the landlord may have on the premises, it is the landlord and not the tenant who is personally liable for payment of the mortgage. Again, the landlord is permitted by law to deduct that portion of the mortgage payments that are the interest on this debt.

Should the landlord, as fee simple owner, decide to sell his interest in the rented premises, he may do so, and in almost every situation the new owner will be required by the law to continue the rental agreement. This means that normally the only modification in the rental agreement that will result from the sale of the fee simple title will be a substitution of the new owner for the former owner as landlord. In a very few situations the law may permit the new owner to unilaterally continue, modify, or terminate the rental agreement. In order for him to have this right however, the new owner must have acquired his title without having had any knowledge of the fact that the premises was subject to a rental agreement. This requirement of a lack of knowledge is very difficult to establish because the mere occupancy and use of the premises by a tenant is almost always sufficient to impart such knowledge to any potential new owner.

In the event that the tenant suffers any financial loss due to the rental agreement's early modification or termination, after the sale of the premises to a new owner, his only legal remedy may be to file a lawsuit against his former landlord and claim damages on the grounds of a breach of the contract between them.

The tenant has no equity in the premises. Therefore, at the time of sale of the premises, only the landlord as fee simple owner, and not the tenant, will be entitled to the proceeds of the sale, including any profit that might be realized.

Today, however, when we speak of the various methods by which Americans can acquire their rights to occupy their homes, we must include not only traditional ownership and rental methods, but also two additional ones, condominium and cooperative. Both condominium and cooperative are hybrids that have been created by law to provide a type of actual ownership, and thus carry many of the same legal ramifications of traditional fee simple ownership. But, as hybrids, they are designed for a housing situation that involves the sharing of certain parts of the premises by more than one owner and thus also contain some of the legal ramifications generally associated with home rental. Condominium and cooperative forms of ownership are

distinct from the traditional fee simple form and also differ one from the other in many significant ways. Therefore, they will be described separately.

CONDOMINIUM OWNERSHIP

An owner of a condominium home, which can be an ordinary house, a town house, or an apartment in a large building, actually has a fee simple title to the underlying land. This is true even if his particular unit is many floors above the ground on which it rests. His fee simple title is granted to the condominium owner by law and like any land title is certified by a deed that is on file at the county land records office. The fee simple title that is involved in a condominium is different, however, in some respects from that which is found in the traditional land ownership situation. While the title includes a resulting individual ownership of the particular dwelling unit in question, as would any fee simple land title, it also includes an undivided joint ownership, along with all the other owners in the same condominium complex, in all the land that is part of the complex. This title also includes a resulting undivided joint title to all those areas and parts of the building or buildings that are intended to be used by more than one owner. Thus a condominium owner, while he acquires many of the same rights and privileges of any fee simple land owner, also acquires certain rights and obligations with respect to the other owners in the same condominium complex. These additional rights and obligations arise due to the very nature of condominium ownership and can be imposed either by law or by the particular condominium agreement in question.

As a fee simple land owner who uses his land as a home, the condominium home owner is in a legal position to take advantage of all those laws that are designed to foster home ownership by individuals. He can, for example, take advantage of homestead declaration laws, and thereby protect his home from certain types of claims by his creditors.

Perhaps, however, the greatest legal advantage that a condominium owner shares with a traditional home owner is that he is in the same legal position to grant a mortgage on his property. Therefore, he can use this device should he need to borrow money either for the initial purchase of his condominium home or for any other qualified reason. A mortgage on one unit in a condominium is simply that. It is completely independent of the titles and mortgages of the owners of the other units and can be enforced by foreclosure only against the one