

HUD, Congressional Action Needed to Stop Tide of Condo Lawsuits



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In the midst of an already depressed Florida residential real estate market, individuals who purchased condo units in good faith in recent years are now facing yet another threat to their property's value in the form of mushrooming litigation by some speculative pre-construction investors.

The rising tide of lawsuits, based on perceived loopholes in the four-decades-old Interstate Land Sales Full Disclosure Act and governing regulations issued by the U.S. Department of Housing and Urban Development, represents a serious problem for the residential real estate market, particularly in Florida, that needs to be quickly addressed by Congress and HUD.

ILSA was originally intended to protect unknowing home buyers from unscrupulous developers who were selling property on swampland or wasteland unsuitable for development. Passed in 1968, the legislation was never intended to apply to real estate developments in highly urbanized areas, such as the major metropolitan areas of South Florida today. At the time, ILSA made sense in its requirement that developers who market 100 or more residential units using a "common promotional plan" follow specific filing and contractual requirements, which include registering the property with the government and providing buyers with an extensive property report before the purchase agreement is signed.

The statute also laid out several exemptions that, while containing complicated wording subject to conflicting interpretations, nevertheless provided developers and home buyers with some flexibility for complying with otherwise time-consuming and costly ILSA requirements.

A prime example is the commonly used "two-year exemption," which encourages developers to complete and deliver a project within two years in order to be released from the ILSA requirements. HUD set forth regulatory guidelines that allow some leeway for nonperformance or delays caused by force majeure, which could include acts of God or other unforeseeable events that are effectively beyond the builder's control. These exceptions are particularly necessary for developers in Florida, who have to contend with unpredictable hurricanes and the labor and material shortages that follow.

Now that the condo market is in a slump, some purchasers are taking advantage of the ambiguously worded regulations to argue that because the contracts contained a force majeure clause, the developers were not specifically obligated to complete the project in less than two years and, therefore, were not exempt from ILSA. Based on this interpretation, the contracts would be subject to a section of ILSA stipulating that if a property report was required but not provided to the buyer before the purchase agreement was signed, the buyer has the option to revoke the contract.

The majority of buyers behind these lawsuits are speculative short-term investors, commonly referred to as "flippers," who purchased units in highly developed areas of Florida but are now worried they won't be able to resell the units or make as much of a profit as they had hoped. While buyers have the right to get what they contracted for, such claims have nothing to do with unsatisfactory workmanship, increased maintenance costs, construction defects or any other failure on the part of the builder. In these lawsuits, the two-year rule is being turned around and used unfairly against developers who in fact completed their projects on time and met all of

their contractual obligations with the expectation that the buyers would honor the contract as well.

Whether the lack of a property report alone is enough to revoke the contract will be left up to the courts to decide, and a lack of case law on the matter makes the outcome difficult to predict. However, if these lawsuits are successful, it will set a dangerous precedent for large numbers of buyers skipping out on their contracts every time the market takes a downward turn, despite being provided with the completed unit they originally purchased.

If speculators are allowed to take advantage of ILSA in order to get out of their contracts, it will discourage developers and lenders from doing business in Florida, and, more

importantly, it will make matters even worse for the majority of buyers who honor their contracts but will pay the price for living in half-empty condominiums.

While it may be too late to affect the pending lawsuits, Congress and Florida legislators in particular need to work together with HUD and take immediate action to close the loopholes in ILSA before the real estate market is dragged down even further, harming not only developers and lenders but the true consumers the law was originally designed to protect.

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