

Issues abound when struggling condo projects get taken over

As lenders end up with buildings from developers that defaulted on their loans, a host of concerns arises

With the mortgage market fallout, single-family home and condominium sales across the country are taking a hit. And Oregon is no exception.



**CONSTRUCTIVE
ADVICE**

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Large condo projects in Portland and elsewhere could soon be owned by lenders that financed the projects if the condo developers default on their loans. And successor developers could soon be buying projects from original developers that are financially unable to continue. So what do those new condo owners need to worry about?

The Oregon Condominium Act makes clear that a successor that's not affiliated with the original developer isn't liable for any misrepresentations or warranties made by the original developer, nor is it responsible for any breached fiduciary obligations by the first developer. Specifically, the new developer isn't liable for the statutory warranty the original developer must have offered to unit owners under the Oregon Condominium Act, even if the new developer is selling units that the original developer built. The new developer is, however, liable for the statutory warranty for any common elements or units that the new developer builds.

For common elements and units built by the original developer, the new developer can disclaim all express and implied warranties and covenants, including the Oregon statutory warranty and warranties provided by other sources, such as the Magnuson-Moss Warranty Act or the Uniform Commercial Code. The new developer can therefore sell the units "as is," subject only to the buyer's right to an inspection before purchase.

If the new developer knows of construction defects or other problems at the time of sale, it may have an obligation to disclose them to potential buyers. But disclosure obligations can be vague and difficult to pin down, and the extent of disclosure necessary is an often-litigated issue. Also, new developers can perform little or no investigation of potential problems and can further assume (perhaps wrongly) that problems that have been or will be fixed need not be disclosed.

As the owner of any unsold units, the new developer is jointly responsible for the condo association's common expenses

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(such as administration, maintenance and repair costs), under-funded assessments and inadequate reserves. The new developer should study these issues before takeover as part of its due diligence.

Another issue relates to unbuilt parcels that could in the future be annexed into the original condo. If an adjacent parcel isn't already annexed, the new developer may decide it's better to start a new condo rather than annex it, which can prevent existing condo problems from plaguing the new units. But before making this decision, the new developer should ensure that adequate easements exist for a separate condo and that utility services can be separated between the two projects.

If the original developer turns over the property to a lender or new developer, that original developer isn't relieved of any obligation or liability arising before the transfer, and it remains liable for warranty obligations imposed under the state Condominium Act. This may be little consolation to unit owners; if a new developer takes over, the original developer (often a single-project limited liability company) may have no substantial assets. For construction defects and certain other liabilities, the original developer's insurance policy may provide coverage, but an insurance remedy is usually not quick to come.

The original condo developers, their successors and unit owners should all be aware of these issues before they dive into a transaction. In addition to the provisions of the Oregon Condominium Act, a careful review of each project's declaration, bylaws and unit sales agreements, and the association's finances and record keeping, is warranted.

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