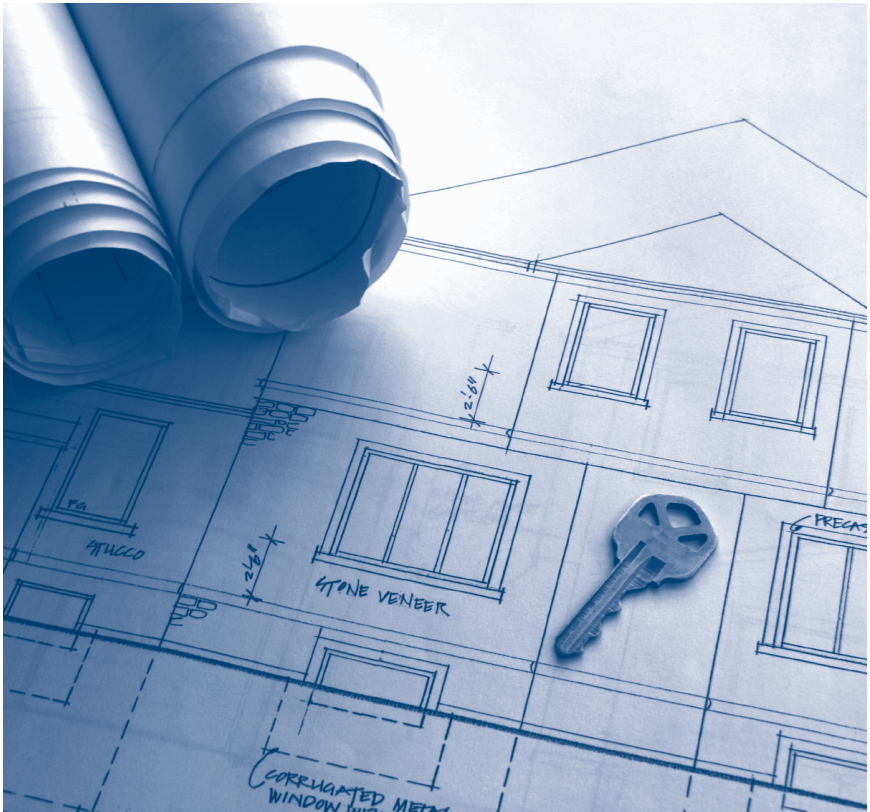


# DEVELOPER TURNOVER:

*Avoiding Pitfalls During  
the Transition Process*





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## A. Transition - What it is and is not.

Except for a few isolated instances, there is no legal distinction between the association's function under a developer-controlled board and under a unit owner-controlled board. The fiduciary responsibility of board members and the corresponding obligations and liabilities are basically the same regardless of who controls the board.

One exception is that after control has been turned over to the unit owners, the association has standing to maintain a representative action on behalf of the unit owners. Conversely, prior to transition, actions initiated by the unit owners would have to be brought as individual or class actions.

However, if during the period of developer control any provision of the Condominium Act or any rule promulgated thereunder is violated by the association, the developer is responsible for such violation and is subject to the administrative action provided in this Chapter. [See Florida Statutes §718.301(5)].

The transition process begins when the developer has conveyed 15% or more of the total number of units that will ultimately be operated by the association and continues until unit owners are in complete control of the association and its operation.

### **Transition is not:**

1. The act of transfer or acceptance of the common elements - that transfer takes place as each individual unit is closed.
2. The ratification of the actions of prior boards.
3. The waiver of unit owner rights.

## **B. Why would the Developer want to retain control of the Association?**

### **1. He who controls the purse strings controls the purse.**

A developer designated board has greater control over association expenditures and can preclude unnecessary capital projects from being bankrolled during the period of a developer “maintenance guarantee.”

- a. If the declaration so provides, a developer who owns condominium units or who has an obligation to pay condominium expenses may be excused from the payment of its share of the common expense which would have been assessed against those units during the period of time that it has guaranteed to each purchaser in the purchase contract, or by agreement between the developer and a majority of the unit owners other than the developer, that the assessment for common expenses of the condominium imposed upon the unit owners would not increase over a stated dollar amount and has obligated itself to pay any amount of common expenses incurred during that period and not produced by the assessments at the guaranteed level receivable from other unit owners. The guarantee may provide that after an initial stated period, the developer has an option or options to extend the guarantee for one or more additional stated periods. [F.S. §718.116(9)(a)(2)]
- b. However, as long as the developer is in control, the board may not impose an assessment for any year which is greater than 115% of the prior fiscal or calendar year’s assessment without approval of a majority of all the voting interests.
- c. During the first two years of control, the developer may vote to waive the statutory mandated reserves. After the first two years, reserves can only be waived or released upon the vote of a majority of all non-developer voting interests voting, in person or by proxy, at a duly called meeting of the association. [F.S. §718.112(2)(f)(2)]

## **2. Precludes Litigation Against the Developer**

Prior to transition, an association cannot maintain a representative action on behalf of the unit owners for construction defects.

### **Post Transition Options**

- a. Mandatory arbitration
- b. Prior approval of 75% of the unit owners.

## **3. Precludes Disruption of Sales Activities by Denial of Access to Common Areas and/or Sales Office**

Reservation of developer's right to use parts of common areas for sales and construction activities.

## **4. Preclude amendment of Condominium documents**

The Condominium Act affords the developer protection. [F.S. §718.301(3)]

If the Developer holds units for sale in the ordinary course of business, none of the following actions may be taken without approval in writing by the developer:

- a. Assessment of the developer as a unit owner for capital improvements.
- b. Any action by the association that would be detrimental to the sales of units by the developer. However, an increase in assessments for common expenses without discrimination against the developer shall not be deemed to be detrimental to sales of units.

The Developer is obligated to pay special assessments levied to fund litigation against the developer for warranty defects (See *Margate Village Condominium Ass'n, Inc. v. Wilfred*, 350 So. 2d 16 (Fla. 4th DCA 1977)).

## C. Timing of Transition

The developer can voluntarily effect transition whenever the developer desires, unless otherwise restricted by the Declaration of Condominium.

Transition begins to be mandated when unit owners other than the developer own 15% or more of the units that ultimately will be operated by the association. It is completed three years after 50% of the units that will be operated by the association have been conveyed, or three months after 90% of the units that will be operated by the association have been conveyed. [F.S. §718.301] The developer may provide in the documents for an earlier transition date, such as “on or before January 1, 20\_\_\_\_”.

Transition also will be triggered by the occurrence of certain other events, such as the following:

1. When all the units that will be operated ultimately by the association have been completed, some of them have been conveyed to purchasers, and none of the others are being offered for sale by the developer in the ordinary course of business. [F.S. §718.301 (1)(c)]
2. When some of the units have been conveyed to purchasers and none of the others are being constructed or offered for sale by the developer in the ordinary course of business. [F.S. §718.301 (1)(d)]
3. When the developer files a petition seeking protection in bankruptcy.
4. When a receiver for the developer is appointed by a Circuit Court and is not discharged within 30 days after such appointment.
5. Seven years after recordation of the declaration of condominium; or, in the case of an association which may ultimately operate more than one condominium, 7 years after recordation of the declaration for the first condominium it operates; or, in the case of an association operating a phase condominium created pursuant to Florida Statutes §718.403, 7 years after recordation of the declaration creating the initial phase, whichever occurs first. [F.S. §718.301 (1)(e)]

§718.301 (2) requires:

Within 75 days after the unit owners other than the developer are entitled to elect a member or members of the board of administration of an association, the association shall call, and give not less than 60 days' notice of, an election for the members of the board of administration. The election shall proceed as provided in F.S. §718.112(2)(d).

**Note:**

- a. The notice may be given by any unit owner if the association fails to do so.
- b. Once control is tendered, the unit owners must accept operational responsibilities. [F.S. §718.301(4)]

## D. Developers Obligations During Transition

### 1. Transition Audit

Financial records, including financial statements of the association and source documents since the incorporation of the association through the date of turnover, must be reviewed by an independent certified public accountant. The accountant performing the review examines supporting documents and records, including the cash disbursements and related paid invoices, to determine if expenditures were for association purposes, and reviews the billings, cash receipts, and related records to determine whether the developer was charged and paid the proper amounts of assessments. [F.S. 718.301 (4) (c)]

See Rule 61B-22.0062 - Transition Statements; Turnover Audit

- (1) Period covered. The audit required by F.S. §718.301 (4) (c) applies to all transfers of association control from developers to unit owners pursuant to F.S. §718.301 (4) occurring on or after April 1, 1992. The audit shall cover a period beginning with the date of incorporation of the association, or from the end of the fiscal period covered by the last audit if all fiscal periods have been audited, and ending with the date of the transfer of association control to unit owners other than the developer. Nothing herein precludes the developer from exceeding the requirements of this rule by engaging a certified public accountant to audit the entire period of developer control rather than from the period covered by the last audit.
- (2) Additional disclosure requirements for turnover audits. The financial statements, notes, or supplementary information shall present the revenues and expenses separately for each fiscal year and any interim periods included in the audit. The notes to the financial statements shall contain the following disclosures.
  - (a) A statement that the financial statements were prepared pursuant to F.S. §718.301 (4) (c)

- (b) A statement of total cash payments made by the developer to the association;
- (c) If the developer claims to have paid common expenses of the association which do not appear on the books and records of the association, the amount and purpose of each such expenditure shall be identified separately; and,
- (d) If a guarantee pursuant to F.S. §718.116(9) existed at any time during the period covered by the audit, the financial statements shall disclose the following:
  - 1. The period of time covered by the guarantee;
  - 2. The amount of common expenses incurred during the guarantee period;
  - 3. The amount of assessments charged to the non-developer unit owners during the guarantee period;
  - 4. The amount of the developer's payments pursuant to the guarantee; and
  - 5. Any financial obligation due to or from the developer resulting from the guarantee.

## **2. Association Records**

At the time of the transfer of control, the developer must deliver to the association, at the developer's expense, all property of the association, including, but not limited to, association funds, minute books, copies of the recorded declaration, the plans and specifications, insurance policies, and all warranties. [F.S. 718.301 (4)]

The developer is also required under F.S. §718.301 (4) (p), effective October 1, 2008, to provide a report, under seal of an architect or engineer authorized to practice in this state, attesting to required maintenance, useful life,

and replacement costs of the following applicable common elements comprising a turnover inspection report:

1. Roof.
2. Structure.
3. Fireproofing and fire protection systems.
4. Elevators.
5. Heating and cooling systems.
6. Plumbing.
7. Electrical systems.
8. Swimming pool or spa and equipment.
9. Seawalls.
10. Pavement and parking areas.
11. Drainage systems.
12. Painting.
13. Irrigation systems.

In essence, this report is a partial reserve study.

### **3. Warranties**

Following transition, prudent unit owner-controlled boards will engage a competent independent engineer to ascertain whether:

- a. The buildings and improvements are built in accordance with the building codes in effect at the time the building permits were issued.
- b. The buildings and improvements are built in accordance with approved plans and specifications.

- c. The buildings and improvements are built in a good and workmanlike manner.
- d. There are no design defects from the failure of a design professional to properly design, inspect, and supervise when there was a responsibility to do so.

A developer is deemed to have given a statutorily implied warranty of fitness and merchantability. The warranty is for a period of three years from the date of the building's certificate of occupancy (C.O.) or one year from transition, whichever is later, but not more than five (5) years.

The Statutes of Limitations do not begin to run until the date of transition. Accordingly, even if transition was to take place seven years after the condominium was C.O.'ed, the time frame for initiating a warranty action would not commence until the date of transition and would run for four (4) years. The plaintiff would have the burden of showing that the alleged defects arose during the warranty period.

Commencing May, 2003, the Florida Legislature adopted a statutory scheme requiring notice of opportunity to cure before a claim for construction defects can be filed in Court. This statutory scheme is known as Chapter 558 Florida Statutes. It requires the Association to give notice in reasonable detail of defects to potentially responsible parties and an opportunity to inspect and cure those defects. As applied to Associations having more than 20 units, a potentially responsible party has 50 days from receipt of a Notice of Claim to inspect the improvements and 75 days to respond to the Notice of Claim. A response can include a monetary offer to resolve the claim, an offer to do work to resolve the claim, a denial of the claim or a potentially responsible party may forward the claim on to its insurance carrier. There is no sanction if a potentially responsible party receiving a Notice of Claim fails to take any action in response to the claim. The service of the Notice of Claim and waiting 75 days for response (and denying an offer to settle if one is made) are prerequisites to filing a lawsuit.

## E. How well has the Developer laid the groundwork for a smooth transition?

Things that should be done by the Developer prior to transition:

1. From inception of the condominium, treat the association as a separate and unrelated entity:
  - a. Establish association bank accounts
  - b. Segregate reserve funds and/or capital start-up funds from operating revenues
  - c. Utilize developer employees, not association employees for sales and punch-lists.
  - d. Developer should pay assessments on developer owned units and/or short fall of guaranteed budget directly to the association. Never transfer unit owners' assessments to developer entity with developer entity then paying the bills. The association should pay its own obligations.
2. Engage independent management.
3. Engage independent legal counsel for the association.
4. Enforce the covenants and restrictions and the rules and regulations in a timely and uniform fashion.
5. Implement a uniform collection program, applied equally to non-developer and developer owned units.
6. Monitor and control activities of sales department
7. Prepare a realistic operating budget.
8. Tie warranties of contractors and sub-contractors into warranties afforded unit owners - run co-existent

9. Implement a claims avoidance program:
  - a. Preserve evidence
  - b. Address problems immediately upon notice
  - c. Follow the code and the approved plans and specifications - don't cut corners
  
10. Establish and Maintain Communications with the Unit Owners
  - a. Respond in a prompt and courteous fashion to individual punch list items
  - b. Publish newsletters
  - c. Hold open Board Meetings
  - d. Encourage unit owners to serve, when appropriate, on the board and/or committees
  - e. Sponsor social functions.

## F. Post-Transition Priorities

1. Make sure all books and records have been received (See attached checklist).
2. Employ a certified public accountant to review the financial activities of the Developer - controlled Board, and to work with the Board to establish sound practices for budgeting and recordkeeping.
3. Engage an engineer to prepare a comprehensive report on the physical condition of the property.
4. Review all contracts and determine whether any contracts entered into by the Developer - controlled Board should be cancelled as may be allowed by law.
5. Understand the requirements of law involved in the operation and administration of the Association affairs.

## DOCUMENT TURNOVER RECEIPT

### RECEIVED:

1. \_\_\_ The original or a photocopy of the recorded Declaration of Condominium and all amendments thereto. If a photocopy is provided, it shall be certified by affidavit of the developer, or an officer or agent of the developer, as being a complete copy of the actual recorded Declaration.
2. \_\_\_ A certified copy of the Association's Articles of Incorporation.
3. \_\_\_ A copy of the recorded By-Laws and all amendments thereto.
4. \_\_\_ The minute books, including all minutes, and other books and records of the Association, if any (which minutes shall be retained for a period of not less than 7 years).
5. \_\_\_ Any Rules and Regulations which have been promulgated.
6. \_\_\_ A current roster of all unit owners, their mailing addresses, unit identifications, voting certificates, and if known, telephone numbers; and voting proxies, which shall be maintained for a period of 1 year from the date of the meeting for which the proxy was given.
7. \_\_\_ All current insurance policies of the Association and the condominium operated by the Association.
8. \_\_\_ A current copy of any management agreement, lease (for common elements or any others), or other contract including but not limited to employment or service contracts, to which the Association is a party or under which the Association or the unit owners have an obligation or responsibility; directly or indirectly, to pay some or all of the fee or charge of the person or persons performing the service.

9. \_\_\_ Bills of sale or transfer for all property owned by the Association.
10. \_\_\_ All rental records where the Association is acting as agent for the rental of condominium units.
11. \_\_\_ Resignations of officers and members of the Board of Administration who are required to resign because the developer is required to relinquish control of the Association.
12. \_\_\_ A copy of the plans and specifications utilized in the construction or remodeling of improvements and the supplying of equipment to the condominium and in the construction and installation of all mechanical components serving the improvements and the site, with a certificate in affidavit form of the developer, his agent, or an architect or engineer authorized to practice in this state that such plans and specifications represent, to the best of their knowledge and belief, the actual plans and specifications utilized in the construction and improvement of the condominium property and for the construction and installation of the mechanical components serving the improvements.
13. \_\_\_ List of names and addresses of all contractors, sub-contractors and suppliers used in the construction.
14. \_\_\_ Copies of any Certificates of Occupancy which may have been issued for the condominium property.
15. \_\_\_ Any other permits issued by governmental bodies applicable to the condominium property in force or issued within 1 year prior to the date the unit owners other than the developer take control of the Association.
16. \_\_\_ All written warranties of the contractor, subcontractors, suppliers, and manufacturers, if any, that are still effective.

17. \_\_\_ Accounting records for the Association and the condominium, according to good accounting practices. All accounting records shall be maintained for a period of not less than 7 years. The accounting records shall include, but are not limited to:
- \_\_\_ a. Accurate, itemized and detailed records of all receipts and expenditures.
  - \_\_\_ b. Bank statements for all association accounts.
  - \_\_\_ c. A current account and a monthly, bimonthly or quarterly statement of the account for each unit designating the name of the unit owners, the due date and amount of each assessment, the amount paid upon the account, and the balance due.
  - \_\_\_ d. All audits, reviews, accounting statements and financial reports of the Association or condominium.
  - \_\_\_ e. All contracts for work to be performed. Bids for work to be performed shall also be considered official records and shall be maintained for a period of 1 year.
  - \_\_\_ f. An audit by an independent certified public accountant of the financial records, including financial statements of the Association, and source documents since the incorporation of the Association through the date of turnover. The minimum report required shall be an audit in accordance with generally accepted accounting standards as defined by rule by the Board of Accountancy. The accountant performing the audit shall examine to the extent necessary supporting documents and records, including the cash disbursements and related paid invoices to determine if expenditures were for Association purposes and the billings, cash receipts,

and related records to determine that the developer was charged and paid the proper amounts of assessments.

\_\_\_ g. A report included in the official records, under seal of an architect or engineer authorized to practice in this state, attesting to required maintenance, useful life, and replacement costs of the following applicable common elements comprising a turnover inspection report:

1. Roof.
2. Structure.
3. Fireproofing and fire protection systems.
4. Elevators.
5. Heating and cooling systems.
6. Plumbing.
7. Electrical systems.
8. Swimming pool or spa and equipment.
9. Seawalls.
10. Pavement and parking areas.
11. Drainage systems.
12. Painting.
13. Irrigation systems.

18. \_\_\_ Association funds or control thereof (checking accounts, certification of deposit, petty cash, etc.).

The foregoing items are acknowledged as received, but are not acknowledged as to their completeness or accuracy.

**ASSOCIATION** \_\_\_\_\_

By: \_\_\_\_\_

Print Name: \_\_\_\_\_

Title: \_\_\_\_\_

Date: \_\_\_\_\_

**DEVELOPER** \_\_\_\_\_

By: \_\_\_\_\_

Print Name: \_\_\_\_\_

Title: \_\_\_\_\_

Date: \_\_\_\_\_