



The Impact of Federal Regulations on the Development and Financing of Common Interest Ownership Developments

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Interstate Land Sales Full Disclosure Act

- 15 U.S.C. 1701 et seq., 24 CFR 1710
- ILSA has two primary purposes:
 - The prevention of fraud and misrepresentations
 - To prevent purchasers from fraud and misrepresentations; the Act requires developers to disclose information by requiring the registration of non-exempt subdivisions

Registration Requirements

- ILSA applies to the sale or lease of undeveloped, subdivided land if the developer, directly or indirectly, makes use of interstate commerce or of the mails, unless the sale or lease is exempt.
- A “Subdivision” is any land located in any State or in a foreign country that is divided or is proposed to be divided into lots, contiguous or not, for the purpose of sale or lease as part of a common promotional plan.

Common Promotional Plan

- Under ILSA, the term “subdivision” includes not only those lots that one developer may offer, but also those lots that are sold through a “common promotional plan.” 15 U.S.C. 1702(3).
- Under HUD’s Supplemental Information to Part 1710, a common promotional plan “is presumed to exist if land is offered by a developer or a group of developers acting in concert and the land is contiguous or is known, designated, or advertised as a common development or by a common name.”

Common Promotional Plan (cont'd)

- Characteristics considered when determining whether there is a common promotional plan:
 - 10% or greater common ownership
 - Same or similar name or identity
 - Common sales agents
 - Common sales facilities
 - Common advertising
 - Common inventory

Common Promotional Plan (Cont'd)

- Additionally, HUD's Guidelines state that the number of lots "covered by each individual offering has no bearing on whether or not there is a common promotional plan."
- Essential elements of a common promotional plan: (1) a thread of common ownership or (2) developers acting in concert.
- HUD's Guidelines also state that "if there is common ownership or if the developers are acting in concert, and there is common advertising, sales agents or sales office, a common promotional plan is presumed to exist."

Registration Requirements (cont'd)

- ILSA prohibits developers from selling any non-exempt lot unless:
 - A statement of record is in effect
 - A printed property report has been given to the purchaser before any contract have been signed
 - The statement of record and property report are true as to every material fact
 - The advertisements are consistent with the information in the property report

180 Day Free Look

- 24 CFR 1710.5 provides that a “presale clause conditioning the sale of a unit on a certain percentage of sales of other units is permissible if it is legally binding on the parties and is for a period not to exceed 180 days” if the sale involves a condominium or multi-unit construction.
- The 180-day provision is calculated from the date the first purchaser signs a sales contract in the project.
- Developers are allowed to enter into nonbinding reservation agreements without being forced to register.

Example of Free Look Language

- Example language: “Developer reserves the right to terminate this Contract by refunding the Deposit paid under this Contract within one hundred eighty (180) days after the date the first purchaser signed a contract to purchase a Unit in the Condominium if Developer does not pre-sell _____ percent (___%) of the total number of Units in the Condominium.”

Exemptions

- Developers are not required to file with HUD in order to be exempt from registration.
- 25 Lot Exemption: 15 U.S.C. 1702(a)(10) and 24 CFR 1710.5(a).
- 25 Lot Exemption applies to subdivisions containing less than 25 lots and exempts Developers from both the anti-fraud provisions and the registration requirements of ILSA.

Two-Year Buildout Exemption

- 15 U.S.C. 1702(a)(2) and 24 CFR 1710.5(b)
- Existing or Proposed Building Exemption (the “Two-Year Buildout Exemption”): if a lot contains an existing building or a developer obligates itself to erect a building within two years, the developer is exempt from both the anti-fraud provisions and registration requirements of ILSA.
- Most popular exemption.
- To qualify for this exemption, the developer’s obligation to perform must be absolute and the purchaser’s remedies must not be limited.
- Lenders are increasingly requiring developers to file HUD registrations in reaction to some developers not completing construction within two years.

Example of Two-Year Buildout Language

- **Example Language:**
- **In Completion Section:** “This Contract may be executed prior to construction of the Unit being substantially completed. In such case, the estimated date of completion of construction of the Unit and all promised improvements is set forth on page 1 of this Contract; provided that the Developer will complete construction of such accommodations or facilities within two (2) years from the date of this Contract barring only events beyond the control of the Developer such as acts of God, inability to obtain materials or utilities, strikes, other labor problems, governmental orders (including governmental regulations, actions or inaction), or any event constituting impossibility of performance for reasons beyond the Developer’s reasonable control. The following sentence will supersede and take precedence over anything else in this Contract which is in conflict with it. If any provision in this Contract serves to limit or qualify (a) Developer’s construction requirements set forth above; or (b) Purchaser’s remedies in the event that such obligation is breached, and such limitation or qualification is not permitted under the Interstate Land Sales Full Disclosure Act pursuant to 15 U.S.C. § 1702(a)(2) (and the regulations, appendices, and interpretive guidelines promulgated by the Department of Housing and Urban Development) then such provision is hereby stricken, made void, rendered unenforceable, ineffective, and made null and void as if never a part of this Contract.”
- **In Default Section:** “On the Developer’s default or breach of any term or condition of this Contract, Purchaser must give the Developer written notice of such default at the address set forth on page ___ and, if within thirty (30) days after receipt of such notice, the Developer fails to commence action that would cure the default within a reasonable period of time, Purchaser will have the right to seek all remedies available to Purchaser at law or equity, including, but not limited to, damages and the right of specific performance by the Developer. Notwithstanding anything in this paragraph to the contrary, in the event that Developer fails to complete construction within the time period set forth in Section ___ below, Purchaser shall have no obligation to provide written notice of such failure to Developer, and Purchaser will have the right to seek all remedies available to Purchaser at law or equity, including, but not limited to, damages and the right of specific performance by the Developer.”

Reservation Agreements

- Developers may take reservations in advance of entering into binding contracts without file a HUD registration.
- A reservation agreement must:
 - Be non-binding
 - Require deposits be placed in escrow with an independent escrow agent and be fully refundable at any time by the request of the purchaser
 - Not become a binding obligation without a subsequent affirmative action by the purchaser

100 Lot Exemption

- 15 U.S.C. 1702(b)(1) and 24 CFR 1710.6.
- 100 Lot Exemption: if a subdivision contains less than 100 lots, the developer is exempt from the registration requirements of the Act (but still is required to comply with the anti-fraud provisions of the Act).
- When determining the number of lots, the developer must count both sold and unsold lots.

Single-Family Residence Exemption

- Exemption requires that lot be subject to and comply with local minimum standards for lot dimensions, plat approval, recordation, roads and access, drainage, flooding, water supply and sewage disposal.
- At closing, each lot must be adjacent to a paved street that meets local standards or a bond must be completed to ensure completion of the roads.
- The HOA or local government must also take responsibility for the roads prior to closing.
- The lot must also have access to potable water, sanitary sewer disposal and electricity prior to closing (or a local government must be obligated to install such utilities to the lot within 180 days).

Single-Family Residence Exemption (cont'd)

- Purchaser must also receive a current title insurance binder or title opinion stating that, subject only to exceptions approved by the purchaser in writing, marketable title to the lot is vested in the developer.
- The Purchase Contract must also provide that warranty deed conveying title free from monetary liens and encumbrances must be delivered to the purchaser within 180 days from the date the purchase contract was signed.
- The developer must comply with the anti-fraud provisions of the Act.
- The purchaser must conduct an on-site inspection.
- **The developer may not provide promotional offers or gifts, trips, dinners or similar techniques to induce purchasers.**

Additional Exemptions

- **Twelve Lot Exemption:** A developer may sell up to 12 lots per 12 month period without filing a HUD registration. The 12 month period begins on the date of the first lot sale.
- **Twenty-acre Lots:** If each lot being sold contains at least 20 acres, the sales are exempt from registration with HUD.
- **Intrastate Exemption:** If lots are sold exclusively through an intrastate marketing plan conducted only in the situs state of the subdivision, the developer does not need to register with HUD provided that: (a) the lots are free and clear of all liens, encumbrances and adverse claims, (b) the purchaser conducts an on-site inspection, (c) the sale contract contains specific disclosures, and (d) and the purchaser executes a receipt of a good faith estimate of the cost of providing electric, sewer, water, gas and telephone services to the lot.

Combining Exemptions

- HUD has issued advisory opinions that allow developers to combine some exemptions.
- HUD has issued an advisory opinion that allowed a developer of a 170 unit subdivision to sell the first 99 units under the One Hundred Lot exemption and the remaining 71 units under the Two-Year Buildout exemption.
- Cannot piggyback exemptions with registration.

Administrative Penalties and Remedies

- The Secretary of HUD has authority to
 - (1) Suspend a statement of record if it appears to include any untrue statement of a material fact or omits any material fact
 - (2) Bring injunctive actions to enforce the Act
 - (3) Impose civil penalties whenever any person “knowingly and materially violates” the Act
 - (4) provide information to the Attorney General, who may then institute criminal proceedings

Private Civil Actions

- Purchasers or lessees may bring civil claims against developers for:
 - Selling nonexempt lots without an approved statement of record
 - Selling nonexempt lots without providing purchasers with a property report
 - Selling nonexempt lots with a record or property report that contains an untrue statement or omission of a material fact

Private civil actions (cont'd)

- Displaying or delivering promotional material or advertising that is inconsistent with the property report
- Employing any device, scheme or artifice to defraud
- Engaging in any practice that would operate as a fraud or deceit on the buyer
- Representing that roads, utilities, or amenities will be provided without including a covenant to do so in the purchase contract

Equal Credit Opportunity Act

- 15 U.S.C. Section 1691, 12 CFR 202
- Requires financial institutions and those who extend credit to make credit equally available to creditworthy customers.
- Prohibits discrimination against applicants based on race, color, religion, national origin, sex, marital status, age, or because all or part of the applicant's income derives from any public assistance program.

Impact on Hospitality and Common Interest Developments

- Due to the expensive nature of marketing, developers frequently attempt to focus their marketing activity on those consumers who they believe are most likely to purchase their product.
- Developers often compensate referral sources only for prospective purchasers who meet certain criteria.

Potential ECOA Violations

- ECOA violations have arisen in the following situations:
 - Marketing programs targeted towards certain age groups.
 - Interview scripts that discourage applications on a prohibited basis.
 - The use of any oral or written statements in advertising that would discourage members of a protected class from making or pursuing an application.

ECOA Overview

- Applies to both commercial and personal loans.
- Upon written request by applicant, creditor must *promptly* provide applicant with:
 - A copy of the appraisal report for loans that will be secured by a lien on residential real property
 - Creditor may require applicant to reimburse the creditor for the cost of the appraisal.

ECOA Overview (cont'd)

- The Act broadly defines “credit” and “credit transaction.”
- Regulation B makes it clear that a credit transaction includes all aspects of a borrower’s dealings with the creditor—not only the application and credit determination, but also advertising, pre-application information, and collection.

ECOA Regulations

- ECOA's coverage can begin even before any formal relationship between the creditor and the borrower.
- A potential borrower can become an applicant without actually making a formal application.
- The Official Staff Interpretation states that an inquiry becomes an application when the creditor "evaluates information about the application, decides to decline the request and communicates this to the applicant."

Factors Creditors May Take Into Account

- Lack of Citizenship (however, discrimination based on national origin is still prohibited!)
- Military Status
- Employment Status
- Income
- Criminal Record
- Age (in limited circumstances when evaluating an applicant's creditworthiness)

Gender and Marital Status

- Prohibition on gender discrimination protects both men and women
- Requires creditors to treat unmarried couples jointly applying for credit the same as married couples
- Prohibits creditors from requiring the signature of an applicant's spouse if the couple is not jointly applying

Notification Provisions

- Requires creditors to notify applicants within 30 days of action of the applicant's application
- If an adverse action has been taken, within 30 days the creditor must notify applicant in writing that applicant is entitled to request a statement of reasons for such action.
- Statement must be in writing and contain the specific reasons for the adverse action taken

Penalties Under ECOA

- The Act is generally enforced by the Federal Trade Commission (FTC)
- The FTC and Attorney General may enforce the Act by bringing a civil action
- Damages: (1) All actual damages suffered by aggrieved applicant, including for embarrassment, humiliation and mental stress; (2) Punitive damages not to exceed \$10,000 for individual claims or \$500,000 in a class action

Penalties Cont'd

- Courts may grant equitable and declaratory relief to enforce the Act
- Attorney's fees and costs are an available remedy to successful plaintiffs (attorney's fees are available even in cases where Creditor failed to comply with notice requirements; no requirement to prove a substantive violation)

Fair Credit Reporting Act

- 15 U.S.C. 1681 et seq., 16 CFR 600
- The Act requires consumer reporting agencies to adopt reasonable procedures for collecting financial information that also protect consumers' privacy and prevent improper use
- The purpose of the Act is to make credit reporting fair, accurate, confidential and relevant
- FCRA issues often arise in the granting of credit and insurance in the context of mortgage loans

The Consumer Report

- A “consumer report” is “any written, oral or other communication of any information by a consumer reporting agency bearing on a consumer’s credit worthiness, credit standing, character, general reputation, personal characteristics...”

FCRA Overview

- FCRA primarily regulates 3 groups:
 - (1) Consumer reporting agencies: entities involved in the collection and dissemination of financial information
 - (2) Furnishers: those who furnish consumer reporting agencies with consumers' financial information
 - (3) Users: entities who use information distributed by consumer reporting agencies

FCRA Overview (cont'd)

- The FCRA is very circular.
- To fall within the purview of the FCRA an entity must be a consumer reporting agency.
- Consumer reporting agencies provide consumer reports and consumer reports are provided by consumer reporting agencies.

Consumer Reporting Agencies

- Must ensure that consumer reports are accurate and contain no obsolete information
- Must provide copies of consumer reports free of charge
- Must limit the disclosure of medical information
- Must allow consumers to include notice of any dispute as to the accuracy of any information in their consumer report

When May a Reporting Agency Furnish a Consumer Report?

- A consumer reporting agency may furnish a consumer report to a person who (1) has a legitimate business need or (2) in connection with a business transaction (requires application for credit or express written consent).
- Consumer consent is required for employer access.
- The Act imposes liability on consumer reporting agencies for violations of the act but does not impose liability on those who use improperly obtained consumer reports.

Additional Consumer Rights

- Consumers have the right to know what is in their consumer report.
- Consumers have the right to dispute incomplete or inaccurate information.
- Consumer reporting agencies must remove incorrect information.
- The Act limits prescreened credit offers.

Furnishers

- Anyone furnishing information to a reporting agency must provide accurate information
- Anyone who regularly furnishes information to a reporting agency is required to promptly notify a reporting agency if they furnished inaccurate or incomplete information
- When a consumer disputes information, any information furnished to a reporting information must include notice that the accuracy of the information is disputed by the consumer.

Obligations of Users

- Users may only obtain a consumer report for certain permissible purposes.
- Users may not obtain a consumer report from a consumer reporting agency under false pretenses.
- Users must, when using a consumer report or third-party information to make adverse decisions about a consumer, give the consumer notice of either of where such information can be checked if provided by a consumer reporting agency, or that the consumer has the right to request that the user disclose the nature of the information if it was provided by a third party other than a consumer reporting agency.

Enforcement and Remedies

- FCRA allows for two types of civil actions: (1) willful noncompliance and (2) negligent noncompliance
 - (1) Willful noncompliance: any person who willfully fails to comply with FCRA is liable for (a) actual damages or damages of not less than \$100 and not more than \$1,000, (2) actual damages or \$1,000, whichever is greater, against a natural person who obtains a consumer report under false pretenses, (3) punitive damages, and (4) costs and reasonable attorney fees if the plaintiff is successful.

Enforcement and Remedies (cont'd)

- Negligent noncompliance: any person who is negligent in failing to comply with any requirement of FCRA is liable for (1) actual damages sustained by the consumer and (2) costs and attorney fees if the plaintiff is successful.

Enforcement and Remedies: Criminal Liability

- FCRA provides that “any person who knowingly and willfully obtains information on a consumer from a consumer reporting agency under false pretenses” or to “any officer or employee of a consumer reporting agency who knowingly and willfully provides information concerning an individual from the agency’s files to a person not authorized to receive that information” can be fined, imprisoned for no more than 2 years or both.



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