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**CONDOMINIUMS WITH SERVICES:
A GROWING TREND**

by

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Recently, there has been a notable rise in the level of interest in developing condominiums or other for-sale properties with significant services that cater to senior residents. Around the country, a wide variety of different equity retirement community prototypes has emerged. They can be structured as single-family homes or multi-occupancy buildings, high-rise or campus-style, condominium, cooperative, cond-op and other variations. Some have been licensed as continuing care retirement communities and may include assisted living and nursing facilities. Others are unlicensed and provide hospitality services only. In some, homeowners own and control all aspects of the property and its management. Others tie together separately-owned residential units and service facilities through deed covenants, easements, service contracts and/or club memberships. Some guarantee the availability of onsite services through a comprehensive service agreement; others have merely co-located service facilities and residences and made hospitality, home health, and other services and amenities available "as a convenience."

A related trend is the appearance of condominium hotels in many cities. In both cases, homeowners receive services, comprehensively managed by an independent third party, that formerly were available only in a leasehold environment.

Pros and Cons

A senior condominium (or cooperative) structure has a number of advantages when compared to entrance fee or rental arrangements:

1. Residents or their estates may recover their initial investments or enjoy appreciation upon resale, but there is no imputed interest problem as with a refundable entrance fee, and the right to resale proceeds is secured by the resident's interest in real property;
2. The tax advantages of home ownership are available to residents, including up to \$500,000 of tax-free capital gain on resale per couple, interest and property tax deductions, and a stepped-up tax basis when a spouse dies;
3. Consumers may be more familiar with and prefer homeownership;
4. Resident equity can be used by the service provider as security for the payment of service fees;
5. By retaining a repurchase option, the developer has the flexibility to offer condominiums either for sale or for lease, depending on customer preferences.

Among the drawbacks of an equity project are: (1) complexity of the documentation, (2) dealing with homeowner control issues, (3) the homeowner's risk of loss on resale, and (4) the stigma of construction defect or other lawsuits against condominium developers.

Since the late 1980s, when senior condominiums with services first appeared in the marketplace, many developers and operators have addressed these issues and achieved a level of success that once might not have been thought possible.

Controlling Service Delivery

Perhaps the greatest challenge in designing the business structure of a senior condominium with services is to secure control over the delivery of services. Homeowners' associations can be notoriously dysfunctional managers of real estate . . . a problem that is likely to be compounded by the addition of dining, housekeeping, transportation and/or health services. A worthwhile objective in structuring a service-enriched senior condominium is to offer all residents the advantages of home ownership while retaining the management structure of an entrance fee or rental community.

Condominium laws usually contemplate that the project will be managed by a homeowners' association. Such laws also contain restrictions against the developer awarding itself a long-term management contract when the developer controls the association's voting power and before a majority of the condominium units have been sold. One way to address the operational control issue is to physically separate Service Areas (such kitchen, dining, recreational and administrative areas, and care facilities) from the residential units, and to include only the residential units in the condominium regime. The Service Area can be a separate, but adjacent, real estate parcel, even if it is located in the same building as the condominiums. Deed covenants running with the land can require each owner to enter into a Service Agreement with the Service Area owner. Service contracts with individual owners, rather than with the association, may also be helpful in avoiding restrictions on management contracts created when the developer controls the association's voting power. Reciprocal easements running between the condominium and Service Area properties allow residents to use the Service Area to obtain benefits under the Service Agreement, and permit the service operator to enter the condominium property to deliver services such as housekeeping and building maintenance.

Transfer Fees

In order to duplicate the ongoing revenue stream created by resales of apartments at entrance fee properties, some condominium or cooperative community operators have established transfer fees. Transfer fees often consist of a fixed percentage of the original or resale price, and may include a percentage of appreciation in the unit upon resale (up to 75%). One rationale for the fixed component of the transfer fee is the operator's

maintenance of an ongoing marketing program. Shared appreciation creates an incentive for the manager to provide both quality and value in the operation and maintenance of the community, so that maximum possible appreciation in the value of residential units can be achieved on resale.

Litigation Stigma

Condominiums have a reputation for attracting plaintiffs' lawyers ready to pursue construction defect litigation. Traditionally, condominium developers have addressed this concern with alternative dispute resolution agreements and insurance. However, while there appears to be no empirical study on the subject, anecdotal evidence points to the conclusion that service-enriched communities, where the developer remains on hand after sell-out to manage and respond to homeowner concerns, have fewer problems that end in litigation.

Conclusion

Senior condominiums with services can be complicated and present challenges regarding the rights of homeowners and of the developer or its management company to operate the project. Since the late 1980's, several pioneering developments have sprung up, mostly on the East and West Coasts, and proven that these projects can be successful. Today, major national developers are pursuing development of the model. While equity retirement communities with services occupy a relatively small portion of the senior community marketplace, they definitely represent a fast-growing niches.

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