



## Foreclosing Lender Liability Covered in SB 1196

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Today's column continues our review of SB 1196, which becomes effective July 1, 2010. One change to the law created by SB 1196 involves the liability of a foreclosing lender for unpaid condominium assessments. For many years, the law has provided that a first mortgage is superior to the association's lien. However, when a first mortgagee takes title to a unit through foreclosure, the foreclosing lender is liable for six months of the unit's unpaid common expenses and regular periodic assessments which accrued or came due during the six months immediately preceding the lender's acquisition of title, or one percent of the original mortgage debt, whichever is the less.

Let us assume that Mr. Smith took out a \$250,000.00 mortgage to buy a \$300,000.00 condominium unit. The unit is now worth \$200,000.00, and Mr. Smith has stopped paying both his mortgage and condominium assessments. Let us further assume that the association's assessments are \$300.00 per month. When the lender forecloses on its mortgage and wipes out the association's lien, the lender would be liable to the association for \$1,800.00, six months of unpaid assessments.

SB 1196 amends the law by providing that the lender's liability is now increased to twelve months of unpaid assessments. However, the one percent cap was not changed. Using our same hypothetical

scenario, a foreclosing lender would now owe the association \$2,500.00, one percent of the original mortgage debt. Twelve months of unpaid assessments would be \$3,600.00, so the lender has the advantage of the one percent cap.

There are a number of questions that remain unanswered about this new law. For example, does the law only affect mortgages entered into after July 1, 2010, or does it affect existing mortgages as well? Another question is whether a condominium association whose documents incorporate the old six month mortgagee liability language needs to amend its documents to take advantage of the new law, it would seem at least prudent to do so.

There is also a significant question as to how the mortgage markets will react to this change in the law. Many banks that lend money to consumers for the purchase of real estate, including condominium units, do not hold on to the mortgage debt in their portfolio. Rather, many loans are sold on what is known as the "secondary mortgage market", which involves, among others, the Federal National Mortgage Association ("Fannie Mae") and the Federal Home Loan Mortgage Corporation ("Freddie Mac").

Section B4-2.1-06 of Fannie Mae's lending guidelines states that if a condominium or PUD

project (which would typically include a homeowners' association) is located in a jurisdiction that allows for more than six months of regular common expenses to have priority over Fannie Mae's lien, Fannie Mae will not purchase a mortgage loan secured by a unit in the project.

The law for homeowners' associations has contained a twelve month liability standard for several years, and I am not aware of that issue having impacted the availability of mortgages for single family homes. How the secondary mortgage market will react to Florida's change in the condominium law remains to be seen. Obviously, Florida is a major market for real estate and the related industries of lending money and the packaging and selling of mortgage loans.

A second significant change in the law made by SB 1196 applies equally to condominiums, cooperatives, and homeowners' associations. Each of the relevant statutes has been amended to state that if a unit or parcel is occupied by a tenant, and the unit/parcel owner is "delinquent in paying any monetary obligation due to the association", the Association may make a written demand "that the tenant pay the future monetary obligations" related to the unit or parcel directly to the association. An association can evict a tenant who does not comply.

There are several key points to keep in mind. First, the association may demand rent be paid over when the owner is delinquent in paying "any monetary obligation." Presumably, this would apply not only to regular assessments, but also special assessments, fines, and other charges which an owner might owe to the association.

One issue which is already being heavily debated is whether the statute's statement that the tenant

must "pay the future monetary obligations" related to the unit means only assessments and obligations that accrue after the association demands the rent, and not past-due obligations. Such a restrictive interpretation would certainly blunt the effectiveness of the new law.

Proponents of a broader interpretation of the law argue that the "future monetary obligations" related to the unit or parcel refer to the tenant's obligations, which is all the rent the tenant owes to the landlord/unit owner. It has also been argued that when a unit owner is delinquent in the payment of monetary obligations to the association, his or her "future monetary obligations" include all past-due amounts, since those sums are still due and owing, and are a continuing obligation. Also, the law provides that "any payment received by an association" must be applied first to any interest accrued by the association, then to any administrative late fee, then to any costs and reasonable attorney's fees incurred in collection, and then to delinquent assessments. Under this logic, since existing law requires that payments received by the association be applied to oldest debts first, and keeping in mind that statutes are supposed to be read in harmony with each other, one would argue that the association may justly demand receipt of all rents until the unit's account has brought current.

Since the law is not even effective yet, it is impossible to predict how all of these issues will play out.

Next week, we will shift gears and look at some significant operational changes required by SB 1196, including how official records are kept, new owner privacy laws, and the availability of personnel and payroll records of association employees.

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