CONDOMINIUM REGULATION: BEYOND DISCLOSURE

Inspired by President Kennedy's call "to provide decent housing for all of our people," Congress amended the National Housing Act in 1961 to allow for guaranteed mortgage insurance for the relatively untested condominium form of ownership in real property. It did so with the express purpose of "provid[ing] an additional means of increasing the supply of privately owned dwelling units," thus responding to the increasingly serious housing problems of the nation's middle- and lower-income citizens. In response to this federal imprimatur, most of the states subsequently approved enabling legislation providing the legal framework necessary to the development of these new and presumably low-cost projects. Unfortunately, many of the state statutes were patterned on the FHA model established on the federal level and were pushed through to legislative enactment with little reflection or independent analysis of the problems that were likely to occur. As a result, the enabling acts are often unclear in many important areas. Since condominiums were virtually unknown to the American legal community before the 1960's, many of the problems inherent in this new interest in real property were not even addressed by these statutes. Consequently, many developers have succeeded in manipulating and abusing the spirit, if not the letter, of the laws to the detriment of individual purchasers.

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2 In relevant part, the present text reads:
   The Secretary is authorized, in his discretion and under such terms and conditions as he may prescribe . . . to insure any mortgage covering a one-family unit in a multifamily project and an undivided interest in the common areas and facilities which serve the project . . . .
3 Id. § 1715y(a).
6 U.S. Federal Housing Admin., Dep't of Housing & Urban Development, Model Statute for Creation of Apartment Ownership (Form 3285, 1962).
7 See, e.g., notes 151-54 infra & accompanying text.
8 See notes 21-33 infra & accompanying text.
As a result of such developer abuses, demands for renewed legislative intervention have frequently arisen from an aggrieved consumer public. Although this public outcry has increased substantially in recent years, it has never been particularly well focused or articulated.\(^9\) Despite this lack of concentrated public pressure for reform, the great numbers of complaints have had their impact. Regrettably, this confused clamor for industry supervision has been mirrored in the legislative and administrative regulatory responses. The result: a peculiar melange of haphazard, unrelated regulation which has, until recently, failed to offer substantial protection against the special problems of condominium development and ownership.\(^10\)

This Comment will examine the numerous existing layers of public regulation as well as the recently proposed National Condominium Acts. Do any of the existing or proposed forms of regulation effectively speak to the special problems and abuses inherent in condominium ownership and development? Are these systems of control proper and meaningful expansions of the regulatory schemes? If not, what is an effective regulatory alternative?

I. THE PRESENT PATTERN: BACKGROUND

The condominium form of ownership developed in response to a highly concentrated and growing urban population within some of the European capitals.\(^11\) The concept of horizontal ownership has evolved to its present status, however, primarily in American land use patterns.

Common to all condominium forms and central to all modern enabling statutes is "the allowance and protection for exclusive ownership of airspace, with essential concomitants of common ownership."\(^12\) Even in the absence of specific condominium

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\(^9\) It was recently announced that a lobby group was being formed in Washington to attempt to focus attention on the consumer problems of condominium development and sale. See [2 Current] BNA Hous. & Dev. Rep. 169 (July 15, 1974). This group, which calls itself the National Association of Condominium Owners, might have an enormous impact if it can succeed in giving direction to the now amorphous special interests. For a similar example of organized consumer interests on the state level, see N.Y. Times, Apr. 21, 1974, § 8, at 1, col. 2.

\(^10\) In introducing S. 4047 on Sept. 26, 1974, Senator Proxmire recognized the risk of poorly focused, layered regulation:

If [regulation] is done in a piecemeal and patchwork fashion, then we will end up with a maze of differing and conflicting local standards which will cause more confusion and invite further abuses.


\(^12\) Id. 3.
enabling legislation, the common law provided the basic framework for individual ownership of apartment units. One could construct a fee interest in air space and also convey an undivided percentage interest as tenant-in-common in the structural parts and other facilities. However, the common law was unable to resolve two specific problems. Because a tenant-in-common could always require a partition of the jointly held property, any one tenant-in-common could, at his whim, bring the tenancy to an abrupt end and destroy the underlying legal structure. In addition, the common law was powerless to enforce any but the most minimal affirmative covenants providing for the maintenance and improvement of the commonly held elements.

Even assuming that these problems could be solved through a system of mutual covenants and restrictions which would be understood as running with the land and thereby enforceable, the real difficulty facing the common law was to develop a mechanism which would provide for the contingency of partial or total destruction of the building by fire or other natural disaster. Although there were, perhaps, existing means of drafting a scheme of covenants answering these problems as well, the extremely fragile construction of a common law condominium resulted in negative responses from real estate developers and lenders who were doubtful about the acceptability and continued viability of this unusual form of fee ownership.

Consequently, before any financing would be committed towards condominium development, builders, lenders, and title companies required specific legislative approval which would assure the safety of their investments. This approval came in 1961 with the enactment of section 234 of the National Housing Act and the subsequent state enabling acts.

Developers have poured money into condominiums in the last decade, but not in the anticipated manner. Instead of developing low-cost urban projects designed as primary residences for those who could not afford traditional forms of residency ownership, the surge of condominium development has been in the high-income market: as resorts (often combined with a rental pool arrangement for the periods not owner occupied), as second homes, and as primary residences in prestige locations.

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13 See Krasnowiecki, Townhouse Condominiums Compared to Conventional Subdivision with Home Association, 1 REAL ESTATE L.J. 323, 324 (1973).
15 Id. 604.
17 See notes 1-5 supra & accompanying text.
Perhaps this should not have been surprising in view of the tax incentives behind condominium ownership, which are of greatest advantage to high-bracket taxpayers. Perhaps developers and their creditors were reluctant to try marketing this new form of housing in any but the lowest risk markets. After a decade of financially successful marketing in the high-income area, condominiums today are widely predicted to become the single most widely developed form of fee ownership in densely populated urban areas. Thus, a gradual return to the original purpose of the enabling legislation may be approaching, with condominium developments aimed at satisfying the need for middle- and low-income primary residential housing. In light of this eventual transformation in the market, a fresh look at the experience under the established regulatory schemes is appropriate.

II. DEVELOPER ABUSES UNDER CURRENT REGULATION

The condominium developer can expose the purchaser to two general classes of risks: misleading or fraudulent advertising, and the more sophisticated arrangements that, although not misrepresentations, may still ensure exorbitant returns to the developer at the expense of the purchaser. Generally speaking, both federal and state regulation has been aimed

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18 See, e.g., N.Y. Times, June 2, 1974, § 1, at 1, col. 5 ("People who once rented apartments or lived in single-family detached homes are moving into condominiums at such a rapid rate that Federal officials expect half the population to live in them within 20 years."); id. Sept. 23, 1973, § 8, at 1, col. 5 (one expert "predicts that in 10 years the condominium will be the prevailing form of home ownership throughout the United States.").

19 A favorite deceptive sales device, for example, is for the developer grossly to underestimate monthly maintenance and recreation charges. He can put his own money in at first (so that the charges per owner appear lower than they will after the developer has departed), fail to include items in the initial charges that will have to be included later, or simply neglect to explain that the monthly charges will (legitimately) increase. Cf. N.Y. Times, June 2, 1974, § 1, at 1, col. 5-6; id. Feb. 14, 1971, § 8, at 6, col. 6-7.

The remarks made by Senator Proxmire when he and Senator Brooke introduced S. 4047 are also informative:

Open the real estate pages of any metropolitan area newspaper and you will be bombarded with advertisements that promise your dreams will come true when you buy your own condominium. Prospective buyers are told that they will have all the advantages of homeownership, without the headaches of maintenance and repair. They are lured with visions of swimming pools and tennis courts—country club living at apartment prices.

But too often bright promises fade in the face of sad realities, and the condominium owner finds himself faced with unanticipated problems and unexpected expenses.

The monthly condominium fee charged for maintaining common areas
at the first risk, requiring “full disclosure” of all terms prior to sale. But it is the second class of risks, those that may be disclosed but whose significance is only recognized by the sophisticated analyst, that have resulted in more serious consequences to the condominium purchaser. For those subject to such risks, current federal and state regulation offers little in the way of protection or remedy.

Five examples of this second class of risk will be briefly presented for purposes of illustration. They are the use of deposits, sweetheart leases, management contracts, extended control, and liability for shares of unsold unit expenses. Each of these practices may be technically lawful under the “full disclosure” regulation now applied by the federal and most state governments. So long as the terms of sale permitting such abuses are disclosed, the purchaser has little recourse against the unscrupulous developer for the abuses.

Many developers must secure a minimum number of pre-construction subscriptions before a lender will commit itself to financing the project. This external pressure may lead to hasty sales programs which describe, through colorful and enticing literature, the future appearance of what, at that point, is most likely a totally unimproved or only partially excavated parcel of land. Deposits are collected from the subscribed purchasers. Most of the state statutes make no provision for the use or ultimate disposition of the deposit receipts, which are, at this early stage, high risk money. There is often no direct or indirect

and other building expenses doubles or triples, because the developer understated the expenses in the promotional material.

The swimming pool he thought he had bought along with the house turns out to belong instead to the developer, who rents it out to the condominium owners at an exorbitant fee.

The project’s owners are locked into a long-term contract with a management company, often one in which the developer has an interest, so they are not free to select the management and negotiate the rates.


20 See text accompanying notes 34–111 infra.


22 However, a few states have attempted to remedy this particular abusive practice by requiring escrow accounts for such prepayments. See Fla. Stat. Ann. § 711.25(1) (Supp. 1974), amended & redesignated, Fla. Stat. Ann. § 711.67 by Fla. Laws 1974, ch. 74-104, § 13 (Supp. Fla. Session Law Service No. 2, 1974). This control is limited, though, and the funds may be used by the developer so long as he is willing to clearly disclose his intentions to the purchaser in 20-point type. Id. § 711.67(3).

Hawaii also provides for the protection of deposit money. The statute demands that “[a]ll moneys paid by purchasers prior to issuance of final reports shall be deposited in trust under escrow arrangement . . . .” Hawaii Rev. Laws § 514-40 (1968).
prohibition against using the money to defray construction costs of that particular project or, in fact, of any other of the developer's projects. Purchasers generally acquire no lien or other priority against the property, and they may ultimately be left with nothing but a worthless general claim if the project fails and the developer becomes bankrupt. With respect to the safety of his deposits, the purchaser's lack of remedy creates a substantial risk factor in most investments in a condominium under construction. For this reason New York requires the developer to include a warning for depositors which reads, "If this offering is not consummated for any reason you may lose all or part of your investment."\footnote{24}

Another area of abuse is the so-called "sweetheart lease" agreement. Here the developer keeps title to the land and leases it to the condominium owners at exorbitant rates.\footnote{25} According to some courts, the developer owes no fiduciary duty to the purchaser to guarantee fairness in the terms of these rental arrangements.\footnote{26} A related practice is the "sweetheart" recreation lease, under which the developer conveys the unit in fee but retains title to certain of the recreational common facilities and leases them back to the development at inflated values and excessively long tenancies.\footnote{27} This developer self-dealing is accomplished prior to the sale of the first unit, when the sponsor is in complete control. During this time, there is no actual or implied

\footnote{23} But see State Sav. & Loan Ass'n v. Kauaiian Dev. Co., 50 Haw. 540, 445 P.2d 109 (1968). Here the Supreme Court of Hawaii concluded "that the overall objectives of the H.P.R.A. [Horizontal Property Regimes Act] will best be effectuated by recognizing the rights of purchasers under the contracts as superior to those of a subsequent mortgagee with knowledge of those interests." \textit{Id.} at 553, 445 P.2d at 119. However, no change was mandated in the junior position of purchasers with respect to mechanics' and materialmen's liens. \textit{Id.} at 560, 445 P.2d at 123.


\footnote{27} A recent New York Times article indicates that such developer abuses are one of the many about which consumers are complaining. The three basic targets of purchaser dissatisfaction are "shoddy construction, unfair increases in maintenance fees and builders who exercise unexpected control over key facilities for long periods of time." N.Y. Times, June 2, 1974, § 1, at 1, col. 5, 6. Florida's Attorney General has recently claimed that the long term recreation leases that a major condominium development firm included in two of its largest projects violated state antitrust laws. [2 Current] BNA Hous. & Dev. REP. 409 (Sept. 9, 1974).
duty to future purchasers. Thus, for the most part, developers may profiteer without legal restraint.

Developers have also been able, under most state statutes, to enter into lengthy management contracts with the condominium association, which they control, at inflated rates of compensation. Here also, the courts have been unwilling to interfere with the agreements. The courts have consistently failed to imply any quasi-fiduciary relationship between seller and buyer.

Condominium documents are often drafted so that control effectively remains with the developer for longer periods of time than the state statutes had envisioned. For example, although


Although the concept of "abusive profits" is not specifically defined in the cases, the Internal Revenue Service has determined that eight percent of the cost of recreation land and improvements is a "reasonable rate of return" for rental income from recreation leases. Returns above that rate are considered excessive, and all excesses are given special tax consequences. See text accompanying notes 87-91 infra.

In response to the court's unwillingness to cast a developer in the role of a fiduciary with respect to future purchasers, the Florida legislature originally amended its condominium statute to provide for cancellation of management or maintenance contracts "at any time subsequent to the time any individual unit owners assume control of their association by vote of no less than 75 percent of said individual unit owners." Fla. STAT. ANN. §§ 711.13(4), 711.30 (Supp. 1974-75), repealed. Fla. Laws 1974, ch. 74-104, §§ 8, 14 (Supp. Fla. Session Law Service No. 2, 1974). This provision has been substantially altered in the new Florida amendments, Fla. STAT. ANN. § 711.66(5), Fla. Laws 1974, ch. 74-104, § 16 (Supp. Fla. Session Law Service No. 2, 1974). The impact of this cancellation provision will be examined in more detail. See notes 151-54 infra & accompanying text. For a discussion of the recent changes in the Florida statute, see text accompanying notes 155-175 infra.

The recently enacted Virginia Condominium Act, VA. CODE ANN. §§ 55-79.39 to 79.103 (Supp. 1974), has dealt with the problem of extended control more directly. By implicitly recognizing the lack of clarity in most state statutes with respect to the vesting of control, the Virginia act specifically allows the condominium documents to enable the developer to maintain extended control over the owners' association. This control, however, must cease "after units to which three fourths of the undivided interests in the common elements appertain have been conveyed." Furthermore, "[t]he time limit initially set by the condominium instruments shall not exceed five years in the case of an expandable condominium, three years in the case of a condominium containing any convertible land, or two years in the case of any other condominium." Id. § 55-79.74. These specific limitations have attempted to balance the conflicting interests of both parties.

The Virginia act also provides that no management contract, recreation lease, or any other contract or lease which was entered into while the developer maintained control of the association shall bind the unit owners after the expiration of the period of control unless specifically renewed or ratified by the unit owners. Id. For more discussion of the Virginia act, see notes 126, 178 infra & accompanying text.
most state statutes tie voting rights in the association to the percentage interest in common elements, they do not expressly require that these rights vest immediately. Many developers will include a provision in the master plan or by-laws which prevents exercise of the franchise for a period of five years or until the last unit is sold. During this time, the developer may act in his own self interest.

Finally, developers might refuse to pay their allocable share of monthly assessments as “owners” of the unsold “units.” The condominium documents will limit the description of a unit to a narrow, technically defined concept rather than to the broader definition suggested by the underlying statutes. A “unit,” for example, may not exist for purposes of paying monthly assessments until a certificate of occupancy is issued—an event which will not occur, according to the documents, until after sale and settlement.

III. REGULATORY RESPONSES

A. State

For the most part, the states have not amended their originally inadequate enabling statutes. In those states that have not yet drafted any additional statutory controls, legislative reluctance to interfere with a freemarket philosophy as well as an implicit dedication to the common law doctrine of caveat emptor appear to be the only justifications for inaction.

A handful of states have begun to impose schemes of industry regulation in response to many of the previously described abusive practices. New York construes a condominium as a cooperative interest in realty within the scope of and regulated

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31 See, e.g., Pa. Stat. Ann. tit. 68, § 700.312 (1971). This section requires only that at any meeting of unit owners, votes be in the same percentage as the percentage interest the owner maintains in the common elements. These “meetings” of unit owners, however, will often not occur, according to many associations' by-laws, for a long period of time.

32 See text accompanying notes 151-54 infra.

33 Since most state statutes define a unit as a part of the property intended for individual ownership and use, a unit would exist, in the absence of any provision to the contrary, as soon as the original property is subdivided and brought under the condominium plan. See text accompanying notes 103-05 infra.

34 See N.Y. Times, June 16, 1974, § 1, at 1, col. 4 (“In all but a handful of states, consumers caught up in the booming condominium market can expect little protection against deception or fraud under the real estate laws.”).

35 For a discussion of the doctrine of caveat emptor and the inroads made by implied warranty and related theories in the area of real property transfers, see 6 R. Powell, Real Property ¶ 938.2-3, at 370.29-48 (1971). See also Note, Regulating the Subdivided Land Market, 81 Harv. L. Rev. 1528, 1531 (1968).
In order to sell a condominium unit in the state, a developer must first register an offering statement which requires a fairly detailed list of facts to be fully and fairly disclosed to any potential purchaser. Although it is clear that some of the information required under the New York securities laws can be of value to the purchaser of a condominium unit, much of the information contained in an offering statement is of

36 The New York Condominium Act specifically provides that "[a]ll units of a property which shall be submitted to the provisions of this article shall be deemed to be cooperative interests in realty within the meaning of section three hundred fifty-two-e of the general business law." N.Y. REAL PROP. LAW § 339-ee (McKinney Supp. 1974-75). Consequently, the New York Blue Sky laws control the sale of condominiums existing within its boundaries or offered to one of its citizens. New York therefore will assert jurisdiction over "securities constituted of participation interests or investments in real estate . . . when such securities consist primarily of . . . investments in one or more real estate ventures, including cooperative interests in realty . . . ." N.Y. GEN. BUS. LAW § 352-e 1.(a) (McKinney Supp. 1974).

37 The specific requirements of the New York statute are, in relevant part, a full disclosure of:

The detailed terms of the transaction; a description of the property, the nature of the interest, and how title thereto is to be held; the gross and net income for a reasonable period preceding the offering where applicable and available; the current gross and net income where applicable and available; the basis, rate and method of computing depreciation; a description of major current leases; the essential terms of all mortgages; the names, addresses and business background of the principals involved, the nature of their fiduciary relationship and their financial relationship; past, present and future, to the property offered to the syndicate and to those who are to participate in its management; the interests and profits of the promoters, offerors, syndicate organizers, officers, directors, trustees or general partners, direct and indirect, in the promotion and management of the venture; all restrictions, if any, on transfer or participants' interests; a statement as to what stock or other security involved in the transaction, if any, is non-voting; a statement as to what disposition will be made of the funds received and of the transaction if not consummated, which statement shall represent that all moneys received from the sale of such securities until actually employed in connection with the consummation of the transaction as therein described, shall be kept in trust and that in the event insufficient funds are raised through the offering or otherwise to effectuate the purchase or purchases or other consummation of the contemplated transaction, or that the intended acquisition shall not be completed for any other reason or reasons, then such moneys, less such amounts actually employed in connection with the consummation of the transaction, shall be fully returned to the investor; which of the securities offered are unsecured; clearly distinguish between leasehold and fee ownership, between fact and opinion; a commitment to submit annual reports to all participants, including an annual balance sheet and profit and loss statement certified by an independent certified public accountant; clearly distinguish between those portions of promised distributions which are income and those which are a return of principal or capital; and such additional information as the attorney general may prescribe in rules and regulations promulgated under subdivision six hereof as will afford potential investors, purchasers and participants an adequate basis upon which to found their judgment and shall not omit any material fact or contain any untrue statement of a material fact.

N.Y. GEN. BUS. LAW § 352-e(1)(b) (McKinney 1968).
marginal use at best. While there are aspects of a condominium which are security-like, the inadequacy of an exclusively full disclosure approach to condominium regulation has been demonstrated by the abuses which have continued under it. Until 1974, Florida operated a similar full disclosure system which, while not a part of its Blue Sky laws, borrowed extensively from that regulatory philosophy. Before the sale or offer of any unit in the state, the developer was required to provide full information about certain enumerated subject areas. Thus, a Florida purchaser was armed with a full battery of highly technical papers and documents, and could sue for rescission or damages if he relied, to his disadvantage, upon any “material statement or information that is false or misleading, published by or under authority from the developer.” The fact that Florida has substantially changed its regulatory approach to include many substantive regulations suggests that state’s dissatisfaction with the previous disclosure approach.

Hawaii and Michigan have adopted somewhat different methods of regulation. In Hawaii, a developer must file a notification of intention to sell, complete a questionnaire, and provide for a full inspection of the property by the real estate commission. The commission will then issue a public report “which shall contain all material facts reasonably available.” In order to use a public report for selling purposes, a developer must also file a copy of a sample contract for sale and a copy of an escrow agreement for deposit money. A contract for sale made under a preliminary report is not enforceable against a purchaser until he has had a full opportunity to read the final report of the real estate commission. If the final report differs in any material respect from the preliminary report, the purchaser has the right to cancel his contract.

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38 It may be questionable, for example, how much practical use a potential unit owner would make of such required disclosures as “the basis, rate and methods of computing depreciation; . . . a statement as to what stock . . . is non-voting”, or “a commitment to submit annual reports to all participants . . .” Id.
39 See notes 67-68 infra & accompanying text.
40 See notes 19-33 supra & accompanying text.
42 Id. § 711.24(3).
43 See notes 155-75 infra & accompanying text.
46 Id. §§ 514-31 to -32 (1968).
48 Id. § 514-36 (1968).
49 Id. § 514-38
from Florida and New York by requiring, in addition to registration and public availability of development documents, that its real estate commission issue the report itself. However, there is no provision that the underlying project be fair and equitable. The developer must disclose but need not amend. Presumably, developers can continue to exploit unwary and unsophisticated purchasers so long as they do not misinform them as to material facts which are often buried within a mountain of incomprehensible legal documents.

Michigan too requires submission of relevant documents to its state commission which, after appropriate inspection and investigation, issues a permit to sell. This permit, however, is merely an assurance that the property conforms to its description. Thus, so long as the proposal is consistent with the master deed and other papers and "clearly and fairly represents the property offered for sale and will not tend to work a fraud or imposition on the purchasers or the public . . . ," the commission appears to have no authority to deny approval. In essence, this system seems to operate as a disclosure statute. There is no express duty that the developer offer just and equitable terms to the purchaser, nor is there power to require that preventative affirmative actions be taken on the developer's part before a permit may issue.

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50 For a closer examination of the impact and effect of full disclosure, see notes 139-54 infra & accompanying text.
51 Full disclosure will be effective in at least warning purchasers of the potential risks involved only if most condominium investors employ an attorney or other independent advisor experienced in interpreting such documents. This reliance on independent professional advice is normal in the pure securities field; but it cannot be assumed to be the rule in the real property area, particularly when low- and middle-income purchasers are involved.

A purchaser may have remedies available in some circumstances even when there is no statutory protection. Courts in several jurisdictions have been willing to find implied warranties in the sale of new and improved real estate where fraud in failure to disclose material facts has been shown, Carpenter v. Donohue, 154 Colo. 78, 388 P.2d 399 (1964); Bethlahmy v. Bechtel, 91 Idaho 55, 415 P.2d 698 (1966), or where negligence in construction is proved, Schipper v. Levitt & Sons, Inc., 44 N.J. 70, 207 A.2d 314 (1965).
53 Id. § 559.26 (1967).
55 However, it is not clear what additional effect may be read into the word "imposition" in § 559.26. Perhaps it could be argued that this requires the Michigan commission to scrutinize the project not only in order to ascertain accuracy of description, but also to assure fairness and equity. Cf. notes 56-57 infra & accompanying text. It is not insignificant that the section also seems to give standing to the "public." Accord-
California, in contrast, uses a permit regulatory system which allows an administrative body to deny the required permit to build for specific grounds including inability to deliver good title, inability to demonstrate adequate financing, failure to show that the parcels are fit for the use intended, and a showing that the sale would constitute misrepresentation, deceit, or fraud. An additional and more general criterion applies only to out of state developments sold or offered for sale within the state—a permit may be denied if the proposed sale is not "fair, just and equitable."

B. Federal

1. Securities Regulation

Attention on the federal level to condominium consumer protection issues has shifted over the years from the Federal Trade Commission and the Post Office Department to the Securities and Exchange Commission, the Federal Reserve Board, and to an extent even the Internal Revenue Service. In 1962, the FTC took jurisdiction over deceptive real estate sales practices accomplished through instruments of interstate commerce. However, it soon relinquished its limited control to the Post Office Department, which was responsible for regulating mail fraud. The FTC properly recognized that it was "functionally unsuited to deal with the problem." The Post Office, however,
could act only when the mails themselves were employed. As one commentator correctly noted, "a broader solution than mail fraud regulation [was] necessary." 61

Attention then shifted to the SEC, which, it was hoped, could provide more effective remedies. 62 The Securities Act of 1933 requires that every sale of a "security" must be registered under that Act, unless an exemption is available. 63 The term

rulemaking, see, e.g., Shapiro, The Choice of Rulemaking or Adjudication in the Development of Administrative Policy, 78 Harv. L. Rev. 921, 954-67 (1965), has been specifically overruled, National Petroleum Refiners Ass'n v. FTC, 482 F.2d 672 (D.C. Cir. 1973), cert. denied, 415 U.S. 951 (1974), the power that does exist allows the FTC merely to require complete accuracy of description. In the area of consumer protection, the FTC is only invested with the power to prohibit deception. See 15 U.S.C. § 45 (1970). In fact, the substantive regulation approved in Petroleum Refiners only allowed the Commission to require the posting of octane ratings on gasoline pumps. It was designed to assure full and fair disclosure of exactly what the consumer was purchasing. Full disclosure, however, may not be the most appropriate regulatory response to the problems of condominiums. See notes 139-54 infra & accompanying text.

61 Note, supra note 35, at 1537.


63 If it meets the investment contract test, see text accompanying note 66 infra, the Securities Act will cover practically any condominium offering. The traditional statutory exemptions—the small offering, 15 U.S.C. § 77c(b) (1970); the intrastate offer, id. § 77c(a)(11); and the private placement, id. § 77d(2)—offer little hope of escape. As a practical matter the intrastate and private placement exemptions are governed by SEC regulations. The intrastate exemption requires strict precautionary measures assuring that no security will be sold or offered to any non-resident. 17 C.F.R. § 230.147(c) (1974). With shotgun advertising techniques and the ease of interstate mobility, it is unlikely that any condominium developer will be able to satisfy the fairly rigid requirements. In addition, there are limitations on resale which would be wholly inconsistent with the concept of traditional home ownership. See id. § 230.147(e). Such limitations might also prove a powerful disincentive to banks, which run the risk of violating the Securities Act if they are forced to foreclose.

Rule 146, adopted on June 10, 1974, requires that any offeree in a private placement be provided with sufficient information to evaluate his investment properly. Furthermore, any offeree must have a high degree of sophistication in order to understand the merits and the risks. Lastly, there are an absolute limitation of 35 purchasers and a very strict resale provision. 1 CCH Fed. Sec. L. Rep. ¶ 5718B (1974). See 17 C.F.R. § 230.144 (1974) (resale of restricted securities). These strict limitations do not readily lend themselves to the sale of a form of residential housing.

Finally, a developer may avoid registration if the project qualifies under Regulation A, 17 C.F.R. § 230.251-263 (1974), although certain disclosure requirements still
"security" is defined broadly to include "investment contracts" or "certificates of interest or participation in any profit-sharing agreement," as well as stocks and bonds. The leading case on the scope of these terms, SEC v. W.J. Howey Co., adopted a definition of "investment contract" which is now widely accepted:

a contract, transaction or scheme whereby a person invests his money in a common enterprise and is led to expect profits solely from the efforts of the promoter or a third party, it being immaterial whether the shares in the enterprise are evidenced by formal certificates or by nominal interests in the physical assets employed in the enterprise.

Under this definition, it was not difficult for the SEC to conclude that an offering of resort condominiums together with a rental arrangement could constitute an "investment contract" and thus a "security." SEC jurisdiction, however, does not extend to the offer and sale of condominiums used primarily as residences. Since many condominium projects fall somewhere between the pure residence and the pure resort rental pool investment, the attempts to define the SEC's jurisdiction have produced uncertainty and confusion among developers. Under present SEC criteria, a condominium offering is within the agency's jurisdiction only if...
it involves an arrangement such as a rental pool, a required rental agreement, or a rental arrangement sold with emphasis on the economic benefits to be derived by the purchaser from the managerial efforts of others.\textsuperscript{70}

Many commentators have opposed SEC regulation of condominium sales on the grounds of legislative intent, the SEC's lack of real property expertise, and the unnecessary burdens imposed on developers.\textsuperscript{71} The industry has also failed to comply voluntarily with the SEC efforts to impose the entire regulatory structure of the Securities and Exchange Act of 1934 on these real estate projects.\textsuperscript{72} Developers and promoters offering condominiums with rental or "economic benefit" arrangements are required to register as securities broker-dealers under the Act,\textsuperscript{73} which entails net capital, reporting, and record-keeping rules and which requires salespersons to pass a largely irrelevant general securities examination.

Moreover, the Federal Reserve Board maintains that its regulation T,\textsuperscript{74} which regulates the extent to which a broker-dealer may arrange for the extension of credit for the purchase of securities, is applicable to the sale of condominium "securities." The impact of this regulation can be a severe one: if the SEC has jurisdiction over the condominium offering, it is unlawful for the developer to arrange a mortgage loan for the purchase of the unit if the developer-cum-securities broker-dealer participates in the offering. Although the FRB has traditionally exempted the sale of real estate contracts from the margin requirements applicable to the sale of other forms of securities, it has recently attempted to promulgate an amendment to the margin requirements reversing this position.\textsuperscript{75} Since a prospective condominium purchaser normally expects to give

\textsuperscript{70} Id. 1736. The SEC has also specifically exempted offerings of condominiums which include commercial space that is employed to generate income if:
(a) the income from such facilities is used only to offset common area expenses and (b) the operation of such facilities is incidental to the project as a whole and are not established as a primary income source for the individual owners of a condominium . . . unit.
Id. 1736.


\textsuperscript{72} By January 1973, only 42 offerings had been registered, despite some estimates that as many as 700 resort condominium projects which the SEC would consider subject to the Act had been offered. Wall St. J., Apr. 10, 1973, at 14, col. 4.


\textsuperscript{74} 12 C.F.R. §§ 220.1 et seq. (1974).

\textsuperscript{75} The proposed amendment reads, in relevant part: "Credit for the purpose of purchasing or carrying any part of an investment contract security (for example,
only a relatively small down payment and to finance the balance through a developer-arranged mortgage, this FRB proposal would have a drastic impact on the market.\textsuperscript{76}

In contrast to the attempts of the SEC to adopt clear limitations on its own jurisdiction, two Second Circuit decisions have suggested a much broader basis for interpreting condominium offers as securities. The opinions in \textit{Forman v. Community Services, Inc.}\textsuperscript{77} and \textit{1050 Tenants Corp. v. Jakobson}\textsuperscript{78} contain language which extends the "investment contract" theory of \textit{Howey} beyond its previous interpretation, presumably in the interests of greater consumer protection under the securities laws for purchasers of condominiums and cooperative apartments.

In \textit{Forman}, a group of residents of New York's enormous low- and middle-income Co-op City development brought suit against the developer for violations of the anti-fraud provisions of the federal securities laws. Their complaint alleged that monthly carrying charges had been understated and that other misleading statements and omissions had been contained in an information bulletin that was part of the sales literature. Because interests in cooperatives are generally evidenced by shares of stock, the court easily concluded that the cooperatives were subject to the securities laws.\textsuperscript{79} More significantly, the court held further that the cooperative interests were securities under the investment contract theory even where no stock certificates were issued.\textsuperscript{80} To support this holding, the court adopted a three-way test for whether the purchaser could expect to profit from his investment. First, the cooperative contemplated that the tenant shareholders would enjoy income generated by certain commercial establishments within the cooperative community. Second,


\textsuperscript{79} "[I]f a given instrument is a share of stock 'on its face' it is literally within the ambit of the statute," 500 F.2d at 1253. The court held that even where the transfer of stock certificates was involved, the introductory phrase to the definitional sections of the 1934 Act, "unless the context otherwise requires," 15 U.S.C. § 78c(a) (1970), compelled an evaluation of the nature of the underlying transaction. 500 F.2d at 1252.

\textsuperscript{80} 500 F.2d at 1253.
the court held that because the Internal Revenue Code grants certain tax benefits to cooperative tenants in the form of a pro-rata pass through of mortgage interest and other deductions, a "profit," in the shape of a reduced tax liability when compared to traditional apartment residents, was sufficient to find a security. Lastly, the court concluded that since the cooperative tenants do not, unlike apartment residents, pay any additional amount toward the lessor's profit, the cooperative is a less expensive form of property interest. These monthly savings were therefore "profits" resulting from their participation in the cooperative. The Second Circuit subsequently added a fourth test for the expectation of profit in 1050 Tenants Corp. v. Jakobson: the expectation of capital appreciation upon resale of the cooperative stock.

These four tests go far beyond the SEC's own criteria for asserting jurisdiction over condominium offerings. Although condominiums do not issue shares of stock, they share with cooperatives the possibilities of expected profit from commercial leases, tax advantages, lower monthly charges than apartments, and capital appreciation upon resale. In light of these similarities, the Second Circuit might find a condominium subject to the securities laws even when the offering does not meet the SEC's own "rental pool/economic benefit as a result of the efforts of others" jurisdictional criteria.

This result may be explained on consumer protection grounds not articulated by the court's opinions. Faced with a situation in which a developer had improperly taken advantage of unwary housing consumers, and recognizing that no effective remedies existed under the SEC regulations, the court

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81 INT. REV. CODE OF 1954, § 216, allows the tenant to take a deduction for a pro-rata share of the payments made by the cooperative housing association for interest and real estate taxes under certain enumerated circumstances.

82 A third way in which it might be viewed that profits may be realized is in the saving of an expense which would otherwise necessarily be incurred. In other words, where the going rate for rents in a given area is one amount, an investment opportunity offering housing at an amount substantially below that going rate is an offer of a "profit," for housing is a necessity and any saving on that necessity is money in one's pocket.

500 F.2d at 1254.

83 365 F. Supp. at 1176.

84 See notes 69-70 supra & accompanying text.

85 The SEC's own advisory committee on real estate has concluded that differences between the condominium and cooperative are illusory with respect to the securities problems involved:

Cooperative dwelling units should be treated in substantially the same manner as condominium units inasmuch as the form of ownership . . . represents no substantial difference with relation to the securities laws. In each case
broadened the jurisdictional criteria in order to reach a just remedy for the plaintiffs before it. This explanation is consistent with a recognition of the major problem engendered by use of the securities law to regulate condominium purchases. In the absence of a rational and effective regulatory scheme in one area in which abuses occur, a series of ad hoc judicially and administratively imposed controls from unrelated substantive areas has been applied in an effort to provide remedies and at least some indirect controls. In the condominium industry this phenomenon has resulted in a patchwork of partial controls which often appear to exceed the intended scope of the regulatory legislation. The impact on the legitimate developer has become unduly burdensome, raising the price of housing to the purchaser. At the same time, the scheme has failed to offer really effective protection in the context of rental pool and other covered developments, and has offered no protection at all for the purchaser most in need of it—the middle- and low-income purchaser of a condominium as a primary residence.

2. Regulation Through the Tax Law

The Internal Revenue Service may be another agency which is "stretching" the law in order to tax and deter developers whom it perceives to be profiting unduly at the public's expense. Faced with the apparently unregulated evil of developer self-dealing prior to sales of condominium units, the Service has recently forced at least some developers to capitalize the future rental income expected from recreation leases and to treat the present value of the future income as part of the proceeds from the sale of the units. The amount of capitalized rent is deter-

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86 As a result of the recent cases, many large institutional lenders are now refusing to grant construction money to developers who have failed to register with the SEC.

87 According to a member of the Florida tax bar, the "IRS in Florida treats most of the recreation rent as, 'in reality', part of the sale price of the condominium units, and therefore taxable to the [developer] corporation in a lump immediately, before the rent is earned or received." Emanuel, Condominium Developers and the Internal Revenue Service—The Florida Story, 2 Real Estate L.J. 760, 761 (1974).

minded by subtracting from the actual yearly rental income the "reasonable rate of return," established at eight per cent of the cost of the recreational facilities. The difference between the two figures is treated as the annual excess, with the present value of the right to receive this excess calculated by multiplying by ten.\(^8\) This amount is then added to the proceeds of sale in order to determine the taxable gain.

The IRS has taxed the value of long term maintenance contracts in a similar fashion, that is, before receipt of income attributable to actual services rendered. When the developer corporation forms another corporation for the performance of the management contract, the Service has deemed the transaction a sale and has taxed the capitalized full value of the contractual rights as the (fictional) proceeds from the sale.\(^9\)

Although these actions have not yet been fully litigated and tested in court,\(^8\) they have been criticized on the grounds of both tax law and policy.\(^9\) Consumer protection motives may be part of the Service's actions in this area, and the result is still another layer of industry regulation which may be extending the

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\(^8\) Emanuel, supra note 87, at 761.

\(^9\) The IRS maintains that § 482 of the Internal Revenue Code of 1954 allows the government "to rework the transaction as though the contracts had been sold for full value." *Id.* 763.

\(^8\) Only one unreported Tax Court decision is currently indexed in the tax services. *See* note 87 *supra*.

\(^9\) Emanuel, *supra* note 87, at 765-83. A recent revenue ruling by the Service may have been largely colored by the condominium industry's image. The Service has determined that a condominium association is not a tax exempt organization under INT. REV. CODE OF 1954, § 501(c)(4). Rev. Rul. 74-17, 1974 INT. REV. BULL. No. 1974-2, at 11; *cf.* Rev. Rul. 74-99, id. No. 1974-9, at 11 (homeowner's associations). Since it is not an exempt entity, there may be some special problems which arise in certain advertising practices. Condominiums are often compared to more traditional homeownership with emphasis on the equality given both forms with regard to the tax laws. However, certain assessments collected by the condominium association in the form of monthly maintenance charges may be understood as income to the association. For example, assessments often include a reserve for future repairs and capital improvements. By definition, these collections are not offset by any current expense which would result in no taxable income. Such excesses may be construed as income to the non-tax exempt association. The unit owners would, of course, be required to pay their allocable share of this tax liability, resulting in a double tax to them which would not exist if they had, for example, merely saved the capital reserve fund to meet contingencies in a traditional home ownership context. *See generally* Krasnowiecki, *supra* note 13, at 346-48. *But see* Rev. Rul. 74-563, 1974 INT. REV. BULL. No. 1974-47, at 6 (special assessment not income if clearly segregated and used to enhance the value of the individual units); *cf.* Rev. Rul. 70-604, 1970-2 CUM. BULL. 9 (excess assessments not taxable as income because either returned to stockholder-owners or applied against the following year's assessment).

Presently, two bills are pending in Congress to reverse the position taken by the IRS in its 1974 revenue ruling and exempt condominium associations as social welfare organizations. *See* [2 Current] BNA Hous. & Dev. Rep. 23 (June 3, 1974).
law beyond its originally intended limits in order to deter unrelated abuses.

3. The Interstate Land Sales Full Disclosure Act

The Interstate Land Sales Full Disclosure Act\(^9\) was enacted by Congress in 1968 partly in recognition of the practical "inapplicability of securities regulations to the outright sale of real property."\(^9\) The Act gave jurisdiction over some condominium sales to the Department of Housing and Urban Development, the supposed federal expert in the area of property. The Act was understood by President Johnson to be a means of "afford[ing] the public greater safeguards against sharp and unscrupulous practices."\(^9\) It was directed primarily at abuses surrounding the advertisement and sale of undeveloped realty to an ill-informed public. Its fundamental purpose was the protection of the purchaser of unimproved parcels of land. HUD was given control over the sale, through interstate commerce, of any "lot" of land by the registration mechanism established by the Act. According to HUD, condominium units have always been within the purview of the Act.\(^9\) Recent regulations promulgated by HUD have expanded the definition of "lot" under the Act specifically to include condominiums.\(^9\)

Although designed to meet the special problems of real property transactions, the Act is clearly patterned after the regulatory philosophy of the securities laws\(^9\) and functions as another full disclosure scheme. It requires the filing of a statement of record which must contain a laundry list of information designed to allow the potential investor to evaluate his purchase.\(^9\) To this end, a property report must be received by

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\(^9\) 113 Cong. Rec. 3529 (1967).

1. the name and address of each person having an interest in the lots in the subdivision to be covered by the statement of record and the extent of such interest;

2. a legal description of, and a statement of the total area included in, the subdivision and a statement of the topography thereof, together with a map showing the division proposed and the dimensions of the lots to be cov-
each prospective investor.99 Although a cause of action accrues thereunder for false or misleading statements,100 there are no affirmative requirements that the underlying investment be fairly structured. The report need only accurately describe the parcel to be sold.101

Whatever the shortcomings in the substantive regulations, a more fundamental question is whether condominiums ought to be included within the Act's scope at all. The original focus of the Act was the sale of undeveloped land. Since condominiums

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normally contemplate the sale of improved real estate, the central question is whether a condominium is a "lot" for purposes of the Act.

From a policy point of view, HUD is essentially correct in asserting jurisdiction over the sale of units in construction. Taken alone, a unit is an interest in real property much like any other and should not be permitted to escape the provisions of the Act merely because of a slight difference in form. In this regard, it is interesting to note that the typical state enabling statute does not require that a unit be within a completed building. A unit is generally defined as "a part of the property intended for any type of use or uses" or "a part of the property designed or intended for any type of independent use." If the condominium form were exempt in its entirety, any land sales offering could avoid the effect of the Act by declaring the subdivision a condominium, filing the appropriate plans with the state, and selling the "lots" as "units." To avoid this problem, condominiums should not be given automatic exemption.

Consequently, the issue of the Act's coverage of condominium developments should focus on the specific statutory exemption of section 1702(a)(3), which exempts sales when the developer is contractually bound to complete the building within two years of the sale. Under this exemption, whether a particular transaction will be subject to the Act depends upon whether there is a "sale," defined as "[a]ny transaction . . . whereby a purchaser is obligated to acquire . . . a condominium unit directly or indirectly . . . ." This broad definition is clearly intended to provide what protection the Act affords to purchasers who may be forced to take title to empty or only partially completed "lots." But if a purchaser is not, under the terms of

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102 The statutory prohibition is "to sell or lease any lot in any subdivision." *Id.* § 1703(a)(1) (emphasis added).
103 In construing a California statute, the California court of appeal held:
As used in the statute the word "lot" applied to any portion, piece, or division of land and is not limited to parcels of land laid out into blocks and lots regularly numbered and platted.
104 N.Y. *REAL PROP. LAW* § 339-c(13) (McKinney 1968).
106 15 U.S.C. § 1702(a)(3) (1970) provides for an exemption where there is a "contract obligating the seller to erect . . . a building thereon within a period of two years."
107 The Office of Interstate Land Sales Registration has clarified this exemption, stating that it would exempt a contract that had a provision allowing completion beyond the two year period if such delays are caused by conditions which would be legally supportable in the jurisdiction as impossibility of performance for reasons beyond the control of the developer. 39 Fed. Reg. 7824, 7825 (1974).
the contract for sale, obligated to close in such circumstances, then it would seem that there has not been a sale as defined and the Act should not apply.

A sample contract for sale will illustrate. It provides that "Seller is obligated to erect the Building of which the Premises are a part within two (2) years from the date [of signing]." The contract specifically allows the purchaser the right to terminate if the covenant is not fulfilled, at which time all deposit monies shall be returned and the contract shall be at an end.\(^{109}\) It would appear that such an agreement should not fall within the purview of the Act, since the terms of the contract themselves provide a sufficient degree of protection.\(^{110}\)

A proper interpretation of the Act would thus lead, in most instances, to the conclusion that it will not apply to condominium developments in which there is a binding contract to construct and deliver within two years, a provision for rescission by the purchaser on default, and an escrow arrangement for the return of deposit monies. In the absence of these three essential contractual safeguards, HUD should assert jurisdiction. But where these safeguards exist, the statute should not apply.

Since two years is usually sufficient building time,\(^{111}\) the

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\(^{109}\) Agreement of Sale, supra note 21, ¶ 5(c).

\(^{110}\) This, however, does not appear to be the present position taken by the OILSR in the form of guidelines, 39 Fed. Reg. 7824 (1974), the OILSR has indicated that a "sale" will exist for purposes of the act unless there is an absolute obligation that the seller "erect a building or condominium unit within a period of two years." Id. The only exception is a "reservation" whereby a purchaser merely expresses an interest and tenders a deposit held in independent escrow. There is no binding obligation and may be no formal contract for sale. Id. 7825.

In contrast, two years earlier the OILSR had specifically rejected this broad definition of sale:

The only [other] possible meaning . . . would be that all sales of residences . . . are covered by the Act if, at the time of signing the contract of sale, the lot is unimproved and if the date for delivery of the completed building is not firmly fixed within the two year period even though the contract would not require the purchaser to accept an unimproved lot. This would be an inconsistent result from the wording of the statute . . . . Whether it would be desirable to cover such transactions—where the contract calls for delivery after two years, of a completed building on a lot as—[sic] a condition precedent to the purchaser becoming obligated to take title—is not in question. . . . [A]s the Act is written, there is no jurisdiction for coverage.

Exemption Advisory Opinion No. 1710.1(k), at 8-9 (Aug. 20, 1972). This apparent reversal of position may be another example of administrative overreaching. See text accompanying note 86 supra.

\(^{111}\) The two year limitation may not, however, be sufficient for phase developments, for example, which contemplate completion over longer periods of time. Since most state statutes define a "unit" to include the proportionate undivided interest in the appurtenant common elements, e.g., Pa. Stat. Ann. tit. 68, § 700.102(14) (1971), the act would seem to require that all such common elements also be finished within two years. See 38 Fed. Reg. 23866 (1974).
impact of the statutory exemption is to deny the protection of the Act to most condominium purchasers. When the Act does apply, the purchaser's only remedy is for failure to disclose material terms fully. Adequate contractual remedies may not have been included by the developer, leaving the typical condominium purchaser with no effective remedy in many situations. All in all, the Interstate Land Sales Full Disclosure Act offers little protection to the condominium purchaser.

IV. THE CONGRESSIONAL RESPONSE

Both houses of the Ninety-third Congress considered bills which attempted to deal directly with the problems of condominium development and sale. Representative Collins of Illinois introduced a bill which purported "[t]o protect purchasers and prospective purchasers of condominium housing units . . . by providing for the establishment of national minimum standards[,] . . . to encourage the States to establish similar standards, and for other purposes."\(^1\)\(^2\) The proposal, designated as the "National Condominium Act," would have created, within HUD, an Assistant Secretary for Condominiums to coordinate and implement the basic program.\(^1\)\(^3\) In essence, the bill would not allow any "federally assisted condominium loan"\(^1\)\(^4\) to be made to a purchaser unless the developer submits a detailed statement which is approved by the Secretary.\(^1\)\(^5\) The statement requires the usual full disclosure material such as names and addresses of interested persons involved in the development, legal descriptions of the land and all liens attached thereto, the estimated operating expenses, and a statement of the terms of all management contracts.\(^1\)\(^6\)

However, H.R. 15071 also proposed some direct substantive regulations specifically proscribing certain of the previously

\(^{12}\) H.R. 15071, 93d Cong., 2d Sess., Preamble (introduced May 29, 1974).

\(^{13}\) Id. § 4.

\(^{14}\) "[F]ederally assisted condominium housing loan[s]" include the following: [A] loan which is made to finance the transfer of condominium ownership to an individual or family or the purchase, construction, rehabilitation, or conversion of a condominium project by a developer which—

(A) is made in whole or in part by a lender the deposits or accounts of which are insured by any agency of the Federal Government, or is made in whole or in part by a lender which is itself regulated by any agency of the Federal Government; or . . .

(D) is made in whole or in part by any "creditor", as defined in section 103(0 of the Consumer Credit Protection Act of 1968 . . . .

Id. § 3(6). Since almost all major sources of significant mortgage money would fall within this definition, the scope of the act's coverage is quite broad.

\(^{15}\) Id. § 5(a).

\(^{16}\) Id. § 5(b).
enumerated developer abuses. For example, the statement requires "satisfactory assurances that all purchasers . . . will be given a full one-year warranty" on certain specific construction details.\footnote{117} The bill also guaranteed that the maximum period in which a developer may maintain control of the condominium association is one year, and that no management contract may bind the unit owners beyond the period in which the developer may maintain control.\footnote{118} The bill would assist the state and local governments in implementing similar statutes for the purpose of centering the administration and enforcement of condominium regulation in the jurisdictional units best able to supervise the construction and development.\footnote{119} Finally, the bill provided for criminal sanctions\footnote{120} as well as for rescission of the purchase contract in certain situations.\footnote{121} The advantages of the proposed national act are obvious. Most importantly, it would have focused the issues in one central administrative body designed especially to provide comprehensive control. It would also have created national minimum standards which are fairly clear\footnote{122} and which address most of the central problems inherent in the condominium form. Although it was essentially a full disclosure act, the bill offered certain direct substantive controls as well. In addition, the Collins bill recognized that responsibility for enforcement of its provisions cannot reasonably be expected to rest solely in a federal agency. Any meaningful supervision must come from the state and local governments which have more direct contact with the developments.

Just weeks after the introduction of the Collins proposal, Senator Biden of Delaware introduced another bill also designed "[t]o protect purchasers and prospective purchasers of condominium housing units."\footnote{123} However, unlike the Collins bill, S. 3658 was in its entirety a full disclosure statute. Known as the "Condominium Disclosure Act"\footnote{124} the bill was patterned directly after the federal securities laws and required the usual informa-

\footnote{117} The warranty attaches to all "electrical, heating, air-conditioning, and ventilation equipment and [to] the roofing and elevators." \textit{Id.} § 5(b)(4).

\footnote{118} \textit{Id.} § 5(b)(8). For a more complete discussion of the advantages of substantive regulation, see text accompanying notes 139-84 infra.

\footnote{119} \textit{Id.} § 6. Federal subsidies would provide some incentive for state activity.

\footnote{120} \textit{Id.} § 7.

\footnote{121} \textit{Id.} §§ 5(b)(9)(A), (d).

\footnote{122} The act, of course, contains a catch-all section compelling the production of "such other information . . . as the Secretary may require in order to assure that purchasers are protected in a manner consistent with the purpose of this Act." \textit{Id.} § 5(b)(10).

\footnote{123} S. 3658, 93d Cong., 2d Sess., Preamble (introduced on June 17, 1974).

\footnote{124} \textit{Id.}
tion in its statement of record.\textsuperscript{125} The only significant differences between this bill and other full disclosure acts is that in certain areas of disclosure, the Biden bill would have required narrative descriptions rather than the reproduction of legal documents.\textsuperscript{126} In contrast to the House bill, the Biden proposal did not directly proscribe the most common substantive developer abuses. For example, as long as the terms of a lengthy and exploitative management contract or recreation lease were disclosed somewhere in the documents, the developer was free, under the bill, to reap excessive profits. Furthermore, the Senate bill did not envision any federal-state cooperation in implementing the terms of the Act.\textsuperscript{127}

A third bill was introduced by Senators Proxmire and Brooke.\textsuperscript{128} It is clear that the sponsors of S. 4047 understand the basic problems inherent in the industry.\textsuperscript{129} Senator Proxmire, speaking for himself and Senator Brooke, recognized that condominiums today provide an attractive solution to the problems of lower-income housing.\textsuperscript{130}

In essence, S. 4047 combined most of the elements of the House bill with some of the securities-like provisions of the Biden bill. Like the Collins proposal, the Proxmire-Brooke bill required that the statement of record contain “satisfactory assurances” that the unit owners would receive a one year warranty on some basic structural components;\textsuperscript{131} would be able to form the association and thereby to divest the developer of extended control within a maximum period of one year;\textsuperscript{132} and would not be trapped into management contracts which extend beyond the period in which the owners may be excluded from association control.\textsuperscript{133} All other problem areas would be regulated by means of a system of full disclosure. Thus as long as material provisions of long term recreation leases are disclosed,\textsuperscript{134} there

\textsuperscript{125} Id. § 6.

\textsuperscript{126} However, only relatively few disclosures require a narrative description. Copies of actual contracts and condominium documents are included in the statements. See id. §§ 6, 8. On the other hand, the new Virginia act requires narrative descriptions to a greater extent. VA. CODE ANN. § 55-79.90 (Supp. 1974).

\textsuperscript{127} This raises the question whether the federal regulatory effort would be adequately funded, in light of the size of the condominium industry.

\textsuperscript{128} S. 4047, 93d Cong., 2d Sess. (introduced on Sept. 26, 1974).

\textsuperscript{129} See 120 CONG. REC. 17,547 (daily ed. Sept. 26, 1974).

\textsuperscript{130} Senator Proxmire remarked, “Certainly condominiums do represent an attractive housing choice for many people. They offer homeownership and its accompanying tax benefits to people whose incomes are too low to afford conventional housing.” Id.


\textsuperscript{132} Id. § 5(a)(12)(A).

\textsuperscript{133} Id. § 5(a)(12)(D).

\textsuperscript{134} Like the Biden bill, S. 4047 envisions a two-tier process. A statement of record
was nothing in the bill to prevent developer abuses in this area. Unlike the House bill, the Proxmire-Brooke proposal did not envision any continuing relationship between the states and the federal government. The only reference to state law in the proposed act was contained in an "inconsistency provision" which allowed the state to legislate in a manner which affords "greater protection to the consumer."\textsuperscript{135} Exemption provisions were also available to states which regulate under a "substantially similar" scheme.\textsuperscript{136} There was, however, no incentive provided the states to assume primary responsibility for regulation of the industry.\textsuperscript{137}

Although they suffered from many shortcomings, the national acts would have provided an essential element missing from the present regulatory scheme—concentration of control in an agency tailored to deal with the special problems of the condominium industry. Such concentration of control would by itself likely have provided the impetus to reverse the current trend towards layered and unrelated systems of inadequate regulation.\textsuperscript{138} If they accomplished nothing else, the bills would have relieved the legitimate developer from a series of regulatory controls which have done little more than stretch laws beyond their intended scope and add further development costs which are, in turn, passed along to the consumer without a corresponding return in protection. However, it still must be determined whether the full disclosure approach is appropriate as the exclusive regulatory response.

V. Disclosure and its Alternatives

A. The Failure of Disclosure

Thus far it is clear that the existing regulation of the condominium industry is wholly inadequate. At the state level, the great majority of jurisdictions have failed to improve upon their original enactments which, for the most part, afford very little protection. The federal responses, while numerous, have been

\textsuperscript{135} \textit{Id.} § 13(a).
\textsuperscript{136} \textit{Id.} § 13(b).
\textsuperscript{137} Compare \textit{id.} with H.R. 15071, 93d Cong., 2d Sess. § 6(b) (1974).
\textsuperscript{138} Any comprehensive act should specifically amend the securities, interstate land sales, and other relevant acts in order to minimize administrative confusion.
largely ineffectual, if not entirely inappropriate. The regulation that does exist is characterized almost uniformly by full disclosure requirements. In view of the prevalence of this approach, the question which must finally be answered is whether the disclosure laws address the problems in an effective and practical way.

The philosophy of full disclosure regulation is best exemplified in the securities laws. As one commentator in that field has observed, "[e]ver since the enactment of the first federal securities law in 1933, primary regulatory reliance has been placed on a system of disclosure." Disclosure was envisioned as a means of balancing the needs of the purchasing public with the conflicting commitment to minimal governmental interference with the operation of a free market. The philosophy of disclosure is, perhaps, best explained by Justice Brandeis' conclusion that "[p]ublicity is justly commended as a remedy for social and industrial diseases. Sunlight is said to be the best of disinfectants . . . ."

More recently, the effectiveness of a disclosure system has been seriously questioned. Some commentators have pointed to the length and enormous complexity of many prospectuses, and have recognized that the potential investor is not likely to understand or properly evaluate a large percentage of the reproduced material. As prospectuses and other disclosure documents have become more and more complex, the information made available has grown increasingly meaningless to the great majority of the investing public. For example, one survey reveals that from a representative sample of stockholders, "43 percent understood little or nothing from a company's formal financial statements, more than 50 percent could not define the meaning of depreciation, and virtually all were confused by the concept of cash flow." This suggests that one of the fundamental assumptions of an effective system of regulation by dis-

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140 L. Brandeis, Other People's Money 62 (1913).


143 Barack, supra note 139, at 1527.
closure is open to question. For the regulatory system to work, a potential purchaser must be equipped with the basic tools with which to analyze and evaluate the underlying investment. Even the most efficient scheme of full disclosure cannot be of any substantial value to an investor incapable of reacting to information in an appropriate and rational manner.

The securities regulators themselves have recognized that full disclosure is not always an adequate response to all industry problems. In recent years, the SEC has taken some affirmative actions against certain industry practices understood as inherently deceptive or fraudulent. For example, proposed rule 10b-12, under section 10 of the 1934 act, would directly prohibit the distribution of stock dividends by an issuer if earned surplus would not cover the value of the shares distributed. In prefatory explanation, the Commission stated:

Pro rata stock distributions to stockholders in amounts which are relatively small in relation to the number of shares outstanding are a means of conveying [a false] impression . . . . Instances have recently come to the attention of the Commission in which such distributions were utilized . . . creating a misleading impression concerning the results of operations of the company.

The proposed rule does not relate to any requirement of disclosure. The Commission has apparently taken the position that no amount of disclosure is sufficient to legitimize a practice deemed inherently deceptive or abusive. Thus, under certain conditions, something more than disclosure is mandated.

In the condominium industry, the objections to the almost exclusive reliance on full disclosure apply with even greater force. Investors in the securities markets are generally fairly

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144 The Real Estate Advisory Commission, set up by the SEC to examine condominiums, recognized the possible need for substantive regulation. "If . . . improved disclosure and enforcement does not achieve this end, a regulatory approach, perhaps similar to the Oil and Gas Investment Bill of 1972 may be necessary." SEC, REPORT OF THE REAL ESTATE ADVISORY COMMISSION TO THE SECURITIES AND EXCHANGE COMMISSION 4 (1972). Raymond Dickey, the chairman of that Committee, has suggested that the Investment Co. Act of 1940 might be a model for the SEC in the control of high fees and other charges paid under rental arrangements tied to offerings of condominiums units. Dickey & Thorpe, Federal Security Regulation of Condominium Offerings, 19 N.Y.L.F. 473, 491 n.79 (1974).


146 Further examples of direct, prohibitory regulation by the SEC are evidenced by rule 10b-4, 17 C.F.R. § 240.10b-4 (1974) (proscribing "short tendering" in connection with a tender offer), and rule 10b-6, id. § 240.10b-6 (prohibiting certain insider trading).
sophisticated, affording some justification for the use of a less intrusive form of governmental intervention. In the case of condominium purchasers, on the other hand, sophistication may not be assumed so easily. Many condominium purchasers do not have independent expert advice on the merits of a particular investment because they do not retain experienced attorneys to advise them. The securities investor, in contrast, will usually have the services of an independent broker available. Since condominiums are increasingly likely to become a less expensive alternative to the more traditional form of homeownership, prospective purchasers may include many lower-income individuals for whom a home will be a first and last capital investment. While disclosure may be helpful as a limited part of a regulatory scheme, it is as likely to intimidate as to protect when it is relied upon exclusively.

For example, the following provision appears in most condominium by-laws or declarations:

The first meeting at which members may vote shall be held within thirty (30) days after the sale by the Declarant [developer] of the last Unit owned by the Declarant, or within five (5) years after the date of the filing of the Declaration, or within thirty (30) days after declared by the Declarant, whichever shall first occur.

Such a provision enables the developer to maintain control of the project until the last possible moment. With this extended control, the developer may, through the actions of his board of directors, determine the common expenses, grant licenses over the common areas, make any improvements and alterations, and adopt and amend certain rules and regulations. Will simple description, in legal terms, of this seemingly innocuous maintenance of power really provide adequate protection to a lay purchaser unfamiliar with the basic legal structure? Similarly, would Florida's old provision that unit owners could cancel

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147 See text accompanying note 143 supra.

148 The securities laws themselves operate to interpose the securities dealer between the investor and the issuing company and its investment bankers. See Heller, supra note 141, at 301-02 n.6.

149 See notes 4, 130 supra & accompanying text.

150 It may be argued that the mere fact that a developer is required to expose the elements of his transaction accurately, on the public record, itself provides a good deal of discouragement against abusive practices. See text accompanying note 140 supra.

151 By-laws of Meadow Hill Development Corp. art. V, § 4, filed Feb. 11, 1971, Hartford County, Conn.

152 Id. art. IV, § 2.
maintenance contracts provide any real protection where those owners could not act until they had "assume[d] control of their association"?\textsuperscript{153} The developer was able, before the recent legislative changes, to lock those owners into that contract and, apparently, into any other, for as long as the documents provided.\textsuperscript{154}

B. The Florida Response

Since full disclosure is of only limited utility to a large percentage of the condominium purchasing public, direct, substantive regulation seems to be the only sensible alternative. Such a system may be justified, as it has been in the securities field, as an exercise of the power to enjoin inherently abusive practices.\textsuperscript{155} One possible approach is exemplified by the recent changes made in the Florida Condominium Law.\textsuperscript{156} Effective October 1, 1974, the extensive amendments substantially altered the prior law. Apparently dissatisfied with the relatively poor effectiveness of its full disclosure scheme of regulation, the new law speaks directly, and, for the most part, substantively, to the major problems of the industry. For example, the new law directly addresses the problem of the maintenance of control by the developer.\textsuperscript{157} The developer may maintain control by electing a majority of the board of administration. Such power, however, is limited to a system of amortization. When unit owners other than the developer own fifteen percent of the total number of units, those owners are entitled to elect not less than one-third of the members of the board. After seventy-five percent of the units are sold, the developer is absolutely limited to three years of additional majority control. Finally, within three months of the time in which ninety percent of the units are sold, the developer must relinquish control.\textsuperscript{158} Although it may be argued that the time in which the developer may maintain control is too long, at least the Florida legislature has recognized the

\textsuperscript{153} Fla. Stat. Ann. § 711.13(4) (Supp. 1974), repealed by Fla. Laws 1974, ch. 74-104, § 16 (Supp. Fla. Session Law Service No. 2, 1974). Section 16 of the new law has added a section to the Florida Code—§ 711.66(5)—in replacement of the repealed section. This new provision requires that maintenance contracts be "fair and reasonable," besides being subject to cancellation by the unit owners after they have assumed control.

\textsuperscript{154} The recent Virginia Act has addressed this problem directly even though it is, for the most part, a full disclosure scheme. See note 30 supra. The National Condominium Act (Collins bill) also attempts to speak to this particular practice. See note 118 supra & accompanying text.

\textsuperscript{155} See text accompanying notes 144-46 supra.


\textsuperscript{157} See text accompanying notes 31-32 supra.

problem and has struck a balance of the competing interests in a
direct manner providing a clear minimum acceptable standard.

Similarly, Florida now provides that all management con-
tracts must be "fair and reasonable." This answers the prob-
lem of sweetheart management agreements of excessive length
and inflated rates of compensation. Furthermore, the new law
avoids the problem of cancellation only after the unit owners
have assumed control. It now provides that assumption of
control is not a prerequisite to the power of cancellation.
Thus, the Florida legislature has imposed certain affirmative
duties on the developer which the courts refused to impose
under the old law.

In the area of advertising abuses, the Florida law now
gives a cause of action to a unit owner for damages arising out
of reliance on any material statement published by the
developer. These materials include not only the prospectus
and other items of disclosure required by the statute but also
"advertising and promotional materials . . . brochures and newspa-
per advertising." Although there is no direct prohibition on
the issuance of misleading information, the damage action is a
powerful disincentive. The new law also includes a five-year war-
ranty of fitness and merchantability which attaches to the unit,
common properties, and all improvements, and specific provi-
sions which require the developer to pay certain assessments on
any units which he owns prior to sale.

In reference to the sweetheart lease, the Florida law re-
quires that the rental may be adjusted only at intervals of not less
than ten years and further that such adjustments may not be
greater than increases reflected in a nationally recognized price
index.

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159 Id.
160 See text accompanying notes 25-29 supra.
161 See text accompanying note 153 supra.
162 Once owners aggregate 75% of all units, a vote of 75% of those owners may
cancel the contract notwithstanding the fact that the developer may maintain control
for another three years. Fla. Laws § 711.66(5)(b).
163 See note 28 supra.
164 See text accompanying note 19 supra.
166 Id.
167 Id.
168 Id. However, the assessments are limited to those related to capital improve-
ments and would therefore appear not to include normal maintenance charges. In
addition, it is not clear that this provision adequately answers the problem of redefin-
ing a unit in order to limit liability for even the capital improvement assessment. See
text accompanying note 33 supra.
169 Id. See notes 26-28 supra & accompanying text.
The Florida amendments continue to rely in large measure on extensive and bold-faced disclosure provisions to afford protection in other areas. For example, although deposits collected prior to closing must be initially held in escrow, the developer may withdraw such funds for use in actual construction if such use is disclosed in the contract itself.\(^1\) The risks of bankruptcy, however, are not subject to a similar disclosure requirement.\(^2\) Similarly, although the statute limits increases beyond the first ten years of a recreation lease to the cost of living, there does not seem to be any prohibition against drafting an inflated initial rental agreement. The only means of regulation of this practice are contained in the disclosure provisions\(^3\) and in the option granted owners to purchase the leased property at a price which is subject to arbitration.\(^4\)

The Florida law appears to be a balance of direct substantive regulation and the more typical disclosure provisions. The Florida amendments have not, however, gone far enough in the direction of substantive regulation. Too much reliance is placed on the efficacy of full disclosure in areas of importance such as deposit money and initial terms of leaseholds. In attempting comprehensively to define and control specific abuses, the law also suffers from the dangers of inflexibility. The proscription of specific rules in advance risks the possibility that "jurisdiction would be cramped, and perpetually eluded by new schemes which the fertility of man's invention would contrive."\(^5\) Although rules of conduct are important in allowing developers to conform their activities to the law, a degree of flexibility in regulation must also be preserved.

**C. Substantive Regulation Under A Permit System**

An appropriate and effective system of comprehensive regulation which answers these problems most effectively might be a permit system in which the underlying fairness of a particular

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1. Id.
2. See text accompanying note 23 supra.
4. Id. However, the option to purchase does not adequately answer the problem. Even if a price is set through arbitration, the arbitrators are specifically directed to "take into account the capitalization of the current rent." Id. If there is, in fact, no limitation on the power to set inflated initial rentals, the unit owners would then be forced to pay an exorbitant purchase price based on the capitalized value of that current rent which, in the absence of self-dealing, would have more accurately reflected a true fair market value.
development would be determined by an expert administrative body. This board would be invested with the power to enjoin specifically enumerated practices found to be against the public interest after a careful investigation of all of the development's elements. Such a system might resemble the blending of the California permit administrative structure and the substantive criteria contained in the new Florida condominium law. Its basic objective would be to provide effective protection to those investors who might make unwise purchases when faced with a pile of forbidding and usually unread documents.

A model regulatory scheme would require, as a condition precedent to the issuance of a valid construction permit, that a real estate commission check the accuracy of the information provided and, more importantly, that the commission possess the power to deny a permit unless it finds that "the proposed sale . . . is fair, just and equitable." The specific grounds for denying a permit should be bottomed in the practices previously described as abusive. Those grounds should include, as a minimum, findings by the commission that the developer has failed 1) to maintain an escrow account for all deposit and subscription money collected, with provisions for the accrual of interest; 2) to enter recreation leases or management contracts which are not, under duly promulgated standards, excessive in compensation or duration;[supra.] 3) to include specific time limitations for periods in which developers may maintain control of the association; 4) to advertise in such a manner that the development is not described in a false or misleading fashion; 5) to disclose accurately the full maintenance charges attributable to each unit with an explanation of the manner in which any increases may occur; and 6) to provide for the payment of monthly charges attributable to unsold units held by the developer. Although some of these practices have been addressed in the Florida and in various other systems of regulation now existing, none has attempted to deal with them all in a com-

176 See text accompanying notes 19-33 supra.
177 The statute might also cast the developer in the role of a fiduciary with respect to all future owners. See text accompanying note 28 supra.
178 The Virginia Act speaks to these abuses through the medium of full disclosure although it attempts to answer some of the problems of complexity and length by demanding narrative descriptions. See Va. Code Ann. § 55-79.90 (Supp. 1974). In addition, some problems are spoken to more directly in specific prohibitory language. See, e.g., id. §§ 55-79.74 (maintenance of developer control), 55-79.79 (one year warranty against certain structural defects).

Condominium Regulation: Beyond Disclosure

The proposed system of regulation must retain a degree of flexibility so that it may respond to developer practices which have not heretofore been employed, but which would conflict with the purpose of the legislation—the protection of the unwary consumer. Beyond this, many of the positive features of the disclosure systems could also be incorporated into an active permit system.

In order to achieve a degree of uniformity throughout the nation and to avoid the problems of multileveled regulation from fifty or more different sources, it is necessary that Congress provide the guiding hand toward the development of minimum national standards. Such is the specific promise, if not the result, of all three pieces of proposed legislation. However, Congress must also realize that truly effective control is only possible in a system which recognizes that the appropriate units of administration are the state and local governments. Therefore, a cooperative effort is essential. Any national act ought to provide for a system of financial incentives to a state which is willing statutorily to establish an agency which will assume the primary responsibility of administering an effective

Sess. (1974), are patterned after the Virginia Act and share its substantive-disclosure mix. The primary advantage of these provisions is their national focus and their creation of minimum national standards. The majority of other systems presently in existence are, in essence, full disclosure schemes. The only major exception is the California permit system. See notes 56-57 supra & accompanying text.

179 See notes 37, 98 supra. These disclosure requirements could easily be incorporated in a system which directly prohibits certain practices now only reported.

180 In introducing S. 4047, Senator Proxmire specifically stated the need for federal intervention:

Moreover, it is important to do this at the Federal level. If it is done in a piecemeal and patchwork fashion, then we will end with a maze of differing and conflicting local standards which will cause more confusion and invite further abuses. Developers will move from States with strong laws and into States with weaker laws. A person who moves from one place to another will find that the protections he enjoyed formerly are no longer available in his new place of residence.

120 CONG. REC. 17,548 (daily ed. Sept. 26, 1974).

181 See text accompanying notes 112, 123 supra. See also S. 4047, 93d Cong., 2d Sess., Preamble (1974).

182 On the federal level, this permit system could be administered either by a specially created division of the SEC, by a new agency established specifically for condominium regulation, or by HUD.

Notwithstanding the traditional wisdom that states should possess supremacy in controlling real property development, state agencies administering condominium laws are likely to face some formidable problems. Even assuming adequate funding and personnel, state commissions charged with passing upon permit applications would have to deal with powerful local real estate organizations without becoming too heavily influenced by developer interests. Cf. Note, supra note 35, at 1534. A federal regulatory agency can be expected to be less receptive to local developer lobbying efforts than its state counterparts. This advantage, however, could be diminished by the formation
regulatory scheme. Such a proposal is now contained in H.R. 15071, which envisions a system of federal standards with state administration of those or stricter standards.\footnote{H.R. 15071, 93d Cong., 2d Sess. § 6 (1974), provides: (a) The Secretary shall take all possible steps to encourage and assist State and local governments and agencies to establish procedures, standards, and requirements . . . similar to and no less stringent than [those] provided by this Act . . . . (b) The Secretary is authorized to make such grants to the State and local governments and agencies . . . to help them establish special offices to administer and enforce the procedures, standards, and requirements . . . and in general to oversee the development and construction of condominiums . . . .} Direct federal regulation would then only be necessary in those few jurisdictions which have failed to act themselves. An appropriate level of federal subsidy would hopefully make this a rare exception.\footnote{By way of example, the Coastal Zone Management Act, 16 U.S.C. §§ 1451-64 (Supp. II, 1972), has created and operates under a very similar system. Congress here has recognized that "[t]he key to effective protection . . . is to encourage the states to exercise their full authority" to regulate land use. Id. § 1451(h). In order to accomplish this goal, annual grants have been made available to provide up to two-thirds of the funding for local administration, id. § 1454, pursuant to federal minimum standards, id. § 1455(c). See Land Use Planning Act of 1974, H.R. 10294, 93d Cong., 1st Sess.; cf. [2 Current] BNA Hous. & Dev. Rep. No. 4, at A-22 (Oct. 31, 1973).}

VI. CONCLUSION

This Comment has outlined the pressing need for effective and comprehensive regulation of condominium developments and sales. The current pattern of regulation is entirely unsuited to protect those condominium purchasers most in need of it—the low- and middle-income families who increasingly will be buying condominiums as primary residences due to their cost advantages compared to conventional housing.

Many states have adopted regulatory schemes which are patterned after the inadequate disclosure approach of the securities laws. The federal government has no coordinated or centralized regulatory approach: present controls are administered by a patchwork of agencies which are not primarily concerned with condominium regulation. The proposed national legislation of an effective national condominium developers' lobby, or by the filling of the regulatory commission with representatives of developer interests.

Also, limitations on a state's power to regulate activities beyond its boundaries may frustrate its efforts to ensure protection for its own residents. A developer selling units located in a poorly regulated or unregulated state may be able to damage purchasers in a well regulated state. In order to halt such an out-of-state developer's activities, the regulating state would have to bring the developer into its courts; but injunctive remedies are not usually enforced in other states. In addition to this, if violation of a state's condominium laws are only misdemeanors, enforcement and extradition may sometimes be neglected. In light of these problems, federal regulation of this area is warranted.
would go far to remedy this situation, but none of the proposed bills would adequately protect the purchasing public.

A more efficient and effective regulatory approach would be the establishment of a permit-granting administrative commission operating within the statutory context of substantive proscriptions. The interests of the legitimate developer as well as those of the purchasing public would be served by such a system. In considering regulatory legislation in this area, Congress now has the opportunity to make a significant contribution to the availability of "decent housing to all our people" on terms that are fair to them.

185 In the words of one commentator, "the proper control of marginal and fraudulent operators is as great an asset to the legitimate developer as it is to the uninformed purchaser." Note, supra note 93, at 727.