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Recent Legislation

MISSOURI CONDOMINIUM PROPERTY ACT OF 1963

The enactment of the Missouri Condominium Property Act demonstrates the existence of an interest in space other than a mere medium through which astronauts may travel. The interest is in space closer in proximity to the surface of the earth and might possibly be referred to as "heir-space" in that the legislative intent was to facilitate the use of airspace as real property in the sense in which that term is commonly understood by the layman.

I. WHY CONDOMINIA?

A. Background

As population increases, the demand for living accommodations expands and land appreciates in value. One manner of utilizing this greater value is through more intensive use, and the high rise apartment is one such means of placing more living units on a given surface area. Occupants benefit from (1) being able to live close to their work, (2) reduced operating costs resulting from mass purchasing power of the owner, (3) not being required to tie up capital in property investment, (4) consolidation of many housing expenses into one payment in the form of rent, (5) elimination of the risk of depreciation of the property as the result of economic recession, and (6) mobility with permanency through relatively short term leases with renewal options. Still, the apartment tenant finds that ownership offers benefits not available to renters such as (1) the opportunity for investment appreciation, (2) minimization of operating expenses due to control by the owner, (3) elimination of the threat of eviction for breach of any of the many lease covenants, (4) acquisition of an asset suitable for loan collateral or which can be sold or devised at death, and (5) ability to deduct interest and taxes from income for tax purposes without including in income the reasonable value of the benefits.
due to the progressive rate of income taxation, this last factor becomes increasingly important to those in higher tax brackets.

The cooperative apartment is an effort to secure the advantages of ownership while retaining the benefits of renting. Cooperatives take one of two forms, corporate or trust. In the corporate form, a corporation is created which takes title to the property. An individual purchases corporate stock which gives him a proprietary interest, and he is given a lease of the apartment of his choice. In fact, the apartment occupant does not own either "his" apartment or an undivided share of the entire building, but the practical effect of his stock ownership is to give him an indirect ownership interest in the particular apartment. In the trust type cooperative, a group or individual is selected to administer the property, and each occupant conveys his interest in the property in trust to the management. In either corporate or trust form, the financing is secured by a blanket mortgage on the entire development with the corporate management or the trustee making the mortgage payments from the fees charged to the occupants. While these cooperatives give the occupants more of the benefits of ownership than they had as ordinary tenants, they still lack freedom (1) from the multi-covenanted lease and the accompanying threat of eviction, (2) from financial interdependence on other occupants whose defaults in payments to the management could result in a default on the blanket mortgage causing all to lose their investments through a foreclosure, and (3) from repurchase options given to the management at a stipulated price preventing an occupant from realizing the benefits of increments in value. In the search for a scheme to make available still more of the benefits of ownership to the cooperative apartment owner, condominium was discovered in Europe and Latin America and was imported into the United States.5

While it has become common practice to speak of condominium units as being apartments, the condominium principle is equally applicable to commercial and industrial units such as offices, stores, warehouses, etc. Businesses are permitted to deduct for tax purposes their ordinary and necessary business expenses which will include either rent or taxes and interest, and the appeal of the condominium in this respect is not as great as it is to the apartment dweller. Nonetheless, throughout this article, when reference is made to a condominium apartment, it should be kept in mind that the principle is not limited to residential usage.

B. Recent History

Puerto Rico, in 1955, was the first jurisdiction in this country to have condominium legislation,6 and its presently effective law is the Horizontal Property Act of 1958.7

5. "[T]he concept of ownership of property in condominium is literally as old as the hills—the hills of ancient Rome, where it had its beginning." Ramsey, Condominium, 9 PRAC. LAW. 21 (March 1963). But see Buckland & McNair, ROMAN LAW AND COMMON LAW 101 (2d ed. 1952): "But a very important difference between the Roman law and ours is that the Roman law totally excluded superimposed freeholds."
In 1961, the Congress enacted section 234 of the National Housing Act\(^8\) which authorized the insuring of mortgages by FHA on condominium apartments meeting certain minimum standards.\(^9\) In order to obtain the benefit of such loan insurance, the state was expressly required either to have effective legislation or common law holding that real property title and ownership are established with respect to a one family unit which is a part of a multi-family structure. FHA proposed a Model Act\(^10\) which was adopted with minor revisions by a number of states. According to the *Wall Street Journal*, by July 31, 1963, at least thirty-eight states had adopted some form of condominium legislation, and it was pending in five others.\(^11\) Illinois has a brief yet comprehensive statute\(^12\) which was the immediate source of the new Missouri law.

II. CONDOMINIUM LEGISLATION—BASIC PROBLEMS

The problems which had to be covered in condominium legislation fell basically into three areas: (1) problems of creation, (2) problems of operation and financing, and (3) problems of perpetuation and disposition and the effects of the common law rules of property. In addition, every jurisdiction encountered its own local problems which were basic and important, such as the Missouri problem of assessment for real estate tax purposes. We shall attempt to show the conflicts which the drafters had to resolve and the factors which influenced them in making their decisions.

A. Problems of Creation

The Missouri act provides that a condominium may be created by filing for

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record a declaration, a plat, and by-laws of the property. The declaration sets out the percentages of ownership in the common elements attributable to each unit. This is then the basis for sharing the common expenses and the distribution of insurance proceeds in the event of a coincidence of destruction of the property and the decision of the owners not to rebuild.

The by-laws are the rules of the association of owners by which the property will be operated; they provide for a board of managers to operate the common elements for mutual benefit. The act requires that by-laws at the minimum shall at all times cover certain stated problems and also that any amendment must be recorded in the same manner as the by-laws themselves to give notice to potential purchasers and creditors.

The plat must be made by a registered Missouri land surveyor and give information as to the legal description of the parcel, the location of the building on that parcel, and the location within the building of each of the several units. This is accomplished by means of a three dimensional plat with each unit being given an identifying symbol for easy reference. One concern in this area was the possible reluctance of county officials to accept for recordation a new type of plat. By requiring recording, it is clear that a recorder of deeds must accept such a plat. It was to be expected that there would be resistance to this concept of cubicles of space existing in the air and being owned by those who could convey, mortgage, and lease or otherwise deal with them as real property. Conceivably, there are those who will be startled at a legal description expressed in terms of dimensions on the surface, but existing between two horizontal planes at given distances from official datum.

Since taxes are a lien on the property, a blanket assessment would mean a blanket lien and a deterrent to mortgagability. Specific provision was made for unit assessment rather than assessment of the entire parcel. By establishing the individual units on the plat and assigning to each an interest in the common elements, separate taxation and assessment of the common elements was prevented. This is in keeping with the basic objective of preventing any type of blanket lien or encumbrance which would attach to every unit. Mechanics of assessment are left

13. For an interesting discussion of what the author says was the first vertical subdivision plat, see Becker, Subdividing the Air, Extra Vol. 1931 Ch. L. Rev. 40.
14. § 448.010, RSMo 1963 Supp. hereinafter cited by section number only.
15. § 448.030.
16. § 448.080.
17. § 448.140 (2), (4).
18. § 448.170.
21. The registration of land surveyors is covered by § 344.010 et seq., RSMo 1959.
22. § 448.040.
23. § 448.100.
24. "There is no mode pointed out by which part of a house can be assessed and not the remainder. Such a proceeding is no where contemplated by the statute." Wyman v. City of St. Louis, 17 Mo. 335, 337-8 (1852).
to local officials, but, as a practical matter, probably will be effected by determining a value for the entire project and applying the declaration percentages to that figure to obtain the unit assessments.

B. Problems of Financing and Operations

It has been correctly said that "condominium can exist under the common law, but whether it will flourish without statutory provision is doubtful." The Missouri statute was designed to give lenders the best possible security in order to make financing readily available. Each unit owner is at liberty to arrange his own mortgage as best suits his need within the limits of availability of mortgage money. The lender receives a first mortgage on the unit, the type of security preferred by all lenders and required by law of some, such as the savings and loan associations. Only taxes on the specific units may take precedence over the mortgage, not unlike a single family residence loan. Thus, the drafters accomplished the goal of creating a climate in which condominium financing could thrive in competition with the demands of other types of real estate investment.

Of major concern in this area was a means of enforcing payment of the common expenses. The board of managers will probably supervise those who will maintain the common elements and provide certain essential services. These costs are prorated among the unit owners based on the declaration percentages and are known as the common expenses. If not paid promptly, they are a lien of record upon the filing of a notice by the board of managers. Among the expenditures made by the board is the premium for insurance covering full replacement cost which is required by the act. The benefit of this insurance inures directly to the mortgagee through the loss payable clause, and it would seem, at least to this extent, that the common expense lien should be given the highest priority, but placing it superior to the first mortgage would discourage lenders from making loans. Thus practical considerations led the drafters to make the common expense lien prior to all other liens except those duly recorded before the filing of notice and liens for taxes and assessments which are by law superior to pre-existing recorder encumbrances. This lien for common expenses can only be enforced by foreclosure through judicial action and not by a non-judicial public sale under a power of sale as in the case of a Missouri deed of trust in usual form.

The common expense lien may present another problem. Some authorities feel it is in the nature of an equitable mortgage for securing future advances, and when a foreclosure of a senior lien takes place, the right to the lien for future common

26. § 448.180 (1), (6), (9).
27. § 448.080. (1).
28. § 448.080 (2).
29. § 448.120. For an extensive discussion of the unique problems of condominium insurance, see Rohan, Disruption of the Condominium Venture: The Problems of Casualty Loss and Insurance, 64 COLUM. L. REV. 1045 (1964).
30. § 448.080 (2).
31. § 448.080 (3).
expenses will be forever extinguished by foreclosure much the same as a junior mortgage is extinguished by foreclosure of a senior mortgage. The drafters apparently feel that they have kept the lien alive at least in the case of tax deeds and sheriff's deeds by making those who take under these deeds subject to all the provisions of the act and the declaration, plat and by-laws, all of which are of record, and any other deed in force which affects their interest. No mention is made of the effect of a foreclosure under a first mortgage on the common expense lien right, but it should be held that the continuation of the right is inferred from the above provisions. The act is silent as to what happens to liens in favor of the board of managers for common expenses which are eliminated by a foreclosure of a prior lien where sale does not bring enough to satisfy the common expense lien. It would seem that, the expenditure already having been made, is no choice but to prorate this indebtedness to the other unit owners.

It is beyond the scope of this article to speculate as to the effect of federal tax liens under United States v. Buffalo Savings Bank and related cases.

No lien, common expense, mechanic's or otherwise, shall attach to a unit unless the owner has consented to the work giving rise to the lien, but the act provides that such consent shall be deemed to have been granted in the case of emergency repairs or work ordered done by the board of managers. This is an obvious necessity, to give the management the power to promptly care for breakdowns in vital services. Nowhere in the act has "emergency repairs" been defined, that task having been left to the courts as they view the circumstances and practical considerations of each case.

The board of managers will undoubtedly carry liability insurance, but each unit owner should make sure he is adequately protected as to the common elements since he now may have a tort liability which was non-existent when he was a mere tenant. In the corporate cooperative, the liability falls on tenants indirectly to the extent that the value of their sock can be wiped out by a judgment against the corporation and execution on the property.

C. Perpetuation and Disposition—Effect of Rules of Property

The statute expressly provides that the Rule Against Perpetuities and the rule against unreasonable restraints on alienation "shall not be applied to defeat any of the provisions of this chapter." As this area is discussed it will be seen that this was a necessary and practical solution to many of the problems presented.

The rule against unreasonable restraints on alienation and the Rule Against Perpetuities prevent, respectively, unreasonable restrictions on the free alienation of real property and future interests which might under any conceivable set of circumstances vest too remotely.

32. § 448.110.
33. § 448.080 (4).
34. 371 U. S. 228 (1963).
35. § 448.090 (2).
37. Eckhardt & Peterson, Possessory Estates, Future Interests and Conveyances in Missouri, §§ 65, 73, 23 V.A.M.S. 58, 64 (1952).
The condominium unit is the space occupied by the apartment, office, or store. The common elements are the remainder of the property including but not limited to the land, foundations, walls, roof, halls, corridors, lobbies, stairs, basements, yards, parking areas, mechanical services such as heating, air conditioning and ventilation, electrical power supply, gas piping, plumbing, and incinerator. It is readily apparent that separation of the unit from its common elements would render each valueless, and logically any such separation should be prevented, but to do so might be construed as restraining alienation. Separation or subdivision of a unit, or of a unit from its share of the common elements was prohibited, and section 448.210 avoided the effect of the rule against restraints on alienation.

It is further provided that any instrument affecting a unit shall be applicable to the common elements incident to that unit whether mentioned in the instrument or not. This might be considered as interference with freedom not to alienate an interest, and treated as analogous to a restraint on alienation.

No unit owner is permitted to bring a partition action for division of the common elements, but the co-owners of a unit may seek partition of that unit, other than in kind, where such right would otherwise be available to them. Thus, a court by partition sale may dispose of a unit concurrently held by two or more owners who cannot agree on disposition. This could occur where a unit has been devised to or inherited by several persons as tenants in common or where there is an expressly created joint tenancy (excluding a tenancy by the entirety). Since it may be impractical for the co-owners to have joint occupancy, partition is the logical solution. The prohibition on partition in kind might be considered a restraint on alienation, but is protected by section 448.210.

It is possible that the building could be totally or substantially destroyed, the insurance proceeds could fall short of the amount necessary to reconstruct, and all this might occur at a remote date. If the unit owners will supply the difference needed, there is no problem, but what follows if they are not willing to do so? The statute allows the owners 180 days to act, after which the board of managers may record a notice which has the effect of converting all interests into a tenancy in common with the declaration percentages applying, and all liens which formerly were against individual units become liens against the interests of the various tenants in common. It should be noted that here each owner has been divested of his interest receiving in its stead a new type of property interest. This change in character of the interest owned might be viewed as an executory interest normally subject to the Rule Against Perpetuities. The notice filed by the board of managers after the 180 day period also makes the property subject to partition action so that it may be sold, and the proceeds plus the insurance moneys divided.

38. FHA Model Act § 2. (f).
39. See Haeussler v. Missouri Iron Co., 110 Mo. 188, 19 S.W. 75 (1892), holding a perpetual covenant not to partition void as a restraint on alienation.
40. § 448.050 (2).
41. § 448.050 (2).
42. § 448.050.
43. § 448.070.
44. § 448.140 (1), (2), (3).
in proportion to the interests, less applicable liens.\textsuperscript{45} Absent this provision, the unit owners would continue to own their air lots individually, and the problems of getting the property back into some productive use would be, from a practical point of view, incapable of solution. Some jurisdictions have handled the problem by giving each unit owner a fee simple determinable, terminating upon destruction of the property concurrent with non-agreement to rebuild. However, lending institutions are hesitant to make loans on anything less than a fee simple absolute even though in this case the determining event would be a condition precedent to their receiving the insurance proceeds under the loss payable clause.\textsuperscript{46}

Another instance where the exemption from the rule against unreasonable restraints on alienation was necessary is found in section 448.160 which requires a unanimous vote of all unit owners and lienholders before the project can be removed from the condominium statute and converted into a corporate or trust cooperative or some other disposition made of it.

Because of the changing character of the neighborhood and natural deterioration of the building over the years, a time could be reached when the property is obsolete for use as a condominium apartment house. The act permits certain minimum percentages of unit owners (varying with the number of units in the project) to elect to sell the property.\textsuperscript{47} In such a case, the buyer would take by a shifting executory interest as to the owner of a unit who was opposed to the sale, as if a power of appointment had been exercised. Executory interests are subject to the Rule Against Perpetuities, and are void if by any conceivable course of events the conditions precedent may happen and the interests vest more remotely than a period of lives in being and a period of twenty-one years thereafter and any actual periods of gestation.\textsuperscript{48} In jurisdictions applying the rule, unless lives are named, a gross period of twenty-one years is allowed for vesting.\textsuperscript{49} The sale pursuant to election might occur more remotely than the allowable perpetuities period. Our statute exempts this part of the act from the effects of the perpetuities rule.

As stated in the beginning of this section, the statute provides that the Rule Against Perpetuities and the rule against unreasonable restraints on alienation “shall not be applied to defeat any of the provisions of this chapter.” If a by-law is adopted attempting to restrict who shall be a future owner by controlling the right of sale of a unit, the rule against unreasonable restraints on alienation and the Rule Against Perpetuities would seem to be applicable, and to be safe, must be taken into account, for the by-law is not required by the act, and the effect of these property rules would only be inapplicable where their application would

\textsuperscript{45} § 448.140 (4).
\textsuperscript{47} § 448.150.
\textsuperscript{48} Eckhardt & Peterson, \textit{Possessory Estates, Future Interests and Conveyances in Missouri}, § 66, 23 V.A.M.S. 59 (1952).
\textsuperscript{49} In California, unlike Missouri, the rule applies to condominium legislation, and it is said to have been customary to provide that the interest shall be effective until “twenty-one years after the death of the survivor of the now living descendants of John F. Kennedy, President of the United States of America.” Berger, \textit{Condominium: Shelter on a Statutory Foundation}, 63 Colum. L. Rev. 987, 1019, n. 192 (1963).
defeat any of the provisions of the chapter. If a right of first refusal is given to the board of managers, this will not be a restraint on alienation, but it is in the nature of an option and subject to the Rule Against Perpetuities. Of course, since the Supreme Court decisions in Shelley v. Kraemer and Barrows v. Jackson, it is certain that the courts will not enforce any by-law which permits discrimination based on religion, race, or color.

III. Conclusion

No attempt has been made here to cover all problems which may arise nor to explain the statute in great detail, for there may develop conflicts between the act and existing law which are not obvious and cannot be readily anticipated. For example, lawyers working with clients on condominium projects should give special attention to zoning, platting, and subdivision acts and their effect on the project. As with all new legislation, the courts will have to do a great deal of interpretation as the problems reach them.

A note of caution should be sounded to the potential condominium buyer. While condominium has the tax advantages of ownership as one of the stronger arguments in its favor, investment should not be based solely on the hope of gaining tax deductions. Former Special Assistant Secretary of the Treasury, Dan T. Smith, in proposing tax reforms, suggested, "It would be preferable not to allow deductions for any taxes paid. . . . It would help remove the present discrimination in favor of homeowners who can deduct their property taxes, while renters have no deduction for any part of their rent." His article continues the attack saying, "The interest deduction gives a further benefit to homeowners with mortgages over renters. . . . The deduction might well be removed as part of a general reform." This typifies the thinking of some governmental economic advisers, and should remind existing and potential property owners that they have no vested interest in the present deductions, which Congress may revoke at any future time.

In the last analysis, success of condominium depends on the acceptance by the general public and lending institutions. Lenders may object to the greater cost of processing many small mortgages, as opposed to a single large one, but these costs are normally passed on to the borrower. Life insurance companies, finding a particular appeal in the opportunity to sell mortgage life insurance to each mort-

50. Gale v. New York Center Community Cooperative, 21 Ill.2d 86, 171 N.E.2d 30 (1961), holding that the right of first refusal merely provides an alternative buyer.
52. 346 U.S. 249 (1953).
53. California held a condominium building to be a subdivision. See Ross, Condominiums in California—The Verge of an Era, 36 So. Cal. L. Rev. 351, 370 (1963). Also see Note, 3 Melbourne L. Rev. 535 (1962), for a case where a city refused a condominium plat as it was not a proper subdivision plat as required by the ordinance.
55. Id. at 68.
gagor, may be expected to seek out such loans. Undoubtedly, the greatest concern is the fear of a repetition of the disaster which overtook cooperative apartments during the last depression.66 Foreclosures always seem to reach a peak in the depths of economic depression, and it is at this same point that resale prices fall to an all-time low. Lenders might also fear that individual condominium units will not be as salable at foreclosure as an entire apartment house might be. At least to date, FHA insured loans have not been as favorable as to required percentage of down payment on condominiums as on other types of cooperative apartments, and this has resulted in most condominiums being constructed for the higher income group who can afford larger down payments. Prices and mortgage payments have not been within the financial ability of the great bulk of would-be purchasers. Construction has concentrated in areas of high cost land and has appealed to childless couples or "senior citizens." The typical units would not attract the segment of the buying public seeking to house a family, generally not having been designed for family living. Essentially, the market would be restricted to the high income couple who no longer have children at home, and who desire to live in an area of high population density. This considerably limited market for purposes of resale in the event of foreclosure could tend to cause lenders to prefer loans on other types of property which have a wider appeal. Factors such as described affect the public's interest which in turn influences the lender's attitude, and thus determine the future of the condominium in Missouri.

WILLIAM H. KARCHMER

66. "[M]any such buildings were lost through foreclosure with the result that the movement all but disappeared." RAMSEY, CONDOMINIUM: THE NEW LOOK IN CO-OPS 3 (1961).