

## Memorandum on Special Declarant Rights

FROM: Jim Smith, Reporter

TO: Subcommittee on Special Declarant Rights: Bill Breetz, Carl Lisman, Dave Ramsey

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This Subcommittee will prepare a new draft of the provisions dealing with transfers of special declarant rights. Special declarant rights exist only if reserved by the declarant in the declaration.<sup>1</sup> UCIOA authorizes 10 types of special declarant rights, defined in Section 1-103(33):

“Special declarant rights” means rights reserved for the benefit of a declarant to:

(A) complete improvements indicated on plats and plans filed with the declaration or, in a cooperative, to complete improvements described in the public offering statement pursuant to Section 4-103(a)(2);

(B) exercise any development right;

(C) maintain sales offices, management offices, signs advertising the common interest community, and models;

(D) use easements through the common elements for the purpose of making improvements within the common interest community or within real estate which may be added to the common interest community;

(E) make the common interest community subject to a master association;

(F) merge or consolidate a common interest community with another common interest community of the same form of ownership

(G) appoint or remove any officer of the association or any master association or any executive board member during any period of declarant control;

(H) control any construction, design review, or aesthetic standards committee or process;

(I) attend meetings of the unit owners and, except during an executive session, the executive board; and

(J) have access to the records of the association to the same extent as a unit owner.

Section 3-104, *Transfer of Special Declarant Rights*, as it presently stands covers all voluntary and involuntary transfers of special declarant rights. The section is long and complicated. It addresses two major issues: (1) What are the liabilities of other original declarant and subsequent transferees (defined as successor declarants) after a transfer of one or more special declarant rights? (2) What happens to special declarant rights when a mortgage lender or other lienholder forecloses on property owned by a declarant? The November 2020 draft reorganizes existing Section 3-104 into three sections: Section 3-104, *Transfer of Special Declarant Rights*, Section 3-104A, *Liability after Transfer of Special Declarant Rights*, and Section 3-104B, *Foreclosure of Special Declarant Rights*. At the end of this memorandum, Appendix 1 contains all of the November 2020 draft of these sections with Reporter’s Notes and selected Comments.

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<sup>1</sup> UCIOA § 2-105(a)(8), quoted in note 2 *infra*.

The Drafting Committee at its prior meetings extensively discussed the nature of special declarant rights; specifically, are they real property or personal property? The question is of more than theoretical interest. It has consequences as to how special declarant rights are transferred and how lenders and other persons may foreclose on them. The existing UCIOA text does not give a definitive answer, although some language tends to indicate that at least some of the special declarant rights are real property.<sup>2</sup> The November 2020 draft does not attempt to resolve the question. Instead the draft presented two alternatives for the Committee to consider. Alternative 1 views special declarant rights as contract rights (personal property) that allow the declarant to alter the legal status of real estate and to exercise rights concerning governance of the common interest community. Alternative 2 views special declarant rights as appurtenant to particular parcels of real estate (real property). This means that their ownership may not be severed from those particular parcels. At the November 2020 meeting, the Committee did not endorse either Alternative. Instead, a consensus emerged that prefers the simplicity and flexibility of Alternative 1, which drops many of the restrictions on transfer in existing Section 3-104; but the Committee prefers to define all special declarant rights as real property. This subcommittee is charged with the task of implementing this plan, which may prove to be challenging.

Other issues concerning special declarant rights, which emerged during our November 2020 discussion, are:

1. What must the declaration say about special declarant rights? Carl Lisman reported that Vermont declarations often have a generic declaration: The declarant hereby reserves all special declarant rights. If special declarant rights are real property (servitudes) it seems that the declaration must describe the servient estate (the real estate that is subject to the special declarant rights).
2. What happens if development rights or other special declarant rights relate to land not yet owned by the declarant? The declarant may have an option to buy adjacent land, or the declarant may simply hope to acquire adjacent land when and if it becomes available.
3. What provisions should be added to make special declarant rights as financeable as possible?
4. Does bankruptcy present issues concerning special declarant rights, which UCIOA's treatment of special declarant rights may affect? E.g., if a declarant enters bankruptcy and special declarant rights are contract rights, are they rejectable as executory contracts?

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<sup>2</sup> UCIOA § 2-105, *Contents of Declaration*: “(a) The declaration must contain: . . . (8) a description of any development right and other special declarant rights reserved by the declarant, together with a legally sufficient description of the real estate to which each of those rights applies, and a time limit within which each of those rights must be exercised; . . .” UCIOA does not say what happens if the declaration has a reservation but fails to describe real estate or describes it insufficiently. Possible omission means the rights do not exist.

5. What happens under Section 3-104A if a new developer uses a facility constructed by the original declarant? David Ramsey gave the example of a detention pond built in Phase 1, with a new developer for Phase 2 using the detention pond for Phase 2. Section 3-104A(e) may mean that the new developer does not undertake liability for defects in the detention pond.

## Appendix 1

### SECTION 3-104. TRANSFER OF SPECIAL DECLARANT RIGHTS.

*Note: In the process of preparing proposed amendments to this section, the discussions of the Drafting Committee have revealed a fundamental and practical issue regarding the nature of special declarant rights. There are 10 types of special declarant rights, defined in Section 1-103(33), which exist only if reserved by the declarant in the declaration recorded to create the common interest community. The first view considers special declarant rights to be contract rights that allow the declarant to alter the legal status of real estate and to exercise rights concerning governance of the common interest community. This means that the rights are personal property and generally freely alienable, whether or not conveyed with real estate to which they apply. The second view considers special declarant rights to be appurtenant to particular parcels of real estate. This means that their ownership may not be severed from those particular parcels. This draft contains two alternatives for further consideration (Alternative 1 and Alternative 2), which try to implement the two competing views, respectively. THESE ALTERNATIVES ARE NOT PROPOSED AS ALTERNATIVES TO BE RECOMMENDED TO THE STATES IN THE FINAL ACT; rather they are intended to assist in further discussion, with the thought that the final act will pick one of these alternatives or some variation thereof.*

#### Alternative 1

(a) A declarant may transfer a special declarant right (~~Section 1-103(29)) created or reserved under this [act] may be transferred~~ only by an instrument evidencing the transfer recorded in every [county] in which any portion of the common interest community is located. The instrument is not effective unless executed by the transferee. executed by both parties.

(b) Except as otherwise provided in Section 3-104B(c), a declarant that transfers fewer than all its special declarant rights retains the special declarant rights that are not transferred.

#### Alternative 2

(a) A declarant may transfer a special declarant right (~~Section 1-103(29)) created or reserved under this [act] may be transferred~~ only by an instrument evidencing the transfer recorded in every [county] in which any portion of the common interest community is located.

The instrument is not effective unless executed by the transferee, only to a person that owns real estate to which the special declarant right applies, as described in the declaration under Section 2-105(a)(8). The transfer must be evidenced by an instrument executed by both parties.

(b) If a declarant transfers fewer than all its special declarant rights, the declarant retains only its special declarant rights that are appurtenant to real estate the declarant continues to own as described in the declaration under Section 2-105(a)(8). Other special declarant rights automatically terminate.

### **End of Alternatives**

(c) An instrument that transfers a special declarant right must be recorded in every [county] in which any portion of the common interest community is located. The instrument is not effective until recorded.

### **Reporter's Note (10/23)**

Observations from our August 2020 informal Zoom session on the act included:

- (1) We should provide clear rules for the transfer, financing, and encumbering of special declarant rights.
- (2) Development rights are often especially valuable, and their transfers are common.
- (3) Under the act as it stands now, title insurance companies are not willing to issue insurance on transfers of special declarant rights.

### **Reporter's Notes**

1. The Study Committee Report (topic # 15) calls for consideration of issues concerning declarant liability and the liability of successor declarants, both those who are affiliates and not affiliates of the original declarant. See Study Committee Report pp. 51-58.

The Drafting Committee at its January 2020 meeting discussed many of the issues and asked the committee Chair and the Reporter to attempt to rewrite and reorganize the set of rules contained in existing Section 3-104. Their effort included the division of content from existing Section 3-104 into a series of six

new sections in the April 2020 meeting draft and the addition of a new definition of “Non-affiliate successor,” now in Section 3-104A below, which serves as a companion to the existing definition of “Affiliate of a declarant” in Section 1-103(1). Discussion by the Drafting Committee at its April 2020 meeting resulted in the Reporter’s consolidation of the material into three sections: Section 3-104 (above) and Sections 3-104A and 3-104B (below).

2. The Drafting Committee at its April 2020 meeting discussed whether special declarant rights are real property or personal property. UCOIA as presently drafted may assume that special declarant rights are real property, but it does not say so directly. Some cases hold that development rights are real property in some contexts. E.g., *Village at Treehouse, Inc. v. Property Tax Adm'r*, 2014 COA 6, 321 P.3d 624 (Colo. Ct. App. 2014) (condominium development rights are “interests in real property” subject to ad valorem taxation); *Layden v. City of Rutland*, 737 A.2d 894 (Vt. 1999) (development rights acquired with undeveloped land in condominium project are subject to ad valorem taxation). But some of the special declarant rights, perhaps most of them, may be intangible personal property (contract rights). If so, in financing transactions they are general intangibles under UCC Article 9. The Committee did not reach a consensus at its April 2020 meeting on how to handle the issue of classification. It requested that the Reporter consider two approaches: deferring to other law to make the determination or adding provisions making all special declarant rights real property interests or treating them as if they are real property. The two Alternatives in this section and in Section 3-104B below attempt to implement these two approaches.

3. Alternative 1 in subsections (a) and (b) addresses to a concern raised by the Study Committee based on a sentence in existing Comment 3 to Section 3-104: “The transfer by a declarant of all of his interest in a project to a successor without a concomitant transfer of the special rights of a declarant pursuant to this subsection, results in the automatic termination of such special declarant rights and of any period of declarant control.” See Study Committee Report p. 56 (Issue Six). The Drafting Committee at its January 2020 meeting discussed this issue, with the consensus that special declarant rights that are not transferred remain with the declarant. The Comment does not have support in the existing statutory language. Alternative 1 calls for the opposite outcome, and if adopted, Comment 3 should be deleted (see Comment 3 below).

4. Alternative 1 also responds to a question raised by the Study Committee. The Study Committee asks whether there should be limits on how many persons may receive and hold special declarant rights at one point in time, asking whether it would be preferable to identify a single declarant who is in control and responsible. See Study Committee Report p. 55 (Issue Four). The Drafting Committee at its January 2020 meeting discussed the issue, with the

consensus that the intent of existing Section 3-104 is not to limit transfers and the fragmentation of special declarant rights. Alternative 1 in subsections (a) and (b) makes it clearer that the act imposes no limits. Usually a developer will not find it advantageous to divide special declarant rights among more than a few persons. Fragmentation when it occurs may sometimes make it harder for third parties, including unit owners, to determine who holds what special declarant rights and who is responsible for certain obligations and liabilities. The recording rule discussed above (Note 3) and the reorganization of the rules addressing obligations and liabilities (see new sections below) should allow third parties to find this information.

5. Alternative 2 reflects the practical reality that special declarant rights have value only when connected to real estate within the common interest community or that may be added to the community interest community pursuant to a development right reserved in the declaration. In addition to describing all special declarant rights reserved by the declarant, the declaration must identify the real estate that is subject to special declarant rights. Section 2-105(a)(8) requires that the declaration contain “a description of any development right and other special declarant rights reserved by the declarant, together with a legally sufficient description of the real estate to which each of those rights applies, and a time limit within which each of those rights must be exercised.” This requirement may imply a legal linkage between special declarant rights and parcels of real estate. If the rights are real property, they do not qualify as servitudes (a real covenant or equitable servitude running with the land) because a person cannot own a servitude in his own property. In other words, if the declarant has a development right to create units on undeveloped real estate owned by the declarant, that right is not a servitude. *Restatement (Third) of Property (Servitudes)* § 7.5 comment a (2000) (“A servitude benefit is the right to use the land of another”); *Woodling v. Polk*, 473 S.W.3d 233 (Mo. Ct. App. 2015) (deed purporting to grant driveway easement to developer over one of its lots does not create easement). But the rights may still be real property if they are viewed as appurtenant to the ownership of land.

6. A transfer of a special declarant right does not have to consist of the entire special declarant right. For example, a declarant may own an undeveloped 50-acre parcel within a 300-acre common interest community. The declarant decides to sell the 50-acre parcel to another developer, and along with the conveyance of the parcel, the declarant transfers development rights and the right to maintain a sales office with respect to the 50-acre parcel. The declarant retains development rights and sales-office rights for his remaining 250 acres. The buyer becomes a successor declarant.

7. The Study Committee questions whether a transfer of special declarant rights should be effective between the transferor and transferee before recordation. See Study Committee Report p. 54 (Issue Two). The language of existing Section 3-104(a) appears to indicate the transfer is effective only upon

recordation. The Drafting Committee at its January 2020 meeting discussed the issue, with the consensus that recording is necessary. New subsection (c) makes this explicit, tracking the language used in Section 2-118(b) for the effectiveness of termination agreements. This is an exception to the normal rule that agreements and conveyances are effective between the parties when executed, prior to recordation. The purpose of delaying effectiveness, even between the parties, is to perform a notice function. Recording allows all third parties, including unit owners, to ascertain who holds and may exercise special declarant rights at all times, and thus who has obligations and liabilities stemming from special declarant rights.

At its April 2020 meeting the Drafting Committee discussed new subsection (c) and whether to require the sending of notice of the transfer of special declarant rights to all unit owners. New Jersey requires that when a declarant amends its public offering statement, the declarant must notify prior buyers of units. After discussion, the consensus was not to make a change to require notice.

### Comment

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3. ~~Subsection (a)~~ This section provides that a successor in interest to a declarant may acquire the special rights of the declarant only by recording an instrument which reflects a transfer of those rights. This recordation requirement does not mean that special declarant rights are real property. Recording is important to determine the duration of the period of declarant control pursuant to Section 3-103(d) and (e), as well as to place unit owners on notice of all persons entitled to exercise the special rights of a declarant under this Act. ~~The transfer by a declarant of all of his interest in a project to a successor without a concomitant transfer of the special rights of a declarant pursuant to this subsection, results in the automatic termination of such special declarant rights and of any period of declarant control.~~

Other state law determines whether special declarant rights are real property or personal property. Some are almost certainly intangible personal property; for example, the declarant's right to appoint or remove association officers and board members and the declarant's right to make a common interest community subject to a master association. Some are sufficiently connected to real estate that they may be servitudes; for example, a declarant's right to use easements to make improvements and a declarant's development right over land owned by another person. If a special declarant right is a servitude, it is a servitude in gross. See *Restatement (Third) of Property (Servitudes)* § 2.6 (2000): "The benefit of a servitude may be created to be held in gross, or as an appurtenance to another interest in property . . . ." Special declarant rights, if servitudes, are not appurtenant servitudes because this section makes all special declarant rights freely alienable to any person, regardless of whether that person acquires or owns units or other real estate.

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## Reporter's Notes

1. The above proposed revisions to Comment 3 reflect Alternative 1. If Alternative 2 is adopted, different revisions to the Comment will be needed. The Comment revisions delete the last sentence of the first paragraph of Comment 3 because it is inconsistent with the existing statutory text of Section 3-104 and with Alternative 1. See Reporter's Note 3 to Section 3-104 (above).

2. Alternative 1 makes special declarant rights freely transferable, but it is agnostic as to whether they are personal or real property. The Comment revisions clarify that the recording requirement does not imply that special declarant rights are real property. The new proposed second paragraph to Comment 3 offers brief guidance on the issue of classification.

3. Alternative 2 in subsection (b) incorporates the substance of the last sentence of the first paragraph of Comment 3. See Reporter's Note 5 to Section 3-104 (above).

4. The proposed new language at the end of the first paragraph of Comment 3 clarifies that the recording requirement does not imply that special declarant rights are real property.

### **SECTION 3-104A. LIABILITY AFTER TRANSFER OF SPECIAL DECLARANT**

#### **RIGHTS.**

(a) In this section, "non-affiliate successor" means a person that succeeds to a special declarant right and is not an affiliate of the declarant that transferred the special declarant right to the person.

(b) ~~Upon transfer of any special declarant right, the liability of a transferor declarant is as follows:~~

~~(1) A transferor is not relieved of any obligation or liability arising before the transfer and remains liable for warranty obligations imposed upon him~~ If a transferor declarant transfers a special declarant right to an affiliate of the declarant, the transferor and the successor are jointly and severally liable for all obligations and liabilities imposed upon either party by this [act] or the declaration. Lack of privity does not deprive ~~any~~ a unit owner of standing to

maintain an action to enforce ~~any~~ an obligation or liability of the transferor or transferee.

~~(2) If a successor to any special declarant right is an affiliate of a declarant (Section 1-103(1)), the transferor is jointly and severally liable with the successor for any obligations or liabilities of the successor relating to the common interest community.~~

~~(3) If a transferor retains any special declarant rights, but transfers other special declarant rights to a successor who is not an affiliate of the declarant, the transferor is liable for any obligations or liabilities imposed on a declarant by this [act] or by the declaration relating to the retained special declarant rights and arising after the transfer.~~

~~(4) A transferor has no liability for any act or omission or any breach of a contractual or warranty obligation arising from the exercise of a special declarant right by a successor declarant who is not an affiliate of the transferor.~~

(c) If a declarant transfers a special declarant right to a non-affiliate successor, the transferor remains liable for any obligation or liability arising before the transfer, including a warranty obligation imposed on the transferor by this [act]. The transferor is not liable for any obligation or liability arising after the transfer which is imposed on the successor by this [act] or the declaration relating to the transferred special declarant right.

~~(c) Unless otherwise provided in a mortgage instrument, deed of trust, or other agreement creating a security interest, in case of foreclosure of a security interest, sale by a trustee under an agreement creating a security interest, tax sale, judicial sale, or sale under Bankruptcy Code or receivership proceedings, of any units owned by a declarant or real estate in a common interest community subject to development rights, a person acquiring title to all the property being foreclosed or sold, but only upon his request, succeeds to all special declarant rights related to that property held by that declarant, or only to any rights reserved in the~~

~~declaration pursuant to Section 2-115 and held by that declarant to maintain models, sales offices, and signs. The judgment or instrument conveying title must provide for transfer of only the special declarant rights requested.~~

~~(d) Upon foreclosure of a security interest, sale by a trustee under an agreement creating a security interest, tax sale, judicial sale, or sale under Bankruptcy Code or receivership proceedings, of all interests in a common interest community owned by a declarant:~~

~~(1) the declarant ceases to have any special declarant rights, and~~

~~(2) the period of declarant control (Section 3-103(d)) terminates unless the judgment or instrument conveying title provides for transfer of all special declarant rights held by that declarant to a successor declarant.~~

~~(e) (d) The liabilities and obligations of a person who succeeds to special declarant rights are as follows:~~

~~(1) A Except as otherwise provided in this section, a successor to any a special declarant right who is an affiliate of a declarant is subject to all obligations and liabilities imposed on the transferor by this [act] or by the declaration.~~

~~(e) A non-affiliate successor that acquires fewer than all special declarant rights held by the transferor is not subject to an obligation or liability that relates to special declarant rights not transferred to the successor.~~

~~(2) A successor to any special declarant right, other than a successor described in paragraph (3) or (4) or a successor who is an affiliate of a declarant, is subject to the obligations and liabilities imposed by this [act] or the declaration:~~

~~(i) on a declarant which relate to the successor's exercise or nonexercise of special declarant rights; or~~

~~(ii) on his transferor, other than:~~

(f) A non-affiliate successor is not subject to an obligation or liability that relates to:

~~(A) (1)~~ a misrepresentations by any a previous declarant;

~~(B) (2)~~ a warranty obligations on an improvements made by any a previous declarant; or made before the common interest community was created;

~~(C) (3)~~ breach of any a fiduciary obligation by any a previous declarant or his the previous declarant's appointees to the executive board; or

~~(D) (4) any liability or obligation~~ an obligation or liability  
imposed on the transferor as a result of the transferor's acts or omissions after the transfer.

~~(3) (g) A successor to only a right reserved in the declaration to maintain models, sales offices, and signs (Section 2-115);~~ A non-affiliate successor to which only a special declarant right to maintain an office, sign, or model is transferred may not exercise any other special declarant right; and is not subject to any obligation or liability or obligation as a declarant, except the an obligation to provide or liability related to a public offering statement [,] and any liability arising as a result thereof [,] and an obligations under [Article] 5].

(h) A successor that acquires a special declarant right after foreclosure of a security interest, tax sale, judicial sale, or sale in a bankruptcy or receivership proceeding and complies with the requirements of Section 3-104B is not subject to an obligation or liability as a declarant other than liability under Section 3-103(d) for the successor's act or omission.

### **Reporter's Notes**

One concern raised by the Study Committee is whether the existing language of Section 3-104(b) is sufficiently clear with respect to the allocation of liability for warranties between the transferor declarant and the transferee declarant. The proposed amendments clarify the issue. When the transferee is an affiliate, the joint and several liability of both parties under Section 3-104A(b) "for all obligations and liabilities" includes all warranty obligations, regardless of

when improvements are made and when a breach occurs.

When a transferor declarant transfers a special declarant right to a non-affiliate successor, under Section 3-104A(c) the transferor remains liable for “a warranty obligation imposed on the transferor.” A transferee declarant who is not an affiliate of the transferor becomes liable for all warranty obligations except for “a warranty obligation on an improvement made by a previous declarant or made before the common interest community was created” under Section 3-104B(f)(2). In other words, the transferee declarant is liable for warranties on improvements made after its acquisition of special declarant rights.

#### **SECTION 3-104B. FORECLOSURE OF SPECIAL DECLARANT RIGHTS.**

(a) In this section, “foreclosure sale” means a sale of property owned by a declarant pursuant to a foreclosure of a security interest, deed in lieu of foreclosure, tax sale, judicial sale, or sale in a bankruptcy or receivership proceeding.

***Note: Below are two alternatives following the choices indicated in Section 3-104 (above). Alternative 1 treats special declarant rights as free-standing rights that are usually personal property. Alternative 2 treats special declarant rights as appurtenant to real estate.***

##### **Alternative 1**

(b) If a foreclosure sale of real estate includes a special declarant right, the purchaser may elect to acquire or reject the special declarant right. The judgment or instrument conveying title must provide for transfer of only the special declarant rights acquired.

##### **Alternative 2**

(b) Unless an instrument creating the security interest being foreclosed provides otherwise, a person acquiring title to all property being foreclosed may request to acquire all special declarant rights related to the property held by the declarant or only to a special declarant right to maintain an office, sign, or model pursuant to Section 2-115. The judgment or instrument conveying title must provide for transfer of only the special declarant rights acquired.

##### **End of Alternatives**

(c) If, after a foreclosure sale, the declarant no longer owns real estate in a common

interest community:

(1) the declarant ceases to have any special declarant rights, and

(2) the period of declarant control (Section 3-103(d)) terminates unless the judgment or instrument conveying title provides for transfer of all special declarant rights held by the declarant to a successor declarant.

~~(4) (d) A successor to all special declarant rights held by a transferor who succeeded to those rights pursuant to a deed or other instrument of conveyance in lieu of foreclosure or a judgment or instrument conveying title under subsection (c); A purchaser of a special declarant right at a foreclosure sale is a successor declarant that may declare its intention in a recorded instrument the intention to hold those rights solely for transfer to another person. Thereafter, until transferring all special declarant rights to any person acquiring title to any unit or real estate subject to development rights owned by the successor, or until recording an instrument permitting exercise of all those rights, that successor may not exercise any of those rights~~ After recording the instrument, the successor declarant may not exercise a special declarant right, other than any a right held by his the transferor to control the executive board in accordance with Section 3-103(d) for the duration of any period of declarant control, and any attempted attempt to exercise of those rights a special declarant right in violation of this section is void.

#### **Alternative 1**

The successor declarant, before the period for exercising a special declarant right expires pursuant to Section 2-105(a)(8), may transfer some or all its special declarant rights to any person.

#### **Alternative 2**

The successor declarant, before the period for exercising a special declarant right expires pursuant to Section 2-105(a)(8), may transfer some or all its special declarant rights to a person acquiring title to real estate to which the special declarant right applies, as described in the declaration.

### ***End of Alternatives***

(e) ~~So~~ As long as a successor declarant ~~may not exercise special declarant rights under this subsection~~ described in subsection (d) complies with this section, the successor declarant is not subject to any obligation or liability ~~or obligation~~ as a declarant other than liability for ~~his~~ its acts and omissions under Section 3-103(d).

~~(f) Nothing in this section subjects any successor to a special declarant right to any claims against or other obligations of a transferor declarant, other than claims and obligations arising under this [act] or the declaration.~~

### **Reporter's Notes**

1. This proposed new section is a reorganization of the parts of existing Section 3-104 that address foreclosure sales with the transfer of special declarant rights from the defaulting declarant to a foreclosure purchaser. In the draft for the April 2020 Drafting Committee meeting, the Chair and Reporter reorganized without attempting to make changes of substance to the existing statutory text.

The Reporter, however, recommends that the Drafting Committee review the substance and consider whether changes are advisable, either to make changes of substance or to clarify how the provisions are intended to operate. Points to discuss include the following:

- The scope of the provision is the foreclosure of real estate when the declarant owns development rights. Development rights are defined in Section 1-201(16) and they are one of the ten types of special declarant rights. See Section 1-201(33)(B). What if the declarant does not have development rights at the time of the foreclosure but owns other special declarant rights? Should the scope be expanded to cover transfer of special declarant rights in this situation?
- The provision may mean that the foreclosure purchaser has three choices: take all of the declarant's special declarant rights, take none

of them, or take only the special declarant right under Section 1-201(33)(C) to maintain offices, signs, and models. Should the purchaser have the right to “pick and choose,” the same as in a voluntary transfer under Section 3-104 above?

- The Reporter believes that most of the special declarant rights defined in Section 1-201(33) are intangible personal property; specifically, general intangibles under UCC Article 9. The existing provision appears to treat special declarant rights as if they are real property. Although the statute does not say this directly, Section 3-104 Comment 7 states that a declarant’s “right to create additional units . . . is an interest in land which may be sold or in which a security interest may be granted.” UCOIA defines “security interest” as “an interest in real estate or personal property, created by contract or conveyance, which secures payment or performance of an obligation.” We should consider how our Section 3-104C, D, and E provisions fit with Article 9.
- Which involuntary transfers should the provision cover? Section 3-104 Comment 7 refers to “a conveyance in lieu of foreclosure” but this is not in the statutory text.
- The provision appears to contemplate that a foreclosure sale will transfer all of the declarant’s units and real estate in the community. What if a foreclosure or other involuntary sale transfers only some of the declarant’s units or property? Is that within the scope of the provision, and if so, what happens?

At its April 2020 meeting the Drafting Committee discussed these questions and other issues, with the consensus that further redrafting including changes in substance is desirable.

2. New subsection (a) serves as a scope provision for this section with a new definition of “foreclosure sale.” The scope is expanded to cover any foreclosure of special declarant rights. The new definition also expressly includes a deed in lieu of foreclosure. Although almost always the creditor’s foreclosure will consist of the sale of both real estate and special declarant rights, subsection (a) does not require the sale of real estate; the definition refers to “a sale of property owned by declarant.” In principle, a creditor may foreclose only on special declarant rights, presumably in order to transfer them to a person who already owns real estate or has a stake in the common interest community.

Like existing Section 3-104(c), subsection (a) uses the term “security interest,” which is broadly defined in the Act to include interests created by mortgages, deeds of trust, and UCC Article 9 security agreements. Section 103(32). Therefore, the defined term “foreclosure sale” includes a



foreclosure of personal property under UCC Article 9.

3. Alternative 1 in subsections (b) and (d) reflects the principles that special declarant rights are freely transferable as a general matter and in the context of foreclosures. Existing section 3-104(c) appears to give the foreclosure purchaser the right to obtain special declarant rights, whether or not the mortgage lender's security agreement includes special declarant rights as part of the collateral. Those rights appear to be automatically tied to the real estate. Instead, this new section transfers special declarant rights to a purchaser only if "a foreclosure sale of real estate includes a special declarant right" under Alternative 1 subsection (b). As explained in the proposed Alternative 1 revision to Section 3-104 Comment 3 (above), the special declarant rights may be real property (appurtenant rights or servitudes in gross) or intangible personal property, subject to UCC Article 9. This new section applies only if (1) the mortgage lender's collateral includes special declarant rights and (2) the mortgage lender has organized its foreclosure sale to include the sale of special declarant rights. This Act does not tell a mortgage lender how to obtain a security interest in special declarant rights.

If the special declarant rights are personal property, the mortgage lender has mixed collateral. It may foreclose using the foreclosure procedures of Article 9. If the mortgage lender is selling units or other real estate at the same time, the mortgage lender may choose to sell both types of collateral at a real estate foreclosure. See UCC § 9-604 (*Procedure if Security Agreement Covers Real Property or Fixtures.*)

Similar issues arise with respect to the other types of involuntary sales within the scope of this section. In bankruptcy, the declarant's bankruptcy estate consists of all of the declarant's property, so a bankruptcy sale may include the declarant's special declarant rights. Tax sales and judicial sales are within the scope only if the subject of those sales includes the declarant's special declarant rights, whether they are real or personal property.

4. Alternative 1 in subsections (b) deletes the provision in existing section 3-104(c) allowing the foreclosure purchaser to request only the right to maintain model units, sales offices, and signs. According to section 3-104 Comment 7, this provision "is designed to protect mortgage lenders and contemplates the situation where a lender takes over a project and desires to sell out existing units without making any additional improvements to the project." Instead of this special choice, new subsection (b) broadens the purchaser's choice by allowing the purchaser to pick and choose among any of the special declarant rights that are advertised as part of the collateral being sold at foreclosure.

5. Alternative 2 in subsections (b) and (d) preserves the substance of existing Section 3-104(c) with respect to the foreclosure purchaser's rights to obtain special declarant rights. The foreclosure purchaser always has three

choices: take all the rights, none of the rights, or only the rights to maintain offices, signs, and models. It does not matter whether the mortgage lender has a security interest in the special declarant rights. They transfer automatically if the purchaser requests them. Under subsection (d) the purchaser may transfer special declarant rights only to a person who acquires the relevant real estate to which the rights are attached.