

GUILT BY ASSOCIATION: ASSESSMENT LIABILITY TO HOMEOWNERS' ASSOCIATIONS AFTER FORECLOSURE

J. Martin Knaust*

I. INTRODUCTION

A large number of residential properties in Florida are subject to rules of homeowners' associations (HOAs).¹ HOAs are a product of their recorded declarations, which serve to establish HOA rules, authority, and powers.² One of the most significant powers HOAs possess is the ability to level assessments against the properties subject to their authority.³ Because of the recent rise in mortgage defaults, increasing numbers of individuals and businesses are taking title to properties by purchasing them at foreclosure sales.⁴ This rise in foreclosure sales presents a signifi-

* © 2012, J. Martin Knaust. All rights reserved. Associate at the law firm of Adams & Reese, LLP, Saint Petersburg, Florida. The Author practices in the firm's Corporate Transactions Department, with emphasis on institutional loan workouts and foreclosures.

1. Solomon Genet, *Homeowners' Associations in Florida: Issues & Analysis for the Real Estate Developer*, Fla. B. Real Prop., Prob. & Trust L. Section (Summer 2008) (available at <http://www.algpl.com/publications/actionlinearticle.pdf>). As of 2008, Florida had more than 11,000 HOAs. *Id.* (noting that the number of HOAs in Florida will continue to increase as developers build more communities to accommodate Florida's increasing population).

2. *See id.* (explaining that HOA documents, along with statutory requirements, determine the breadth and scope of an HOA's powers). HOAs are non-profit entities that own, manage, maintain, and repair a community's common property. *Id.* HOAs are governed by their recorded HOA documents, which define the breadth and scope of an HOA's authority, including an HOA member's obligation to pay assessments. *Id.*

3. *See* Gemma Giantomasi, Student Author, *A Balancing Act: The Foreclosure Power of Homeowners' Associations*, 72 *Fordham L. Rev.* 2503, 2511 (2004) (noting that paying assessments "is not voluntary, nor is payment at the discretion of the homeowner"). A property owner is automatically subject to an HOA's authority when the owner takes title to the property, and most HOAs may institute a lien against a property owner for unpaid assessments. *Id.* at 2509, 2516.

4. Prentiss Cox, *Foreclosure Reform amid Mortgage Lending Turmoil: A Public Purpose Approach*, 45 *Hous. L. Rev.* 683, 687-688 (2008).

cant issue because many of these properties are subject to unpaid assessments from HOAs.⁵

As this Article will explain, liability for HOA assessments can survive the transfer of title through foreclosure. Still, determining what unpaid assessments are owed to an HOA is not as clear as one might imagine. Part II discusses the foundations of liability for assessments. Part III examines in depth the nature of assessments and HOA powers regarding them. Part IV analyzes the conflict between HOA declarations and the relevant statutory language from Florida Statutes, Chapter 720.⁶ Part V offers a brief conclusion.

II. BASIS FOR ASSESSMENT LIABILITY

The HOA's right to level an assessment against properties that are subject to it stems directly from the HOA's recorded declaration.⁷ Similarly, the HOA's right to file a lien to secure these unpaid assessments must also stem from the HOA's recorded declaration.⁸ While rooted in the underlying declaration, the issue of assessment liability has been significantly modified by statute in recent years. Before 2007, Florida did not permit liability actions against previous homeowners for past-due assessments.⁹ This changed in 2007, when the Florida legislature amended Chapter 720 (HOA Statute) by adding Section 720.3085, in particular, Section 720.3085(2), which provides that "[a] parcel owner is jointly and severally liable with the previous parcel owner for all unpaid assessments that came due up to the time of transfer of title."¹⁰ Before the addition of this statutory language, an HOA could only

5. When homeowners stop paying their mortgages, they often stop paying their HOA assessments.

6. Fla. Stat. §§ 720.308–720.3085 (2011).

7. "For any community created after October 1, 1995, the governing documents must describe the manner in which expenses are shared and specify the member's proportional share thereof." *Id.* at § 720.308(1).

8. An association can place a lien on a parcel to secure payment for unpaid assessments when the association's governing documents permit such an action. *Id.* at § 720.3085(1).

9. See Fla. Stat. § 720.308 (2006) (containing no provision for liability).

10. Fla. Stat. § 720.3085 (2007).

recover unpaid assessments chargeable to a previous owner if the HOA's underlying declaration provided for such liability.¹¹

The HOA Statute underwent another significant change in 2008 when the "safe harbor" provision was added to Section 720.3085(2)(c).¹² This provision states:

Notwithstanding anything to the contrary contained in this section, the liability of a first mortgagee, or its successor or assignee as a subsequent holder of the first mortgage who acquires title to a parcel by foreclosure or by deed in lieu of foreclosure for the unpaid assessments that became due before the mortgagee's acquisition of title, shall be the lesser of:

- (1) The parcel's unpaid common expenses and regular periodic or special assessments that accrued or came due during the [twelve] months immediately preceding the acquisition of title and for which payment in full has not been received by the association; or
- (2) One percent of the original mortgage debt.¹³

Adding this safe harbor provision limits liability for assessments to the first mortgagees who take title to a property.¹⁴ There are two important limitations on this liability. First, this limitation only applies to a "[f]irst mortgagee, or its successor or assignee as a subsequent holder of the first mortgage. . . ."¹⁵ In *Bay Holdings*,

11. Compare Fla. Stat. § 720.308 (2006) (containing no joint-and-several-liability provision) with Fla. Stat. § 720.3085(2) (2007) (providing for joint and several liability with a previous parcel owner).

12. Compare Fla. Stat. § 720.3085 (2007) with Fla. Stat. § 720.3085 (2008).

13. Fla. Stat. § 720.3085(2)(c)(1)–(2) (2008).

14. It is unclear how the "[o]ne percent of the original mortgage debt" limitation would apply if the mortgage contemplates modifications and future advances that dramatically increase the amount of money secured. Would the "original mortgage debt" include these future advances? Similarly, would an amended and restated mortgage (which takes the place of the original mortgage while maintaining the first mortgage's priority position relative to other recorded liens) be the operative starting point for determining "[o]ne percent of the original mortgage debt?" Or would one start with the amended and restated mortgage? Similarly unclear is how "[o]ne percent of the mortgage debt" would be applied in a situation in which multiple properties were pledged under a single mortgage.

15. Fla. Stat. § 720.3085(2)(c) (2011).

Inc. v. 2000 Island Boulevard Condominium Association,¹⁶ the Florida Third District Court of Appeal specifically held that an assignee of a final judgment who took title to a property was not a first mortgagee, successor, or assignee within the meaning of the statute, and, therefore, did not fall under Section 718.116(1)'s safe harbor provision.¹⁷ *Bay Holdings* involved a condominium association, which is governed by Florida Statutes, Chapter 718 (the Condo Statute), whereas HOAs are governed by Florida Statutes, Chapter 720. Still, its holding is equally applicable in the HOA context.¹⁸ The ramification of this holding is that a first mortgagee who wants to take title in the name of another entity¹⁹ needs to make that determination before final judgment is entered. If the mortgage is assigned before final judgment, the assignee would become the holder of the first mortgage and would be able to avail itself of Section 720.3085(2)(c)'s safe harbor provision.²⁰

The other important limitation on the safe harbor provision requires joinder of the association in the underlying foreclosure action.²¹ This requirement is another illustration of the subtle differences between the Condo Statute and the HOA Statute. While the Condo Statute's language requiring joinder of the association is part of the "[o]ne percent of the original mortgage debt" language found in Section 718.116,²² the joinder-of-association language in the HOA Statute is found in a separate, floating paragraph after the "[o]ne percent of the original mortgage debt"

16. 895 So. 2d 1197 (Fla. 3d Dist. App. 2005).

17. *Id.* at 1197; *see* Fla. Stat. § 718.116(1) (2006) (governing condominium associations).

18. The language of the safe harbor provision governing condominium associations in Chapter 718, Florida Statutes, is virtually identical to the language of Chapter 720, Florida Statutes, governing HOAs. *Compare* Fla. Stat. § 718.116 (2011) *with* § 720.3085 (2011).

19. Banks often want to take title to a property in the name of a special-purpose entity to minimize (or rather, quarantine) possible tort liability.

20. *See Bay Holdings*, 895 So. 2d at 1197 (implying that if the subsequent assignee of a final condominium foreclosure judgment had been the first mortgagee, it would have fallen under the Condo Statute's safe harbor provision).

21. Fla. Stat. § 720.3085(2)(c)(1)–(2).

22. The Condo Statute's safe harbor provisions only apply if the first mortgagee joined the association as a defendant in the foreclosure action. Fla. Stat. § 718.116(1)(b) (2011). "Joinder of the association is not required if, on the date the complaint is filed, the association was dissolved or did not maintain an office or agent for service of process at a location which was known to or reasonably discoverable by the mortgagee." *Id.*

provision.²³ Arguably, not joining a condominium association would prevent a first mortgagee from being able to avail itself of “[o]ne percent of the mortgage debt” language, but could still limit its liability under the “[twelve] months worth of assessments” language. Conversely, it would appear that failure to join an HOA would prevent a first mortgagee from availing itself of the HOA’s safe harbor provision entirely.

Liability for unpaid assessments is still unlimited as to anyone else.²⁴ Thus, if a party with a junior lien forecloses and then takes title, he or she is responsible for all assessment obligations that accrued before the title transferred. Third-party bidders at a foreclosure sale must keep this in mind as well; the property they buy at foreclosure sales may end up costing them more than just the purchase price.

III. ASSESSMENTS

With an understanding of the statutory scope of assessment liability when title is transferred through foreclosure, the question then becomes, what exactly is an “assessment?” The HOA Statute defines an “assessment” or an “amenity fee” as:

[A] sum or sums of money payable to the association, to the developer or other owner of common areas, or to recreational facilities and other properties serving the parcels by the owners of one or more parcels as authorized in the governing documents, which if not paid by the owner of a parcel, can result in a lien against the parcel.²⁵

23. Fla. Stat. § 720.3085(2)(c)(2). This HOA provision provides:

The limitations on first mortgagee liability provided by this paragraph apply only if the first mortgagee filed suit against the parcel owner and initially joined the association as a defendant in the mortgagee foreclosure action. Joinder of the association is not required if, on the date the complaint is filed, the association was dissolved or did not maintain an office or agent for service of process at a location that was known to or reasonably discoverable by the mortgagee.

Id.

24. The HOA Statute’s safe harbor provision only limits liability for a first mortgagee or the first mortgagee’s successor in title; it does not mention limiting liability as to any other parties. *Id.* at § 720.3085(2)(c)(1)–(2).

25. *Id.* at § 720.301(1). The definition of “assessment” has not changed since 2006. *See* Fla. Stat. § 720.301(1) (2006–2011) (defining “assessment” among other terms).

In practice, it is common for attorneys representing HOAs to try to include other costs and expenses in the estoppel letters they prepare under the concept that these are also “assessments.”²⁶ These other costs and expenses are usually attorneys’ fees related to the first mortgagee’s foreclosure action, as well as attorneys’ fees and title costs related to filing a lien.²⁷

An analysis of the use of “assessment” throughout the HOA Statute seems to indicate that assessments do not include attorneys’ fees and other costs; however, Section 720.3085(5)(a) states that an association may recover reasonable attorneys’ fees incurred in filing a lien foreclosure action.²⁸ Still, Section 720.3085 of the HOA Statute, which addresses an association’s right to file a lien for unpaid assessments, clearly treats assessments as being separate and distinct from attorneys’ fees, as it provides:

The claim of lien secures all unpaid assessments that are due and that may accrue subsequent to the recording of the claim of lien and before entry of a certificate of title, *as well as interest, late charges, and reasonable costs and attorney’s fees incurred by the association incident to the collection process*. The person making payment is entitled to a satisfaction of the lien upon payment in full.²⁹

Similarly, the HOA Statute section that addresses the ways associations apply payments for assessments and installments to past-due assessments, provides in pertinent part that “[a]ny payment received by an association and accepted shall be applied first to any interest accrued, then to any administrative late fee, then to any costs and reasonable attorney’s fees incurred in collection, and then to the delinquent assessment.”³⁰

Also, Florida Statute Section 720.308, which addresses an HOA’s right to level assessments, mandates that assessments be

26. If an HOA brings an action for unpaid assessments, it is entitled to recover “reasonable” attorneys’ fees that it incurred in bringing the action. Fla. Stat. § 720.3085(5)(a) (2011). The HOA Statute is silent, however, on whether “assessments” include attorneys’ fees.

27. *Id.*

28. *Id.*

29. *Id.* at § 720.3085(1)(a) (emphasis added).

30. *Id.* at § 720.3085(3)(b).

leveled based on a “member’s proportional share of expenses.”³¹ Accordingly, it would seem that trying to recover attorneys’ fees incurred in an underlying foreclosure action against a new parcel owner would be impermissible because the assessment would not be based on that member’s proportional share. In an analogous situation, the Florida Fifth District Court of Appeal held that a condominium could not treat a “fine” as a “common expense” (for which a lien could be filed for non-payment), in part because “[t]he fine [was] not collectible from all unit owners in proportion to their ownership interest” as required under Florida Statutes, Section 718.115(2).³²

Because the HOA Statute clearly treats “assessments” as being separate and distinct from late charges, interest, attorneys’ fees, and other collection costs, a unit owner who takes title through the foreclosure process is not liable to the association for these other costs. The association would still have a right to recover the costs, but it would only be through an action to foreclose its lien and claim, and then only against the original parcel owner.³³

IV. THE CONFLICT BETWEEN THE DECLARATION AND THE HOA STATUTE

Liability for assessments is a creation of both contract and statute, with the underlying declaration giving rise to the right to level assessments in the first place.³⁴ These liability sources create an inherent conflict, as the statutory changes to the HOA Statute brought about by the 2007 addition of Section 720.3085 created statutory joint and several liability when none had previously existed.³⁵ Crucially, many declarations contain some form of

31. *Id.* at § 720.308(1)(a).

32. *Elbadramany v. Oceans Seven Condo. Ass’n, Inc.*, 461 So. 2d 1001 (Fla. 5th Dist. App. 1984).

33. Fla. Stat. § 720.3805(5)(a). To hold otherwise could create a situation whereby the prevailing party in a foreclosure action, the first mortgagee, is obligated to pay the non-prevailing party’s attorney’s fees.

34. *See Genet, supra* n. 1 (explaining that HOAs are governed by the recorded HOA documents, which, along with statutory requirements, determine an HOA’s authority to make assessments and assert liens).

35. Fla. Stat. § 720.3085.

provision subordinating the HOA's right to assessments to a first mortgagee.³⁶

The Second District Court of Appeal addressed this issue in *Coral Lakes Community Association, Inc. v. Busey Bank, N.A.*³⁷ In *Coral Lakes*, the trial court awarded final summary judgment of the foreclosure in favor of the appellee bank, finding that the bank would have no liability to the appellant HOA for past-due assessments.³⁸ In that case, the bank had recorded its mortgage in 2006, before the statutory amendment in 2007, which provided for joint and several liability with the previous property owner.³⁹ The HOA's declaration subordinated its right to assessments to a first mortgagee who took title through foreclosure.⁴⁰ The court held that "because of the Declaration's plain and unambiguous language subordinating any claim for unpaid HOA assessments to a first mortgagee's claim upon foreclosure or deed in lieu of foreclosure, it controls and absolves the Bank, as first mortgagee, from liability for any assessments accruing before it acquires the parcel."⁴¹

This decision was based in part on a recognition that the declaration's unambiguous language should be given a "strong presumption of validity"⁴² and also on the fact that the HOA had chosen to limit its rights under the declaration.⁴³ The court further held that the bank was the intended third-party beneficiary⁴⁴

36. *Coral Lakes Community Ass'n, Inc. v. Busey Bank, N.A.*, 30 So. 3d 579, 581 (Fla. 2d Dist. App. 2010). The court noted in *Coral Lakes* that in regards to a homeowner's declaration, which subordinated their lien to a first mortgagee who took title, "This section was likely added to the Declaration to induce lenders to aid homeowners purchasing property in the community by awarding them priority over the HOA's claims for unpaid assessments." *Id.* at 581 n. 1.

37. 30 So. 3d 579.

38. *Id.* at 581.

39. *Id.* at 581–583.

40. *Id.* at 583.

41. *Id.* at 583–584.

42. *Id.* at 584 ("Restrictions found within a Declaration are afforded a strong presumption of validity, and a reasonable unambiguous restriction will be enforced according to the intent of the parties as expressed by the clear and ordinary meaning of its terms. . . .") (quoting *Shields v. Andros Isle Prop. Owners Ass'n*, 872 So. 2d 1003, 1005–1006 (Fla. 4th Dist. App. 2004); *Emerald Estate Community Ass'n. v. Gorodetzer*, 819 So. 2d 190, 193 (Fla. 4th Dist. App. 2002)).

43. *Id.*

44. *Id.* The language in the declaration subordinating the lien was included to the "benefit[] [of] all first mortgagees of homes in the community." *Id.*

of the declaration's language, subordinating the HOA's lien.⁴⁵ As such, the bank had a vested contractual right to the favorable subordination language of the declaration that could not be removed by subsequent statutory changes.⁴⁶ "To hold otherwise would implicate constitutional concerns about impairment of vested contractual rights."⁴⁷ Almost no amount of impairment of contract is constitutionally permissible.⁴⁸ In light of *Coral Lakes*, a first mortgagee who recorded his or her mortgage before June 30, 2007, can take advantage of any limitation on liability found in the HOA's declaration.

The mortgage in *Coral Lakes* was recorded before the statutory change in 2007, so the question of whether the declaration had been modified by statute was not at issue.⁴⁹ The statutory modification issue has been addressed in the context of condominium cases and should guide the analysis in the context of HOAs.⁵⁰ Most of these cases involved the statutory invalidation of "escalation clauses" in condominium declarations. By virtue of a statutory change in 1975, these provisions became void as against public policy.⁵¹ The courts held that retroactively applying the statute would be unconstitutional in that the statute could only be applied *prospectively*.⁵²

The issue of "impairment of contract" was circumvented because the underlying declarations in *Kaufman* included a clause providing that the declaration was subject to change by modifications to the statute.⁵³ Florida courts have routinely held that a provision in a recorded declaration that provides for the incorporation of subsequent statutory modifications is disposi-

45. *Id.*

46. *Id.*

47. *Id.* (citing Fla. Const. art. I, § 10 ("No bill of attainder, ex post facto law or law impairing the obligation of contracts shall be passed.")).

48. *Pomponio v. Claridge of Pompano Condo., Inc.*, 378 So. 2d 774, 780 (Fla. 1979).

49. 30 So. 3d at 581. The *Coral Lakes* court specifically declined to address the issue of whether the declaration had been modified by statute. *Id.* at 585 n. 6.

50. *E.g. Pomponio*, 378 So. 2d 774 (analyzing the statutory modification issue).

51. *Kaufman v. Shere*, 347 So. 2d 627 (Fla. 3d Dist. App. 1977) (explaining that Florida Statutes § 711.236 prohibited enforcement of escalation clauses).

52. *Id.* at 628; *see also Fleeman v. Case*, 342 So. 2d 815, 817 (Fla. 1977) (explaining that "[s]tatutes are presumed to be prospective in application unless the Legislature manifests an intention to the contrary").

53. 347 So. 2d at 628.

tive.⁵⁴ Based on this authority, if the declaration contemplates amendment by statute, there is no impairment of contract.

For cases in which the underlying declaration did not provide for amendment by statute, a more complex issue is presented. In *Palm-Aire Country Club Condominium Association No. 2, Inc. v. F.P.A. Corporation*,⁵⁵ the Fourth District Court of Appeal held that the statutory changes did not become part of the declaration because there was no provision providing for amendment by statute.⁵⁶ In *Steinhardt v. Rudolph*,⁵⁷ the Third District Court of Appeal allowed the application of a statutory change to a declaration without a provision for amendment by statute, but only by finding that the provision modified by statute was unconscionable “from its inception” and thus unenforceable.⁵⁸

Thus, it would appear that if an HOA’s declaration does not provide for amendment by changes to the HOA Statute, a provision limiting a first mortgagee’s liability would still control and the declaration would be unaffected by the addition of Florida Statutes, Section 720.3085. Still, an HOA might try to argue that adding the provisions of Section 720.3085, Florida Statutes, would be a permissible degree of contractual impairment.⁵⁹

When joint and several liability with a previous parcel owner results solely from the addition of Section 720.3085, the court would be enforcing the provision despite the HOA having never contracted for the provision itself. Courts have been highly deferential to the terms contained in recorded declarations.⁶⁰ Additionally, as pointed out by the court in *Ecoventure*, an HOA has the right to amend its declaration to incorporate statutory changes.⁶¹ It would seem that an HOA that never granted itself a

54. See *Ecoventure WGV, Ltd. v. St. Johns N.W. Residential Ass’n, Inc.*, 56 So. 3d 126, 128 n. 3 (Fla. 5th Dist. App. 2011) (citing *Angora Enters., Inc. v. Cole*, 439 So. 2d 832 (Fla. 1983)); *Coral Isle E. Condo. v. Snyder*, 395 So. 2d 1204, 1205 (Fla. 3d Dist. App. 1981); *Golden Glades Club Rec. Corp. v. Ass’n of Golden Glades Condo. Club, Inc.*, 385 So. 2d 103, 104 (Fla. 3d Dist. App. 1980); *Palm-Aire Country Club Condo. Ass’n No. 2, Inc. v. F.P.A. Corp.*, 357 So. 2d 249, 251 (Fla. 4th Dist. App. 1978).

55. 357 So. 2d 249.

56. *Id.* at 251–252.

57. 422 So. 2d 884 (Fla. 3d Dist. App. 1982).

58. *Id.* at 895 (finding that a rent escalation clause in a condominium declaration was unconscionable).

59. *Cf. Pomponio*, 378 So. 2d at 780.

60. See *supra* n. 54 (listing cases).

61. 56 So. 3d at 128 n. 3 (citing *Angora Enters., Inc.*, 439 So. 2d 832).

right in the first place, and took no steps to avail itself of a right provided by statute, would be unable to overcome “an express constitutional prohibition against any law ‘impairing the obligation of contracts.’”⁶²

V. CONCLUSION

Assessment liability is an issue of growing importance, as many properties are being sold through the foreclosure process. With mortgage defaults continuing to occur, both lenders and HOAs are struggling with homeowners not making payments to them. These parties’ interests used to be aligned, as HOAs wanted lenders to finance home ownership in their community and lenders wanted to lend money to finance these purchases. With the foreclosure crisis unfolding, an inherent conflict has been created as lenders are now taking title to properties they only intended to finance, and not to own. In these situations, both sides are now owed more money, usually from the same person, and neither will be likely able to obtain a full recovery.

Accordingly, disputes between lenders and HOAs that are similar to the situations in this Article can be expected to continue unabated, at least until courts more thoroughly address such key issues as joinder of associations and retroactive application of HOA statute changes, and thus create more settled law.

62. *Pomponio*, 378 So. 2d at 782 (quoting U.S. Const. art. 1, § 10).