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Recorded Declaration and By-laws Control Corporate Governance: An Offering Plan is a Sales Disclosure Document

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The primary governing documents of condominiums and homeowners associations are the declaration and by-laws recorded in the county clerk's office where the property is located. An offering plan, on the other hand, is a sales disclosure document distributed by the sponsor-developer to the initial prospective purchasers in a condominium or homeowners association community. Where things can get confusing is that a copy of the community's declaration and by-laws are contained within every condominium and homeowners association offering plan. However, the copy of the declaration and by-laws contained within the offering plan received by the initial purchasers might be different in form and substance than the declaration and by-laws that are actually recorded in the county clerk's office. As explained below, based on a recent court decision won by our firm, when the recorded versions of the declaration and by-laws are in conflict with the versions contained within an offering plan, the recorded versions are controlling.

Another frequent source of confusion, and disputes, pertaining to condominiums is that statutorily common charges are required to be allocated based on common interest, but there is an exception within the same statute. This exception allows for variations in the allocation of common charges based on usage for items like utilities when there is a commercial unit involved. This exception to the rule often leads to payment disputes and litigation when parties cannot agree on the calculation of usage.

Recently, our office successfully litigated a dispute between a condominium board and a commercial retail unit owner in a Manhattan condominium building that dealt with both of these issues. In this dispute, the formula for calculating the commercial retail unit owner's common charges in the recorded declaration and by-laws was a flat 13% based on common interest and the common charge formula in the version of the declaration and by-laws contained within the offering plan was approximately 5% of the building's expenses and was calculated in part based on usage.

We were initially retained to pursue the collection of common charges from the commercial retail unit owner when it fell behind in the payment of common charges that were calculated based on the 5% formula. We quickly realized that the 5% formula the condominium board was using to bill common charges to the commercial retail unit owner was taken from the version of the declaration and by-laws contained within the offering plan, which excluded the commercial unit owner from contributing towards common electricity, elevator maintenance and other building wide expenses. We took the position that the 5% formula being utilized, which was taken from the offering plan, was incorrect, and that the correct formula for calculating the commercial retail unit owner's common charges was a flat 13% based on common interest as set forth in the condominium's recorded declaration and by-laws. We communicated the billing error we perceived to the commercial retail unit owner's legal counsel and proposed a settlement wherein

the commercial retail unit owner would pay its arrears to date based on the 5% formula and pay common charges prospectively based on the 13% formula.

Settlement negotiations broke down, and we filed a motion for summary judgment (a mini trial based on documentary submissions to the court) asking the court to declare that the 13% common charge formula set forth in the recorded declaration and by-laws was controlling, and not the 5% common charge formula set forth in the different version of the declaration and by-laws contained within the offering plan. Surprisingly, there is not a lot of case law on this issue, and the judge created a new legal precedent by clearly stating in his decision that the offering plan was merely a sales document and that the common charge formula set forth in the recorded declaration and by-laws was controlling.

In his decision, the judge adopted the argument we made in our summary judgment motion that the commercial retail unit owner's deed ratified the recorded declaration and by-laws. Similarly to most condominium deeds, in this case, the commercial retail unit owner's deed referenced the recorded declaration and by-laws, which logically would lead to the conclusion that the commercial retail unit owner agreed to be bound by the recorded declaration and by-laws when it accepted the deed and took title to the commercial retail unit. The judge also adopted our argument based on the legal doctrine of deed merger, which simply stated provides that when a purchaser of real estate accepts a deed and takes ownership, the contract of sale is merged into the deed and any representations made prior to closing that are not reflected in the deed are extinguished. Here the judge ruled that, pursuant to the doctrine of deed merger, when the commercial retail unit owner accepted the deed for its unit, whatever representations were contained within the offering plan, including the different common charge formula, were extinguished and that the 13% formula contained within the recorded declaration and by-laws was the correct formula.

We believe this decision has created some valuable new case law precedent since it is the first decision we are aware of where a New York Court has applied the doctrine of deed merger in connection with a condominium purchase and closing, as well as being one of the few decisions to rule that an offering plan is only a sales document and that the recorded declaration and by-laws are the controlling governing documents for condominiums (and implicitly homeowners associations).