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Leasing Restrictions

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Often investors will purchase a dwelling purely for the purpose of relying on the rental income from the dwelling. The common understanding among owners is that a high number of rental dwellings and the subsequent reduction in the number of owner-occupied dwellings within a community may adversely affect resale values, the maintenance of the property and the availability of certain mortgages. In response to these concerns, community association boards routinely ask us what can be done to limit the number of dwellings in their community that may be leased.

After the real estate boom from 2000-2005, we have seen an increase in the number of community associations asking us to draft leasing restrictions for their particular community. Before any association implements leasing restrictions there are a few key issues that an association's Board and residents should consider.

First, the association's Board should discuss with legal counsel whether the association's governing documents allow for the implementation of leasing restrictions. In most cases, the implementation of a leasing restriction requires the association membership to approve an amendment to the association's founding documents (i.e. its Declaration or Bylaws).

Second, the association's Board should discuss with legal counsel the court decisions (largely from other jurisdictions) that have invalidated

leasing restrictions on the basis that they are unduly burdensome or unfair to certain owners. In these cases, the common argument against leasing restrictions is that they restrain an owner's right to convey the title or possession of their dwelling. Consequently, most leasing restrictions must include economic hardship exceptions to ensure that owners who can establish that they will be harmed by the implementation of the leasing restriction may be granted an exception to allow them to lease their dwelling.

Third, the association's Board should discuss with legal counsel whether the implementation of a leasing restriction may give rise to a claim under the Fair Housing Act. A very limited number of cases in the past few years (from other jurisdictions) have alleged that leasing restrictions are discriminatory because they limit the pool of rental housing available to certain protected classes. These lawsuits typically allege that minorities, single mothers, and handicapped individuals are statistically more likely to rent rather than own housing. Therefore, these lawsuits allege that association imposed leasing restrictions limit the housing available to these protected individuals and, as such, the restriction may be discriminatory in its impact upon certain minorities, single mothers and handicapped individuals.

Fourth, the Board should consider the problem that it seeks to address by imposing a lease restriction. In many instances where our attorneys have been asked to draft leasing

restrictions, we have been able to work with our clients to develop a less restrictive means to address and resolve the problems caused by certain tenants and unresponsive investor-owners. For instance, leasing policies that require all owners as well as their tenants to abide by the association's rules and regulations and that hold owners responsible for the costs of any enforcement action necessitated by their tenants' actions or inactions have worked for some of our association clients to alleviate problems with tenant misconduct and unresponsive owners.

Fifth, many associations believe leasing restrictions are necessary to comply with the underwriting criteria of certain mortgage lenders (i.e., Freddie Mac and Fannie Mae). Under an announcement issued December 16, 2008, Fannie Mae now requires condominium projects consisting of attached units to have an owner-occupancy ratio of at least 51% at the time the loan is originated (purchase or refinance) in order for these loans to meet Fannie Mae's requirements. Fannie Mae has clarified that bank-owned properties listed for sale are deemed to be "owner-occupied" units for purpose of this calculation, which should benefit associations so they are not penalized by lenders for having a large number of foreclosed properties. Freddie Mac also has an owner-occupancy ratio requirement of 51% for its eligibility standards for most classes of condominiums.

In closing, the process of adopting and implementing leasing restrictions is often difficult for many associations to accomplish. Moreover, there are often other, less restrictive, ways for association boards to address tenant or

owner issues without the necessity of limiting those units available for lease. If your Board is interested in reviewing the possibility of adopting a leasing restriction or other restriction, please contact any one of our community association attorneys.