August 9, 2007

Joaquin Turner-Lloveras, Chair
Blue Ribbon Commission
c/o Gary Patton, CEDA Deputy Director
City of Oakland

RE: Negative Impact of Homeowner Assessments on the Affordability of Condos Converted from Apartments

Dear Joaquin:

Attached is the San Francisco ***Chronicle*** article published on the front page of Sunday's Business Section. The article lays out some of the key issues I have stated in previous testimony to the Commission and also to the City Council during deliberations on the condo conversion issue.

Proponents of the plan to convert a substantial portion of Oakland's rental housing stock into condominiums are marketing the plan as "affordable homes for the first-time homebuyer." Does this sales slogan stand up to close scrutiny? I think if the Commission takes a close look not only at the ***Chronicle*** article, but also at the supporting material (attached to the article), it will conclude that marketing converted condos as affordable housing for the first-time homebuyer is a dubious proposition.

Why is that?

Buying a condo in an older apartment building is like buying a used car: it might have a new paint job and shiny spinning hubcaps, but what exactly is under the hood? Drive it off the lot if you want, but don't be surprised if the transmission goes out after 500 miles.

Likewise, consumers who buy a pretty condo in an older converted apartment building shouldn't be shocked when the plumbing explodes or dry rot is discovered and they get slapped with a huge special assessment to fix the problem. This is exactly what happened to Barbara Hernandez, the subject of Sunday's ***Chronicle*** story and of previous news articles.

Her regular monthly assessments started at $410, when she bought her unit in 2004. Now her association proposes raising monthly assessments to $756 for her 450 sq ft studio – and it has the legal authority to do just that. If regular assessments go up another 20% next year, her assessments will exceed her mortgage.

Last year she was also hit with a $4000 special assessment. The association has the legal authority to levy this too. Two weeks ago she got another letter saying another special assessment was in her future: this time the assessment is **estimated** to be between $7,700 and $12,800 per unit. It could be higher, says the July 16 letter she got in the mail. Where's she going to get the money? She has no idea, since she has already liquidated much of her retirement savings to pay for the previous hikes in assessments.

What are the new assessments for in her July 16 letter?

- Paying lawyers to sue the developer for construction defects in the converted building plus paying them for miscellaneous legal services
- Putting money in the reserve accounts (since the developer didn't do it.)
- Buying earthquake insurance (this is a San Francisco building.)
- Buying building security equipment
- Beefing up regular assessments, which are too low to operate the building

Is Barbara's situation unique or extraordinary for the first-time buyer of a unit in a converted building?

No, it isn't, as the Chronicle article clearly indicates, but it provides a great case study for Oakland's Blue Ribbon Commission.

Her situation isn't unique for reasons that I have not heard the Commission discuss. Let me list them below:

- When the consumer buys a condo (in a converted building or a new one), he also buys an undivided interest in the entire building and its common areas. The new home buyer is responsible not only for the maintenance of his own unit, but for the entire building. <u>It is the rare consumer who understands this basic fact of association life.</u>
- The association is, legally-speaking, a California corporation operating under state law.
- State law – and not local government – governs all homeowner assessments: regular assessments and special and emergency assessments. Local government has no authority to regulate the assessments, as Barbara found out when she appealed to the San Francisco Mayor's Office of Housing for help with her homeowner dues.
- State law lets the association board raise regular assessments 20% a year without a vote of the homeowners. Barbara's assessments have been raised 20% at least twice.
- State law lets homeowners vote on special assessments only if they exceed 5% of the gross budgeted expenses for the current fiscal year.
- Local government doesn't necessarily require the developer/landlord to bring an older building up to code prior to the conversion. Yes, local government may require health and safety improvements – seismic work, a new sprinkler system,

e.g. – but it doesn't require that the building's infrastructure be sound. [See the Nov 14, 2006 CEDA report to the City Council, p. 11 on this point.]

- Developers typically low-ball the initial assessments as part of their marketing strategy in order to sell the units quickly. The developer has no interest in the long-term fiscal health of the association. His goal is to sell units fast and move on to the next project. Not until the building is turned over to the homeowners and they open up the books, do they learn what it <u>really</u> costs to keep the lights on, to pay the janitor, and the insurance premiums.
- Dept of Real Estate regulations do not require the developer to fund the reserve accounts. He may be required to <u>estimate</u> what funded reserves ought to be, but he is not required to fund them.
- Insurance on common interest developments is getting harder to buy and is more expensive. Some insurers are dropping association insurance altogether.

Is it any wonder that the first-time homebuyers of condos in this converted building are facing huge assessments? A matrix of state laws, Department of Real Estate regulations, and the business practices of developers trap the homeowner in a financial maze from which it is difficult to escape.

Barbara Hernandez has no idea how she is going to pay the next $7700 to $12,800 special assessment. What would the commission suggest she do?

Sincerely,

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