

## *When residents reject the flip...*

## PROPRIETARY LEASE

### TRY, TRY AGAIN

**T**ime and again I am consulted by cooperative boards wanting to do something that is not authorized by the governing documents, particularly by the proprietary lease. The most common issues involve collection of money for purposes other than maintenance and special assessments, in particular, the imposition of a transfer fee, also known as a flip tax. The same issue pops up with respect to levying fines on tenant-shareholders and others who breach the obligations set forth in the proprietary lease or house rules.

Last year, I was consulted by the board of a large luxury Manhattan co-op that wanted to add a flip tax as an option to replenish its reserve account for capital improvements.

There are varying opinions on the pros and cons of instituting a flip tax to address a building's financial needs. Some feel that it is an inconsistent source of income; others are concerned that apartment values will decline, or that it is unfair to departing shareholders who receive no benefit from the payment.

However, many buildings look at a transfer fee as a way to reduce their reliance on special assessments which may impose a hefty burden on shareholders, and on lines of credit, which result in interest charges.

My client had proposed a flip tax two years earlier. The board put forward an amendment to the proprietary lease, circulated it to the shareholders, and asked them to approve it at a special meeting. Unfortunately, the process was not easy. The shareholders did not approve the proposed amendment. Some opposed it because they hoped to sell their apartments in the next few years. Others feared the flip tax would be triggered by a gift or bequest that might be made as part of estate planning. A third group simply opposed it on principle to discourage building spending. Finally, a significant number of shareholders weren't motivated to vote.

In talking with the board members in charge of bringing the issue forward again, we agreed that for the flip tax amendment to pass, several key steps had to be implemented. First, the updated amendment was sent to shareholders, along with an explanation of the amendment and how it would work. We also prepared a list of frequently asked questions, along with the answers, to resolve many of the misunderstandings that arose during the prior vote. The updated amendment covered many of these concerns, including delaying implementation of the amendment for a period of time so shareholders already in the sales process would not be burned by a last-minute fee.

Next, the board organized a building-wide campaign to ensure that shareholders would support the amendment and to collect proxies from those who could not or would not attend the meeting. Volunteer "floor captains" and "hall captains" visited their neighbors to follow up and ensure the greatest possible participation.

This time, the amendment passed. The building approved a modest transfer fee, with appropriate exceptions for estate planning and other zero-consideration transfers. A year later, hardly anyone seems to remember a time before there was a flip tax.

One other lesson to consider: the best time to amend a proprietary lease is before you need to. We recommend that a board order its attorney to conduct a "wellness" checkup to ensure the co-op's governing documents are current, in line with best practices and recent court decisions, and have an eye toward future needs.

**MARC A. LANDIS**  
*Managing Partner*  
**Phillips Nizer**