

What You Need to Know About State Land Sale Regulations

By W. Leighton Lord III

Retirement is big business in the state of South Carolina. For reasons that are obvious to those of us who live here, the state is an extremely attractive place to retire. The number of Midwesterners and Northeasterners retiring in South Carolina increases every year. In turn, many South Carolina lawyers directly benefit from this retirement industry.

One area from which lawyers benefit is the representation of the developers who develop and build the planned subdivisions and condominium projects that are most attractive to the average retiree. Lawyers tend to get involved in every aspect of the project – the purchase of the initial property, the financing and development of the infrastructure and the actual sale of the lots to individuals.

One extremely important aspect of this process that lawyers tend not to get involved in is the marketing of condominium units, lots and completed houses to out of state residents. Indeed most developers and marketers are unaware that they need to talk to their lawyer before marketing their project outside of South Carolina.

A surprising number of developers and lawyers are unaware that there is an extensive body of state law that regulates the marketing of out of state real property. These regulatory schemes are most extensive in states such as New Jersey, New York, Michigan and Connecticut, where South Carolina developers tend to market the heaviest. What is clear is that every lawyer who represents anyone who develops property with the hope of selling that property to out of state residents needs to be aware of the various state land sale regulatory schemes.

State land sale regulations go back to the '70s when Florida swampland was being sold to the naive and unsuspecting residents of states like New York. These cases of outright fraud were what most likely inspired a great deal of the land sale regulation legislation. On top of that was the problem of well-meaning developers who would start a project, sell lots to collect seed money for the infrastructure and then, regardless of good intentions, go under before the infrastructure could be completed. The citizen of Connecticut would then be stuck with a lot that had no water or sewer hookup and no access.

Various state legislators decided that if a developer or marketer wanted to come into their state to try to sell a lot, home or condominium unit to one of their citizens, they had to register that land so the state's regulators could better protect its citizens. In some ways the states simply followed the federal government, which also regulates interstate land sales through the Interstate Land Sales Act, known as a HUD filing. The state land sale registrations are similar to the HUD filings for single-family developments. Don't be confused, however. A HUD registration does not take care of state registration obligations. Although in some states, if a developer is registered with HUD, he or she will be exempt in that state or only be required to file an abbreviated filing. A HUD registration is not the same thing as a state land sale registration.

One of the keys to understanding state land sale registrations is to understand what the regulators in most states are trying to obtain to protect their citizens. Basically, they want to know that the developer is real and has the resources to complete the project as

offered and sold. In addition, the regulators want to determine that the property is good property – in other words, not in a flood plain – and that either the infrastructure (water and sewer and roads) is in or there has been a bond posted to be sure that it will be put in even if the developer goes bust during the development.

Before a developer in South Carolina can market a lot in Myrtle Beach to a resident of Connecticut, the developer must convince the regulators, through the land sale registration, that he or she is a real developer with real money and that, no matter what happens, the Connecticut resident will end up with a lot that he or she can access and build a home on. Although some states have slightly different angles and agendas, this is basically what each state is trying to obtain in its registration process. Although some of the requests and requirements in the registration process don't appear to make sense, most of them are trying to reach this basic goal.

REGISTRATION

The first question a client will have is do I need to register? The question back to them should be do you plan to market outside of South Carolina and what are your marketing plans? If the developer and marketing company will simply have a sales office in downtown Myrtle Beach and wait for people to walk in and buy a unit or lot, they generally do not need to be registered. That developer or marketing company has done nothing to attract the out of state buyer and, in fact, the out of state buyer has been attracted to them. Above that, the question becomes more difficult.

If the developer or marketing company is advertising only in the state of South Carolina, then again, registration is most likely not required. Once the advertising and marketing goes beyond, and is directed outside the state of South Carolina, it becomes much more likely that registration is required.

The murkiest area in this body of law involves the frequent advertisements seen in golf and retirement magazines and national newspapers. Under the definition of marketing in most states requiring registration, advertising in such magazines and newspapers would, in fact, trigger the requirement to register the property. That being said, most of these states don't tend to actively enforce the registration statutes on developers who simply place passive advertisements in national magazines and newspapers.

When developers take the next step and send mailings to out of state residents, contact out of state residents by phone or visit states through home shows, home expos and retirement expos, there is no question that the developer needs to be registered, or exempt, in that state. A large number of developers in South Carolina visit many of the Midwestern and Northeastern states through home expos.

Most of the home show organizers are very good at being sure that a developer does not sign up for the home show unless the developer has registered with that state hosting the show. Those that, however, slip through the cracks and attend home shows without being registered are often asked to leave by regulators who visit the site. Considering that attending these home shows can cost a great deal of money in fees and employee time, being asked to leave a home show is an embarrassment to the developer and the community being marketed, as well as being a very costly mistake.

As mentioned, if a development is registered with HUD, it can generally be more expeditiously registered with the various states requiring registration. Most states have what is known as a pass- through registration

for these projects. The legal costs in preparing the registration is *generally about half* and the process takes a lot less time. The developer and lawyer, however, have to be careful to amend the state land sale registration whenever the HUD registration is amended.

EXEMPTIONS

___Some states also offer attractive exemptions from registration. For example, in Florida all subdivisions that only contain lots being sold for more than \$50,000 are exempt. In Illinois, if marketing costs plus commissions are a certain percentage of the aggregate land value, a project will be exempt after filing an affidavit from an accountant attesting to these percentages.

In most states, the sale of very few lots, generally under 25, is exempt. There are also several states that require no registration at all for most developments. Mastering the exemptions will save your clients a lot of time and money. After determining that a client needs to register his or her property, the second step is to determine whether or not an exemption is available.

REGISTRATION PROCESS

Some states are easier to register in than others. Generally, the state of New York is thought of as the most difficult state in which to register. The registration process in New York is akin to a securities registration and takes a great deal of time, effort and expense on behalf of the lawyer and the client. In addition, the registration goes through several series of approvals by legal, architectural and engineering. Generally, the registration gets sent back or rejected at each approval level so the process can stretch out for three to six months.

Other states such as New Jersey, Connecticut, Ohio and Michigan are not as time consuming or as expensive to the client as New York. Each state also has registration fees, which run from approximately \$3,000 to \$4,000 in New Jersey to as low as a couple hundred dollars for other states. It is helpful to give clients a schedule of the fees for each state before beginning the registration process.

Most lawyers also find that the legal fees will vary greatly from state to state and depending on whether or not the development is HUD registered. Again, it is helpful for the client in deciding whether or not they want to market in that state to know the cost of registration. Some developers choose not to go to certain states due to the expense in registration.

THE REGISTRATION

Most state land sale registrations require at least the following elements.

Offering Statement. This is a general statement that describes the project, any risk factors, the surroundings, the developer, the individuals making up the developer, status of improvements and the various amenities, as well as issues involving the purchase and development of a lot. Most statements must follow a statutory form.

Title Work. Land sale registrations generally require a copy of the title policy or title opinion showing that the developer has good and marketable title. Copies of all relevant easements and restrictions are also required.

Subdivision Plat. In most states, only those lots that have been subdivided and platted can be registered. A good subdivision plat is required. Registrations generally must be amended if new lots are brought on.

Marketing Materials. All marketing materials are generally required.

Sales Contracts and Transfer Documents. All documents that will be used in the sale of a lot are generally required.

Miscellaneous. Each state will also have its own miscellaneous requirements and requests. Some have questionnaires and others have various affidavits and forms that go with a registration. The developer will be required to consent to the jurisdiction of the state real estate commission or attorney general.

The process of registering a subdivision is as much an organizational exercise as a legal project. While there are a great deal of legal and regulatory issues, getting all of the documents together with the registration application is part of the battle. Registration applications will be rejected if they are incomplete.

Once registered, most states require annual renewal of the registration. Annual renewals are fairly simple and inexpensive. If additional property is added to a development or if the development changes in a material way, an amendment to the registration may be required. Registration can take place during any stage of a development's progress. However, registration is more difficult in the earlier stages.

PENALTIES

The penalties for not registering, as mentioned, can range from embarrassment to financial ruin. Generally, if a developer is a first time offender attending a home show unregistered, the regulators will ask them to take their booth down and leave and possibly pay a small fine. Regulators have the authority to fine a developer anywhere from \$500 to several thousand dollars. Regulators can also prevent a developer from working in their state. Although most states have the ability to prosecute, in the recent past they have not done so.

One of the most powerful tools that the various states have is to force the rescission of any contracts already entered into. If the developer has been banking on a large number of contracts from a given state, this can cause financial ruin if the contracts are immediately rescinded or put into doubt.

INTERNET

An area of increasing concern is the use of the Internet to market developments. Many subdivisions in South Carolina have Web sites. An important distinction in the state land sale area is whether or not it is a "passive" or "active" Web site. A passive site is generally one in which someone can visit and look at information. An active site, however, allows a potential buyer to visit and then *communicate back and forth* with the developer through e-mail.

New Jersey has taken the position, and is currently involved in several cases to enforce the position, that an active Web site that contacts or replies to New Jersey residents requires the subject development to be registered. New Jersey has also taken the position, although there is no published directive, that a passive Web site does not require registration. This is a developing area that needs close attention.

CONCLUSION

For anyone who represents developers or companies that market property, it is worth asking how they intend to market and whether or not they are registered in those states. Determining whether or not a client should be registered will eventually save the client a lot of time, money and embarrassment.

W. Leighton Lord III is a partner with Nexsen, Pruet, Jacobs and Pollard, LLP in Columbia.