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B. L. Hoisington

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# Condominiums and the Corporate Securities Law

By B. L. HOISINGTON\*

UP to this time there has been no certain resolution either by the courts or the legislature of the question of whether or not a condominium interest is subject to the Corporate Securities Law. Nevertheless, thousands upon thousands of dollars are being invested in condominium developments by persons and institutions in the face of this uncertainty which could radically affect the organization and methods of sale and resale of such interests. The courts and the legislature will inevitably be drawn into this picture to resolve the conflicts. This article hopes to highlight the problems involved in such a resolution by reviewing and attempting to rationalize the relevant statutory provisions and certain of the cases construing them.<sup>1</sup>

The nature of condominium ownership has been described at some length in other articles appearing in this volume and in other contemporary publications. It will be assumed, therefore, that the reader possesses an understanding of what condominiums are and how they work.

## *An Introduction to the Problem*

The starting point of analysis must be the statute itself. The California Corporate Securities Law defines a security in very broad terms:<sup>2</sup>

“Security” includes all of the following: (a) Any stock . . . any certificate of interest or participation; any certificate in a profit-sharing agreement; any certificate of interest in an oil, gas, or mining title or lease; any transferable share, investment contract, or beneficial interest in title to property, profits, or earnings. . . .

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\* Member, State Bar of California; L.L.B., Hastings College of Law (1960). Assisted by Vernon A. Harris, second year student.

<sup>1</sup> The cases considering the application of the Corporate Securities Law to “unusual” types of interests are collected in numerous places, and this article will discuss only those principal decisions which seem to bear most closely on the condominium question. See BALLANTINE & STERLING, CALIFORNIA CORPORATION LAWS, § 347 *et seq.* (4th ed. 1962), for leads into the cases generally.

<sup>2</sup> CAL. CORP. CODE § 25008.

There are several specific exemptions, among them:

Any bona fide joint adventure interest, except such interests when offered to the public.<sup>3</sup>

Any security (except notes, bonds, debentures, or other evidences of indebtedness, whether interest-bearing or not) issued by a company organized under the laws of this State exclusively for educational, benevolent, fraternal, charitable, or reformatory purposes and not for pecuniary profit, no part of the earnings of which inures to the benefit of any private shareholder or individual.<sup>4</sup>

Bills of exchange, trade acceptances, promissory notes and any guarantee thereof, and other commercial paper issued, given, or acquired in a bona fide way in the ordinary course of legitimate business, trade, or commerce.<sup>5</sup>

In 1948 the attorney general considered the applicability of the Corporate Securities Law to an arrangement in which six couples each purchased an undivided one-sixth interest as tenants in common in an apartment building.<sup>6</sup> Each couple was designated "owner" of a particular apartment in the building. It was suggested that each of these interests was a "beneficial interest in title to property" and accordingly were securities. The attorney general said:<sup>7</sup>

We note, however, that conveyances of real property to purchasers as tenants in common have always been held an acceptable form of realty transaction. In the normal case no one has ever considered that a security in such cases was issued within the meaning of the Corporate Securities Act. . . .

However, the schemes in question vary from the ordinary tenancy in common realty transactions. Normally a seller selling real property merely offers the property for sale at a price. He is not interested whether the buyer is a single purchaser or whether several purchasers combine to take tenancy in common fractional interests. In the instant case the seller is offering to the public fractional interests in the whole property to separate purchasers. This in a sense is offering for sale a "beneficial interest in title to property."

The opinion quotes from the case of *People v. Davenport*<sup>8</sup> language to the effect that the literal meaning of words in the Corporate Securities Law does not operate to carry the enactment beyond the "general purpose or scheme entertained by the Legislature in passing the statute . . .,"<sup>9</sup> and concludes as follows:<sup>10</sup>

<sup>3</sup> CAL. CORP. CODE § 25100(m).

<sup>4</sup> CAL. CORP. CODE § 25102(a).

<sup>5</sup> CAL. CORP. CODE § 25102(b).

<sup>6</sup> 11 CAL. OPS. ATT'Y GEN. 81 (1948).

<sup>7</sup> *Id.* at 82.

<sup>8</sup> 13 Cal. 2d 681, 685, 91 P.2d 892 (1939).

<sup>9</sup> 11 CAL. OPS. ATT'Y GEN. 81, 82.

<sup>10</sup> *Id.* at 83.

One inherent difference, however, between the transaction in question and those at which the act is directed is that the purpose in selling and in buying interests in the apartment is to sell to persons who buy merely in order to secure a place to live. There is no element of investment in the sense that buyers purchase an interest in the property in the expectation or hope of securing capital gain or interest, the latter being characteristics of a security transaction under the act.

This attorney general's opinion highlights many of the critical considerations involved in determining the applicability of the Corporate Securities Law to condominiums, and the following questions, raised in the opinion, will recur repeatedly, in one form or another, in the analysis which follows:

1. What is the "general purpose" or "scheme" of the Corporate Securities Law?
2. Is the expectation of "capital gain" or "interest" an essential element of every "security transaction"?
3. Is *any* fractional interest in real property a "beneficial interest in title to property" within the meaning of the Corporate Securities Law?
4. What is the legal effect of the "home purchase" motive on the classification of an interest as a security?

### *Understanding the Purpose of the California Law*

Unlike the federal securities act and the securities laws of most other states, the California Corporate Securities Law is aimed at more than the mere protection of investors against sales fraud.<sup>11</sup> The required administrative review is undertaken for the purpose of determining whether the proposed plan of business as well as the proposed issuance of securities is "fair, just, and equitable."<sup>12</sup> Thus, in a sense, the California Law undertakes to regulate the organization and structure of certain businesses as well as the representations and circumstances of the sale of interests therein. Not merely "the risks of the sale" but also "the risks of the business relationship" created by the sale are regulated.

An awareness of this broadened purpose of the California Corporate Securities Law can be helpful in determining whether any particular type of interest is subject to that law. However, a peculiar fallacy of reasoning often creeps into analyses of the law at this point. There is a noticeable tendency among many persons faced with these problems to confuse the standard of *review* with the standard of *definition*. Obviously, a particular corporate structure may be eminently fair, just,

<sup>11</sup> *In re Leach*, 215 Cal. 536, 12 P.2d 3 (1932); *Geisenhoff v. Mabrey*, 58 Cal. App. 2d 481, 137 P.2d 36 (1943); *Moore v. Stella*, 52 Cal. App. 2d 766, 127 P.2d 300 (1942).

<sup>12</sup> CAL. CORP. CODE § 25507.

and equitable and yet remain subject to this law; while, in contrast, a particular joint venture may be most speculative, unfair and inequitable to certain participants in it and yet, so long as such interests are not offered to the public, remain outside the scope of the securities law. "Fairness" and "justice" may be a part of the standard of review, but they are not a part of the standard of definition.

How, then, does the broadened purpose of the law mentioned above assist in formulating a definition of a security? It does so by pointing out where to look for the definitive characteristics of a security; namely, at the *kind of business relationships* created between the parties and the *character of the risks* created by that relationship. Since the purpose of a regulatory law such as the Corporate Securities Law is to protect against risks and not to discourage certain types of business relationships, where it is clear that the risks sought to be protected against are absent from a particular business relationship, there would be no "purpose" in regulating the terms of that relationship. This is, or should be, the case regardless of the labels which have been, though usually for wholly different reasons, attached to the relationship. The well-worn principle of "looking through form to substance" is really only another way of saying that the definitive characteristics of an activity are found in the "risks" and "relationships" involved and not in the "names" or "labels" associated with it.

It has been suggested in some quarters that since the concern of this law is risks, any analysis of it should focus primarily on the risks inherent in an activity rather than on the kind of relationship involved in the activity. This approach has two disadvantages. First, there is the ever present danger of confusing the concept of a particular *kind* of risk with the element of "riskiness" involved in a particular activity (which is a variety of the fallacy of confusing the standard of review with the standard of definition, mentioned above). And secondly, as a practical matter it is very difficult to characterize a risk by separately setting out its definitive characteristics apart from the practical, human situation in which it arises. This latter difficulty, while seldom if ever expressly acknowledged, is a basic problem throughout the field of regulatory law. In response to this problem, regulatory laws have been organized or arranged around "relationships" rather than risks. For example, where the risk is that of "cheating by misrepresentation," the Real Estate Law has been designed to approach the problem in the setting of real estate sales relationships while the Installment Sales Law approaches the same risk in a totally different relationship-setting. With certain risks that are considered extreme, the Penal Law attacks

the risk directly and as such (*viz.*, fraud), but regulatory laws customarily do not.

The Corporate Securities Law, then, purposes to protect persons against certain risks arising out of *certain specialized* types of relationships—not *all* relationships. Accordingly, the question of this law's application to condominium interests is one of determining whether any of the relationships created by the sale of condominium interests are the *kind* of relationship which the legislature intended to regulate under that law.

### ***Some Established Security Relationships***

The shareholder-corporation relationship is probably the clearest example of the kind intended to be regulated by the securities law. Its typical characteristics are: (1) the investment of capital (2) with the expectation of monetary gain (3) in return for a fractional interest (4) in a profit-seeking enterprise (5) which usually is to be managed by others.

While these characteristics are denoted "typical," it must be recognized that not all non-profit corporations are exempt from the law. In such non-profit corporations where the shareholder does not expect monetary return, he nevertheless maintains an interest in an enterprise which he expects to see operated in a fashion which will result in some sort of continuing benefit to him. For this interest he supplies, in most cases, a portion of the capital with which the enterprise is to operate. Where the shareholder neither supplies risk capital nor invests for profit, there is good reason to argue that the Corporate Securities Law should have no application even though a corporate form of organization is employed by the enterprise. It surely should have no application where the corporate form is not employed.

The document which evidences the shareholder-corporation relationship is called "stock." While stock is literally defined as a "security," it is not the label attached to the document evidencing the relationship which is sought to be regulated but rather the relationship itself. Therefore, in determining the law's "purpose," the emphasis must be on the relationship and not the document. It is not really very important whether one arrives at this conclusion by saying that while the document is labeled "stock" and looks like stock it is *not really* stock, or by saying that *not all* "stock" is subject to regulation, so long as one recognizes what is being used as the basis of definition.

Where the relationship is such that the investor actively participates in a non-corporate business venture in order to create the profit in which he is to share, the courts have declined to find the Corporate Securities

Law applicable.<sup>13</sup> In *People v. Syde*<sup>14</sup> the court said: "The expectation of financial return . . . might have been raised by hopes falsely induced. But since the agreement contemplates actual participation . . . it cannot be considered as a security within the meaning of the statute: and neither numbers of participants nor possible fraud in its creation may transmute the instrument into a security which in legal effect it is not."

Where the relationship is such that the investor is not to participate actively in the enterprise and someone else is to manage the property from which the investor is to realize a profit, the courts may hold the Corporate Securities Law applicable even though the investor may be the outright owner of the property involved.<sup>15</sup> Thus, in *Hollywood State Bank v. Wilde*,<sup>16</sup> defendant sold chinchillas by the pair with the agreement that he would be permitted to raise, care for, breed and ultimately sell the animals on the purchaser's behalf. The court had little difficulty in finding a security transaction. In *Domestic & Foreign Petroleum Co. v. Long*<sup>17</sup> there were sales of undivided interests in oil leaseholds. In holding such interests subject to the securities law, the court emphasized that the purchasers (grantees) were not to have any voice concerning the operations. They were investors who were buying nothing more than a right to share in profits produced by others. This element of "passivity" on the part of the investor is one of the most firmly established characteristics of a "security relationship."<sup>18</sup>

In the recent case of *Silver Hills Country Club v. Sobieski*,<sup>19</sup> members of the public were asked to invest money with a developer who proposed to build a country club for the enjoyment of those who invested in it. The prospective members were given no ownership in the club, no

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<sup>13</sup> *People v. Syde*, 37 Cal. 2d 765, 235 P.2d 601 (1951); *People v. Gould*, 37 Cal. 2d 885, 235 P.2d 604 (1951); *Maguire v. Lees*, 74 Cal. App. 2d 697, 169 P.2d 411 (1946); *People v. Anderson*, 35 Cal. App. 2d 23, 94 P.2d 627 (1939); *People v. Steele*, 2 Cal. App. 2d 370, 36 P.2d 40 (1934).

<sup>14</sup> 37 Cal. 2d 765 at 769, 235 P.2d 601 at 603; cf. *People v. Staver*, 115 Cal. App. 2d 711, 252 P.2d 700 (1953).

<sup>15</sup> *Oil Lease Service, Inc. v. Stephenson*, 162 Cal. App. 2d 100, 327 P.2d 628 (1958); *Hollywood State Bank v. Wilde*, 70 Cal. App. 2d 103, 160 P.2d 846 (1945); *Gracchi v. Friedlander*, 93 Cal. App. 770, 270 Pac. 235 (1928); see cases cited *infra* note 18.

<sup>16</sup> *Ibid.*

<sup>17</sup> 4 Cal. 2d 547, 51 P.2d 73 (1935).

<sup>18</sup> See note 14 *supra*; cf. *People v. Miller*, 192 Cal. App. 2d 414, 13 Cal. Rptr. 260 (1961); *People v. Rankin*, 160 Cal. App. 2d 93, 325 P.2d 10 (1958); *Goldberg v. Paramount Oil Company*, 143 Cal. App. 2d 215, 300 P.2d 329 (1956); *People v. Hoshor*, 92 Cal. App. 2d 250, 206 P.2d 882 (1949); *People v. Woodson*, 78 Cal. App. 2d 132, 177 P.2d 586 (1947); *Moore v. Stella*, 52 Cal. App. 2d 766, 127 P.2d 300 (1942); see also *People v. Ferguson*, 134 Cal. App. 41, 24 P.2d 965 (1933).

<sup>19</sup> 55 Cal. 2d 811, 13 Cal. Rptr. 186, 361 P.2d 906 (1961).

participation in its construction or subsequent operation, and no promise of profit. The California Supreme Court declared the promotion to be subject to the Corporate Securities Law. This case has wide implications for the future direction of the California Corporate Securities Law. But its effect can be over-emphasized. The case involved the solicitation of funds from many members of the public to promote the future construction of an enterprise in which the public investors were to have purely beneficial interests. The public investors were not to participate in any way in the expenditure of their funds but were "gambling" that the promoter would keep his word and construct the facilities which the investors expected to enjoy.

One can see that the "labels" involved in the cases construing the Corporate Securities Law have run the gamut from animal husbandry agreements, through mineral leases, mortgage notes<sup>20</sup> and contracts for the sale of the right to a chemical process,<sup>21</sup> to agreements for memberships in an unbuilt country club. It is fair to conclude that when the California courts are confronted with the question of whether or not a condominium interest is subject to the Corporate Securities Law little moment will be given the fact that these are "home purchases" of "tenancy in common" and "fee simple" interests in "real estate" in the form of "apartments" conveyed by "deeds" if the courts are otherwise satisfied that a security relationship is present.

### ***A Comparison of Condominium Relationships***

#### ***Developer-Purchaser***

The first obvious relationship involved in condominium ownership is that between the developer and the unit purchaser. Where the developer approaches the purchaser before the condominium apartment house is built and receives an investment of capital from the purchaser in exchange for the developer's promise to build and deliver, the relationship is quite similar to that involved in *Silver Hills* and in many respects the benefits expected from the investment are much more substantial. However, if such subscriptions were held subject to the securities law, the position of certain contractual relationships regarding the construction of homes in subdivisions would have to be distinguished. In conventional subdivision development single family dwellings, each to be wholly owned by its occupant, are sometimes purchased in advance under a contract for construction and delivery. From the standpoint of the risks involved there are many similarities between such relationships and those in a pre-construction condominium sale.

<sup>20</sup> *In re Leach*, 215 Cal. 536, 12 P.2d 3 (1932).

<sup>21</sup> *People v. Gregory*, 12 Cal. App. 2d 7, 54 P.2d 770 (1936).

The critical distinction may be simply that the home-construction contract of sale is regulated under the Real Estate Law and, regardless of the similarity of risks, the Corporate Securities Law is not intended to overlap in such basic and typical real estate transactions. Whether this reasoning of implied exclusion should be extended to a pre-construction solicitation of capital for a condominium apartment house is not at all clear. The similarities to *Silver Hills* are very strong where the purchase money is solicited in advance of construction, and a condominium is not a simple, typical and common real estate transaction.<sup>22</sup>

Where the apartment house is fully constructed and the developer fully performs his promises to the unit-purchaser upon delivery of the deed, there has ceased to be any risk-relationship between the developer and the purchaser at all. Hence, one would not expect *that* relationship to be the subject of "securities" regulation.

Where the apartment house is constructed, but the developer has promised to complete additional projects or perform additional acts benefiting the purchaser after the sale (as, perhaps, paying assessments due from unsold units, endeavoring to sell the remainder of the units on similar terms, or constructing a swimming pool) the application of securities regulation is more uncertain. The answer should revolve around whether the purchaser has supplied the developer capital which the developer is to utilize in a promised manner in order for the purchaser to realize whatever benefit has been expected by him. In most situations it would appear doubtful that this developer-purchaser relationship would properly be characterized as a "security relationship" where the developer has merely promised incidentally to do something in the future. However, if that "something" amounted to a promised "swimming pool" for which others were contributing similar funds, the similarities with the *Silver Hills* situation become more prominent.<sup>23</sup>

### *The Relationship of the Property Owners Inter se*

Adjoining land owners have a relationship which is well defined in the law of real property.<sup>24</sup> It usually bears little resemblance to that of security holders. The rights, powers and privileges which inure to the benefit of land owners come to them not through the fulfillment

<sup>22</sup> As a practical matter it would be extremely difficult to finance construction of a condominium apartment project with funds solicited in advance from prospective purchasers. See Bus. & Prof. Code §§ 11013.1-11013.5.

<sup>23</sup> Note again the practical effect of §§ 11013.1-11013.5 *supra* note 22, and the operation of such provisions of the Real Estate Law as an implied exclusion from the Corporate Securities Law.

<sup>24</sup> A notable exception to this statement is the ever growing number of subdivisions or "localities" which are sold subject to a vast number of recorded restrictions, some of which go very far in subjecting the manner of enjoyment of the individual home to decisions of a

of another's promise, which is typically the case with securities, but through the legally enforceable incidents of property ownership. The benefits which land owners expect to realize from their investments are to result from *their own* efforts and activities in the exercise of their established property rights. This is probably why individual home owners in subdivisions are never thought to be subject to securities regulation. Condominium owners are, at least in so far as their fee ownership is concerned, "land owners," and it is difficult to imagine their being subject to the Corporate Securities Law on this account.

The tenancy in common aspect of condominium ownership is closer to the line, however. The so-called "common elements" make up the tangible assets of a condominium arrangement. These elements are owned in common by all unit-purchasers without the right of severance. In the language of the shareholder-corporation relationship, there has been an investment of capital in exchange for a fractional interest in an enterprise to be operated by others, *i.e.*, the management board.<sup>25</sup> Important elements of the typical security relationship are missing, however. There is no expectation of monetary gain present in the purchase of a condominium interest except in the sense in which any home owner expects his home to appreciate in value.<sup>26</sup> But, as has been said earlier, many non-profit *corporations* are held subject to the Corporate Securities Law. And, in the non-corporate setting the element of monetary profit or gain has not been held essential where there is an element of "risk capital" involved.<sup>27</sup> In many non-corporate securities transactions the investor is promised a right or privilege which he could not exercise so as to realize his expected benefit without the promoter's future performance. This is probably the most important distinctive feature of condominium ownership. The unit-owner, in so far as his tenancy in common interest is concerned (and apart from the effect of the management contract on the situation) has from the very outset all

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"local" property owners association. While these groups, so long as they are unincorporated, have never been thought of as being subject to the Corporate Securities Law, the risk-relationship between the parties is quite similar to that of condominium owners under the management agreement and are, in many respects, perhaps as deserving of regulation.

<sup>25</sup> It may be argued that the operation by the management board is really a *species* of self-operation, but in many proposed condominium setups the relationship of the individual owner to the managing board is, at least in so far as risks are concerned, similar to that of a shareholder and the corporate board of directors. See the discussion *infra*.

<sup>26</sup> This excludes the possibility that some owners will purchase condominium interests not for occupancy but speculating on a future resale at a profit. This possibility should not affect the classification of the interest for purposes of the Corporate Securities Law. Many parcels of real estate are purchased on speculation, as are items of personal property, without thereby transforming them into "securities."

<sup>27</sup> *Silver Hills Country Club v. Sobieski*, 55 Cal. 2d 811, 13 Cal. Rptr. 186, 361 P.2d 906 (1961); see Note, 14 *HASTINGS L.J.* 187 (1962).

of the rights and privileges which he expects to receive from the developer. Whether or not he realizes his expected benefits from his tenancy in common condominium interest is a matter of his own, and not someone else's, future performance. In this respect the relationship of tenancy in common ownership bears only slightly more resemblance to that of typical security holders than does the relationship of owners in fee simple. Therefore, it would appear that, where the apartment building is fully constructed and the developer has promised substantially no more than to deliver a good deed to real property, no typical security relationship is created by the delivery (or promised delivery) of that deed. There remains, however, an important additional feature of condominium ownership which must be considered.

### *The Management Agreement*

The precise relationship created between the unit-owners in a condominium under their management agreement is, of course, dependent on its particular terms. In general, most proposed agreements provide for a management board of limited powers and authority elected by the unit-ownership and charged with the responsibility of collecting monthly assessments, providing for common liabilities, and keeping the apartment building and other "common elements" in good repair. In so far as the duties of the board are fixed by the agreement and their discretion limited, the whole arrangement would appear to constitute little more than the delegation of certain common responsibilities by the individual owners to a committee of their choosing for their mutual convenience. Where owners of single unit dwellings in more conventional circumstances undertake to arrange their affairs in a similar manner, seldom, if ever, does one hear the suggestion that the Securities Law is applicable to their arrangements. But the condominium management contract is, or may be (depending upon how it is written), substantially different from a simple arrangement of property owners.

First, it is a "contract" which is offered as part of a "package deal" to prospective purchasers *before* they become property owners. It is not something they negotiate after their ownership is complete.<sup>28</sup>

Secondly, the arrangement is vastly more complex.

Thirdly, the terms of the arrangement are, or may be (depending upon the way the restrictions are written), extremely important to the

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<sup>28</sup> If the promoter retains interests in the condominium, the non-negotiated, complex nature of the deed and accompanying restrictions increases the risks of over-reaching in the terms of sale. However important these increased risks are, as such, they should not affect the interest's classification, unless the promoter were to retain in some manner substantial control of the management board.

realization of the benefits and enjoyments which the condominium owner expects to receive from his ownership. If the management board is given, for example, broad discretion to establish common rules and regulations governing the manner in which the unit-owner may "live" (e.g., hours for entertaining guests, the presence and number of guests, the rental of units, pets, colors of furnishings, the use of common recreational facilities, noises, washing facilities, etc.), a point may be reached where the realization of the expected benefits is derived more from the activities and decisions of the management board than from the activities of the individual unit-owner. When this point is reached the similarities between the shareholder-management relationship in a corporate organization and the owner-management relationship of a condominium are very great.

These distinctions are admittedly matters of "degree," but so are most difficult distinctions. A simple arrangement of single family unit-owners for the cooperative management of certain matters incidentally beneficial to the enjoyment of their property may well not be properly classified as a security, while a complex arrangement of tenants in common for the cooperative management of the physical premises of their "homes," which management is absolutely determinative of the nature and existence of their beneficial enjoyment of their individual and common property, might well be properly classified as a security. It is obvious that, at the extremes, matters of degree become differences of kind.

Nevertheless, there are important differences between the condominium owner-management relationship and that of the shareholder-corporation relationship. Condominium owners *live* with the organization. They are in day to day contact with the operation. Their information, or a large part of it, does not come through complicated financial statements or reports but through "first hand" observation. Moreover, the board of directors of a corporation has an "open-ended" discretion to cause the corporation to buy, sell, invest and pursue any endeavor or venture it sees fit within its business judgment. The management board of a condominium is a limited agent of the joint owners, empowered only with such prerogatives as are expressly given in the recorded restrictions. The board is quite limited in its functions and capacities to "risk" the security of the common elements. These are important distinctions in terms of both the risk to which the interest-owners are subjected at the hands of management and the kind of relationship which exists between owner and management.

On balance then, there are important distinctions between the condominium management arrangement and the typical cooperative

arrangement of local (single family unit) property owners, but there are also important differences with the shareholder-corporation relationship and other typical securities relationships. The condominium is obviously very accurately described as a "hybrid."

### *Some Conclusions*

Most of the cases in other jurisdictions involving cooperative apartment transactions and securities regulation are distinguishable from the California condominium situation for the reason either that public investment was solicited in advance of construction,<sup>29</sup> or that the particular securities law involved exempted real property sales expressly,<sup>30</sup> or that the corporate form of organization was employed.<sup>31</sup> Accordingly, they are of little assistance in determining the application of the California Law to most of the proposed forms of condominium developments.

Most of the cases construing the California Law's application to non-corporate transactions involve an investment for profit by the public purchaser. However, the clear implication of the language of the statute is that it is not necessarily limited to investments for profit nor issues of profit-making companies. The *Silver Hills* case has made it clear that investment for profit is unnecessary at least where there is a solicitation of risk capital from the public.

The purchase of a unit in a completed condominium apartment house involves neither an investment for profit nor a supplying of risk capital to a promotional venture. *Except for the relationship created by the management arrangement*, the relationship created by the purchase of a condominium interest is that of adjoining and joint landowners, and there is little reason to believe the legislature intended to regulate such relationships under the Corporate Securities Law.

There are, in general, at least two respects in which the relationship under the management agreement is typically similar to that of security holders; namely, (1) each owner participates in a manner similar to that of shareholders in a corporation in the management of an organization from which each expects to derive a continuing benefit, and (2) each owner purchases a fairly complex and non-negotiated bundle of rights

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<sup>29</sup> *Brothers v. McMahon*, 351 Ill. App. 321, 115 N.E.2d 116 (1953).

<sup>30</sup> *State v. Silberberg*, 166 Ohio St. 101, 139 N.E.2d 342 (1956).

<sup>31</sup> *State v. Hirsch*, 101 Ohio App. Rep. 425, 131 N.E.2d 419 (1956). The court held no security was involved, but the Ohio statute expressly excludes sales of real estate. Compare *Sire Plan Portfolios v. Carpenter*, 8 Ill. App. 2d 354, 132 N.E.2d 78 (1956).

and duties in an organization in which each owns only a fractional interest.<sup>32</sup>

There are also two typical dissimilarities; namely, (1) the purchaser neither invests for profit nor supplies risk capital to a profit-seeking venture, and (2) the funds paid over, including the assessments paid to management, are presumably (depending upon how the management restrictions are drafted) given for a rather immediate *quid pro quo* received by the purchaser either in the form of recognized property rights or in the form of benefits for which the purchaser would otherwise have had to pay on his own.

The purchase price of a condominium interest is paid for two things: (1) an immediate bundle of property rights, and (2) a continuing future benefit or enjoyment to be derived from the proper management of the common elements. Perhaps the feature of condominium purchase most similar to the risk capital element of the typical security relationship is found in this second purchase object. The distinctions with the *Silver Hills* case, at least where the condominium is fully constructed and the promoter or developer retains no interest in the operation, are substantial. There is no risk of the promoter's unsuccessful future performance. The structure or asset which the purchaser expects to enjoy is present, existing and ready for enjoyment. If there is "capital" "risked," it is risked in the continuing management operation which is a sort of joint venture, and this is much more analogous to the sale of memberships in an existing facility than to the solicitation of capital for a future one (if the *Silver Hills* analogy is to be followed). If the condominium interest were to be held a security, it would appear to be simply because money is supplied for an operation in which the supplier has a continuing beneficial, fractional interest and which operation is managed by others in a manner similar to the way in which a corporation is managed.

It can readily be seen that it is impossible to state flatly whether or not a condominium interest is subject to securities regulation. Much may depend upon the stage of development at which the interest is offered and/or the terms of the instruments creating it. Nevertheless, the question is one which should be resolved. It would be a fairly simple matter for the legislature to resolve most of the doubts surrounding this question. It would be more difficult for the courts to do so without creating as many uncertainties as were resolved. But the present uncertainty has a decided depressive effect on the development of this new

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<sup>32</sup> See Anderson, *Cooperative Apartments in Florida*, 12 U. OF MIAMI L. REV. 13, for a view stressing this element of "complexity" as a basis for classification as a security.

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possibility for convenient urban living. There are, no doubt, some who feel that such a depressant is practically valuable. It is not. If securities regulation is needed it should be asserted clearly and understandably so that matters may proceed in compliance with it. If securities regulation is not needed, any unreasonably prolonged period of uncertainty can only operate to raise unnecessarily the costs of condominium ownership to future purchasers and to injure the market generally.