

# Comparative survey of the legal challenges faced by mixed-use sectional title (condominium) developments

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## 1 Introduction

Over the years mixed-use sectional titles (strata titles, condominium) schemes have become increasingly popular over the world and also in South Africa. A mixed-use sectional titles scheme consists typically of a combination of residential and commercial units, but the term can also apply to the combination of residential units and office units or a combination of residential, commercial and office units.<sup>1</sup> The increased popularity of mixed-use residential and commercial schemes<sup>2</sup> can be attributed to the increased popularity of residential strata title homes in general. Again, the ability to combine the carefree lifestyle afforded by strata title ownership with the conveniences of in-house shops, offices and restaurants appeals to many house buyers.<sup>3</sup>

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<sup>1</sup> Lundquist “Mixed use condominiums under the Minnesota Uniform Condominium Act” 1984 *William Mitchell Law Review* 97 at 102 also includes the following developments under the term mixed-use developments: a residential scheme consisting of a high rise elevator building and a low-rise garden apartment building; office schemes housing various kinds of professionals; commercial condominiums containing various businesses such as a supermarket housing various kinds of shops. At 99 Lundquist suggests that purely commercial condominiums should be evaluated as mixed-use projects because the owners’ businesses will normally differ from one another in terms of energy consumption, customer traffic and maintenance requirements. See also Rolando “Governing documents for mixed use developments” 2006 *The Practical Real Estate Lawyer* 46, who interestingly mentions that garages or parking facilities can be construed as a separate component in a mixed-use commercial and residential scheme. See also Van Atta, Buckley and Saft “Issues for mixed use/mixed ownership developments – facing the realities of troubled times” <http://files.ali-cle.org/thump/datastorage/skoob/form/BKAC1110-Tab13-Va-Att> (20 April 2016) at 3 for mixed-use projects of a more horizontal nature, such as a planned development community with blocks of residences, commercial and recreational components. At 4 they state that mixed-use projects can range in magnitude from one building with residential condominiums and a relatively small commercial component on the ground floor, to large multiple building structures situated on parking podiums with a mixture of several uses, such as hotel, retail, office, and residential. They continue that in some instances there are combined central plants, parking facilities, and other operational facilities shared by some, if not all, of the different components.

<sup>2</sup> See however Van Atta *et al* (n 1) 1-3 on the impact of the financial and market crisis of 2008-2010, which in their words was “nowhere more acute than on mixed-use, combined residential and commercial projects” in the United States. They refer to the complexity of modern financing of large mixed-use projects and at 4 they state that higher density are generally more expensive to build and operate than traditional residential housing developments. In addition, obtaining construction financing for these more exotic projects and obtaining take-out financing for the purchase of units in the residential components are becoming problematic.

<sup>3</sup> Winston “Challenges of mixed use developments” 2007 *Probate and Property* 38.

The increasing scarcity of land and the increased focus on urban regeneration and smart growth<sup>4</sup> make the combination of densely populated strata title schemes combining retail units, offices or other uses along with traditional residential units a very attractive development. The business user is offered a highly desirable urban location, bolstered by an existing set of potential customers. Developers, businesses, professionals and residents can each achieve significant benefits from a well-designed and meticulously implemented mixed-use strata title (condominium) titles project.<sup>5</sup>

The initial focus of this paper is to examine the planning and development challenges faced by the developer of a mixed-use sectional titles scheme. This will be followed by a discussion of how the main challenges facing mixed-use sectional titles schemes can be addressed. Ultimately, the success of a mixed-use scheme depends on the ability of the developer and the unit owners corporation (body corporate) to accommodate the often competing interests of the unit owners in the different components of a mixed-use strata title scheme.<sup>6</sup> This paper will explore mainly New South Wales and United States materials but will be interspersed with references to pertinent South African legislation, regulations and academic literature<sup>7</sup> on mixed-use sectional titles schemes.

## 2 *Planning and development challenges*

### 2.1 Introduction

The initial planning of a mixed-use project requires careful consideration of the mixture of units in the scheme and the manner in which the scheme is going to be developed. Most developers start with a plot of bare land and design a mixed-use building or buildings from the ground up. Some developers base their plan on existing buildings and construct around and above them in order to convert a single-use property into a well-designed mixed-use strata title (sectional titles) scheme. In designing the project, all developers must grapple with issues such as reciprocal servitudes, zoning, building regulations and permitting processes and developers' agreements pertaining to management structure and financing.<sup>8</sup>

### 2.2 Design

In the planning and development phase, the design of the mixed-use project is of the utmost importance. Developers (and those advising them) should realise that the issues set out above are generally more complicated in a vertical mixed-use project (as opposed to a horizontal mixed-use project), as the uses in a vertical project are physically interdependent on each other and the common property in the scheme. In a prudent consideration of the arrangement of the various units within the scheme

<sup>4</sup> Smart growth is an approach to development that encourages a mix of building types and uses, diverse housing and transportation options, development within existing neighbourhoods, and community engagement. See Grant "Encouraging mixed-use in practice" in National Center for Smart Growth Research and Education *International Planning Symposium on Incentives, Regulations, and Plans – The Role of States and Nation-States in Smart Growth Planning* (Sept 2004) 7-8 and 13.

<sup>5</sup> Winston (n 3) 38 and 42.

<sup>6</sup> Lundquist (n 1) 98.

<sup>7</sup> See for example Kelly "Mixed use, multi-layered developments" *Paddocks Press Newsletter* (5-11-2010) 2.

<sup>8</sup> See in general Winston (n 3) 39-40; Rolando (n 1) 44-45.

and their individual uses, it is important to attempt to provide as much autonomy as possible to each use within a mixed-use strata title (sectional titles) project.

Consequently, it is preferable in a mixed-use project featuring residential and commercial units to isolate these uses as far as possible by providing separate entrances, elevators, utility systems, parking areas, loading docks and other services. Potential disruptions and disputes concerning common expense allocation, maintenance and management will be avoided or at least diminished where the design of the building minimises shared areas, services, and interaction between the commercial and residential users. On the contrary, where facilities or amenities will be shared by different users,<sup>9</sup> the governing documents for the project should specify how costs will be allocated and should allocate responsibility for managing and maintaining the shared-use areas. In this regard, the following issues must be considered:

- (a) whether the facilities and amenities located within the project are intended to be used exclusively by a single user type (for example commercial uses or residential uses) or whether they will be shared by two or more user types (for example, commercial and office) including the extent to which the facilities and amenities are shared; and the allocation of costs and expenses and responsibility for management and maintenance of the shared areas between the unit owners in question;
- (b) which users will own, operate and maintain the parking facilities and loading areas; and
- (c) how the utilities for the project will be provided to the different user components and whether the utilities will be separately metered and sub-metered.<sup>10</sup>

### 2.3 Reciprocal servitudes

The integrated nature of mixed-use sectional titles schemes necessitates the consideration of some reciprocal servitudes (easements). For example, the management may require access to units; however, owners of commercial units such as banks and jewellery stores may have security concerns and will be reluctant to provide unrestricted rights of access for such purposes. In a properly designed mixed-use project within which each component of the scheme is largely self-sufficient, disputes can be avoided by providing a separate servitude (for example for access) to each of the user components. Reserved servitudes should in principle be avoided where interaction between users is not reasonably anticipated and should in general be limited to uses that do not adversely affect the other owners and users.<sup>11</sup>

### 2.4 Zoning and building regulations

The developer will need to make sure that the proposed mixed-use project does not conflict with land use and zoning designations and must keep in mind that the relevant local municipality's approval and permitting process may be rigorous and

<sup>9</sup> Van Atta *et al* (n 1) 3 states that mixed-use projects often depend on interrelated facilities and structures, such as podiums, garages, utilities, central plants, and infrastructure.

<sup>10</sup> Winston (n 3) 39; Annexure 1 prescribed management rule 29(3) and (4) of the Sectional Titles Schemes Management Regulations GNR 1231 of 7 Oct 2016 in GG 40335 of 7 Oct 2016 makes provision for the installation of separate meters and prepayment meters in sectional titles schemes.

<sup>11</sup> Winston (n 3) 39. See in general on reciprocal servitudes (easements) Van Atta "Mixed-use, mixed ownership developments air space subdivision techniques and issues" 2003 *ACREL Papers* 7.

time-consuming. In addition the developer will have to take account of planned phasing of the construction of the project, the timing of use or occupancy permits and the consequent delay arising from the collection of multiple occupancy permits in a phased mixed-use project.<sup>12</sup>

### 2.5 Development agreements

In a mixed-use project involving multiple developers, extensive negotiation may be required in order to enter into a development agreement. Some of the issues to be resolved will relate to responsibility for securing local authority approvals and permissions; responsibility for securing the utility services required and the allocation of costs in this context; responsibility for the coordination and scheduling of construction by the multiple developers involved in the project; and responsibility for completion of construction of the buildings and improvements on the site.

Special consideration should also be given to the question of how to phase the development; whether the developers should obtain ownership of components within the project; the manner in which the construction of each component is financed; and the incorporation of the structure of the mixed-use strata title (condominium) scheme into the development agreement.<sup>13</sup>

## 3 *Governing documents*

A sectional titles scheme is established and operated by four basic documents,<sup>14</sup> namely the title conditions of the scheme;<sup>15</sup> sectional titles plan (strata title plan, condominium plats and plans) which subdivides the building and the land into units, common property and exclusive use rights (limited common property);<sup>16</sup> the prescribed management rules (by-laws) which essentially regulate the operation of the owners' management association (body corporate) and the affairs of the strata

<sup>12</sup> Winston (n 3) 39-40.

<sup>13</sup> Winston (n 3) 40; for more detail on development agreements see Rolando (n 1) 47.

<sup>14</sup> Lundquist (n 1) 99-100; Note "Common rights and obligations among unit owners under the Minnesota Condominium Act" 1984 *William Mitchell Law Review* 166-167. Attention must be drawn to the fact that American condominium schemes in addition need a declaration (a specific kind of articles of incorporation) which must be recorded for the establishment of the owners' management association. In South Africa, the body corporate is established as soon as the developer furnishes a copy of a certificate certifying that the first unit in the scheme has been transferred to a purchaser to the chief ombud or the ombud service in the head office of the ombud service in Sandton. See the amendment of s 36(1), (2) and (3) of the Sectional Titles Act 95 of 1986 by item 18 of the schedule to the Sectional Titles Schemes Management Act 8 of 2011. According to Rolando (n 1) 43 the declaration of United States condominium schemes requires for the establishment of a condominium scheme the constitution of the scheme or the comprehensive statement of the rights and duties of the owners. She states at 43-44 that the governing documents of a project is driven by the following four factors: whether one or more developers and possibly an anchor tenant makes decisions concerning the content of the governing documents; whether the project consists of a single high-rise building with multiple uses or several buildings, each with its own independent systems; whether the uses are roughly equivalent or whether there is a dominant use; and the cost allocation for areas and facilities that are shared. See also Van Atta *et al* (n 1) 5 on the questions to be addressed by the governing documents and Van Atta (n 11) 2 for the complexity of the documents for multi-storey mixed-use multiple owner developments.

<sup>15</sup> See s 11(2) and (3)(b) of the Sectional Titles Act 95 of 1986.

<sup>16</sup> See in general Tudzarov "Platting the condominium: is it required?" 1986 *Real Estate Law Journal* 22.

title (sectional titles) scheme in general;<sup>17</sup> and the management rules added by the developer and the body corporate by a unanimous resolution to attend to the peculiarities of the particular scheme.<sup>18</sup>

In general, the governing documents must be carefully tailored to reflect the particulars of the site, buildings, uses and users of the project. The counsel preparing the governing documents must be thoroughly familiar with the project and must understand how the developer intends to develop the project and sell or lease the units in the project.<sup>19</sup>

The title conditions (declaration in the United States) of a mixed-use scheme supplemented by sectional titles plans (plats and the condominium plan in the United States) must carefully and accurately set out which areas, features, services and utilities are shared exclusively by the owners of the commercial or residential components in the scheme and which aspects are shared by all the owners in the scheme.<sup>20</sup> The basis for such allocation must also be shown. As far as shared areas are concerned, most condominium statutes distinguish between general common elements (common property) and limited common elements (exclusive use rights), with general common elements being at the disposal of all owners and limited common elements being demarcated for the use of only some owners (for example, owners of commercial units). General common property (exclusive use rights) include roads, driveways, drop offs, sidewalks, landscaped areas, open spaces, passenger elevators, lobby areas, signage for the project, parking lots, and parking garages. However, in a mixed-use condominium drop-off areas,<sup>21</sup> lobby areas and signage for a particular component of the scheme may be demarcated as limited common elements for the sole use of the owners of the commercial component, while special elevators for reaching the residential component of the scheme on the higher storeys of the building may be demarcated as limited common property for the sole use of owners within the residential component.<sup>22</sup>

The governing documents of the mixed-use condominium scheme must also try to balance the diverse operations in the different components of the scheme. On the

<sup>17</sup> The prescribed management rules are contained in Annexure 1 of the Sectional Titles Schemes Management Regulations.

<sup>18</sup> Sectional Titles Schemes Management Act 8 of 2011 s 10(2). In terms of s 10(5) the chief ombud must examine any amendment of the prescribed management rules of Annexure 1 and must approve it if he or she is satisfied that such amendment is reasonable and appropriate to the scheme. If the chief ombud approves the amendment, he or she must issue a certificate to that effect. An amendment comes into operation on the date the certificate is issued or on the opening of the sectional titles register for the scheme, whichever is the latest.

<sup>19</sup> Rolando (n 1) 45-46.

<sup>20</sup> Van Atta (n 11) 4 states that although some portions of the project might be discrete to certain components such as independent elevator lobbies and shafts for elevator cabs, independent utility facilities, and, at times, separate facilities for heating, ventilating and air conditioning, there are almost invariably some base facilities which are common to all of the components, including the roof areas, the building exterior, common area lobbies and similar areas. The governing documents must indicate who has responsibility for what particular facilities, and how decisions will be made with respect to the budgeting, management, maintenance, operation, and replacement of these facilities over time. At 5 he points out that parking facilities and structures require special attention in the governing documentation.

<sup>21</sup> According to Rolando (n 1) drop-off areas include shipping and receiving areas, truck docks and truck ramps and approaches, areas for truck loading, unloading, parking or turnabouts, freight elevators, and service elevators.

<sup>22</sup> I adapted the examples mentioned by Winston (n 3) 41 to fit traditional condominium structures. See also Rolando (n 1) 44, who distinguishes between general shared facilities and limited shared facilities.

one hand owners within the commercial component must be allowed to operate their businesses in accordance with their intended uses and at the level that commercial operators would typically expect.<sup>23</sup> On the other hand the needs of owners of the commercial component must be balanced with the reasonable expectations of the owners of the residential component of the scheme.<sup>24</sup>

Accordingly, some general matters that must be addressed in the governing documents are as follows: architectural controls and flexibility for retail users; security;<sup>25</sup> insurance requirements;<sup>26</sup> expropriation (condemnation) and casualty losses<sup>27</sup> and the obligation to rebuild and/or right to terminate the condominium;<sup>28</sup> review, approval and oversight of proposed construction work;<sup>29</sup> common promotion of the project; reapportionment of size of units; mortgage creditor's (lender's) rights;<sup>30</sup> rights to freely lease, transfer and finance the unit;<sup>31</sup> and rights of first offer or first refusal.<sup>32</sup>

In order to market and sell residential units in a mixed-use commercial and residential scheme, prospective purchasers will need to be assured that commercial uses in the building would be compatible with a residential family lifestyle.<sup>33</sup> Although the prohibition of certain "offensive" business enterprises such as tattoo parlours and adult book stores may be uncontroversial, limitations on the scope and nature of uses such as restaurants, bars, and dry cleaners, which may be deemed offensive by some residents given possible noise, odour, and concerns over hours of operation, should be carefully considered.<sup>34</sup>

Equally, the governing documents should address potential concerns of the owners of units in the commercial component. These concerns generally relate to

<sup>23</sup> Rolando (n 1) 50 suggests that the governing documents must allow tenants of commercial units to operate in accordance with their intended uses and to assume that they will have the protection afforded to commercial unit owners.

<sup>24</sup> Winston (n 3) 42.

<sup>25</sup> Rolando (n 1) 45 mentions that security measures are particularly important at the boundaries between commercial and residential components of mixed-use schemes. At 53 she mentions that security includes monitoring and alarm systems, monitor cameras and viewer screens, gates and manned security centres and roving surveillance personnel.

<sup>26</sup> Sufficient insurance must be contracted to insulate the unit owners against liability for accidents or damages occurring to or within the shared areas and facilities. See Rolando (n 1) 45; Jones "Office condominiums: Developer opportunities. Marketing and structuring" 1981 *Real Property, Probate and Trust Journal* 502, 507 states that serious thought should also be given to the introduction of business interruption insurance which protects a business from losses, including loss of net profits, due to inability to operate because of fire and other hazards.

<sup>27</sup> Namely losses suffered on account of the complete or partial destruction of the sectional title building.

<sup>28</sup> Van Atta (n 11) 10-11.

<sup>29</sup> Van Atta (n 11) 8.

<sup>30</sup> Rolando (n 1) 50 suggests that mortgagees must be allowed to finance the purchase of the entire property at the initial stage and the purchase of individual units in later stages. Leeds, Peterson and Van Atta "Cost allocations in mixed use, mixed ownership developments" 2014 *American College of Real Estate Lawyers* 13 note that the United States Uniform Common Interest Ownership Act's six months' priority lien over a prior registered mortgage for common expense in favour of the owners' association has been adopted in several United States jurisdictions.

<sup>31</sup> Rolando (n 1) 51.

<sup>32</sup> Winston (n 3) 42.

<sup>33</sup> Rolando (n 1) 51 suggests that the governing documents must contain limits on or prohibitions against undesirable uses in order to maintain the quality of life.

<sup>34</sup> Winston (n 3) 41-42. Rolando (n 1) 50 suggests that except in commercial dominated mixed-use projects, the governing documents must discourage commercial uses so as not to discourage residential uses.

the ability to lease, transfer, and finance commercial units;<sup>35</sup> equitable allocation of costs for shared facilities; equitable voting and management operation; signage; security; control of specific areas within the project; exclusive operating rights and the right to restrict competitors;<sup>36</sup> use restrictions;<sup>37</sup> parking availability and cost to customers for parking privileges;<sup>38</sup> appearance and uniform maintenance and repair standards for the project;<sup>39</sup> trash disposal;<sup>40</sup> deliveries of goods; hours of operation; and possible conflict with the right of access to the general public within schemes.<sup>41</sup>

In the final analysis, the governing documents should have provisions that prevent the management board (trustees) from introducing rules that would discriminate against commercial and residential uses and management decisions that would adversely and materially restrict commercial or residential uses. It is equally important that the governing documents contain provisions that allow for flexibility in altering the governing documents to accommodate changes in the marketplace and the future operation and viability of the project.<sup>42</sup>

As the management of a mixed-use strata title (condominium) scheme involves the management and operation of the facilities within the scheme, the governing documents need to identify who will own the various facilities within the project; which facilities are intended to be shared; and who will be responsible for paying the costs of operating and maintaining the facilities. In a mixed-use strata title (condominium) project, it is also advisable to have provisions in the governing documents that set forth who will control special events within the project<sup>43</sup> and whether the commercial operators will have the right to use outdoor areas for sales, kiosks, services, and/or promotions (either all year round or on a seasonal basis).<sup>44</sup>

With regard to the management of shared facilities, the governing documents of a mixed-use scheme should require that decisions affecting these facilities should be taken at management board (trustees) level. The owners of each component of the mixed-use scheme should be given the right to appoint one or two members of the board. It may also be necessary for the governing documents to require unanimous

<sup>35</sup> Rolando (n 1) 51.

<sup>36</sup> Rolando (n 1) 51 suggests that the governing documents should contain reasonable control on other types of businesses to maintain the proper operation of existing businesses.

<sup>37</sup> Van Atta (n 11) 5-6 warns that thought must be given to use restrictions, as commercial owners will not want to be subject to charges or enforcement by the owners of the residential component. The owners of the non-residential and residential portions of a mixed-use property may have their own expectations as to the degree of flexibility of uses and limitations on types and nature of uses to protect their own use and comfort, and also, as owners of separate interests, their long-term investment in the property. Areas of particular concern will include the use and storage of hazardous substances and activities that might require modifications of the physical structure of the building to accommodate persons with disabilities.

<sup>38</sup> Rolando (n 1) 54 suggests that the governing documents should address whether the parking is general or limited common property; the required parking ratios for the different components; charges for parking (monthly, hourly, daily, or special events); valet parking; employee parking areas; operation of parking areas; and allocating income and expenses from parking.

<sup>39</sup> Winston (n 3) 42. Rolando (n 1) 51 suggests that the documents should prescribe clear standards of maintenance and repairs of the scheme as well as mechanisms to enforce the standards.

<sup>40</sup> According to Rolando (n 1) 52 this includes trash handling and disposal facilities, including trash rooms, shoots, compactors, trash recycling systems and trash removal.

<sup>41</sup> Rolando (n 1) 45.

<sup>42</sup> Winston (n 3) 42; Rolando (n 1) 51 and 56.

<sup>43</sup> Rolando (n 1) 45 suggests that the governing documents must assign responsibility for the grand opening of the commercial component of the scheme as well as continued promotion and marketing. At 52 she includes art shows, festivals, concerts and holiday events under promotional and special events.

<sup>44</sup> Winston (n 3) 42.

resolutions of the board for important decisions and the consent of the owners of a particular component to decisions that could adversely affect the interests of the members of their component.<sup>45</sup> For example, a decision by the management board to adopt design guidelines for signage should generally require the concurrence of the board member designated by the commercial owners.<sup>46</sup>

#### 4 *Various management structures*

##### 4.1 General

One of the critical issues for consideration when drafting the governing documents is the management structure of the condominium. The developer must choose one of the following three alternative management structures:

- (a) a single management structure;
- (b) a two-tier management structure consisting of a master owners' association and subsidiary associations; and
- (c) a linked scheme connecting a number of independent condominium schemes.

Regardless of the structure that is used, it must be sufficient to satisfy the needs of the project and the future owners within the project.<sup>47</sup>

##### 4.2 Single management structure

The simplest structure is where a single management association (body corporate) is created in terms of applicable legislation or by the governing documents of the scheme. This association has sole responsibility for maintaining and operating the shared facilities and providing the services within the strata title scheme.<sup>48</sup> Single management associations are prevalent in single building strata title (sectional titles) schemes containing a mixture of residential and commercial components with roughly equal voting strength.<sup>49</sup> This is usually the case where the design of the condominium building is such that the residential and commercial components of the scheme are well isolated.<sup>50</sup> In circumstances where such isolation does not exist, the single association structure will be fraught with many potential problems given the potential for conflict between the owners of the residential and commercial components.<sup>51</sup>

The single association provides several advantages: economies of scale lead to more efficient management, maintenance and other necessary services; contracts are more economical than separate contracts entered into by each separate association as in a two-tier management association; and common elements are operated more efficiently, benefiting all units and facilitating communication among all owners.

<sup>45</sup> Rolando (n 1) 50 suggests that the management association should be prevented from changing the by-laws or rules pertaining to commercial or residential components or discriminating against the commercial or residential component; and from adopting resolutions that would adversely affect or prohibit commercial use. At 56 she suggests that unit owners should be given a veto right to prevent certain material amendments such as changes in the scheme, addition of a competitor and major renovations.

<sup>46</sup> Winston (n 3) 42.

<sup>47</sup> Lundquist (n 1) 101; Winston (n 3) 41.

<sup>48</sup> Winston (n 3) 41.

<sup>49</sup> Lundquist (n 1) 101.

<sup>50</sup> Lundquist (n 1) 102.

<sup>51</sup> Winston (n 3) 41.



In summary, the key advantages of a single association are simplicity, efficient management and maintenance, and ease of communication among owners.<sup>52</sup>

A single management association management structure can operate efficiently only if the developer can accommodate the variation in maintenance requirements, energy consumption, management goals, and customer traffic in an equitable manner. If these matters can be resolved equitably, a mixed commercial and residential or a mixed commercial and office strata title scheme can operate effectively despite a mixture of business, professional and retail units and despite the fact that the businesses, professional specialties, product lines and hours of business may vary substantially.<sup>53</sup>

The allocation of common expenses creates difficulties due to the fact that it is typical for condominium statutes to provide that all common expenses are to be allocated on the basis of a fixed percentage interest assigned to each strata title unit. The formulas employed are generally based on proportionate size (square footage or volume) or value of a unit, failing which expenses are shared equally.<sup>54</sup> However, the use of the residential and commercial units in a mixed-use strata title scheme do not always generate common expenses proportionate to their size or value. Although the size of a section might be appropriate for the allocation of common expenses in a strictly residential project consisting of units of equal size and having approximately the same number and type of occupants, it might be entirely inappropriate in a mixed-use project consisting of residential units, offices, a hotel and commercial stores in a single high-rise building. All owners might be required to share in the common expenses in proportion to the size of their units, yet these owners use the available utilities and facilities of the property to a radically different degree. Commercial units are only utilised for a limited number of hours per week and may, depending on the type of business involved, require a disproportionately greater amount of electricity than residential sections. All these variations militate against an allocation of common expenses on the basis of a rigid criterion such as the floor area or value of units.<sup>55</sup>

In terms of section 11(2) of the Sectional Titles Schemes Management Act 8 of 2011 the developer may on submission of an application for the opening of a sectional title register or the body corporate may later (subject to certain conditions) by special resolution make rules by which the liability of the owner of any section to contribute to common expenses is modified.

<sup>52</sup> Lundquist (n 1) 101-102.

<sup>53</sup> Lundquist (n 1) 102.

<sup>54</sup> In terms of s 32(1) and (2) of the Sectional Titles Act 95 of 1986, the quota of a sectional owner of a residential section is calculated on the floor area of the section, while the quota of non-residential section is determined by the developer. In terms of the Minnesota Uniform Condominium Act § 515A.2-108(a) (2015 version), common expenses are allocated in such manner that each of the items is equally allocated or is allocated according to the proportion of the area or volume of each unit to the area or volume of all units, and the items need not be allocated the same for all purposes. The declaration may provide that a portion of each common expense assessment may be allocated on the basis of equality and the remainder on the basis of area or volume of each unit.

<sup>55</sup> Judy and Whittie "Uniform Condominium Act: selected key issues" 1978 *Real Property, Probate and Trust Journal* 460; Note (n 14) 180. In terms of s 11(2) of the Sectional Titles Schemes Management Act 8 of 2011 the developer may on submission of an application for the opening of a sectional title register or the body corporate may later (subject to certain conditions) by special resolution make rules by which the liability of the owner of any section to contribute to common expenses is modified. The formulation of a special rule in this regard to apportion common costs in such a manner that each component would have to pay its own cost would be possible. The ideal solution would be to adopt a two-tier management structure as set out below.

Consequently, as different services and facilities may be utilised by or benefit different user groups in different ways, some strata title statutes allow the developer to consider the use of alternative cost allocation, especially in the case of a mixed-use scheme. On a careful review of all shared-use areas and shared services, some commentators conclude that the use of an alternate cost allocation schedule, based on the anticipated use by the unit owners of each component of the shared use area or the service in question, would be the most appropriate and equitable means of allocating costs in a mixed-use scheme.<sup>56</sup> This is manifested in the statutory provisions of some jurisdictions that allow the association to charge use fees for the use of common elements such as recreational facilities, laundry machines, and parking areas.<sup>57</sup> Again, the different use levels for janitorial and trash disposal services in the case of commercial units are readily measurable and may be allocated directly to the unit that is benefitted. In terms of the Uniform Common Interest Ownership Act the condominium declaration can allow class voting on certain matters which would allow each group of owners to vote on the apportionment of common expenses pertaining to their particular units.<sup>58</sup> Alternatively the judicious designation of limited common elements can separate maintenance obligations and responsibilities, common expense obligations, and rights of use and access among different groups in a mixed-use condominium and avoid conflicts in those areas.<sup>59</sup>

Some statutes allow the allocation of some common expenses on actual consumption based on actual measurement and metering, as in the case of expenses relating to the heating and air conditioning of units.<sup>60</sup> Allocation according to actual consumption or use is also preferable for expenses relating to security systems, personnel, parking, and recreational facilities. The extent of use and the expenses generated by such use may vary substantially depending on which type of unit the residents occupy or the type of building in which the unit is located.<sup>61</sup> As metering of owners' consumption provides an exact measurement of benefits to particular units, it easily qualifies as an appropriate exception to the allocation of common expenses on the basis of equality or unit size or value.<sup>62</sup> To ensure that the association can use these methods of allocation, the statute or the constitutive documents (declaration) must make provision for separate metering and measurement.<sup>63</sup>

In mixed-use commercial-residential projects, the broad powers of the management board (trustees) and the management corporation (body corporate) must be restricted to prevent inequities. The commercial minority, which typically occupy a minority position both in total size and voting strength, must be assured that the residential majority will not unreasonably interfere with their economic

<sup>56</sup> Winston (n 3) 43.

<sup>57</sup> The Minnesota Uniform Condominium Act § 515A.3-102(8) (2015 version), which provides that unless limited by the provisions of the declaration (constitutive document) the association may "(8) impose and receive any payments, fees, or charges for the use, rental, or operation of the common elements other than limited common elements".

<sup>58</sup> UCIOA § 2-107(d)(iii) and see comment 9 on § 2-107.

<sup>59</sup> Lundquist (n 1) 103.

<sup>60</sup> Annexure 1 prescribed management rule 29 (3) and (4) of the Sectional Titles Schemes Management Regulations GNR 1231 of 7 Oct 2016 in GG 40335 of 7 Oct 2016 makes provision for the installation of separate meters and prepayment meters in sectional titles schemes. This could take care of certain of the common costs generated by the various components.

<sup>61</sup> Lundquist (n 1) 111.

<sup>62</sup> Lundquist (n 1) 112. At 112 and 113 he examines the alternative theory of actual consumption allocation of common expenses, namely that of estimation of energy levels in schemes where it is impractical to install energy metering devices for each unit or each type of unit.

<sup>63</sup> Lundquist (n 1) 112.

use of commercial units, for instance by introducing noise restrictions in its by-laws (conduct rules) that would restrict the use of an industrial unit. Likewise, a chiropractor in a medical clinic condominium must be assured that the majority will not prohibit his practice within the project.<sup>64</sup>

The consumer protection provisions in many strata title statutes are unfavourable to a single building project containing residential and non-residential units. These statutes require the developer to provide a complete disclosure statement to all prospective residential unit purchasers. As compliance with the disclosure requirement can be an expensive procedure,<sup>65</sup> a developer may seek to avoid it when dealing with commercial customers, some of whom may want to negotiate some of the items that would normally be stipulated in a disclosure statement. As a result protracted negotiations could be required before a disclosure statement with non-residential purchasers is agreed.<sup>66</sup>

As already alluded to, a developer can avoid potential conflicts through careful architectural planning and documentation designed to separate exclusive use areas (limited common elements) used predominantly by the owners of a particular component of the single building. Limited common elements, including corridors, elevators, entries, and other pedestrian areas within the building, can be established for exclusive use by owners of a particular component of the building. In practice, the pedestrian areas in the project's residential and commercial portions are often separated to ensure adequate security. Residential owners may wish to restrict access from the commercial portion; whereas commercial owners may wish to restrict access from the residential portion during non-business hours. Similarly, recreational, laundry, and parking facilities may be allocated as limited common property for the exclusive use by owners of a particular component of the single strata title building.<sup>67</sup>

Most condominium statutes assume that limited common areas must be maintained by the owners to whom these areas have been allocated. In a single building strata title scheme, containing both residential and commercial units, the pedestrian area, toilets and parking spaces serving the commercial units as limited common property may be maintained and funded exclusively by the commercial owners, who typically employ their own maintenance contractors. The residential pedestrian areas, on the other hand, will in all likelihood be maintained by the association, but the costs will be allocated exclusively to the residential units.<sup>68</sup> Similarly, if the recreational facilities are designated as limited common elements benefiting only the residential units, they need not be made available to the commercial owners, their guests, or employees. However, the commercial owners would not have to share the costs of maintaining and operating those facilities.<sup>69</sup>

<sup>64</sup> Lundquist (n 1) 100 and 105.

<sup>65</sup> Lundquist (n 1) 104 note 32 states that disclosure statements tend to be complex documents that require time-consuming and expensive preparation. These statements also increase a developer's risk, because inaccurate assertions or information may be the basis of a claim by a purchaser.

<sup>66</sup> Lundquist (n 1) 104.

<sup>67</sup> Lundquist (n 1) 109.

<sup>68</sup> See for instance the Minnesota Uniform Condominium Act § 515A.3-114(c) (2015 version): "Except as provided by the declaration any common expense associated with the maintenance, repair, or replacement of a limited common element shall be assessed against the unit or in equal shares against the units to which that limited common element was assigned at the time the expense was incurred."

<sup>69</sup> Lundquist (n 1) 109-110.

Consequently, by careful design and establishment of limited common elements, the developer can demarcate separate portions of the strata title scheme to prevent unwanted access from other portions. The developer can also make provision for differing levels of use and maintenance and ensure that the cost of operating and maintaining limited common areas will be borne solely by the relevant owners rather than by the owners as a whole.<sup>70</sup>

However, it should be noted that despite the flexibility afforded to developers and associations in statutes and constitutive documents to adjust the allocation of common expenses, procedures that result in unsystematic or unreasonable allocation of common expenses should be prohibited. Lundquist<sup>71</sup> warns that the association (body corporate) should not be able to allocate the cost of carpet cleaning and replacement on the ground floor of the building to the units on that floor simply because the traffic levels are higher on that floor. He argues that the higher traffic levels on the first floor will usually be generated at the convenience of all unit owners, not merely those on the lower levels, and that the appearance of the common elements on the lower level is of value and importance to all owners. He also suggests that roof repair should not be allocated to the units on the top floor, because the effects of roof deterioration will generally appear there first.

#### 4.3 Two-tier management structure with a master owners' association and subsidiary owners' associations

In larger, more complicated mixed-use schemes, it may be preferable to manage the scheme by a two-tiered management association consisting of a master or main management association (body corporate) and several subsidiary management associations (bodies corporate).<sup>72</sup> The fact that each subsidiary association has its own organs (namely a general meeting and an elected executive board (trustees)), ensures autonomy to the owners of the various commercial, residential and office components of the scheme to manage their own affairs in tandem with the master

<sup>70</sup> Lundquist (n 1) 110.

<sup>71</sup> Lundquist (n 1) 114 note 66.

<sup>72</sup> According to Lundquist (n 1) 104 a two-tier condominium consists of a master condominium and subsidiary condominiums. Within the master condominium certain areas are designated for either commercial or residential uses. These areas comprise the components of the building that form the second-tier condominium. At 104 note 33 he explains that, typically, the declaration and floor plan of the master condominium will designate a large area or areas comprising partial, single, or multiple floors as a single unit. Thereafter, a second-tier condominium can be created within each of those units. The declaration and floor plans of the second-tier condominiums further subdivide these components of the building into units for purchase and occupation by businessmen or residents. At 104 Lundquist warns that it is important to include the boundaries of the second-tier condominiums in both sets of condominium documents as this will ensure that maintenance responsibilities for, and ownership of the condominiums are clearly defined. See also Winston (n 3) 41; Rolando (n 1) 48, 49 and 50 and Van Atta (n 11) 5. In my opinion the two-tier structure concerns only the management of the strata title schemes. By referring to master and subsidiary condominiums, it is suggested that the authors fail to draw a clear distinction between two-tier schemes and the linkage of several independent condominiums into an amalgamated structure. For the application of a two-tier management system in the Netherlands, see Groetelaers and Ploeger "The Management of redeveloped industrial areas with mixed use in the Netherlands" 2010 *Journal of Legal Affairs and Dispute Resolution in Engineering and Construction* 73-80.

management association.<sup>73</sup> As each component has autonomy for allocation of expenses and the adoption of appropriate by-laws, a fairer allocation of expenses and a more harmonious governance of the scheme are accomplished.

The two-tier management structure must be established by the developer in the constitutive documents of the scheme.<sup>74</sup> In Singapore the areas governed by subsidiary management corporations (bodies corporate) are indicated on the strata or condominium plans as *limited common property* allocated to the owners of the component of the building governed by the subsidiary condominium association concerned.<sup>75</sup> Thus the entire land and buildings in the scheme are divided into general common property governed by the master condominium association and various components of limited common property governed by appropriate subsidiary associations. The same happens in the case of a mega scheme where the individual buildings are governed by subsidiary condominium associations in tandem with a master association for the whole scheme. The idea is that a two-tier structure will facilitate the management of a mixed-use strata title development by allowing the formation of layered management components (the rationale being that each component is managed by a subsidiary management corporation representing the interests of a specific user group).<sup>76</sup> The two-tier approach is appropriate for several types of projects: a mixed residential and commercial project; a resort or residential project containing traditional apartment units and hotel or recreational units; and a commercial project containing separate areas for professional, retail, and industrial uses.<sup>77</sup>

In a mixed residential and commercial project, the master association is responsible for maintaining the building's exterior, structure and grounds, including landscaping and gardening. It is also responsible for regulating the use of common areas open for use by both residential and commercial components as well as the interface between the rules and regulations adopted in one particular component and the effect they may have on the use of units in another component. Lundquist<sup>78</sup> cites as an example the scenario where the residential component within the guise of general rules and regulations enacts noise restrictions preventing the operation of certain retail businesses in the commercial component or requiring as a reasonable security measure that all doors to the condominium scheme could be opened only by key or buzzer. In order to avoid unfair treatment of unit owners in a particular component, the master condominium association, consisting of representatives

<sup>73</sup> According to Lundquist (n 1) 105 the master association administers the common management of all units in accordance with the provisions of the master declaration, which limits the power of the master association to manage the units comprising the second-tier condominium. Consequently, each second-tier association is responsible for those aspects of management primarily affecting its unit owners. At 108-109 Lundquist states that in a multi-storey building where the second-tier condominium comprises one or more floors, the exterior boundary of the second-tier condominium is usually the interior surface of the exterior walls. In a two-tier condominium consisting of two or more buildings, each of which is a separate second-tier condominium, the boundary of each second-tier condominium is normally the exterior wall of its building. At 109 note 50 he reiterates that the boundary specification between the master condominium and the second-tier condominium is important because of its effect on maintenance responsibilities, adding that another consequence of such specification is the extent to which one association must have access to common elements in order to accomplish its maintenance responsibilities.

<sup>74</sup> Winston (n 3) 40-41.

<sup>75</sup> Sections 77 and 78 of the Building Maintenance and Strata Management Act 47 of 2004.

<sup>76</sup> See also Winston (n 3) 40.

<sup>77</sup> Lundquist (n 1) 104.

<sup>78</sup> Lundquist (n 1) 105.

of the various subsidiary associations in the particular strata title scheme, should operate in an equitable and non-discriminatory manner. It could for instance require the consent of commercial owners to amendments to the declaration limiting the commercial use of a second-tier commercial component.<sup>79</sup>

The subsidiary residential condominium association is responsible for the maintenance and management of the residential component of the scheme. Besides its responsibility for the maintenance and management of the commercial component of the scheme, the subsidiary commercial condominium association is also responsible for meeting the particular business requirements of the units in the commercial component. This may include overseeing the regular cleaning of commercial corridors; providing comprehensive security; enhancing cooperative promotional efforts; and enforcing rules and regulations governing commercial activities.<sup>80</sup>

#### 4.4 Linkage of a large number of independent condominium schemes

As an alternative to a two-tier management structure, the developer can link several autonomous schemes which are developed on separate adjacent plots of land with its own condominium plan, by-laws and management association. Each autonomous scheme is linked to the other by reciprocal easements, title conditions (covenants) and reciprocal arrangements. This is most appropriate for mega strata title schemes (multi-building projects) consisting of a large number of separate residential, commercial or office buildings or a large single building scheme consisting of residential and commercial units. In these schemes coordinated management and maintenance are not essential on a continuing basis.<sup>81</sup>

The principal advantages of such a linked scheme is that each association is responsible only for the operation of its own scheme. As the administrative burden is reduced, each association is free to concentrate on the unique problems facing its own unit owners. The major disadvantage is that due to the lack of adequate communication, there is a lack of solidarity among the owners of the multiple buildings. The developer also has to give up some of the economies of scale, continuity of management and ease of communication among owners that is a key feature of the single association framework.<sup>82</sup>

The documentation regulating the relationships between the distinct strata title schemes is both extensive and complicated. Servitudes for support, access and utilities must be created with the constitutive documents of each strata title scheme specifying the location and extent to which the easements may be used. The conditions of title establishing the servitudes, covenants and restrictions regulating the relations between the various independent strata title schemes must

<sup>79</sup> Lundquist (n 1) 105-106. Winston (n 3) 40 submits that the governing documents for the master condominium may provide that each owner within the master association (for example, a retail owner, residential owner, and office owner) has the right to appoint a member to the executive board of the master association as well as an equal vote on the master association's decisions. It may also be helpful to include a "deadlock" provision in the governing documents whereby third-party mediation and/or arbitration is used if the board of directors is unable to reach consensus.

<sup>80</sup> Lundquist (n 1) 105 mentions these examples in his discussion of two-tier management associations. See further Van der Merwe and Paddock "Two-tier governance for mixed-use and large-scale sectional titles schemes" 2008 *SALJ* 573 585-591.

<sup>81</sup> See in general Inglis "Expanding condominiums in Ohio" 1978 *Case Western Reserve Law Review* 228; Van der Merwe and Sonnekus I *Sectional Titles, Share Blocks and Time-sharing – Sectional Titles* (Service Issue 21 November 2016) 12-6 – 12-12; Winston (n 3) 41; Van Atta *et al* (n 1) 4.

<sup>82</sup> Lundquist (n 1) 106-107.

be carefully prepared and must contain provisions regarding the effect of damage to and destruction of any of the distinct schemes, expropriation (condemnation), insurance and required levels of maintenance. This specificity differs sharply from the mere implication of the existence of easements in single building condominiums with a single association or a two-tiered management system.

Furthermore, as separate sectional title schemes are not bound by an overall master association, the constitutive documents must set out the overall structure of the linked schemes and mechanisms for arriving at common decisions, for the resolution of disputes, and payment of expenses relating to the maintenance of items of mutual use and benefit. Matters of mutual interest such as the overall structure of the linked schemes, large-scale renovations and the economic and political issues facing the linked schemes need to be dealt with. Lundquist suggests that arbitration should be provided to resolve disputes and to the extent that these disputes involve maintenance, repair, rehabilitation or renovation, that architects and other appropriate professionals should be included on the board of arbitrators.<sup>83</sup>

## 5 Conclusion

As mixed-use condominiums become more widespread,<sup>84</sup> the marketplace will establish standards for management, expense allocation, and interaction among differing types of owners to balance the diverse needs and objectives of the multiple-user components in a particular strata title scheme. Modern strata title legislation offers developers and owners' associations sufficient flexibility to construct an efficient and harmonious strata title scheme. In choosing the single association, the two-tier structure or by linking autonomous strata developments, a developer can balance the competing management aspirations of the different components and ensure that each individual component is operated fairly. Intelligent architectural design, appropriate designation of limited common elements and sensible adaptation of provisions relating to the allocation of common expenses will allow an equitable distribution of the costs of the strata title schemes among the units in a given scheme.<sup>85</sup>

## SAMEVATTING

### REGSVERGELYKENDE STUDIE VAN SOMMIGE VAN DIE UITDAGINGS VERBONDE AAN DEELTITELONTWIKKELING WAT VIR GEMENGDE GEBRUIK VOORSIENING MAAK

Die toenemende skaarsheid van bekostigbare boupersele in middestede, en die vernuwing van middestede dwarsoor die wêreld, maak gemengde deeltitelontwikkeling 'n aantreklike opsie vir voornemende kopers. Die kopers van besigheids- en kantooreenhede, verkry 'n gesogte lokaliteit in die middestad sowel as 'n aantal potensiële klante in dieselfde gebou. Buiten 'n gesogte middestad-lokaliteit, bekom die kopers van residensiële eenhede ook die gerief om moeiteloos inkopies in dieselfde gebou te kan doen en aldaar van professionele dienste gebruik te kan maak.

<sup>83</sup> Lundquist (n 1) 106-107.

<sup>84</sup> For the popularity of mixed-use sectional titles schemes in South Africa, visit Google: South Africa mixed-use sectional titles schemes and click on More Images for South African mixed-use sectional titles schemes; see however Van Atta *et al* (n 1) 1-3 on the impact of the financial and market crisis of 2008-2010, which in their words was "nowhere more acute than on mixed-use, combined residential and commercial projects" in the United States. At 2 they refer to the complexity of modern financing of large mixed-use projects.

<sup>85</sup> Lundquist (n 1) 114; Winston (n 3) 43; Rolando (n 1) 55-56.

Die ontwikkelaar moet die bestuursdokumente van die skema sorgvuldig met die nodige regsadvies voorberei ten einde die belange van die eienaars van die verskillende samestellende dele van die skema so goed as moontlik te probeer balanseer en ook voorsiening te maak vir aanpassings by toekomstige veranderende ekonomiese en sosiale omstandighede.

In hierdie bydrae word aangetoon dat die uitdagings wat gemengde deeltitelontwikkelings in Suid-Afrika in die gesig staar, dieselfde is as wat ontwikkelaars in Australië en die Verenigde State van Amerika ondervind. Die bydrae wys die verskillende kwessies uit waaraan aandag gegee moet word by die opstel van die bestuursdokumente van 'n gemengde deeltitelskema. Daar sal oorweeg moet word of die besondere skema deur 'n sentrale bestuursliggaam bestuur moet word en of daar voorsiening gemaak moet word vir afsonderlike subsidiëre bestuursliggame vir elkeen van die samestellende komponente van die gemengde deeltitelskema. Verdere sake wat aandag verdien, is onder andere hoe die koste vir die gesamentlike gebruik van sekere fasiliteite tussen die komponente verdeel moet word; hoe spesiale feestelikhede in die besigheidskomponent gereguleer moet word; die verlening van uitsluitlike voordele aan sommige komponente, byvoorbeeld die reg om mededinging te verbied; watter gebruiksbepelings ingevoer moet word; die beskikbaarheid van parkeerplekke vir eienaars, hul besoekers, klante en kliënte; universele onderhoudsvereistes vir die hele gebou; versekeringskwessies; en die aanvaarding van geskikte gedragsreëls vir die onderskeie komponente van die betrokke deeltitelskema.

#### **A PRINCIPLED vs A CASUISTIC APPROACH TO JUDGMENTS**

“Mansfield (the judge in the well-known restitution case *Moses v Macferlan* (1760) 2 Burr 1005; 97 ER 676) was a Scot; Scotland did not have two separate systems of law and equity – north of the border lay fusion. As a Scottish civilian-trained lawyer, Mansfield had the broad frame of mind developed in a legal system built on principle and by logical deduction, not by empirical induction from decided cases. He looked not for the writ, but for the principle; not to the decision in the decided case, but to the principle underlying the decision” Allsop “Restitution: some historical remarks” 2016 *Australian Law Journal* 561 569-570.