



Condo Mania

Success Rests on Experience of Team

[by Ken McCullough and Michael Rodgers]

The rationale for condominium conversion is deceptively simple: selling individual apartment units as condos will result in a substantially higher total price than selling the same property to a single buyer. Apartment owners considering such a strategy, however, are heading into unfamiliar territory, and should make sure they have experienced team members to help them avoid the pitfalls.

The economics of condo conversion can be lucrative for owners who understand the complexities of the business, or disastrous for those who miscalculate the market. It's significant that most successful conversions are conducted not by long-term owners, but by specialists who buy properties for the purpose of converting them within a couple of years.

Atlanta is a case in point. More than 3,000 condominiums have been sold in recent years in downtown Atlanta, a market where the condo concept was not widely accepted for most of the past two decades. The rising acceptance is due to a variety of factors, including an interest in downtown living to avoid lengthy commutes,

an influx of residents from condo-friendly cities such as New York and Chicago, and a trend toward "empty nesters" desiring proximity to cultural centers in a maintenance-free lifestyle. The condo surge started with industrial loft conversions, and has quickly spread to include new construction and conversions of existing apartment buildings. In the current environment, downtown apartment projects have been shelved while condo construction and conversion continues, with at least six additional projects in the pipeline.

The Atlanta condo boom has been fueled by local and out-of-town firms buying apartment properties cheaply and converting them at a significant profit. The problem is that only a few local real estate brokerage firms understand how to successfully market condos, and there is a similar dearth of attorneys and architects with direct experience in this unique market niche.

Marketing Approach

Finding an experienced marketing and sales agent is vital, if for no other reason

than the challenge of correctly pricing units. A typical strategy is to price condos low initially and raise prices gradually, in order to build momentum, create a sense of urgency and reassure buyers that their units will appreciate in value. In the wrong hands, this strategy can go awry very quickly. For instance, one property in Atlanta sold most of its units in one weekend at the initial low price, cutting into the seller's profit margins.

In other cases, converters have found that too much disparity in unit prices, even at a property with a similar disparity in unit sizes, creates problems because buyers of \$1 million condos often don't want to live in the same building as buyers of \$200,000 units.

In the conversion business, all the profit is made on the sale of the last few units. If the first 90 percent of units sell quickly, but the last 10 percent languish on the market, the converter can't achieve a return on investment to justify the labor-intensive conversion process.

If the converter reduces prices to sell the last few units, residents who bought at higher numbers are likely to be upset and may initiate frivolous litigation against the developer. On the other hand, if the last units take too long to sell, the converter may face competition from resales within the same building as well as from nearby new and/or converted projects.

Pricing condo units is somewhat easier for new construction projects, where the cost of amenities and materials can be compared to prices buyers will pay for those features, than it is for conversions, where the ability to add amenities and other features may be limited by the existing infrastructure.

To determine the feasibility and salability of various features, owners must engage



Essex House Condominiums started the conversion from apartments to condos in January.

architects and other design specialists with in-depth knowledge of condo buyers' priorities.

Know the Rules

Compliance with applicable state condominium statutes creates another set of difficulties for developers. Like many states, Georgia requires converters to provide each purchaser with a laundry list of relevant documents, including the condominium declaration and plan, the proposed budget for assessments and the developer's statement regarding the condition of the building.

Moreover, state statutes often require specific language to be included in the sales contract for the purchaser's benefit. Failure to comply may result in non-binding purchase agreements as well as civil penalties against the developer. Working with an attorney experienced with condo conversions is critical to avoiding complications under these statutes.

Even a firm with ample conversion experience must be cautious in entering a new market. For example, the strength of the Chicago condo market traditionally has depended on interest rates — when low rates permit condo mortgages for less than the cost of rent, the condo market takes off.

By contrast, demand in Atlanta has been driven more by demographic changes, such as downtown population growth and shifts from one submarket to another based on changes in the way neighborhoods are perceived.

Another factor in converting in Atlanta is the availability of tax credits for historic buildings as well as buildings in historic districts, which includes virtually every downtown property built before 1936.

The Georgia tax credit program effectively freezes the property assessment at the property's pre-conversion value for nine years after conversion, creating a major tax advantage for condo buyers

and a major selling point for converters. However, due to the lack of attorneys and others skilled in applying the historic tax credit program, few local converters have taken advantage of this program.

The condominium market in recent years has re-emerged as a powerful force in many downtown areas across the country. For some apartment owners, conversions will produce higher returns than maintaining properties as rentals. Owners that choose such a course, however, are well-advised to find the most experienced team of brokers, attorneys and architects to provide the expertise that will ensure a successful conversion. ■

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