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**REAL ESTATE FINANCE BUREAU**

**M E M O R A N D U M**

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Re: Certificates of Occupancy and Part 20 Offering Plans

October 13, 2015

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The Department of Law publishes this memorandum as a guidance document pursuant to New York State Administrative Procedure Act § 102(14).

**I. Background**

New York General Business Law (“GBL”) § 352-e(2-b) requires that:

[A]ll deposits, down-payments or advances made by purchasers of residential units shall be held in a special escrow account pending delivery of the completed apartment or unit and a deed or lease whichever is applicable, unless insurance of such funds in a form satisfactory to the attorney general has been obtained prior thereto.

The purpose of GBL § 352-e(2-b) is to prevent sponsors from using purchasers’ down payments for construction purposes, and to ensure that each sponsor completes its project. *See* L. 1977, c. 856, § 1, eff. Aug. 11, 1977, Departmental Bill, Sen. Intro No. 4402 (May 19, 1977).

For purposes of GBL § 352-e(2-b), in New York City, a completed unit is a unit for which the City’s Department of Buildings has issued a permanent certificate of occupancy (“PCO”). The Department of Buildings issues a PCO, sometimes also called a final certificate of occupancy, when the building is completed and substantially conforms to the plans previously filed with the Department of Buildings. New York City Administrative Code § 28-118.6.<sup>1</sup>

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<sup>1</sup> A temporary certificate of occupancy (“TCO”) may be issued by the Department of Buildings before a building is completed, if occupancy will not jeopardize life, health or property. New York Multiple Dwelling Law (“MDL”) § 301(4). A TCO expires 90 days after issuance, if not earlier, but may be renewed. *Id.* Upon the expiry of a TCO, a condominium’s lack of a certificate of occupancy has

## **II. Failures to Procure a PCO**

Each year, the Department of Law receives numerous complaints from condominiums across New York City that their buildings lack a PCO, despite having been substantially completed and occupied for years. There are myriad reasons why a condominium may find itself so-situated, some of which are unrelated to the soundness or habitability of its residential units. For example, issues sometimes arise related to the customization of a condominium's commercial unit (sometimes known as a "white box" unit when minimally finished) or renovations undertaken by an individual unit owner that must be completed before the Department of Buildings will issue a PCO that covers the entire building.

To be clear, sponsors of newly-constructed or gut renovation condominiums are obligated to procure a PCO for the entire building or the offered residential component in instances where the Department of Buildings will issue separate PCOs for different parts of the same building, notwithstanding the aforescribed or other issues. Sponsors should organize their sales of units and devise appropriate methods and measures that prevent foreseeable obstacles to issuance of a PCO from arising in the first place. Sponsors should also work cooperatively and in good faith with all necessary parties so as to minimize delays that prevent the Department of Buildings from issuing a PCO.

## **III.A Sponsor's Duty to Estimate, Document and Disclose the Sums and Work Needed to Procure a PCO**

Pursuant to his authority under GBL § 352-e(2-b) the Attorney General has promulgated regulations that provide that if a sponsor of a condominium closes title with unit purchasers without first having obtained a PCO, sponsor must maintain all purchaser deposits and funds in a special escrow account unless an engineer, architect or other qualified expert certifies that a lesser amount than that being held in the special escrow is reasonably necessary to obtain a PCO. *See* New York Compilation of Codes, Rules & Regulations ("NYCRR"), title 13, § 20.3(t)(13). In that event, the sum exceeding the so-certified amount may be released from the special escrow account (a "Permitted Periodic Reduction"). Alternatively, a sponsor may deposit with an escrow agent an unconditional, irrevocable letter of credit or a surety bond, or other collateral acceptable to the Department of Law, in the amount sponsor's expert has so certified.<sup>2</sup> *Id.* Creating

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substantial effects on its unit owners: without a certificate of occupancy, unit owners may find it impossible to renew their homeowner's insurance policies, refinance or resell their units.

<sup>2</sup> In certain circumstances, funds held by a sponsor's lender may be acceptable as an alternative form of collateral, so long as the lender is obligated to advance or escrow funds needed to procure a PCO, notwithstanding that a sponsor may have defaulted on the terms of its loan agreement(s). The acceptability of this form of collateral will be determined by the Department of Law upon application by a sponsor. The Department of Law must be furnished with appropriate documentation establishing a lender's agreement and obligation to advance or escrow such funds to satisfy 13 NYCRR § 20.3(t)(13).

a separate cash escrow account shall also be acceptable to the Department of Law.<sup>3</sup> The intent of this regulation is to ensure that at all times there remain reasonable funds available to sponsor to procure a PCO.

#### **IV. General Guidance**

To ensure that sponsors of Part 20 offering plans are making the appropriate provisions to timely obtain a PCO covering all residential units, the Department of Law offers the following guidance for complying with GBL § 352-e(2-b) and 13 NYCRR § 20.3(t)(13):

1. If a sponsor conveys units prior to procuring a PCO, the formation, balance, and terms of the monies or other collateral set aside pursuant to 13 NYCRR § 20.3(t)(13) are and remain material information requiring updated disclosure to all offerees under the offering plan – including those unit purchasers who have closed title to their units – until such time as local authorities issue a PCO. Such monies or other collateral must remain in escrow until such time as sponsor procures a PCO.<sup>4</sup>
2. Sponsors who intend to sell one or more units as “white space” units should (i) ascertain and disclose what minimal work is needed to complete such unit(s) in order for the Department of Buildings to issue a PCO covering all residential units, and (ii) disclose whether sponsor will undertake that work. A best practice would be for a sponsor to obtain some form of security or written assurance from the purchaser of a “white space” unit that obligates the “white space” purchaser to perform whatever work may be necessary to its unit in order for the Department of Buildings to issue a PCO.<sup>5</sup> If the purchaser of a “white space” unit enters into an alteration agreement with sponsor, sponsor should disclose a copy of that agreement as an exhibit in the offering plan. If sponsor does not obtain any such security or agreement from the purchaser, sponsor must disclose that fact as a special risk in its offering plan, along with an affirmative statement that sponsor remains fully obligated to procure the PCO.<sup>6</sup>
3. The disclosure that a sponsor will maintain control of a condominium’s board of managers until it procures a PCO does not supply a reasonable investor with sufficient information with which to make an informed purchase decision and

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<sup>3</sup> In such cases, a sponsor shall provide a copy of the escrow agreement controlling that account in its post-closing amendment to its offering plan. The cash escrow account shall also comply with the requirements of GBL § 352e-(2-b) and the applicable laws and regulations concerning escrow agreements discussed herein.

<sup>4</sup> Lender-held funds must be available to sponsor on terms satisfactory to the Department of Law.

<sup>5</sup> By way of example, an agreement between sponsor and the “white space” unit purchaser that (i) requires the unit purchaser to perform the necessary work to obtain the PCO and (ii) is enforceable by sponsor.

<sup>6</sup> Sponsors that sell “while-space” units pursuant to a no-action letter granted by the Department of Law should also update their offering plans to disclose the relevant facts associated with the sponsor’s ability to obtain a PCO following the sale of a “white-space” unit.

could be construed as misleading. *See State v. Rachmani*, 71 N.Y.2d 718, 726-27 (1988). A sponsor may not link its relinquishment of control of the board of managers to its procurement of a PCO, but should provide a more specific point in time when it will relinquish control of a condominium's board of managers.

## **V. Guidance for Sponsors Opting to Close Title to Unit Purchasers with a TCO**

A sponsor that closes title with unit purchasers prior to procuring a PCO should include the following information and documentation in its post-closing amendment to the offering plan:

1. A representation that the Department of Buildings (or other local authority) has only issued a temporary certificate of occupancy for (portions of) the condominium. A copy of the temporary certificate of occupancy should be included as an exhibit to the amendment.
2. A complete copy of the escrow agreement that sets forth all the material terms by which either monies or other collateral are set aside and disbursable to sponsor as a permitted periodic reduction or upon issuance of a PCO.<sup>7</sup> The escrow agent must be an attorney or law firm licensed by and operating within the State of New York. The name, address and phone number of the financial institution holding any monies pursuant to the escrow agreement, together with a list of all persons with signing authority for such account must be incorporated into the agreement. Any amendments to the escrow agreement should be disclosed in a subsequent amendment to the offering plan.
3. The balance of the special escrow account holding monies to secure sponsor's obligation to obtain a PCO.
4. Documentary evidence regarding the amount its expert has deemed reasonably necessary for sponsor to complete the work needed to procure a PCO. This may take the form of a completed Cost Affidavit (PW-3 Form) filed with the Department of Buildings,<sup>8</sup> a completed Certificate of Substantial Completion (AIA Document G704)<sup>9</sup> by sponsor's architect or engineer of record, or other documentation prepared by sponsor's expert and ratified by sponsor (*see Exhibit A* for a sample form).<sup>10</sup>

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<sup>7</sup> In circumstances where the Department of Law is satisfied that lender-held funds adequately secure the obligation to procure a PCO, *see supra* at n.2, an escrow agreement will not be needed.

<sup>8</sup> Available at <https://www1.nyc.gov/html/dob/downloads/pdf/pw3.pdf>.

<sup>9</sup> If AIA Document G704 is utilized, it should be executed by the design professional of record, owner, sponsor (if other than owner), and general contractor. The design professional of record and general contractor should not be affiliated with or related to sponsor or its principals; and include a breakdown of work necessary to procure a PCO using categories set forth in the PW-3 Form.

<sup>10</sup> Where a sponsor intends to satisfy its obligations with respect to 13 NYCRR § 20.3(t)(13) by maintaining purchaser deposits and funds in the special escrow account in the amount certified by its engineer, architect or other qualified construction professional as necessary to complete the work to obtain

The guidance set forth herein shall be effective as of November 1, 2015.

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a PCO, an escrow agreement is not required. However, in those circumstances, the sponsor must disclose in the post-closing amendment and in each non-price change amendment thereafter a statement of the amount then most recently certified by the applicable construction professional and the amount of purchaser deposits and funds in the special escrow account (which shall evidence that at least the minimum required amount remains in the special escrow account at the applicable time).

Exhibit A

[LETTERHEAD OF ARCHITECT OF RECORD OR ENGINEER OF RECORD OR  
OTHER QUALIFIED PROFESSIONAL]

[Date]

[Escrow Agent]  
[Address]

Re: *Certification Regarding Sponsor's Work and Costs to Obtain a Permanent  
Certificate of Occupancy for [Condominium] ("Condominium")  
Offering Plan Filing No.: [\_\_\_\_\_]*

Dear sirs:

The undersigned is the [registered architect/professional engineer of record or other qualified professional] with respect to the development of the Condominium. [Sponsor] ("Sponsor") has retained the undersigned to supply this certification regarding the remaining work and costs necessary for Sponsor to obtain a permanent certificate of occupancy ("PCO") from [the Department of Buildings of the City of New York/[Name of relevant local authority] for the Condominium.

The undersigned hereby represents and warrants that it is a [registered architect/professional engineer/[professional corporation/limited liability partnership/professional limited liability company] of [registered architects/professional engineers or other qualified professional] duly licensed in the State of New York.

This certification is being made specifically to be relied upon by (i) [Name of Escrow Agent], as escrow agent, ("Escrow Agent"), and (ii) Sponsor.

FOUNDATION FOR CERTIFICATION

In rendering this certification, the undersigned represents that [he/she/it] has an adequate basis to form the opinions herein, and has considered the following:

1. the current state of construction of the Condominium, including all major building systems and components;
2. all documents related to the costs of outstanding construction work or sign-offs necessary to complete construction of the Condominium, including without limitation, [the New York City Department of Buildings' "B-Scan List of Required Items"/relevant documents available from local authorities];
3. all documents related to all soft costs necessary to procure the PCO for the Condominium;

4. all documents setting forth an estimated date for the procurement of the PCO for the Condominium;
5. all other reasonable and customary costs and fees likely to be incurred by Sponsor, including without limitation, all expeditors' fees and [Department of Buildings/local authority] fees, to procure a PCO from [the Department of Buildings/relevant local authority] covering the entire Condominium; and
6. all other documents or instruments the undersigned deems necessary or appropriate for rendering this certification.

#### PROFESSIONAL OPINION

Based on the undersigned's examination, inspection and consideration of the foregoing, it is the undersigned's professional opinion that \$\_\_\_\_\_ is the reasonable cost of the work to obtain a PCO for the entire Condominium [or residential portion of a mixed-use Condominium].

This professional opinion is limited to the matters stated herein. It is not intended as a guarantee or warranty of the physical condition of the Condominium or that construction and ministerial acts will be carried out.

#### CERTIFICATION

In addition to the foregoing, the undersigned certifies that:

- (i) this letter affords Escrow Agent an adequate basis upon which to release that portion of purchasers' deposits and funds which are in excess of the amount set forth above, to Sponsor prior to the procurement of the PCO for the Condominium;
- (ii) the amount set forth above is an amount which represents all reasonable costs and work necessary for Sponsor to procure a PCO for the entire Condominium;
- (iii) the undersigned is not owned or controlled by and has no beneficial interest in Sponsor; and
- (iv) the undersigned's compensation for preparing this letter is not contingent on the conversion of the property to a condominium or on the profitability or price of the offering.

Yours faithfully,

[CORPORATE NAME, P.C.],  
a [New York] professional corporation

By: \_\_\_\_\_  
Name of Professional, [P.E./R.A.]  
[Corporate title]

or

[COMPANY NAME, P.L.L.C.],  
a [New York] professional limited liability  
company

By: \_\_\_\_\_  
Name of Professional, [P.E./R.A.]  
Member

or

[PARTENRSHIP NAME, L.L.P.],  
a [New York] limited liability partnership

By: \_\_\_\_\_  
Name of Professional, [P.E./R.A.]  
Partner

or

[if a sole-proprietorship]

\_\_\_\_\_  
NAME OF PROFESSIONAL, [P.E./R.A.]

Acknowledged and accepted:

[SPONSOR]

By: \_\_\_\_\_  
Name:  
Title: