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Are condos a solution to underperforming commercial properties?

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Commercial real estate is facing challenging conditions. Between ongoing high office vacancy rates, ever-expanding e-commerce and volatile trade markets, owners of underperforming commercial properties, including office, retail and light industrial spaces, are considering whether commercial condominium conversions to divide their larger rental assets into smaller, saleable units may offer a solution.

While it might sound like a quick fix, depending on the local subdivision process, site conditions and other legal restrictions, commercial condominium conversions can face roadblocks. Here, we explore the benefits, process, pitfalls and some strategies to make commercial condominium conversions work for you.

Potential benefits of commercial condominium conversions

Converting an existing commercial property into condos can offer several potential benefits since it establishes units that can be separately conveyed and financed. By selling individual

units, owners can access capital, monetizing the larger asset to pay off debt or reinvest in the property or other investments. Additionally, commercial condos can spur investment by new owners and offer ownership opportunities to buyers, including small businesses, professional groups and entrepreneurs who might not otherwise have the ability to purchase an entire commercial building.

Condominiums can also attract buyers in certain markets such as creative office suites, medical clinics or specialized retail that often make significant long-term investments in improvements and may prefer to own their space.

What is condominium mapping?

Given these potential benefits, owners looking to convert their properties to condominiums should familiarize themselves with the process of condominium mapping. Legally, condominiums are a form of subdivision and are subject to requirements under state and local law. At a high level, this means that an

application for a subdivision map is required and is subject to approval by the local land use authority (the city or county). One or more subdivision maps, which may include tentative and parcel or final maps, are required.

Depending on local requirements, approval of tentative or parcel maps may require discretionary approvals from the local planning department, planning commission or city council, which may take several months or even years to complete. Discretionary approvals are also subject to challenge by development opponents. Tentative maps are often subject to conditions of approval that must be met prior to recording the final map approving the condominium units. These conditions may include on-or off-site improvements, right-of-way dedications, or improvements and access improvements.

For the creation of condominiums,

the final map typically approves the creation of condominiums, and one or more separate condominium plan(s) are thereafter recorded with the consent of the record owner and any lenders or other beneficiaries to establish the boundaries of the units, common areas and any association property. State law also requires recordation of a declaration of covenants, conditions and restrictions (CC&Rs) and formation of an owners association to create the condominium regime. The CC&Rs and other governing documents establish necessary easements, cost-sharing between condominium owners, how the project as a whole will operate and be maintained, and often include use restrictions and architectural review requirements, among other provisions.

The condominium structure offers flexibility since the individual unit and common area boundaries can comprise any three-dimensional portion of the property. This allows for the creation of separate airspace units within a building, or units that include entire building struc-

tures, similar to fee title lot ownership. In addition, as long as compliant with the entitlements, the condo plan is initially recorded and can later be amended without any city consent or approvals.

Other pitfalls to watch for

In addition to the mapping itself, local planning regulations such as the city or county's general plan, community or specific plans and local zoning codes may also govern commercial condominium conversions. Regulations may include outright restrictions or limits on condominiums, or development standards such as lot dimensions and minimums that may be applicable in the case of a subdivision that proposes to create new lots. Permits relating to the existing development may include limits or conditions on conversion or intensification, and recorded public and private

restrictions on title (such as existing CC&Rs and master association requirements if the site is part of a larger overall development) may also limit a site's potential for condominium conversion.

Additionally, properties that have certain physical conditions, such as sensitive biological resources, including vegetation, steep slopes or floodplains may be subject to more stringent local or even state environmental permitting, which may be triggered even if physical development is minimal. It is important to have a full picture of site conditions, both legal and physical, impacting the ability to create commercial condominiums.

Strategies to help conversion proceed smoothly

Depending on the jurisdiction and limits imposed by any existing private covenants, some

conversions may be able to take advantage of streamlining under state and local laws that allow for ministerial approval of certain subdivisions in commercial and industrial zones. Subdivisions of less than five total units are also typically eligible for faster processing.

Because of the many factors that impact the ability and process of commercial condominium

conversion, it is important to engage an experienced team from the start, including a civil engineer, surveyor, architect and real estate and land use counsel, to analyze physical and legal constraints on subdivision and strategize on an approach to obtaining all required approvals, both public and private, to effectuate the conversion to individual condo units.

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