Studies H-855, H-856 February 4, 2014

# Second Supplement to Memorandum 2014-9

## Common Interest Development Law (Public Comment)

Memorandum 2014-9 discussed public commentary on two recent Commission-recommended reforms of common interest development ("CID") law.[1] The First Supplement presented public comment on the main memorandum.

We have since received four more letters. They are attached in an Exhibit, as follows:



The content of those letters is discussed below.

### GENERAL OBJECTION

Ms. Artus is uncomfortable with the staff, as government officials, seeking correction of opinions expressed in the media.[2] The reasons for the staff's efforts to seek a correction were explained in the First Supplement and will not be repeated here. The only additional point worth noting is that the staff does not agree with the Los Angeles Times' characterization of the disputed claims as mere "opinion."

David R. Hagmaier supports the Times article and is critical of the staff's actions in response to it.[3] He also argues that the letter from Craig Stevens that

1. Any California Law Revision Commission document referred to in this memorandum can be obtained from the Commission. Recent materials can be downloaded from the Commission's website (www.clrc.ca.gov). Other materials can be obtained by contacting the Commission's staff, through the website or otherwise.

The Commission welcomes written comments at any time during its study process. Any comments received will be a part of the public record and may be considered at a public meeting. However, comments that are received less than five business days prior to a Commission meeting may be presented without staff analysis.

2. See Exhibit p. 3.
3. See Exhibit pp. 6-8.

was presented in Memorandum 2014-9 is evidence of Commission bias, because the group that sent the letter does not contain any "homeowners."[4]

**That perception is based on a misunderstanding of the situation.** The law discussed in Mr. Stevens' letter only affects *commercial* property owners. *It has no effect whatsoever on residential property owners.* It is therefore irrelevant that no residential property owners were included in the group that Mr. Stevens represents. However, *commercial* property owners were well represented. The stakeholder group includes, among others, the California Business Properties Association. CBPA has over 10,000 members, drawn from a broad range of commercial property owners organizations.

## SPECIFIC OBJECTIONS

### "Pro Forma Operating Budget"

Ms. Artus points to one specific change in the new law that caused her some difficulty. Under former law, the term "pro forma operating budget" was used to describe not just the annual operating budget, but also a number of disclosures relating to reserve funding for future repairs and maintenance.[5] In the new law, the term was narrowed so that it no longer refers to the reserve funding documents. This change had no substantive legal effect. All of the existing financial disclosure requirements were preserved, as part of the "annual budget report."[6]

Unfortunately, the change in terminology caused a practical problem for Ms. Artus. She had used the term "pro forma operating budget" in a document that was prepared before the new law went into effect.[7] This led to some complications when she realized that the term's statutory meaning had changed. The staff regrets that the change in terminology caused problems for Ms. Artus. We will bear this feedback in mind in any similar future work.

### Notice Procedures

Attorney G. Randall Garrou provides further explanation of his concerns about the burdens imposed by the requirement that certain notices sometimes be delivered to two addresses. He also reiterates his objection to the new law's

4. See Exhibit p. 6.
5. See former Civ. Code § 1365(a).
6. Civ. Code § 5300.
7. See Exhibit pp. 1-2.

elimination of personal delivery as a method for delivery of individual notices. Finally, he suggests that the law would be improved by the addition of a provision clarifying the meaning of the phrase "address last shown on the books of the association" in Civil Code Section 4040.[8] The staff appreciates this input. We will add these specific concerns to our list of CID topics for possible future attention.

## FURTHER WORK NEEDED

Ms. Artus suggests that the Commission remain open to input on any technical errors that might exist in the new law. She also suggests that the Commission study ways to provide further checks and balances on CID governance, to avoid problems that could arise from association officials exercising legislative, executive, and judicial functions.[9]

Mr. Garrou encourages the Commission to return to a topic it once took up and then tabled: the development of streamlined governance procedures for small CIDs.[10]

## SUPPORT FOR THE NEW LAW

Attorney Kelly G. Richardson writes to express "outrage" over inaccuracies in the Times article.[11] He also writes to express his general support for the new law, which he believes will benefit CID property owners by making the law clearer and easier to use.[12] He also points to specific examples of changes made by the new law that he believes will benefit property owners.[13] Finally, he notes that he has not seen any credible examples of Commission-recommended changes in the law that would disadvantage property owners.[14]

8. See Exhibit p. 9.
9. See Exhibit pp. 2-3.
10. See Exhibit p. 10.
11. See Exhibit p. 1.
12. See Exhibit p. 3.
13. See Exhibit pp. 1 (disclosure requirements clarified), 2 (loophole closed in provision requiring refund of improperly collected assessment; due process hearing required before assessment for property damage).
14. See Exhibit p. 2.

## BACKGROUND

Because most of the current Commissioners were not on the Commission during its study of CID law, it might be helpful to place this discussion in the broader context of that lengthy study.

The Commission began working on CID law in 2000. From the very beginning, it was clear that the study would be unique in the extent to which the public was interested in and upset about the laws at issue. Views on the topic are often sharply polarized and emotionally charged. The higher than usual level of public involvement has been a great benefit to the Commission, as it helps to ensure that the Commission's proposals are scrutinized by those who would be directly affected. But a small fraction of the public comment has been unhelpful. This is the only study in the staff's memory that has produced such uncivil commentary, with repeated attacks on the Commission's integrity.

The animosity that has been directed at the Commission over the years seems to bear no relationship to our actual work on CID law. Since the study began, the following Commission-recommended changes have been made to the law governing residential CIDs:

- Associations are now required to provide members an optional informal dispute resolution process, guaranteeing the right to be heard by the board.[15]
- Associations are now required to provide notice and an opportunity to comment on proposed association rules and members now have the right to reverse unpopular rule changes by referendum.[16]
- Associations are now required to provide basic procedural fairness in making architectural review decisions.[17]
- The law was revised to make clear that an association's architectural standards do not trump statutory safety requirements.[18]
- The law was reorganized and restated to make it easier to understand and use, and a small number of substantive improvements were made.[19]

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15. *Alternative Dispute Resolution in Common Interest Developments*, 33 Cal. L. Revision Comm'n Reports 689 (2003).
16. *Common Interest Development Law: Procedural Fairness in Association Rulemaking and Decisionmaking*, 33 Cal. L. Revision Comm'n Reports 81 (2003).
17. *Common Interest Development Law: Architectural Review and Decisionmaking*, 34 Cal. L. Revision Comm'n Reports 107 (2004).
18. *Preemption of CID Architectural Restrictions*, 34 Cal. L. Revision Comm'n Reports 117 (2004).
19. *Statutory Clarification and Simplification of CID Law*, 40 Cal. L. Revision Comm'n Reports 235 (2010).

In addition, the Commission unsuccessfully recommended the creation of a CID ombudsman in the Department of Consumer Affairs, to provide information and assist in mediating CID disputes.[20] That recommendation was approved by the Legislature twice, but vetoed by the Governor both times.

The staff is not aware of any CID recommendation that the Commission has made that would adversely affect homeowners. The opposite is true. All were designed to make life in CIDs easier and less acrimonious. We have never seen any credible evidence to the contrary.

Respectfully submitted,

Brian Hebert
Executive Director

20. *Common Interest Development Ombudsperson*, 35 Cal. L. Revision Comm'n Reports 123 (2005).

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January 31, 2014

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**Re: Davis-Stirling Act**

Dear Mr. Hebert:

I was outraged to see the inaccuracies and outright falsities in the recent LA Times column by Vanitzian regarding the CLRC project to relocate and reorganize the Davis-Stirling Act. I remember in written communications to the CLRC in recent years she called the Davis-Stirling Common Interest Development Act the "Damn Stupid Act". Such is her bent as regards community associations, on which she offers the public no education or suggestions, but simply venom.

The LA Times continues to publish her column, despite frequent objections from lawyers, homeowners and managers regarding the falsities and bad advice which often characterizes this column. One can only assume that the Times likes the column, similarly to "shock-jocks" on the radio, because it is controversial.

I have followed the long progress of the Davis-Stirling reorganization project since the earlier bill, 2008's AB 1921. I give CLRC great credit for pulling that earlier bill a few years ago when the "stakeholders group" of real estate attorneys throughout the state in a petition asked the CLRC to slow down.

That extra time, extra hearings and further hard work resulted in an excellent product. 2011's AB805, authored by Member Torres, passed in 2012 with no significant opposition, appropriately. The intervening year of 2013, allowing all to prepare for the new Act, was also an excellent element of the legislation. The mainstream common interest development practitioners have put that year to good use, educating managers, lawyers and associations regarding the relocated statutes.

Clearly Vanitzian and her allies have not bothered to read the finished product of 2011's AB805, or they would be unable to make the wild assertions they do. There are a number of substantive changes, but most are extremely technical. Only a handful of the changes make any difference in how associations operate – and the changes make common sense and operate in favor of the homeowners.

For example, for years we have all labored in real estate (I represent many Realtors®, brokers and several Associations of Realtors in my firm, in addition to many common interest developments), under the confusion regarding the various documents a prospective purchase was entitled to receive from the association. Escrows would ask for the "HOA docs" or some other vague description. The statutes providing for the various disclosures were scattered through the Act. Now, we have the Annual Budget Report and the Annual Policy Statement. Those two collections of disclosures are

identical with two minor exceptions to what associations have for years been required to disclose. The exceptions are ADDITIONAL disclosures, not less. Now, a homeowner knows what to ask for – the Report or the Statement, or both. Even the organization of the two collections makes sense. The Budget Report contains items which may very well change from year to year, while the Policy Statement contains items which for the most part do not change frequently.

Another of these very few changes relates to assessments. There was a loophole in the law regarding when an association discovered that it had erroneously pursued a delinquency. Under the prior law, the association only was required to refund all charges (including collection costs) if the error was found during alternative dispute resolution. Now, the loophole has been closed – the association is required to cancel or refund all charges, regardless of how it discovers the error. Would the critics of the CLRC prefer that this loophole remain open?

Still another change relates to the addition of another homeowner protection. Under the relocated Act, a board cannot pursue a reimbursement claim against a homeowner for common area damage unless the board first holds a hearing, in the same process as for member discipline. Previously the law did not explicitly require this. Is this also something that Ms. Vanitzian would prefer not be changed, and this new homeowner protection removed?

Most of the other substantive changes in the law are so minor that it would take too long to describe them, but in my view after thirty years of law practice, the relatively few substantive changes all make sense.

I have yet to read from any source one alleged substantive change which takes away member rights – in fact, due to the reorganization, some people are for the first time finding the Act easier to use, and therefore seeing items in the law they had never before noticed. Ironically, that is a testament to the Commission's good work. The law adds homeowner protections and closes loopholes. That is good, not bad.

Thank you for the relocated Act. It will take some time for us all to learn the new statute numbers, but it is already easier to find things because they are all grouped together in logical groups, without the sub-sub-sub-sub parts we had to cite regarding the previous Act.

There will always be people who rail against common interest communities, yet do nothing to improve them or offer alternatives. In my experience, such people really oppose shared real estate ownership as a concept, but are unable or unwilling to articulate it as such. In most parts of California at least, shared ownership is the only reasonable option for a prospective homeowner or retiree. Railing against those who try to improve the governance of common interest communities, and decrying HOAs as "evil" solves nothing, and does nothing to assist California homeowners.

Best regards,

**RICHARDSON ♦ HARMAN ♦ OBER PC**

Kelly G. Richardson

KGR/pjb

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2 February 2014

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*Via* e-mail: bhebert@clrc.ca.gov

Re: Memorandum 2014-9 and First Supplement

Mr. Hebert:

I am happy that the reorganized Davis-Stirling is getting the press' attention, as I used to be concerned that a large number of Californians, including CID homeowners, remained unaware of the law regulating common interest developments.

Your concern about what you perceive to be erroneous criticisms of the Commission's work is understandable. But I am uncomfortable with a senior public official requesting a newspaper to issue a correction of any statement that it considers to be an opinion.

I read through the new Davis-Stirling early in January. Many sections are certainly clearer, and therefore easier to understand, than the predecessors. For example, § 5600 is a major improvement over its predecessor, which comprised the first sentence of § 1366(a) and a separate § 1366.1. So is § 5605, which continues the second and third sentences of § 1366(a). Its predecessor, notwithstanding its importance, was easy to overlook while reading fast because of the structure of § 1366(a).

On the other hand, I am concerned about some provisions that appear to be new. I thought that I knew the new Davis-Stirling well as I had followed the recodification closely with much interest--until I got very busy with my lawsuit against my condominium association for its violations of various rules, *inter alia*, many Davis-Stirling provisions. The case was settled in May 2013, two years and

a half after the filing of my initial complaint. Seven months later I returned to the court with a motion to enforce several provisions of the settlement agreement. As the reorganized Davis-Stirling became operative before the hearing date, I compared the new Davis-Stirling and the predecessor to see whether the new version made it necessary to adjust the forward-looking components of the proposed order (I have been represented by an excellent attorney, but did not want him to use his precious time on such a simple task). It surprised me that the term "*pro forma* operating budget" was retained in § 5300(b)(1) but was implicitly defined to mean only one component of the former "*pro forma* operating budget" as defined (also implicitly) by § 1365(a).

It's not very nice. Can you imagine how you would react if you were the judge and were told that "*pro forma* operating budget" in one paragraph of a proposed order did not mean the same thing as "*pro forma* operating budget" in another paragraph?

The recodification was a big project. It's not like an amendment of one statute or a modification of a simple contract. Problems such as what I noted might be unavoidable. Some changes may have unintended consequences, favorable to CID homeowners or otherwise. It will take a while to determine the effects of the Davis-Stirling reorganization on common interest developments and CID homeowners. I would like to review the empirical data before evaluating the project.

I am happy to see your remarks that "the staff greatly appreciates receiving input describing specific concerns. Specific input allows the Commission to evaluate whether the law contains problems that need to be addressed." (First Supplement to Memorandum 2014-9, at p. 3.) I wish to urge the Commission to keep the project in its portfolio for a few years and take remedial measures in due course.

In any case, Davis-Stirling is in need also of some substantive reforms, which were left out of the recodification project.

It has been recognized for some time that "[a] homeowners association is in effect a quasi-government entity paralleling in almost every case the powers, duties, and responsibilities of a municipal government." (*Damon v. Ocean Hills Journalist*

*Club* (2000) 85 Cal. App. 4th 468 at p. 475, quoting *Cohen v. Kite Hill Community Assn.* (1983) 142 Cal. App. 3d 642, 651.)
As you observed in 2007, "Homeowner associations are run by volunteer directors who may have little or no prior experience in managing real property, governing a nonprofit association or corporation, complying with the laws regulating CIDs, and interpreting and enforcing the restrictions and rules imposed by the governing documents of an association." (Tentative Recommendation: Statutory Clarification and Simplification of CID Law, June 2007, at 1:14-18.) Those volunteer directors are not necessarily aware even of their fiduciary duties and members' due process rights.

Under Davis-Stirling the board of a CID association consisting of such volunteer directors is allowed to assume executive, legislative and judiciary powers. Unless the governing documents provide otherwise, there is no mechanism for checks and balances. This is not a sound governance model for an entity endowed with powers, duties, and responsibilities similar to those of a municipal government.

The Commission and the legislature sought to limit the board's powers and prevent their abuses by introducing such provisions as regulations of operating rules (§§ 1357.100-1357.150, now §§ 4340-4370), the election statutes (§§ 1363.03 & 1363.04, now §§ 5100-5145), the Common Interest Development Open Meeting Act (§ 1363.05, now §§ 4900-4955), budgetary disclosure requirements (§ 1365(a), now § 5300(a) and (b)) and members' record inspection rights (§ 1365.2, now §§ 5200-5240). However, those rules would not yield the intended effects in the absence of internal checks and balances.

In theory, members can go to the court for redress. However, I have learned from my experience that it won't be a practical solution for many CID homeowners.

I believe that Davis-Stirling should be aligned to homeowners associations' governmental characteristics.

Sincerely,

Kazuko K. Artus

January 30, 2014

FOR PUBLICATION

Mr. Brian Hebert
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The Honorable Edmund G. Brown
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Commissioners – California Law Revision Commission

**Re: Response to, CLRC Memorandum MM14-09 Criticism Including, Thanks and Compliments, Mar-West Real Estate, Dec. 18th 2013 Letter Criticism Rebuttal**

Dear Honorable Governor Brown and CLRC Commissioners:

As a homeowner living in a Common Interest Development and association president for 7 years, I can relate well with Craig Stevens wonderful complement of the CLRC Commissioners on behalf of "The Stakeholders Group". Wow!

I want to acknowledge, The Stake Holders Group is comprised of profiteers to the Common Interest Development Industry(CID). The group is a consortium of attorneys, property managers, brokerage firms, and other industry profiteers that support a failed concept of American living.

I could not find one single CID homeowner name as a member of The Stake Holders Group. The belief the purpose of the CLRC was to represent the PUBLIC interest was a huge mistake. I guess homeowners are not stakeholders at all when it comes to governance of CID properties they have purchased. Tasked with compliance of the HOA Davis-Stirling Act and re-write, are CID homeowners. However, the overwhelming support the act provides industry profiteers, demonstrates prevalence in the commission's decision-making process. We find evidence of this in the laws themselves that promote attorney fees, fines, penalties, foreclosure, liens and a host of other remedies available to boards that use these statutes to harass and torment anyone with opposing opinions. . . "atta boys".

What I find most interesting is the CLRC Commissioners audacity to snivel over criticism from a genuine stakeholder, a homeowner that has dedicated her life to the interests of CID living and homeowner rights. Her dedication has given her the opportunity to write a column in the LA Times Real Estate section titled, "Associations". I find the column to be informative and an often-opposing opinion to that of the industry profiteers. I want to thank Donie Vanitzian for her courage to stand up against the profiteer's status quo remedies with genuine alternatives…"atta girl".

Ms. Vanitzian has a different spin on the subject of CID Living in California. Perhaps it's the many years she has dedicated to the subject or the various books she has written about CID life and governance, after all, she has lived in a CID for many years and has firsthand experience of the problems created by the inadequacies of the Davis-Stirling Act and its re-writes. Mr. Hebert you know all too well about her book. Did you not have some issues with it because she criticized the Commission? Unlike the commissioner's paid positions and pensions, and unlike the well-paid industry profiteers, Ms. Vanitzian receives little or no compensation for her work, but continues her plight nevertheless . . . "atta girl".

Shame on the commission for its continued sniveling over criticism it receives by those directly affected by the shortsighted decisions of the CLRC. I suppose those decisions become clear evidence why she can criticize the Commission. Does she not retain First Amendment rights when airing an argument? The commission cries over anonymous authority cited in a newspaper opinion column limited in size by space availability and a word count…"atta boys".

I believe the commission is overreaching and over-reacting a bit to Ms. Vanitian's assertions, judged only by the overwhelming support from the industry profiteers. I can probably bet your memorandum was well received by them all. I will also bet with 100% accuracy, nothing will change… "atta boys".

As a prudent homeowner as well as many of our neighbors, we can personally relate to heavy-handedness of association boards, commissions, property managers and the like when pursuing dispute resolutions and internal dispute resolutions. The CLRC forgot to include provisions in the re-write that protect homeowner interests or establishes consequences when profiteers violate the final published rules. Also omitted are the consequences against recalcitrant boards. Any homeowner seeking real relief must civically litigate and pay for their own counsel. Should the association prevail, the homeowner may be responsible for the associations' legal expenses, as well. Thanks to the CLRC, industry protection statutes that should create a level playing field are non-existent.… "atta boys".

It is not my intent to illustrate all the inadequacies contained in the re-write but I do want to give one example of its shortcomings. I was involved in a dispute with our association's board and trying to resolve the matter at board meetings was going nowhere. I requested an IDR to settle the matter. About two months after my written request and on two days notice, I received instructions to meet with a board member that was supposed to be knowledgeable in the matter at hand. When we began the IDR, the first thing the board member said was he had no knowledge of the matter. So where was this board member for months on end when we spoke before the board to our matter? I had to take time off from work for this response. No resolution ever came about from this IDR, despite the Davis-Stirling Act that mandates a final board decision. The Davis-Stirling Act represents the useless implication of nonexistent "fairness". Furthermore, the board continued to badger my wife over a hundred dollars she never owed, which she eventually paid just to stop the continual madness month after month. It was never determined who violated who with the fine.

The association president, the driver behind the badgering, does not own a home or any property in our community. He is the father of a homeowner and should not be on the board. However, the Association's CC&R's, written back in 1973 allow for an agent of an owner to be on the board. I interpret that to mean the property owner must first be elected before assigning is rights to a third party or agent. What an endeavor it is to get the word out to 100 homeowners before an election, that a person on the ballot owns no property within the community and is a non-member. The CLRC is a charade and has no interests to help homeowners from rogue boards and non-members. The CLRC was nowhere to be found when homeowners, needed them most…"atta boys".

What the CLRC has been successful at is creating is a lopsided and ultra-biased unlevel playing field as the recourse for homeowners to redress often invented violations that devastate our dignity and quality of life. When do homeowners get fairness in addressing disputes, and dispute resolutions? When will homeowners see some element of enforcement, backing or recourse, to ignored statutes? Going to court with rogue boards at further homeowner expense is not the solution. . . . "atta boys".

Yes, I can agree the Davis-Stirling Act and re-write, represents the Attorneys Full Employment Act and official authorization for association boards to persecute as they please. All these years the CLRC has worked on what homeowners believed to be a level playing field only to learn it is everything but level… " atta boys".

In closing, I would like to advise the CLRC if they are going to throw stones, they had better expect to get them back and when they do, not to snivel about it in a public memorandum. The commission needs to grow up and start representing the public interest and not the interests of the profiteer's fat wallets. Why is that so hard to do? I did not see one letter from a homeowner thanking the CLRC for its work with the public interest in mind. To that I say..." atta boys".

Respectfully,

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## EMAIL FROM G. RANDALL GARROU
## (2/4/14)

Unfortunately, I will not have time to respond this morning, except by this email. I'm hoping you can bring this email to the Commission's attention.

Mr. Herbert:

I appreciate your enlightening me as to some of the nuances of the new act which I incorrectly complained of. By and large, I think the Commission did a positive thing. However, as with any large legislative undertaking, it was not without some glitches.

The one area where you acknowledge it intentionally changed the existing law substantively was in the area of notice. While it is good that it now distinguishes between general and individual notice, unfortunately, it eliminated a simple way of providing notice which would be particularly useful in the numerous smaller associations which are governed by this act, i.e., personal delivery of a notice (e.g., of a Board meeting) to the door of each unit. Now, members who are dissatisfied with Board decisions in a small Association can insist on mailed notice of Board meetings. In a small HOA where no one has the time and resources to do mailings of frequent notices, the removal of this provision from the prior act has not streamlined things, but made them significantly more difficult to administer. If you felt that mailed notice was important for non-resident owners, you could have simply provided an exception solely for service on non-resident owners who have requested mailed notice. That would not be too difficult to administer. I would urge you to consider that for a future modification restoring service of run-of-the-mill notices by personal delivery to the door of each unit.

Secondly, since the revision committee did elect to inject substantive changes into the statutory notice provisions, I feel it is fair criticism to suggest that they did not do a complete job. Specifically, where a resident homeowner has requested individual delivery of notices, and has requested that they be mailed to an address other than his residential address in the project, it is not clear whether the HOA's obligation is to send the mailing to the owner's residential address within the HOA, or to the requested alternative mailing address. The statute (Civil Code § 4040 (a)) only says to address it "to the recipient at the address last shown on the books of the association." However, nowhere in the Davis Stirling act could I find a provision indicating which address should be the one shown on the books of the Association. Should it be the address of the unit, or, instead, should it be any alternate mailing address the owner has provided? Since the Commission elected to undertake the job of updating the notice laws, then this ambiguity in the notice procedures should have been corrected.

Again, when such a large job is undertaken, it is understandable that there will be small areas that have been overlooked. However, I'm hoping the Commission, now that I've brought these two problems to its attention, will introduce amendatory legislation to correct these two problems.

Lastly, I hope the Commission will renew its efforts to simplify and create a separate set of applicable statutes for the innumerable small HOA's throughout the state who cannot find volunteers, much less competent volunteers, to serve on HOA boards, given the huge demands the existing Davis Stirling Act puts on the time of Board members (not to mention the potential liability on those who accept such thankless jobs) who must now comply with a statutory scheme seemingly challenging the Internal Revenue Code in complexity.