TAHOE DONNER ASSOCIATION
BOARD ORIENTATION & DISCUSSION OF COMMUNITY ASSOCIATION LEGAL ISSUES
(Saturday, July 21, 2018)

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ISSUES OF INTEREST TO ALL OWNER ASSOCIATIONS:

1. Introductory Comments. The Orientation will begin with a general introduction of who I am, my experience in the representation of owner associations and other nonprofits, and my previous affiliation with the Tahoe Donner community for many years.

2. What distinguishes HOAs from Other Corporations – Both Profit and Nonprofit? I want to begin by discussing how owner associations differ from other nonprofit corporations, including an overview of the role of the various governing documents: The Declaration of CC&Rs, Association Articles of Incorporation, Association Bylaws and Operating Rules.

   - ***The Governing Documents and the Importance of the Recorded Covenants.*** For most corporations, profit and nonprofit, the principal governing documents are the corporation's Articles of Incorporation and Bylaws and other rules and regulations that are found in either the General Corporation Law (applicable to for profit corporations) and the Mutual Benefit Corporation Law (applicable to nonprofit corporations that are formed to pursue some interest or activity that is for the mutual benefit of the association's members).

   In the case of owner associations (most of which are formed as Mutual Benefit Corporations) perhaps the most important document is not a creature of corporate law, but rather real property law, namely the recorded Declaration of Covenants, Conditions and Restrictions ("***CC&Rs***"). The CC&Rs for any common interest development are of primary importance because they are the Constitution and the glue that establishes the core rules for living in a collective residential environment. Once recorded with the County Recorder, the CC&Rs create what the law calls "covenants that run with the land". That is a legal term that originated in the English Common Law which defines

and identifies rules and restrictions relating to real property ownership which bind not only the developer and the very first buyers of homes or lots, but also all future owners whose property is covered by the CC&Rs.

Here is what the California Supreme Court had to say about the importance of a common interest community's recorded Declaration of CC&Rs:

"Our social fabric is founded on the stability of expectation and obligation that arises from the consistent enforcement of the terms of deeds, contracts, wills, statutes, and other writings. A stable and predictable living environment is crucial to the success of condominiums and other common interest residential developments, and recorded use restrictions are a primary means of ensuring this stability and predictability, recorded CC&R's are the primary means of achieving that stability and predictability so essential to the success of a shared ownership housing development. Enforcement of a common interest development's recorded CC&R's will both encourage the development of land and ensure that promises are kept. . .

When courts accord a presumption of validity to recorded use restrictions and measure them against deferential standards of equitable servitude law [meaning that trial courts are supposed to presume that the restrictions are reasonable and enforceable], it discourages lawsuits by owners of individual units seeking personal exemptions from the restrictions. This also promotes stability and predictability in two ways. It provides substantial assurance to prospective condominium purchasers that they may rely with confidence on the promises embodied in the project's recorded CC&R's". (***Nahrstedt v Lakeside Village Condominium Association*** (1994) 8 Cal 4th 361).

- ***The Hierarchy of the Governing Documents.*** As noted above, the Declaration of CC&Rs is at the top of the pyramid of association governing documents, at least insofar as real estate property use restrictions are concerned. Below the CC&Rs there really isn't a hierarchy of Governing Documents in that each of the core Documents serves an important, yet independent purpose:

(i) ***The Articles of Incorporation.*** The Articles of Incorporation is filed with the California Secretary of State and gives life to a corporation. For any corporation, the Articles are a very brief document that presents the name of the entity, a statement of the entity's purpose, and some information about the location of the development and the association's agent for service of process.

(ii) ***The Association Bylaws.*** The Bylaws are the key document for addressing matters relating to internal governance and management: Who are the members? Who are the directors and how many seats are on the board? How are the directors elected and under what circumstances can a director be removed from office? What are the member voting rights? What are the powers of the Board? What financial information must be given to the members? Typically the subject of an association's authority to assess its members (an important governance issue) is addressed in the CC&Rs, rather than in the Bylaws, because of the Association's authority to collect delinquent assessments through the use of lien and foreclosure rights (i.e., the collection remedies involve a real property issue).

(iii) ***The Association Rules.*** The Association Rules are perhaps of least importance, although they serve the important function of interpreting and perhaps providing procedural details for implementing matters that are addressed in the CC&Rs and the Bylaws. My advice to association clients is to use the Rules to address issues and procedures that might change over time as a result of actual experience in applying the rules or because of changed circumstances. Rules are easier to amend than CC&Rs and Bylaws. NOTE, however, that certain rules that are listed in Civil Code section 4355 can only be adopted by the Board after first being distributed to the Members for a 30 day comment period and those sorts of rules can be challenged by 5% or more of the Members who can demand that the

proposed Operating Rule or Rule Changes be put to a special vote of the Members.

- ***The Mandatory Nature of Association Membership.*** In the case of most nonprofit corporations the members have a choice to participate in the organization either as a contributor, board member, or as an active volunteer. If an individual does not like the way that the nonprofit is being managed or the positions it is taking, that person can either quit the movement altogether or seek another organization that is promoting the issue in another fashion that is more in line with the individual's core beliefs. If you join a golf club because you love the game, but then due to health reasons or other considerations you no longer plan, you can quit the club. But if you buy a home in a common interest development that includes a golf course you cannot refuse to support the course even if you never swung a club, short of selling your home.

In the case of an owners' association absent selling your home or lot in the development or condominium project, your membership is mandatory because it is tied to the ownership of a lot or unit in the development and you cannot avoid the obligation to support the association or to adhere to the community rules and restrictions for so long as you are a property owner. Some individuals view that mandatory nature of common interest living, created by the recorded CC&Rs, as a detriment, while others view the covenants as positively promoting stability and certainty relating to home ownership (as noted by the Supreme Court in the quotation on page 2, above).

- ***Regulation by Two Sets of Statutory Laws Which Are Not Always Consistent, One to the Other*:** The final important distinction between most nonprofit mutual benefit corporations and owners' association is that owner associations are regulated, and subject to, two regulatory schemes, namely the Nonprofit Mutual Benefit Corporation Law and the Davis-Stirling Common Interest Development Act. I was one of the members of the Select Committee appointed by the Legislature to draft the Davis-Stirling Act and because I had also been involved in drafting the Mutual Benefit Corporation Law (which was adopted five years before Davis-Stirling) I advocated for limiting the Davis-Stirling Act to real property law issues related to common interest developments and letting the Nonprofit Law regulate internal governance and member/board voting and meeting issues. That opinion did

not prevail among the members of the Davis-Sterling drafting committee and therefore the Davis-Stirling Act now includes many provisions dealing with internal management and governance. Those provisions are not always consistent with the same topics as addressed in the Mutual Benefit Corporation Law. As a general rule, if there is a conflict, the Davis-Stirling Act provisions prevail.

3. What Distinguishes Owner Associations from Local Governments Such as City Councils or Boards of Supervisors? During this 2018 legislative session a terrible proposal was introduced by State Senator Wieckowski which, in its original form, recklessly expanded the scope of individuals who were qualified to serve on the Board of an owners' association to include owners who have been convicted of certain felonies and owners who were delinquent in the payment of special assessments that the candidate opposed. The statement of legislative intent in the original version of the Bill had this statement: "Common interest developments function as quasi-governmental entities, paralleling in many ways the powers, duties, and responsibilities of local governments."

Many attending this orientation may be thinking: "What is so wrong with that statement?" The answer, which I have reached after 40 years of representing common interest owner associations is that there are, admittedly, some similarities between owner association and local governments and yet it is a crippling mistake to blindly apply all rules applicable to local governmental bodies to owner association boards. There are very important and fundamental distinctions between the role and responsibilities of owner association boards and their directors and the duties and responsibilities of elected governmental officials.

Specifically, boards of directors of owner associations function best when the property owners elect representatives who can work collaboratively and achieve a consensus in their decisions. In contrast, elected officials (council members, assembly members, state senators) represent districts and constituencies and their path to reelection is to represent and to advocate the narrow interests and concerns of their districts. Representatives in the Southern districts of the State need water and want the Big Dig pipeline that will transfer water from the Northern California delta. Representatives in the north are concerned about preserving their water and avoiding adverse impacts on the environment. When Willie Brown was the long-time

Speaker of the California Assembly, he could advocate proposals strictly for the City and County of San Francisco; he didn't have to worry about or take into consideration the needs and concerns of farmers in the San Joaquin Valley or ranchers in Tehama County.

Owner associations perform miserably when the governing board is comprised of directors who dislike each other or when the board includes directors who campaigned for election on some narrow platform or agenda --- what we know in the World of Trump as "the BASE", and those directors cannot get their arms around the principle that they now work for all members and need to make decisions that take into consideration the best interests of all owners and residents. In large community associations that have an in-house management staff, the diverseness among Board Members causes confusion and morale problems at the staff level that can harm the overall performance, effectiveness and cripple the effective implementation of board policies and programs.

Believe me, I am not naïve and I recognize the fact that more often than not there is a key issue that motivates a member to get up off the couch and throw his or her hat in the ring to run for the Board. That is a good thing because each director's experiences and perspective enrich and improve deliberations at the Board level. However, once elected all successful candidates have to truly *listen to the perspectives and opinions of their fellow directors* and once the deliberations are over, to accept the determination of the majority, even if a director's perspective or motion did not prevail.

4. Making Effective Use of Legal Resources When Enforcing the Governing Documents. In the orientation meeting materials that were distributed this morning are sample documents from two actual common interest development cases involving CC&R enforcement actions that were focused on relatively minor, and in my view, benign infractions of the development's CC&Rs. The lesson or "take away" from the ***Ironwood v Solomon*** and ***Fleur du Lac*** cases is that all litigation is expensive and requires a number of judgment calls going into the courtroom battle, including an assessment of the strength of the Association's case, the importance of the issue at hand, the claims and defenses that have been made by the opposing party, and counsel's judgment of the resolve (to continue the fight), and financial resources of the opposition. The

bottom line is that the Board should choose the association's battles wisely. The ***Ironwood*** case involved the planting of eight date palm trees in the defendant's front yard and the ***Fleur du Lac*** case involved an encroachment of a couple of fee by the defendant's patio into adjacent common area.

Civil Code section 5975(c) does instruct that "in an action to enforce the governing documents the prevailing party shall be awarded reasonable attorney's fees and costs". However the road that ends with that award of attorney's fees is often paved with years of invoices from the association's attorneys that must be paid monthly and there is also the possibility of losing the case. Should that occur, then the Association risks being saddled not only with the costs of its own legal counsel, but also the fees of the opposing party's counsel.

The recommendation that Association Boards pick their fights wisely is somewhat in conflict with the obligation that governing boards have to enforce the CC&Rs, but it really gets down to how the directive to "enforce the covenants" is pursued and understood. Efforts should be made during board deliberations to consider fair and expeditious alternatives to resolve a CC&R enforcement conflict short of resorting to costly litigation. Furthermore, the statutory obligation imposed on owner association boards to enforce the governing documents does not eliminate the obligation of the directors to independently evaluate the strengths and weaknesses of a particular alleged violation and engaging in a cost/benefit analysis of the likely cost to the association of insisting on complete compliance by the alleged violator. Under Corporations Code section 7231 nonprofit directors are also under an obligation, *prior to casting their votes*, to consult with qualified professionals if the matter at hand involves issues, data, or principles that require expert input in order to make an informed decision. In other words, the obligations imposed on owners associations to enforce the CC&RS pursuant to Civil Code section 4085 should not be interpreted as a *Charge of the Light Brigade* in Alfred Lord Tennyson's poem: "Boldly they rode and well; Into the jaws of Death; Into the mouth of hell Rode

the six hundred". As noted above, directors are expected and instructed to make informed judgments.

Of course, there is also the possibility that the association is not the initiator of an enforcement action, but rather finds itself dragged into a costly dispute by an owner who has more money than common sense. That was the situation in the ***Fleur du Lac*** case where the stage for the dispute was one of the most exclusive lakefront developments at Lake Tahoe. The plaintiff property owner blatantly disregarded limitations that had been imposed on her patio improvement project that the Board had approved, based on the site plan for the project that the owner had submitted. Once the approval was in hand, the owner added additional square feet to the patio, thereby appropriating common area and contravening lot coverage restrictions imposed by the Tahoe Regional Planning Agency. Had the association in that case done nothing and permitted the patio improvements to remain, the directors could have faced personal liability for not protecting the interests of the other *Fleur* owners in the common area (see ***Posey v Leavitt*** (1991) 229 Cal.App.3d 1236; Doc 1003462). The plaintiff Association also had to consider the possibility of an administrative enforcement action by the TRPA for permitting a violation of improved land coverage requirements.

5. Discussion of the Status of Directors as Fiduciaries Vis-à-Vis the Association and its Members. The importance of the role of directors as fiduciaries and what it means to hold a position that involves "***fiduciary duties***" and "***fiduciary obligations***" cannot be overstated. What a person can and cannot (or should not) do as an ordinary citizen (or in an HOA context, a "member" and "property owner") in contrast to being an elected director requires different mind-sets and the conduct and actions of ordinary citizens and elected directors are governed by different sets of rules. Members of an association who are not serving as directors have no fiduciary obligation to make decisions or proposals, or to take into consideration the best interests of the entire community. Taking into consideration the best interests of that broader community of individuals is at the heart of what it means to be a fiduciary and to properly discharge an elected director's responsibilities as a leader and decision-maker in a community association.

Because board members are entrusted with the money and property of the association they are held to a higher standard than other property owner/members and must avoid ***conflicts of interest***. As noted above, they are deemed "***fiduciaries***" who have a duty to act in the best interests of the membership *as a whole*.

> *"A homeowners association has a fiduciary relationship with its members"* (***Cohen v Kite Hill Community Association*** ((1983) 142 Cal.App.3d 642).
>
> "*It is well settled that directors of nonprofit corporations are fiduciaries."* ***Ravens Cove Townhomes, Inc. v Knuppe Development Company*** ((1981) 114 Cal.App.3d 783).
> *Directors of nonprofit corporations such as the Association are fiduciaries who are required to exercise their powers in accordance with the duties imposed by the Corporations Code. This fiduciary relationship is governed by the statutory standard that requires directors to exercise due care and undivided loyalty for the interests of the corporation* (see ***Francis T. v Village Green Owners Assn*** ((1986) 42 Cal.3d 490).

- Two Broad Duties Define What it Means to be a Fiduciary. Upon their election to the board of a common interest development, directors become fiduciaries with the power to act on behalf of the association. As fiduciaries, directors are held to a higher standard of conduct and have two primary duties, namely: (i) a *duty of care*, and (ii) a *duty of loyalty. These parallel duties are the same for directors of both incorporated* and unincorporated associations.

A. ***The Duty of Care; Due Diligence and the Duty to Investigate.***. Directors must be diligent and careful in performing the duties they have undertaken (***Burt v Irvine Company*** (1965) 237 Cal.App.2d 828). Section 7231(a) of the Mutual Benefit Corporation Law requires directors to perform their duties as directors (including duties as a member of any committee of the Board) in good faith, in a manner that the directors believes to be in the best interests of the corporation, and with such care, including reasonable inquiry, as an

ordinarily prudent person in a like position would use under similar circumstances.

Subparagraph (b) of the same section of the Mutual Benefit Corporation Law states that in the proper performance of a director's duties, a director may rely on "information, opinions, reports or statement, including financial statements and other financial data, so long as the information is obtained from a reliable and competent person who is familiar with the matters presented or from legal counsel, independent accounts, or other persons as to matters that the director believes to be within such person's professional or expert competence.

Directors must:

- Attend and participate in Board and committee meetings (committees to which a director is assigned) so they can be informed about the association's business.

- Make reasonable inquiry regarding maintenance issues, rules violations, reserve requirements and budget planning, etc.

- Make informed decisions.

- Keep corporate records.

- Enforce the governing documents. In fact, published court decisions have upheld the right of members to sue the Association and its directors for their failure to enforce the governing documents (see ***Posey v Leavitt*** ((1991) 229 Cal.App.3d 1236; *Ekstrom v Marquesa at Monarch Beach HOA* ((2008) 168 Cal.App.4th 1111).

B. ***The Duty of Loyalty and the Absence of Self-Dealing by Directors***. Directors must act in the best interests of the association even if that course of conduct is at the expense of their own interests. The concept of self-dealing is more than just obvious examples, such as the embezzlement of funds. It includes conduct and decisions such as steering contracts to family members or taking actions that result in

personal benefits to the director or family members at the expense of the association. Violation could result in (i) liability for all profits received, (ii) all damages caused by the breach, and (iii) punitive damages.

> *"We note that the duty of undivided loyalty applies when the board of directors of the association considers maintenance and repair contracts, the operating budget, creation of reserve and operating accounts, etc. Thus, . . . [directors] may not make decisions for the association that benefit their own interests at the expense of the association and its members."* (***Raven's Cove Townhomes, Inc. v Knuppe Development Co.*** ((1981) 114 Cal.App.3d 783)

The duty of loyalty that a director owes to his or her Association can extend to that director's obligation to support the decisions that are ultimately reached by the Board of Directors on a particular matter or action item. A director can dissent and make adverse comments or offer alternative proposals in a board meeting when the matter is under discussion by the board. In fact an important reason why corporations have governing boards comprised of several individuals, rather than being run by a dictator, is to have the ultimate decision that is reached by the members of the Board, acting collectively, benefit from the diverse views of persons who come from different backgrounds and who bring their unique knowledge and expertise to the Board room. However once a decision is made, it's time to move on. A dissenting director does not have to become a cheerleader for the board's decision but a director goes too far when he or she undermines the board or the agreed-upon course of action. Such behavior can result in a breach of the director's fiduciary duties.

Years ago I was representing a very large Association that had retained my services to update their old governing documents (1970 vintage) to reflect what was then the new Davis-Stirling Common Interest Development Act Among other things, the original CC&Rs for this development limited Board-initiated increases in the annual assessment to three percent of the prior year's assessment. The new Davis-Stirling Act increased the board's discretion to increase annual

assessments by as much as 20% a year without member approval. The new Act also specifically stated (and to this day states) that the assessment authority conferred on the Board in the statute superseded any older CC&R provisions to the contrary.

One of the members of the Board of this association was opposed to the new authority conferred on the board in spite of my efforts to explain to him that the Davis-Stirling Act provision that he opposed was not a provision that could be altered by a more conservative bylaw or CC&R provision. Ignoring my advice the director initiated a very active **VOTE NO** campaign and he went so far as to publish his own community newspaper called "The Mushroom" which contained all sorts of false and misleading "facts" regarding the new CC&Rs. Eventually the new documents were approved by the County Superior Court. However the director's misleading and aggressive VOTE NO campaign cost the Association another $10,000 to obtain a court-ordered approval of the amendments. In response the Board conducted a disciplinary hearing and approved a motion to censure the director and he resigned from his office.

6. Directors are Not Day-to-Day Managers of the Association's Business. Directors and executive management have different roles and responsibilities in any corporate structure and HOAs are no exception. In small, self-managed associations this distinction between board/director responsibilities and management responsibilities is often blurred, however in large associations efficient management requires that there be a clear understanding of the different roles and responsibilities of the board and management.

- Section 7210 of the Mutual Benefit Corporation Law places the Board of Directors at the top of the tree of governance within a nonprofit corporation:

> "Each corporation shall have a board of directors. [Subject to any provisions of law or the corporation's governing documents that require an action to be approved by the members] all corporate powers shall be exercised by or under the direction of the board."

- However, that same section of the Mutual Benefit Corporation law goes on to say that Boards may delegate the management of the activities of the corporation to any person or persons, management company, or committees, however composed, so long as the activities and affairs of the corporation are managed and all corporate powers are exercised under the ultimate direction of the board. In other words, when an owners association has on-site management and staff or employs a management company, it is the role of the Board to set policy which is then implemented by management. In that structure it is also the obligation of the board to provide general oversight to the general manager, senior staff or the management company, but not to meddle in day-to-day managerial or staff decisions. To do so undermines the authority and respect of the persons the Board has hired to run the day-to-day operations.

  Conversely, management is obligated to report to the board at its regularly scheduled meetings, and, in between meetings to bring more urgent matters or developments to the board (typically in a communication to the association president) in case convening a special meeting may be appropriate.

- Published cases have noted that the failure by a governing board to exercise supervision which permits mismanagement or non-management is an independent ground for a claim of breach of fiduciary duty (see ***Ravens Cove***, cited above).

7. <u>The Importance of Maintaining Confidential Communications and Discussions "CONFIDENTIAL".</u> The importance of maintaining the confidentiality of communications from legal counsel to the Board and senior management that are marked as "confidential/attorney-client privilege" as well as discussions between the Board of Directors and the Association's attorney. Although "transparency" (or the lack thereof) has become the battle-cry of the day for critics of association governance, the Davis-Stirling Open Meeting Act expressly permits governing boards to consider and to act upon certain matters in executive session (to the exclusion of the members). That authorization

is included in the Davis-Stirling Act to protect the best interests of the Association and its members by enabling the directors to receive information and to make sound and fair decisions that could be compromised if the discussions were taking place in a public forum.

- ***Loose Lips Sink Ships***. Particularly when a governing board is divided and decisions are not unanimous, the directors on both sides of the debate have got to resist their visceral inclination to gain leverage by (in the words of one of my favorite singers, *Boz Scaggs:* "taking your business to the street and talk'in out loud"). To do so can cause considerable harm to the Association by waiving the privilege that protects the discussions. If a director believes that some issue is inappropriate for consideration and discussion in executive session, that director's obligation is to raise that concern with his or her fellow directors at the inception of the executive session – not to make a unilateral decision to divulge the information in public.

- ***NextDoor****:* Many common interest communities have a presence on the *NextDoor* website which champions itself (these are quotes from the *NextDoor* site) as "believing that waiving hello to a neighbor says "Welcome" better than any doormat" and that "we are simply you and your neighbors, together". However in my experience *NextDoor* too often is used by dissident members of the community who would rather spew their negative comments and agendas on the website than actually join an association committee or run for the Board.

Unfortunately, *NextDoor* has become the Hyde Park, London, Speaker's Corner where any crackpot can publish whatever opinions he or she wishes to express, without fear of editing for accuracy or truth. Recall my earlier comments that once a person is elected to the Board, that individual's ability to talk about association business in public forums is constrained by the concept of being a fiduciary who should not discuss or voice opinions on every issue that might come into the director's head. My advice to directors would be to either suspend your *NextDoor* account while in office or simply use it to monitor the chatter that is going on in the community.

8. <u>Open Meeting Act Requirements; What Constitutes a Meeting; the Preparation of Minutes; and the Authority to Meet In Executive Session.</u>

Refer to Curt's *Summary of the Davis-Stirling Act Open Meeting Requirements.*

9. <u>The Importance of Properly Prepared Minutes; What Information Should be Included in Board Meeting Minutes.</u> Discussion of the Importance of Minutes & How to Prepare Minutes:

- The role of minutes in preserving a clear record of Board actions taken through properly prepared minutes. The guiding principle of minute preparation: "Minutes should be an accurate record of what was done – not a record of what was said." Nevertheless a sufficient background summary leading up to the decision should be presented to enable the minutes to present an accurate record of the logic and analysis leading up to the ultimate decision. Whoever is charged with preparing the minutes of a board meeting should always have in the back of his or her mind that this text may be important in a later judicial proceeding.

- One valid question is whether properly prepared minutes should include comments that property owners make from the floor during an open meeting since the Davis-Stirling Act specifically requires open board meetings to include a member comment period. Often members who take the time to participate in Board meetings, enjoy seeing their comments "in the record" and yet, those same individuals may also have their own agenda for wanting to make a point at the meeting.

  Upon reflection, my conclusion is that in most instances, including member comments from the floor is not necessary or even appropriate. Although the Open Meeting Act provisions of Davis-Stirling do require open meetings to have a time set aside for member comments, the same law also says that the Board can only take actions on those items that are noted in the Board's published agenda as being scheduled for action.

  Because minutes are for the purpose of documenting the actions and decisions of the Board that occur at the open meeting, by definition comments from the floor cannot become action

items at the meeting. If the member's comment from the floor is not with respect to an agendized item, then it is just that member's expression or opinion regarding something on his or her mind and that comment need not make it into the minutes.

There are only two possible exceptions that could merit a comment in the minutes, namely that Civil Code section 4930(c)(2) says that it is OK for a Board to request that the General Manager or other managing agent or staff to report back to the Board at a subsequent meeting concerning any matter [regardless of whether that matter was on the agenda] or take action to direct its managing agent or other agents or staff to place a matter of business on a future agenda.

Accordingly, perhaps if a member comment resulted in a permitted action by the Board (to direct that the issue raised by the member be placed on a future agenda or to be investigated by the staff), then that Board action ought to make it into the minutes. Short of that, general member comments are really for venting (and often by people who have views or agendas that are not in the best interests of the association or a particular ax to grind). There is no reason for the minutes to give credence and further publication to those views.

The only other possible exception (where a note regarding a member's comments from the floor might be appropriate for inclusion in the minutes) is when a member in the audience speaks to an issue on the Board's agenda and his or her comment actually carries the day in fashioning the Board's ultimate decision on the issue.

- The maintenance of executive session minutes. How those minutes differ from Open Meeting minutes? *See page 19 of the Open Meeting Act Summary.*

- <u>Where should executive session minutes by retained</u>? There is no hard-and-fast rule in the statutory scheme as to where minutes of executive sessions should be retained, although some association

boards have the association's legal counsel retain the minutes. At a minimum, executive session minutes ought to be retained in a secure space in the Association's offices that is separate and apart from the area where the general corporate minute book is retained. Members have a right to inspect minutes of any open session of the board and therefore if a member is inspecting his or her inspection rights and executive session minutes are kept in the same place as open session minutes there is a risk of unintended disclosure of confidential matters and discussions.

- Davis-Stirling Act Requirements Regarding Minutes: Minutes or draft minutes must be available to members within 30 days following the meeting (except for executive session minutes) and the Annual Policy Statement must advise members of this right (Civil Code section 4950). *See the Open Meeting Act Summary.* The problem with the Davis-Stirling Act's reference to "draft minutes" being distributed is that draft minutes are not the final act or word of the Board, so they should clearly be marked at being DRAFTS.

10. The Davis-Stirling Act Rules for Dispute Resolution. Resolving Association/property owner disputes (IDR & ADR) and the cost of "getting it wrong" (meaning escalating the conflict with related legal expenses). ***Ironwood v Solomon*** and the ***Fleur du Lac*** case. Footnote: One good example of the reality of the legal dance in very costly homeowner association litigation disputes: ***Auburn Lake Trails v Transamerica Development Corporation.***

When disputes arise between the Association and a property owner, Chapter 10 of the Davis-Stirling Act contemplates a progressive process of dispute resolution beginning with (i) notice and the opportunity of a member who is the potential subject of a fine or other disciplinary action to appear before the Board of Directors, and (ii) then transitioning to more formal efforts at dispute resolution through either internal dispute resolution (called "***IDR***") or the use of alternative dispute resolution (called "***ADR***"). It is only when those out-of-court efforts fail that either party can proceed to file an action in civil court.

- Step One: The Levy of Fines and the Right to Come Before the Board (Civil Code sections 5850 and 5855): The Imposition of fines and member discipline (Civil Code sections 5850 and 5855). Right of Members to Meet with the Board to discuss discipline or imposition of a fine (Civil Code section 5855): At the most basic end of this progressive process, Civil Code section 5855 instructs that when the Board of Directors is scheduled to meet to consider or impose discipline upon a Member, or to impose a monetary charge (fine) as a means of reimbursing the Association for costs incurred by the association in the repair of damage to Common Area or Common Facilities caused by a Member or the Member's guest or tenant, the Board is obligated to notify the Member in writing, by either personal delivery or individual delivery pursuant to Civil Code section 4040, at least ten (10) days prior to the meeting. That notification to the Member must contain, at a minimum, the date, time, and place of the meeting, the nature of the alleged violation for which a Member may be disciplined or the nature of the damage to the Common Area or Common Facilities for which a monetary charge may be imposed, and a statement that the Member has a right to attend the meeting and may address the Board at the meeting. That session with the Member to discuss possible disciplinary action must be conducted in executive session if requested by the Member. Civil Code sections 4935(b) and 5855(b).

  If the Board imposes discipline on a member or imposes a monetary charge on the Member for damage to the Common Area or Common Facilities, the Board must provide the Member a written notification of the decision, by either personal delivery or individual delivery pursuant to Section 4040, within fifteen (15) days following the action.

- Schedule of Fines or Monetary Penalties (Civil Code section 5850). Civil Code section 5850 states that if an owners' association desires to adopt a policy imposing any monetary penalty, including any fee, on any Member for a violation of the Governing Documents, including any monetary penalty relating to the activities of a guest or tenant of the Member, the Board of

Directors must adopt and distribute to each Member, in the Association's Annual Policy Statement (Civil Code section 5310), a schedule of the monetary penalties that may be assessed for those violations. Furthermore, a monetary penalty for a violation of the governing documents shall not exceed the monetary penalty stated in the schedule of monetary penalties or supplement that is in effect at the time of the violation.

- Step-Two, Internal Dispute Resolution or "IDR" (Civil Code sections 5900-5915): On occasion disputes arise between the Association and one or more of its Members that extend beyond routine matters that can be resolved in attendance at a Board meeting. When a dispute between an Association and a member involves the Member's rights, duties, or liabilities under the Davis-Stirling Act, the Mutual Benefit Corporation Law or the Governing Documents of the Association (each a "Dispute"), Civil Code section 5905 instructs that the Association must have in place fair, reasonable, and expeditious procedures for resolving the dispute and at a minimum the procedures must include the following seven features:

  (1) The procedure may be invoked by either party to the dispute. A request invoking the procedure must be made in writing.

  (2) The procedure shall provide for prompt deadlines. The procedure shall state the maximum time for the Association to act on a request invoking the procedure.

  (3) If the procedure is invoked by a Member, the Association shall participate in the procedure.

  (4) If the procedure is invoked by the Association, the Member may elect not to participate in the procedure. If the Member participates but the dispute is resolved other than by agreement of the Member, the Member shall have a right of appeal to the Board.

(5) A resolution of a dispute pursuant to the procedure, which is not in conflict with the law or the governing documents, binds the Association and is judicially enforceable. An agreement reached pursuant to the procedure, which is not in conflict with the law or the Governing Documents, binds the parties and is judicially enforceable. Of course, that agreement should be reduced to writing and signed by both parties.

(6) The procedure shall provide a means by which the Member and the Association may explain their respective positions.

(7) A Member of the Association cannot charged a fee to participate in the process.

Participation by Legal Counsel In IDR Sessions. Although not precluded, attorney participation in the IDR Process is discouraged in order to maintain direct discussions between the principals of the CID Dispute and to maintain the goal of resolution through an expeditious process. To the extent that the Owner indicates that he or she intends to have an attorney present at the IDR session, the that his/her/its attorney attend the IDR Process, the Owner should be required to give five (5) business days' notice to the Association so that the Association can decide if it wants the Association's counsel to also attend.

- Step-Three, Alternative Dispute Resolution (ADR) (Civil Code sections 5925-5960): Short of resorting to civil litigation in Superior Court, the last and most formal pre-litigation dispute resolution process under the Davis-Stirling Act is Alternative Dispute Resolution or "ADR" The Civil Code does not mandate that any particular form of ADR be used. The ADR process can be a mediation, an arbitration, a conciliation or any other non-judicial procedure (Civil Code section 5925(a)). The principal difference between IDR and ADR is that the latter process must involve a neutral third party to hear or facilitate the process. The ADR can also be binding or non-binding with the voluntary consent of the parties. It is much more common to have legal counsel present at

an ADR proceeding since the outcome of the process could be a final decision.

What Disputes are Subject to ADR? Another important feature of the Davis-Stirling ADR process is that the Association or a Member may not file an enforcement action in the Superior Court unless the parties have endeavored to submit the dispute to ADR (Civil Code section 5930(a). However the ADR requirement only applies as a prerequisite to an enforcement action that is solely for declaratory, injunctive or write relief and which pertains to enforcement of the Davis-Stirling Act, the Mutual Benefit Corporation Law or the Governing Documents. If the dispute pertains to one of those three subjects, then it is permissible for a party to also include a claim for damages which does not exceed the small claims court jurisdictional limit (typically $5000.00). See Civil Code section 5930(b). The ADR rules also do not apply to assessment disputes, unless the Member who receives a Pre-Lien Notice pursuant to Civil Code section 5660 requests ADR pursuant to Civil Code section 5660(f).

- Beginning the ADR Process (Civil Code section 5935). Any party to a dispute that is covered by the ADR statutes may initiate the ADR process by serving on all other parties to the dispute a "Request for Resolution". The Request for Resolution does not need to be in any particular format, but must include all of the following:

  (1) A brief description of the nature of the dispute.

  (2) A request for alternative dispute resolution. Parties desiring to initiate ADR are urged to be specific regarding what form of ADR they wish to pursue, since merely demanding ADR is ambiguous. For example an initiating party can say that he or she wishes to participate in non-binding mediation.

  (3) A notice that the party receiving the Request for Resolution is required to respond within thirty (30) days of receipt or the request will be deemed rejected.

(4) If the party on whom the request is served is the Member, accompanying the Request for Resolution must be a copy of Civil Code sections 5925 through 5960.

- Manner of Service of the Request for Resolution. Service of the Request for Resolution must be made by personal delivery, first-class mail, express mail, facsimile transmission, or other means reasonably calculated to provide the party on whom the request is served actual notice of the request.

- Time for Responding to a Properly Served Request for Resolution (Civil Code section 5935(c)). A party on whom a Request for Resolution is served has thirty (30) days following service to accept or reject the request. If a party does not accept the Request within that period, the Request is deemed rejected by the party.

- Time for Completing the ADR Process (Civil Code section 5940). If the party on whom a Request for Resolution is served accepts the Request, the parties shall complete the Alternative Dispute Resolution within ninety (90) days after the party initiating the Request receives the acceptance, unless this period for completion of the ADR is extended by written stipulation signed by both parties. In order to keep within these time-frames it would be helpful to include in the Request for Resolution a recommendation of a qualified third party neutral.

- Application of Evidence Code Mediation Rules (Civil Code section 5940(b). California Evidence Code sections 1115 through 1128 apply to any form of ADR initiated by a Request for Resolution, other than arbitration. Among other things, what this means is that in a mediation no evidence of anything said or any admission made for the purpose of, in the course of, or pursuant to, a mediation or a mediation consultation is admissible or subject to discovery, and disclosure of the evidence shall not be compelled, in any arbitration, administrative adjudication, civil action, or other noncriminal proceeding in which, pursuant to law, testimony can be compelled to be given. However, evidence otherwise admissible or subject to discovery outside of a

mediation or a mediation consultation shall not be or become inadmissible or protected from disclosure solely by reason of its introduction or use in a mediation or a mediation consultation. .

- Costs of the ADR (Civil Code section 5940(c). The costs of the ADR shall be borne by the parties. That statement in the Civil Code is not entirely clear, but was likely intended to mean that the parties must agree on how the expenses of the third-party neutral are to be borne and whether the neutral has authority to award costs or legal fees to the prevailing party.

- Certification to Accompany a Subsequent Civil Action (Civil Code section 5950). At the time of commencement of a civil action in Superior Court, the party commencing the action must file with the initial pleading a certificate stating that one or more of the following conditions are satisfied:

  (1) Alternative dispute resolution has been completed in compliance with the Davis-Stirling Act.

  (2) One of the other parties to the dispute did not accept the terms offered for Alternative Dispute Resolution.

  3) Preliminary or temporary injunctive relief is necessary.

Failure to file a certificate of compliance with the ADR requirements is grounds for a demurrer or a motion to strike unless the court finds that dismissal of the action for failure to comply with the Davis-Stirling Act ADR rules would result in substantial prejudice to one of the parties.

11. Director and Member Inspection Rights.

- Member Inspection Rights (Civil Code sections 5200-5240). The Davis-Stirling Act significantly expands the right of members of owners associations to access, inspect, and copy association documents and records. Civil Code section §5200(a)–(b)

specifically enumerates what "association records" and "enhanced association records" are to be made available for inspection. Under Civil Code §5205(a), a community association must make those records available for the time periods and within the time frames specified in Civil Code §5210(a)–(b) (see §2.112) for inspection and copying by a member of the association or the member's designated representative. If a member desires to designate another person to exercise the member's inspection rights, that designation must be in writing. Civil Code §5205(b). The association may bill the requesting member for the "direct and actual cost" of copying requested documents. Civil Code §5205(f). The association must inform the member of the amount of the copying costs (and the member must agree to pay those costs) before copying the requested documents.

No mention is made in Civil Code §§5200–5240 (the Inspection Rules of the Davis-Stirling Act) of the rights of directors to inspect the books and records of the community association they serve. That omission is likely grounded in the fact that directors of nonprofit mutual benefit corporations enjoy broad inspection rights under Corp C §8334, which provides that every director has the absolute right at any reasonable time to inspect and copy all books, records, and documents of every kind and to inspect the physical properties of the corporation of which such person is a director.

- Director Inspection Rights Should be Tempered by Considerations of Each Director's Fiduciary Obligations. (Corporations Code section 8334). Although the right of directors to inspect books and records of all kinds as well as the properties of the corporation is stated very broadly in Section 8334 of the California Corporations Code, what directors can do with the information they access remains subject to the constraints imposed by the director's status as a fiduciary.

  In other words, just because a sitting director has the right to inspect and to copy documents that have been clearly marked as being confidential or documents that originated in an executive session meeting of the Board does not mean that the director is

free to decide to share the document or information with persons who are not within the circle of individuals that are protected by the rules of confidentiality or the attorney-client privilege. Directors are also prohibited from using confidential association information, including email lists of members, for personal gain or to promote personal interests.