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2016/2017: NEW LAWS & LEGISLATION IMPACTING HOMEOWER'S ASSOCIATIONS

STATE LEGISLATION AND LAWS:

Civil Code § 4775 (Effective January 1, 2017) (aka AB 968)
Responsibility for repair, replacement, or maintenance
Effective: January 1, 2017

Significance: *The new version of Civil Code § 4775* (below) *is a long-awaited legislative clarification regarding the issue of owner versus association responsibilities as to separate interests and exclusive use common areas. The new version now clearly provides that the Association shall have the obligation to repair and replace exclusive use common area and the owners simply "maintain" it. Though not defined in the statute, "maintenance" is generally more of a cosmetic or appearance issue rather than a functionality or structural issue.*

(a) (1) Except as provided in paragraph (3), unless otherwise provided in the declaration of a common interest development, the association is responsible for repairing, replacing, and maintaining the common area.

(2) Unless otherwise provided in the declaration of a common interest development, the owner of each separate interest is responsible for repairing, replacing, and maintaining that separate interest.

(3) Unless otherwise provided in the declaration of a common interest development, the owner of each separate interest is responsible for maintaining the exclusive use common area appurtenant to that separate interest and the association is responsible for repairing and replacing the exclusive use common area.

(b) The costs of temporary relocation during the repair and maintenance of the areas within the responsibility of the association shall be borne by the owner of the separate interest affected.

(c) This section shall become operative on January 1, 2017. (Emphasis added.)

[NEW] Civil Code § 4777 (aka AB 2362)

Common Interest Developments: Pesticide-Notification

Significance: This new law requires an Association or an authorized agent to provide specific notice to homeowners and tenants about the use of pesticides, and identify it as a toxic substance, when the Association or its agent applies any pesticide without a licensed pest control operator at the owner or tenant's dwelling unit or in common areas.

Summary: The law specifies the contents of the pesticide notice to owners and tenants, as well as a notification procedure. It allows for signs to be posted in areas where pesticides are being applied by unlicensed pest control persons. If there is threat of immediate harm by the pest, such as a bee swarm, which makes prior notification unreasonable, then written notice may be posted as soon as practical, but not later than one hour after the pesticide is applied.

While Civil Code ¶ 4777 (a) contains important definitions, subpart (b) lays out the procedures and language to be used when giving notice, as follows:

(b) (1) An association or its authorized agent that applies any pesticide to a separate interest or to the common area without a licensed pest control operator shall provide the owner and, if applicable, the tenant of an affected separate interest and, if making broadcast applications, or using total release foggers or aerosol sprays, the owner and, if applicable, the tenant in an adjacent separate interest that could reasonably be impacted by the pesticide use with written notice that contains the following statements and information using words with common and everyday meaning:

(A) The pest or pests to be controlled.

(B) The name and brand of the pesticide product proposed to be used.

(C) "State law requires that you be given the following information:

CAUTION – PESTICIDES ARE TOXIC CHEMICALS. The California Department of Pesticide Regulation and the United States Environmental Protection Agency allow the unlicensed use of certain pesticides based on existing scientific evidence that there are no appreciable risks if proper use conditions are followed or that the risks are outweighed by the benefits. The degree of risk depends upon the degree of exposure, so exposure should be minimized.

If within 24 hours following application of a pesticide, a person experiences symptoms similar to common seasonal illness comparable to influenza, the person should contact a physician, appropriate licensed health care provider, or the California Poison Control System (1-800-222-1222).

For further information, contact any of the following: for Health Questions – the County Health Department (telephone number) and for Regulatory Information – the Department of Pesticide Regulation (916-324-4100)."

(D) The approximate date, time, and frequency with which the pesticide will be applied.

(E) The following notification:

"The approximate date, time, and frequency of this pesticide application is subject to change."

(2) At least 48 hours prior to application of the pesticide to a separate interest, the association or its authorized agent shall provide individual notice to the owner and, if applicable, the tenant of the separate interest and notice to an owner and, if applicable, the tenant occupying any adjacent separate interest that is required to be notified pursuant to paragraph (1).

(3) (A) At least 48 hours prior to application of the pesticide to a common area, the association or its authorized agent shall, if practicable, post the written notice described in paragraph (1) in a conspicuous place in or around the common area in which the pesticide is to be applied. Otherwise, if not practicable, the association or its authorized agent shall provide individual notice to the owner and, if applicable, the tenant of the separate interest that is adjacent to the common area.

(B) If the pest poses an immediate threat to health and safety, thereby making compliance with notification prior to the pesticide application unreasonable, the association or its authorized agent shall post the written notice as soon as practicable, but not later than one hour after the pesticide is applied.

(4) Notice to tenants of separate interests shall be provided, in at least one of the following ways:

(A) First-class mail.

(B) Personal delivery to a tenant 18 years of age or older.

(C) Electronic delivery, if an electronic mailing address has been provided by the tenant.

(5) (A) Upon receipt of written notification, the owner of the separate interest or the tenant may agree in writing or, if notification was delivered electronically, the tenant may agree through electronic delivery, to allow the association or authorized agent to apply a pesticide immediately or at an agreed upon time.

(B) (i) Prior to receipt of written notification, the association or authorized agent may agree orally to an immediate pesticide application if the owner or, if applicable, the tenant requests that the pesticide be applied before the 48-hour notice of the pesticide product proposed to be used.

(ii) With respect to an owner or, if applicable, a tenant entering into an oral agreement for immediate pesticide application, the association or authorized agent, no later than the time of pesticide application, shall leave the written notice specified in paragraph (1) in a conspicuous place in the separate interest or at the entrance of the separate interest in a manner in which a reasonable person would discover the notice.

(iii) If any owner or, if applicable, any tenant of a separate interest or an owner or, if applicable, a tenant of an adjacent separate interest is also required to be notified pursuant to this

subparagraph, the association or authorized agent shall provide that person with this notice as soon as practicable after the oral agreement is made authorizing immediate pesticide application, but in no case, later than commencement of application of the pesticide.

(6) A copy of a written notice provided pursuant paragraph (1) shall be attached to the minutes of the board meeting immediately subsequent the application of the pesticide.

[AMENDED] Civil Code §6000 (aka AB 1963)

HOA/Construction Defect Law

Under existing law, the Davis-Stirling Common Interest Development Act requires until July 1, 2017, specified conditions to be met relative to attempts to resolve construction defect claims before an association may file a complaint for damages against a builder, developer or general contractor based upon a claim for defects in the design or construction of the common interest development. This law has now been extended until July 1, 2024.

Civil Code §5300 (aka AB 596)

Annual Budget Reports

Beginning July 1, 2016, condominium associations, as part of their Annual Budget Reports, must disclose in separate statements (separate paper) using 10 point font their status as FHA [Federal Housing Administration] approved and as a VA [federal Department of Veterans Affairs] approved condominium project, where applicable. This does not apply to planned unit developments.

SB 918 [An act to add Section 4041 to the Civil Code]

Annual Address Updates for Association Notices

Summary: *This new law requires homeowners to annually verify their address or the addresses to which the association notices are to be delivered, and to specify whether the home is owner-occupied, rented out, vacant or undeveloped. If a homeowner does not comply each year, notices will be deemed delivered to the owner's property address. The statute does not address the consequences of the Association's failure to solicit the information annually. The new statute reads as follows:*

Civil Code § 4041

(a) An owner of a separate interest shall, on an annual basis, provide written notice to the association of all of the following:

(1) The address or addresses to which notices from the association are to be delivered.

(2) An alternate or secondary address to which notices from the association are to be delivered.

(3) The name and address of his or her legal representative, if any, including any person with power of attorney or other person who can be contacted in the event of the owner's extended absence from the separate interest.

(4) Whether the separate interest is owner-occupied, is rented out, if the parcel is developed but vacant, or if the parcel is undeveloped land.

(b) The association shall solicit these annual notices of each owner and, at least 30 days prior to making its own required disclosure under Section 5300, shall enter the data into its books and records.

(c) If an owner fails to provide the notices set forth in paragraphs (1) and (2) of subdivision (a), the property address shall be deemed to be the address to which notices are to be delivered.

SB 3: Minimum Wage Amendments to Labor Code

Expense Impact on Association, its Workers and Vendors

Minimum wage is scheduled to increase for all industries over the next six years. The current minimum wage is at least $10 per hour. Increases are progressive, depend on number of employees, and will be subject to annual determination. This legislation will likely affect the cost of doing business for Associations.

Automatic Installation of Board Members. (Proposed but failed)

AB 1799 -- An act to amend Sections 5100, 5105, and 5145 of the Civil Code.

The California Legislative Action Committee (CLAC) fought hard for the passage of this bill which would have allowed candidates to be automatically installed as board members when the number of candidates was fewer or equal to the number of open seats. Although it passed the full assembly, it was vigorously opposed by anti-HOA groups which claimed it was unconstitutional.

FEDERAL LEGISLATION:

HR 3700 – Housing Opportunity Through Modernization Act of 2016

FHA Condominium Certification Process

On July 29, 2016, President Obama signed into law, legislation which unanimously passed in both the U.S. House and Senate, FHA condominium rules (1) reducing the FHA condo owner occupancy rate down to 35%, (2) directing the FHA to streamline the condo re-certification process, (3) provide more flexibility for mixed use buildings, and (4) make reforms to federally

assisted housing programs to streamline programs involving Title I, Section 8, among other directives.

This legislation should make it easier to obtain a FHA loan.

24 CFR Part 100: Discriminatory Conduct Under the Federal Housing Act

Currently, this law provides rules regarding discriminatory conduct under the FHA. Effective October 14, 2016, the regulations are amended to formalize the standards used in the housing context to evaluate claims of hostile environment and harassment. It defines "quid pro quo harassment" and "hostile environment harassment" as being prohibited under the FHA, and specifies evaluation standards concerning whether conduct is in violation.

(a) General. Quid pro quo and hostile environment harassment because of race, color, religion, sex, familial status, national origin or handicap may violate sections 804, 805, 806 or 818 of the Act, depending on the conduct. The same conduct may violate one or more of these provisions.

(1) Quid pro quo harassment. Quid pro quo harassment refers to an unwelcome request or demand to engage in conduct where submission to the request or demand, either explicitly or implicitly, is made a condition related to: The sale, rental or availability of a dwelling; the terms, conditions, or privileges of the sale or rental, or the provision of services or facilities in connection therewith; or the availability, terms, or conditions of a residential real estate-related transaction. An unwelcome request or demand may constitute quid pro quo harassment even if a person acquiesces in the unwelcome request or demand.

(2) Hostile environment harassment. Hostile environment harassment refers to unwelcome conduct that is sufficiently severe or pervasive as to interfere with: The availability, sale, rental, or use or enjoyment of a dwelling; the terms, conditions, or privileges of the sale or rental, or the provision or enjoyment of services or facilities in connection therewith; or the availability, terms, or conditions of a residential real estate-related transaction. Hostile environment harassment does not require a change in the economic benefits, terms, or conditions of the dwelling or housing-related services or facilities, or of the residential real-estate transaction.

(i) Totality of the circumstances. Whether hostile environment harassment exists depends upon the totality of the circumstances.

(A) Factors to be considered to determine whether hostile environment harassment exists include, but are not limited to, the nature of the conduct, the context in which the incident(s) occurred, the severity, scope, frequency, duration, and location of the conduct, and the relationships of the persons involved.

(B) Neither psychological nor physical harm must be demonstrated to prove that a hostile environment exists. Evidence of psychological or physical harm may, however, be relevant in

determining whether a hostile environment existed and, if so, the amount of damages to which an aggrieved person may be entitled.

(C) Whether unwelcome conduct is sufficiently severe or pervasive as to create a hostile environment is evaluated from the perspective of a reasonable person in the aggrieved person's position.

(ii) Title VII affirmative defense. The affirmative defense to an employer's vicarious liability for hostile environment harassment by a supervisor under Title VII of the Civil Rights Act of 1964 does not apply to cases brought pursuant to the Fair Housing Act.

(b) Type of conduct. Harassment can be written, verbal, or other conduct, and does not require physical contact.

(c) Number of incidents. A single incident of harassment because of race, color, religion, sex, familial status, national origin, or handicap may constitute a discriminatory housing practice, where the incident is sufficiently severe to create a hostile environment, or evidences a quid pro quo.

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A REVIEW OF 2016 CALIFORNIA COURT DECISIONS AFFECTING COMMUNITY AND HOMEOWNER'S ASSOCIATIONS

1. *Nellie Gail Ranch Owners Association v. McMullin* 2016 S.O.S. 5455*
(A Quiet Title and Equitable Easement Case in favor of the Association)

Significance: This case is a victory for HOAs seeking to regain control over their common area encroached upon by homeowners as it clarifies the application of the legal doctrine of adverse possession and prescriptive easements to common areas.

Brief Facts: Plaintiff Nellie Gail HOA sued the McMullins, (Defendants), for quiet title and to compel the McMullins to remove a retaining wall and other improvements they built without HOA approval on more than 6000 square feet of common area that the HOA owned adjacent to the McMullins' property. After a bench trial, the trial court entered judgment for the HOA and awarded them their attorneys' fees. The McMullins appealed, claiming the trial court should have awarded them quiet title, or at least should have granted them an equitable easement over the disputed property based on communications from the Association.

Disposition: The Court of Appeal affirmed the trial court's judgment in favor of the HOA.

Key Findings: The Court noted that the essential elements for equitable estoppel were lacking in the evidence.

Defendants based their equitable estoppel claim on the two written communications they received from the HOA Board of Directors telling them they had decided not to pursue the unauthorized construction of the retaining wall and related improvements as a CC&Rs violation, but instead instructed them to work with the Nellie Gail's architect to develop a landscaping

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plan to screen the wall from view. In reliance, thereon, the McMullins assert they spent $20,000 on a landscaping plan for the area around the retaining wall.

The Court was not sympathetic, finding that the McMullins could not have justifiably relied on the written communications from the Board of Directors since the communications occurred well after the McMullins spent $150,000 to construct the wall and improvements, and that amount did not include landscape screening, irrigation, and drainage around the wall. Moreover, the Court concluded that the HOA did not know all the essential facts regarding the extent of the encroachment when it voted not to pursue the wall as a CC&Rs violation and approved the plans to screen the wall in an effort to reach an amicable solution. The Court also found that the McMullins were not ignorant of the facts because they concealed their rear property line's location from the HOA and knowingly started construction without written approval from the HOA.

(2) The Court of Appeal also disagreed that the McMullins acquired any interest in the disputed property by Adverse Possession ("AP"). The Court concluded that the Defendants did not meet their burden of proving that they either paid taxes on the property at issue, or that no taxes were levied or assessed. Instead, they argued the common area had no value, so there was no taxation. Payment of taxes over a five-year period (or a showing that no taxes were levied or owed) is one required element for AP. It was noted that common areas like the one at issue do have value and the property taxes for it are levied and paid by the individual homeowners of an association.

(3) The trial court's grant of an injunction against the McMullin's encroachment (requiring them to remove the visible portions of the retaining wall and restoring the surrounding area) was confirmed on appeal as not being an abuse of discretion. To do otherwise, would have resulted in an equitable easement for which three factors had to be present. First, the defendant must be innocent, meaning the encroachment must not be willful or negligent. In this case, the Court of Appeal did not even have to consider the second and third factors involving injury and hardship to the parties, because the McMullins were found to be not innocent in constructing the wall on HOA property, and intentionally did not identify their rear property line even though they were asked to supply that information in their applications, and they knew that their previous plans for the retaining wall had been rejected in writing before they constructed it.

2. *Palm Springs Villas II Homeowners Association, Inc. v. Parth* (2016) 248 Cal.App.4th 268 (A Board of Director's Breach of Fiduciary Duty and CCRs Summary Judgment Case – an important test for the Business Judgment Rule)

Significance: This case is important because it tells us there is no *automatic* immunity, presumption of innocence, or deference granted whenever an officer or member of a Board of Directors acts or believes he or she is acting in good faith, but is actually mistaken in the actions

taken, or decisions made because the officer or Board member did not properly investigate or follow the rules in the Association's governing documents. *In addition* to acting in good faith, the individual must exercise "reasonable diligence" by following the governing documents, including CC&Rs and By-Laws, (especially with regard to member or voting approval, and the subject matter at issue), and investigating contractors, and any other contractual (or other) issues before binding the Association. This decision could have significant impact on defenses asserted by members of a Board, as well as on Association D & O insurance issues since the Business Judgment Rule is a prime avenue of defense.

Brief Facts: A condominium homeowners' association sued an individual, 87-year-old former Board Member and President of the Board ("Defendant") for breach of fiduciary duty and breach of the Association's governing documents. At the request of the Association's property management company, the Defendant, who was President at the time, went to the management office and signed multiple construction contracts allegedly without investigation of contractor licenses and without Board approval or a vote. The HOA was later sued by one contractor for breach of contract when they terminated his services early. Over a four-year period, the Defendant also signed at least two large promissory notes secured by Association assets to fund common area paving and walkway projects, and a 5-year landscaping contract extension, with some Board resolution and authorization to do so. However, the Bylaws required member approval for both. Defendant President also found and hired a roofing company on her own (without initial notice or approval by the Board) after the members voted against a special assessment to offset repairs for an estimate submitted by another roofer. Issues later arose about the licensing and [poor] quality of the roofer's work. Defendant also renewed a one-year security company contract without a Board vote and approval, while one Board member was actively obtaining bids from other companies. Defendant testified she acted in good faith, in the best interests of the Association, and did not receive any pecuniary gain or personal benefit.

Disposition: The Court of Appeal reversed the summary judgment granted in Defendant's favor under the Business Judgment Rule. The Court concluded there were genuine issues of material fact as to whether Defendant breached the governing documents, whether she exercised reasonable diligence in investigating and paying the contractors, and whether she acted in good faith. The Court also found that genuine issues of material fact existed as to whether the exculpatory clause in the CC&Rs or the Business Judgment Rule applied at the summary judgment stage.

Key Findings: The Court agreed with the Association, finding that summary judgment could not be granted in Defendant's favor on the basis of the Business Judgment Rule or the exculpatory clause because the record disclosed triable issues of fact that should not have been resolved without a trial

3. *Almanor Lakeside Villas Owners Association v. Carson* (2016) 246 Cal.App. 4th 761
(HOA awarded larger attorneys' fees than the amount of fines it requested.)

Significance: Although *most* of the Association's $54,000 fines were disallowed, it was awarded more than $100,000 in attorneys' fees as the prevailing party, making it the overall winner in the case. The Court recognized that the Association had the right to adopt and enforce its own reasonable rules, and that some of the fines/fees charged were justified.

Brief Facts: Homeowners' Association brought action against unit owners of two properties, seeking to enforce fines and CC&R provisions which were intended to prevent owners from using their properties for rentals less than thirty (30) days in duration, or for hotel purposes, unless the owners provided the board with the rental agreement at least seven days before the rental period.

Disposition: The Court of Appeal affirmed the award of attorneys' fees and the judgment on the owners' Cross-Complaint in favor of the Association, and awarded them costs on appeal.

Key Findings: Although both sides claimed to be the "prevailing party", the Court awarded attorneys' fees to the Association under CCP Section 5975 of the Davis-Stirling Act, deeming it to be the prevailing party in an action to enforce the governing documents. Since the statute and Act do not define "prevailing party", the test to make that determination is "whether a party prevailed on a practical level by achieving its main litigation objectives." Even though both sides achieved some positive net effect (and had mixed results), the Court concluded that since some of the fines were enforceable, the Association had met its objective and satisfied the criteria needed "to enforce the governing documents". Therefore, there was no abuse of discretion in determining the HOA was the prevailing party.

4. Rancho Mirage Country Club Homeowners Association v. Hazelbaker
(2016) 2 Cal.App.5th 252
[Favorable case for Associations granting them attorneys' fees for enforcing a settlement – lawsuit treated as action "to enforce the governing documents"]

Significance: The Association as the party who prevailed by "achiev[ing] its main litigation objectives" was entitled to its reasonable attorneys' fees in a patio dispute which the Court treated as an action to enforce the governing documents, rather than simply as a breach of a settlement agreement, which would have required applying a different standard.

Brief Facts: Homeowners made improvements to exterior patio which the Association contended violated the governing CC&Rs. The parties mediated the dispute pursuant to the

Davis-Stirling Act which resulted in a written agreement. Subsequently, the Association filed this lawsuit, alleging that the Defendants had failed to comply with their obligations under the mediation agreement to modify the patio in certain ways. The homeowners made changes to the patio to the Association's satisfaction during the ongoing lawsuit, but the parties could not come to agreement on the subject of attorneys' fees. The Association believed it was the prevailing party entitled to its fees.

Disposition: The Court of Appeal held that the Association was the prevailing party and that the lawsuit was an action "to enforce the governing documents" within the meaning of the Davis-Stirling Act, entitling the Association to its reasonable attorneys' fees for the lawsuit and on appeal.

Key Findings: Since the focus of the Association's complaint was that the homeowners had not taken certain steps to bring their property into compliance with the applicable CC&Rs, the relief sought is an order requiring defendants to take those steps. The fact that there was a mediation agreement signed to make them comply does not change the underlying nature of the dispute or relief sought. The trial court properly considered the Davis-Stirling Act as the basis for recovery, which provides for mandatory attorneys' fees to the prevailing party. The Association prevailed because they achieved their goal by compelling the Defendants to complete the modifications to the patio.

FEDERAL CASE LAW – PUBLISHED

5. **Castillo Condominium Association v. U.S. Department of Housing & Development (2016) 821 F.3d 92**
   [HUD prevailed in case in which condo association was found to have discriminated against a homeowner by not letting him keep his pet as an emotional support dog.]

Significance: HUD views this FHA discrimination case as a victory for people with disabilities, one that allows them to have reasonable accommodations when proven to be needed, and one which prohibits discrimination based on disability. HOA's will need to make exceptions to "no pets" policies if the facts of the case warrant it. Here, the homeowner had a lifelong history of depression and treating doctors for years had corroborated his account that he suffered from a mental impairment that "substantially limited one or more of his major life activities."

Brief Summary: The Appeals Court confirmed this year a decision made by HUD in 2014 in which it ruled that a condo association violated the rights of a homeowner with disabilities (anxiety and depression) when it refused to allow the homeowner to keep his "emotional support dog" as a reasonable accommodation to its "no pets" policy. The homeowner had

been warned by letter that he would be fined if he kept the dog, and he responded promptly in writing, including a note from his treating psychiatrist, informing the HOA of his disability and need for the dog. It made no difference to the Association and HUD determined that the homeowner was forced to sell his condo and find alternative housing. The Association appealed after being found liable for $20,000 in damages to the homeowner, along with a $16,000 penalty.

6. <u>Desert Pine Villas Homeowners Association v. Kabiling</u>
   In re Kabiling (551 B.R. 440)
   [Association held in contempt for violating a Bankruptcy Court discharge order]

Significance: Homeowner Associations need to consult with qualified attorneys to assist them in determining what course of action to take, if any, once a homeowner files for bankruptcy. The Association may have had a different result if it did not seek attorneys' fees, or make allegations about pre-bankruptcy debts, and/or had specified that it was not seeking any money from the former owners.

Brief Summary: After homeowners filed a Chapter 7 bankruptcy petition and abandoned their unit, the Association acquired it through a nonjudicial foreclosure sale. However, the homeowners were discharged from their outstanding Association debt upon filing for bankruptcy, and the court ordered all creditors to cease attempting to collect any discharged debts from them. The discharge order was mailed to all creditors, including the Association. Notwithstanding, the Association sued the homeowners in an effort to confirm that it held good title to the unit (in order to obtain title insurance), and to demand its attorneys' fees. This was not well received by the Court, which responded by holding the Association in contempt for violating the Court's discharge order when it sued the homeowners for failure to pay assessments, clear title, and sought its attorneys' fees from the discharged homeowners, all of which were based on pre-discharge events. The Association was ordered to pay the homeowners $8,928 in damages for their contempt of the Court's order.