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## Common Interest Developments: Housing at Risk?

*By Julia Lave Johnston  
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*Requested by Senator Tom Torlakson*

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*By Julia Lave Johnston  
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## EXECUTIVE SUMMARY

The state's 34,000 common interest developments (CIDs) house eight million Californians, about 24 percent of the state's population. Approximately 2,500 new CIDs are built each year and they make up the majority of new housing being constructed in some counties. The apparent popularity of CIDs is challenged by the ongoing concerns and criticisms leveled at this housing type by homeowners and professionals who provide services to CIDs.

Common interest developments are characterized by the individual ownership of a house or condominium coupled with the shared ownership or right to use common areas. These common areas can include streets, parks, and recreational facilities. CIDs are managed and maintained by an association, which all homeowners belong to by law. A board of directors, elected by the development's homeowners from their ranks, governs the association. The board is responsible for collecting monthly assessments to fund day-to-day expenses and for the upkeep and replacement of major infrastructure components over time.

Since the first CIDs were developed there have been reports of problems with governance, management, and quality. Although the majority of CIDs seem to function without serious problems, there has been a steady stream of horror stories and infuriated homeowners who have appealed to the legislature to intervene.

Some CIDs professionals argue that the largest issue facing CIDs is that associations are not adequately saving for future maintenance expenses. Aging CIDs will find themselves without the necessary funds to replace deteriorated components and maintain the quality of their buildings. This could cause economic hardship for CID residents in the form of added costs and could lead to blighted neighborhoods.

While there is a great deal of talk about CIDs that have already deteriorated or are on shaky financial ground, finding evidence to confirm this situation is more difficult. There are no standards by which to rate financial health of CIDs, nor do we track CIDs that are currently having or have had financial difficulties. Because of this we do not know how many projects might be experiencing financial difficulties. Nor do we know how many individuals may have had to move, borrow money, or face other hardships because of poor fiscal management.

This report focuses on the current financial mechanisms and practices of CIDs. It became apparent that there were a number of issues that were not necessarily financial in nature but affected the future sustainability of CIDs.

Some of the major issues facing CIDs include:

- Massive noncompliance with state laws governing CIDs. The law has certain financial requirements but these are vague and not often enforced. Some accuse the law of being too complex and difficult for board members to understand,

much less follow. Others claim that the law is adequate but board members, homeowners, and CID professionals fail to follow it.

- Reserve funds that are earmarked for maintenance and the replacement of components are often under-funded due to low assessments and borrowing by the board for other expenses. There is no required funding level or standard for determining whether or not funding is adequate.
- Ineffective governance of some associations. Board members, who are lay people, often manage what can be multimillion-dollar corporations. Associations can hire professional management, but homeowners may balk at the cost or the lack of accountability to homeowners. There are no licensing requirements for community association managers and there are many examples of financial and management errors.
- Relationships between board member and homeowners can become contentious. There is an ongoing debate over what rights and responsibilities the different parties have. This can be caused by a lack of understanding of CID law on both sides. Often the only method to settle these issues is litigation. This can drain both parties' resources and create a hostile living environment.

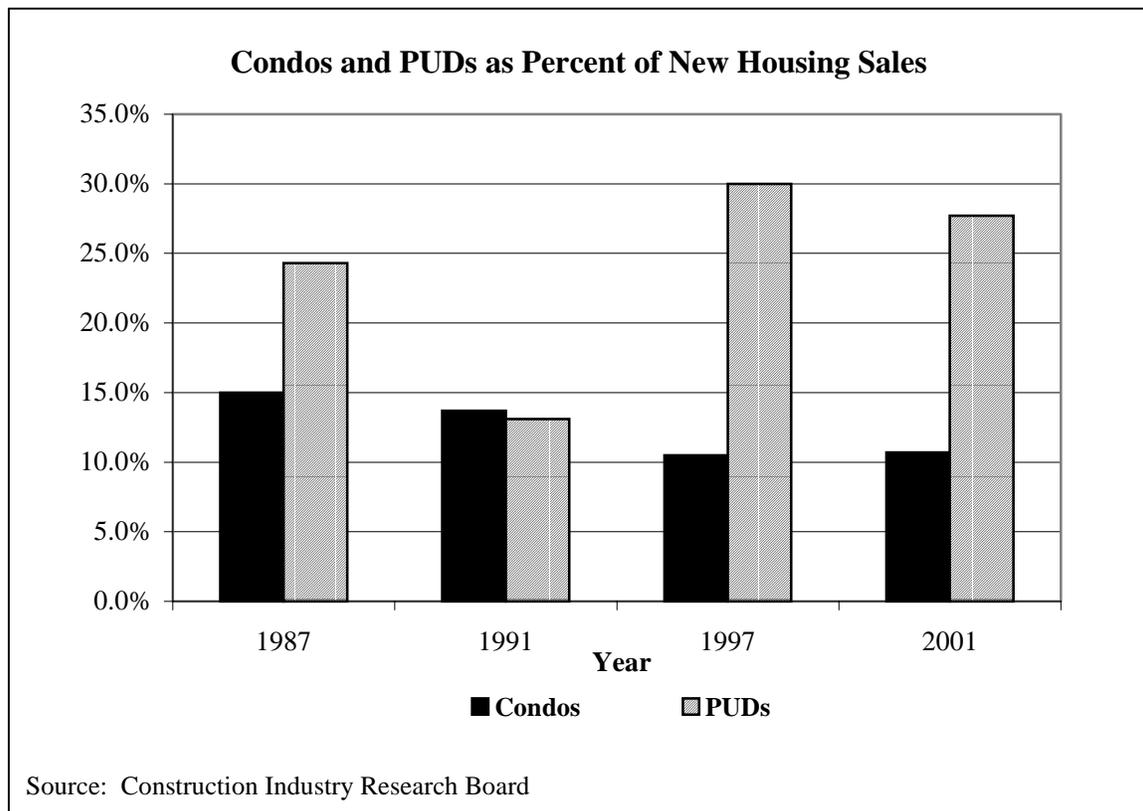
Other states have addressed these issues by creating departments to deal with CID disputes, mandating how reserve funds are calculated and at what level they are funded, and licensing managers. In California, some local governments have also passed laws aimed at addressing CID issues.

## WHAT IS A COMMON INTEREST DEVELOPMENT?

A common interest development, or CID, is a development characterized by the individual ownership of either a housing unit or parcel coupled with the right to use shared common areas and facilities. These common areas can include roads, parks or open space, lakes, clubhouses, gyms, pools, and tennis courts.

Most CIDs in California are either condominiums, which make up about 65 percent of all CID developments, or Planned unit developments (PUDs), which account for 33 percent.\* During the 1990's the percentage of all new home sales that were condominiums declined while the percentage of new homes in PUDs increased from just under 11 percent to almost 28 percent.†

Chart 1



Condominiums are always multifamily, attached housing such as townhouses or apartments. PUDs can be single-family detached or attached units, townhouses, or a mix of these housing types. In some cases, there is no visible difference between a condominium and a PUD.‡ In both types of CIDs, residents are responsible for

\* The remaining two percent are cooperatives. Levy & Company Certified Public Accountants, 2001 *California Community Association Statistics*.

† Information provided by the Construction Industry Research Board (CIRB).

‡ Condominium residents each own a unit and hold an undivided interest in common areas. PUD residents own their unit and the land. The other areas are owned by the association or in common by the residents.

maintaining their individual property while the association maintains all common use areas and exclusive use common areas. This can include roofs, heating systems, doors, windows, roads, lighting, landscaping, etc. Besides maintaining the physical aspects of a CID, an association may also be responsible for services such as security and waste disposal.

The legal definition of ownership determines whether a development is a condominium or a PUD. Typically condominium ownership consists of the right to inhabit a unit, but not ownership of the physical building, and an undivided interest in the development's common areas. PUD residents own a lot or parcel, which may be indistinguishable from a non-PUD development, and the developments common areas are owned by the association or in common by the residents.

Condominiums are always constructed as CIDs because multiple owners share common property, such as walls and roofs. PUDs are developed at the request of a local jurisdiction or because the developer plans on including shared facilities, such as roads or swimming pools.

CID housing can be found at all income levels. Condominiums are often credited with providing much needed affordable housing because they allow apartment ownership. Condominiums do provide less expensive housing when compared to single-family housing in the same geographic location. PUDs can also be cheaper than single-family homes, but this varies by county.\*

## **THE EVOLUTION OF CALIFORNIA CID LAW**

By the end of the 1960s, in response to a jump in condominium development, all 50 states had passed condominium laws. High levels of litigation in CIDs caught the attention of the National Conference of Commissioners on Uniform State Laws (NCCUSL). They attempted to improve the laws governing condominiums, co-ops and PUDs by creating a Uniform Common Interest Ownership Act (UCIOA) in 1982.<sup>†</sup> The UCIOA addresses creation, organization, and management of CIDs. Several states have adopted some form of the UCIOA.

Instead of adopting the UCIOA, in 1983 the Assembly convened a select committee to study the needs of California CIDs. The result was the passage of the Davis-Stirling Act<sup>1</sup> in 1985, which repealed the old condominium act and consolidated a number of sections of the Business and Professions Code and the Civil Code.

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\* Information provided by the Construction Industry Research Board (CIRB). For example, in Santa Clara County--the heart of Silicon Valley--new single-family homes in 2001 sold for an average of \$707,800 while condominiums averaged \$458,600 and PUDs averaged \$658,400. In Los Angeles County, single-family homes averaging at \$396,700 were about the same price as condominiums at \$386,700. PUDs averaged \$502,700.

<sup>†</sup> The Uniform Common Interest Ownership Act was amended in 1994.

In addition to the Davis-Stirling Act, CIDs are still governed by numerous other statutes. During their initial development, CIDs are governed by the Subdivided Lands Act.<sup>2</sup> After their formation, CIDs are required to follow the provisions of the Nonprofit Corporation Law.<sup>3</sup> CID laws and regulations are administered by a variety of state agencies, as will be discussed later in this paper. Most CIDs are formed as mutual benefit corporations. Mutual benefit corporations are nonprofit corporations that are formed exclusively for the benefit of their members. They do not include organizations formed for religious, charitable, or social welfare purposes.

In addition to Davis-Stirling they must also follow sections of the Corporations Code. CID issues keep reappearing at the state level. The State Legislature has held three hearings on CIDs since the passage of the Davis-Stirling Act. (For a summary of hearing findings and other state research in CIDs see Appendix A.) The Act has been amended more than 40 times since its passage.<sup>4</sup> The changes that have been made to Davis-Stirling over the years have moved CIDs away from a purely corporate model and closer to a municipal model. These changes mostly relate to due process issues such as notification and participation, and are aimed at providing homeowners with greater access to information about their CID management and governance.<sup>5</sup>

The California Law Revision Commission (CLRC) is currently studying California CID law, including Davis-Stirling, and will make recommendations in the next few years on how to improve the regulation of CIDs. Many legal experts criticize California CID law as:

- Too complicated and hard to understand;
- Contradictory;
- Uneven in its coverage;
- Difficult to enforce and,
- Offering weak protection for individual rights.<sup>6</sup>

One of the papers written for the Commission points out that Davis-Stirling was never meant to be comprehensive. The Act only provided solutions for those areas on which the represented interest groups reached agreement and did not address many other issues.<sup>7</sup>

## **HOW CIDs ARE GOVERNED**

The developer is responsible for creating a CID's homeowner association and its governing documents. A CID's primary governing document is its covenants, conditions and restrictions (CC&Rs), but also includes by-laws.

If the CID is a nonprofit mutual benefit corporation, it will also have articles of incorporation. These articles include information about the CID, members' rights, and the management of the corporation.<sup>8</sup> The Corporations Code has provisions for amending the articles, which at the minimum requires approval of the board and a majority of a quorum of members present at the meeting. Individual CC&Rs can have

stricter requirements for amendments and some require the approval of a majority of homeowners.

Incorporated CIDs must file their articles of incorporation with the Secretary of State's Office. They must re-file every two years. To receive tax-exempt status, CIDs must also file with the Franchise Tax Board.

A small percentage of CIDs are not incorporated. They are not required to file and do not receive the same tax benefits or the same liability protections as incorporated CIDs. They are, however, required to follow most of the same laws.

When the developer sells enough homes to reduce his ownership to less than 25 percent of the CID, control of the development passes to the CID's Homeowner association (HOA).<sup>\*</sup> California law requires that all CIDs are managed by a homeowner association, which is governed by an elected board of directors. All homeowners are automatically members of their association. The board of directors is charged with enforcing the CC&Rs and maintaining property values. The CC&Rs state, with very little flexibility, the responsibilities, and the duties of the association and its directors.<sup>9</sup>

CC&Rs give HOAs a tremendous amount of power that one would normally consider belonging to a homeowner. For instance, CC&Rs can determine what changes homeowners can make to the outside of their house, such as paint color, as well as what type of curtains they hang in their windows. An HOA can force homeowners to keep their garage door closed or mow their lawn. An association can even enforce how much a pet can weigh. Depending on the type of CID, the HOA can also determine when homes will be upgraded and repaired and how much it will cost. The homeowners do not initially determine these rules; the developer determines them. This means that the developer plays a large role in establishing the character of the community.

The courts have ruled that CC&Rs are binding unless they are found to be unreasonable. They can usually only be superseded by certain state and Federal laws. Homeowners can amend CC&Rs by following the procedures spelled out in their CID's CC&Rs. If there is no provision in the CC&Rs, Davis-Stirling allows for the majority to change them. Davis-Stirling also allows the HOA to petition the courts to amend the CC&Rs.<sup>10</sup>

The rules and regulations are the other governing component of CIDs. The board has more flexibility in the creation of rules. These are not part of the CC&Rs and may not require membership approval.<sup>†</sup>

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<sup>\*</sup> Control passes to the HOA when the developer owns less than 25 percent of the CID because up until that point, the developer has a majority control on the board. This is because the developer receives two votes for every property that he or she owns. After more than 75 percent of the development has been sold, the developer receives one vote per property. While the developer can still vote, he or she no longer has a controlling vote on the board.

<sup>†</sup> The California Law Revision Commission has written about the area of rule making in Study H-851, Memorandum 2001-55, Nonjudicial Dispute Resolution Under CID Law: Due Process in Association Rulemaking and Decisionmaking, June 14, 2001 <<http://www.clrc.ca.gov>> MM01-55-CID-DueProcess.pdf.

While CC&R's and rules and regulations can seem overly restrictive to some, many homeowners welcome these guidelines. They believe that these guidelines protect property values and their quality of life.



## **A BRIEF HISTORY OF CIDS**

Common interest developments have their roots in the utopian ideas of an Englishman named Ebenezer Howard. Writing in the 1890s, Howard dreamed of creating a “new civilization based on service to the community and not on self-interest.”<sup>11</sup> He planned on accomplishing this by building self-sustaining planned communities. These new towns or “garden cities” would be planned to contain industry, houses, agricultural lands, and open space. All the necessities—food, housing, school, recreation, jobs, public works, old age pensions, medical care, etc.—of the community would be met internally. Each city would be surrounded by a greenbelt that would distinguish it from other communities and maintain its sustainable size. The municipality would own all the land in the community and residents would pay rent instead of owning property.

Howard’s communities embraced people of all income levels. There was, however, another type of new community being constructed in the 19<sup>th</sup> century that created exclusive neighborhoods for the rich. These communities were designed to separate and protect residents from the less pleasant aspects of their surroundings.<sup>12</sup> Developers tied restrictive covenants to the land through deeds to make sure that the amenities and exclusivity of the development were maintained. Eventually, developers organized homeowner associations to enforce their covenants. Some of these early covenants are still in effect today over 100 years later.

### **RADBURN—PROTOTYPE FOR TODAY’S CID**

In 1928 the two extremes of utopian and elitist private community met in the planned community of Radburn, New Jersey. The creators of Radburn, who were influenced by Howard, wanted to provide not just housing, but also a way of life. They attempted to build a family-oriented community that integrated home, work, and play. Ultimately, for all its innovations, Radburn failed to become the garden city envisioned by its planners. Howard wanted to create quality affordable housing for working people. This utopian ideology did not work with American capitalism, which was building for profit, not philanthropy.<sup>13</sup>

Radburn’s governance structure was as innovative as its design and more enduring. The Radburn Association governance system was based on a council-manager model of municipal government.<sup>14</sup> This form of government promoted the idea of professionalized government. Reformers at the time thought this model would reduce corruption in local government by taking it out of the hands of ordinary citizens.

Modern CID developers adopted the Radburn model of a depoliticized, managerial government dominated by professionals.<sup>15</sup> This structure is different from today’s CIDs because it separates management and policy development from more immediate homeowner issues. The model consists of a full-time manager who handles administrative issues, a nine-member board of trustees that is responsible for the management of the community and a citizens’ association that represents residents. The citizens’ group gives homeowners a forum to discuss the issues that concern them. The

president of this group sits on the board of trustees. The citizen's group is only advisory to the board.<sup>16</sup>

## THE MODERN CID

The adoption of Radburn's governance model and the popularity of private community developments encouraged the Federal Housing Authority (FHA) to provide mortgage and title insurance for condominiums and planned developments in the 1960s. These actions, along with Federal condominium legislation, encouraged the development of CIDs and their marketing to middle class families.<sup>17</sup> Large planned communities, such as the City of Irvine (200,000 residents) and Sun City outside of Phoenix, Arizona (46,000 residents), helped popularize CIDs by providing successful examples.

In the 1960s and 70s, smaller families, families with both partners working, older residents, and an increase in the marriage age, combined with growing land costs, led to an increased demand for smaller dwelling units. Condominiums, which were less expensive and did not require as much maintenance by the owner, answered this demand.<sup>18</sup>

Another factor leading to the construction of smaller dwelling units was climbing California land prices and population growth in the 1970s and 1980s. This resulted in a decrease of available cheap land, which had made single-family homes affordable to the middle class.<sup>19\*</sup> Added to these factors was the shrinking of local revenues for infrastructure and service provision in the wake of Proposition 13.<sup>20</sup> This situation made CIDs popular with developers, planners, and local elected officials. As land became more expensive, developers wanted to increase property densities to make housing affordable to more buyers. Local governments wanted to avoid the costs of new infrastructure and maintenance expenses. CIDs effectively transferred these costs from the general fund to the developer. The developer then passed these costs on to homebuyers.

As the number of CIDs increased, problems started to arise. Poor construction, financial concerns arising from low assessments and the inability of homeowners to effectively manage their developments threatened the marketability of CIDs. In spite of these issues, CID development boomed and continues to make up a significant portion of new housing constructed in California. Economic issues arising from Proposition 13 may have accelerated the California's CID formation, but it was not the only state experiencing a CID increase. In 1964, there were fewer than 500 homeowner associations in the United States. By 1970, there were 10,000. By 2001, Community Associations Institute (CAI) estimated that there were almost 230,000 common interest developments in the United States, housing 47 million people or one-in-six U.S. residents. They live in 18 million homes and pay approximately \$35 billion in assessments every year,<sup>21</sup> which is slightly less than the 2002 budget for the State of Michigan. In California alone, CID annual revenues are an estimated \$7 billion.<sup>22</sup>

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\* Evan McKenzie, *Privatopia*, pp. 81-82. Developers realize a profit by buying cheap land and then subdividing it into lots that are suitable for housing. In 1948, land and infrastructure such as roads and sewers accounted for 11 percent of the price of a house. By 1966 these costs had reached 19.6 percent and in the late 1970s they were between 25-30 percent.

## ARE CIDS FOR EVERYONE?

CID critic Evan McKenzie argues “CIDs existed because they made enormous economic sense to builders, not because buyers were aching for smaller lots, shared swimming pools and neighborhood governments.”<sup>23</sup> He found that the increased number of CIDs in California is explained by high land costs and fiscal constraints on local government, and not by consumer preference.<sup>24</sup>

A 1991 CIDs report found that the majority of homeowners purchased a CID home because it was less expensive than a traditional single family home. The report theorizes that because these homeowners compromise their desire for a traditional home by purchasing a CID, they are more likely to resent CID restrictions and to break the rules. It also found that 80 percent of current CID homeowners and board members it surveyed were satisfied with CIDs, as a form of housing and at least 73 percent would buy another CID.<sup>25</sup> The report does not address this contradiction.

A 1999 nationwide survey of CID homeowners found that 37 percent would live in a CID again and only 26 percent would not.<sup>26</sup> Those that liked CIDs cited ease of maintenance and security. Those that would not live in a CID again said that it was because the rules were too restrictive and the fees and costs were too high. Sixty-seven percent of the respondents lived in a single-family CID home. A number of reports have suggested that there is less satisfaction with condominiums than single-family CIDs. It is also true that as homebuyers become more aware of what it means to live in a CID, they may become self-selecting, causing satisfaction rates to increase over time. Those involved in developing and servicing CIDs say that 30 to 35 percent of homebuyers avoid CIDs because they do not like the rules and requirements.<sup>27</sup>

While the idea of restrictions and rules do not appeal to some, CIDs do have positive amenities that do appeal to many people. As one CID professional said, “With a good board and good property management, CIDs can be great because you don’t have to cut your own grass.”<sup>28</sup>

Other observers note that the desire to live in a CID “is a quest for community that is lost.”<sup>29</sup> This desire for community, along with heightened concerns for safety, arose at a time that local government did not have the resources to help redefine or develop community. CIDs, especially those that were gated,<sup>\*</sup> were the private sector filling these consumer needs.<sup>30</sup>

CIDs allow homeowners to tailor local services to their needs and to have more control over those services. In a diverse society, CIDs offer homeowners a sense of stability not only by regulating behavior, but also by attempting to maintain high property values. Edward Blakely, who wrote an extensive book on gated communities, argues, “Local governments have walked away from addressing civil decline, but the neighborhood association prevents all that.”<sup>31</sup>

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\* Gated communities must be CIDs because the streets must be private.

## THE FUTURE OF CIDS

Housing analysts almost universally agree that common interest developments will remain part of the housing mix in California.

- The state's aging population is attracted to the amenities, safety and sense of community found in CIDs.
- High land and housing costs throughout the state serve to make CIDs seem like a housing solution rather than a liability.
- New state emphasis on encouraging smart growth development, which emphasizes higher density housing that uses existing infrastructure, may make CIDs even more popular among developers and local governments. So far, CIDs have been one of the few vehicles that have successfully increased density.
- CIDs currently provide hundreds of thousands of housing units. The Department of Real Estate (DRE) approves approximately 2,500 new CIDs for construction every year.<sup>32</sup> These units are crucial given the state's need for housing.



## **CID ISSUES—SHOULD WE WORRY?**

Of all the issues affecting future CID viability, CID professionals are most concerned about the financial security of CIDs.<sup>33\*</sup> The responsibility for managing a common interest development is given to the board of directors through the Corporations Code<sup>34</sup> and the Davis-Stirling Act,<sup>35</sup> and, in most cases a CID's governing documents. Professional managers and other CID professionals point to poor fiscal management in both self-managed and professionally managed developments as the root cause of financial problems in CIDs.

### **BOARD OF DIRECTOR'S FINANCIAL DUTIES**

#### **Davis-Stirling Requirements**

The Davis-Stirling Act requires that a board of directors review:

- The operating budget on a quarterly basis;
- The status of reserve accounts on a quarterly basis;
- The current year's actual reserve revenues and expenses compared to the current year's budget;
- The latest account statements prepared by the financial institutions where the association has its operating and reserve accounts; and
- An income and an expense statement for the association's operating and reserve accounts on a quarterly basis.<sup>36</sup>

A CID's governing documents may impose stricter standards.

The association is also required by Davis-Stirling to annually prepare and distribute to each member:

- An operating budget that includes:
  - (1) An estimate of revenues and expenses;
  - (2) A summary of reserve funds listing:
    - Estimated replacement costs, remaining life and useful life for each major component,
    - Current estimates of cash reserves necessary to address maintenance and repair of major components, and
    - Current amount of cash reserves set aside for the above purposes.
  - (3) A professional review of the financial statement (if the association budget is over \$75,000).<sup>37</sup>

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\* There seemed to be a consensus among the professionals interviewed for this report that financial mismanagement was a serious issue in CIDs.

## Corporations Code Requirements

The California Corporations Code imposes financial responsibilities on the CID board of directors that are similar to corporate boards. One of the CID board's primary responsibilities is to maintain property values. This is done by enforcing CC&Rs and collecting assessments to maintain the development. Boards of directors:

- Owe a duty of good faith that includes following the bylaws, and keeping accurate minutes and financial records;
- Have a duty to exercise reasonable care, which includes supervising community affairs, maintaining adequate funds and acting in a fiduciary capacity for the best interests of the whole community, as well as the corporation's shareholders, or in this case, the homeowners;
- Are responsible for:
  - (1) Complying with tax laws;
  - (2) Contracting for insurance policies; and
  - (3) Investing homeowner association funds.

## FLAWS IN THE SYSTEM

We interviewed community association managers and other professionals involved with CIDs.\* They provide valuable insight into CID issues but they may be biased especially towards the need for professional management. They may also have different priorities than homeowners.

- Most common interest development professionals say that it is crucial for CIDs to have professional management. The majority of professional managers and other CID professionals interviewed were critical of boards that managed their own CIDs. When asked what the most common problem was for CIDs, managers responded that it was boards of directors who did a poor job of managing.
- One common problem is an association's failure to follow state and local laws. One manager felt that 70 percent of self-managed CID boards had never heard of the Davis-Stirling Act.<sup>38</sup>
- Most of the managers did not feel that disregard for the law was intentional, but was caused by a lack of knowledge. Managers agreed that board members do not take the time to educate themselves about their responsibilities or how CIDs function. Some said that Davis-Stirling was hard for board members to understand. The frequent changes in the law made it even more difficult for lay people to keep up with statutory requirements.
- Managers said the types of problems that resulted from self-management ran the full gamut. Some were basic governance and due process issues. One manager

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\* Fourteen phone interviews were conducted with various professionals who provide services to common interest developments between September and December of 2001. This included five community association managers, as well as insurance providers, and other support service providers.

said that she had taken over the management of a 30-year old CID that had been almost exclusively self-managed. When she was hired, she received 30 years of records in one file box. This CID, which had assets of \$100 million dollars, had no corporate records: No copy of the original declaration, no record of any changes, no record of insurance policies, and no meeting minutes.<sup>39</sup>

- Another manager recently took over three CIDs that were not filing taxes or corporate filings with the Secretary of State. They were violating the law by approving their budgets after the fiscal year had already started. They were also still following CC&Rs that discriminated against children even though such restrictions have been ruled unconstitutional.<sup>40</sup>
- One manager finds that many board members do not respect rules and procedures. The problem, he believes, is the lack of checks and balances to their power. In this unconstrained environment, “It is human nature to take the route that is most expedient” and to watch out for one’s own interests.<sup>41</sup>
- Many board members do not find it easy to take on financial leadership and impose fines and fees on their neighbors. While professional management may help, ultimately the board is responsible for all financial decisions.

There are many stories told by frustrated managers and angry homeowners that document the poor management and leadership skills of boards of directors. A less subjective source is the first Department of Real Estate (DRE) study done in 1987, which conducted case studies of individual CIDs. The authors observed board members in action. Their findings back up the comments made by managers in this study. The DRE authors write: “We observed in our case studies... that many board members were not thoroughly knowledgeable about their own associations. Several were mistaken in their understanding of the contents of their association’s governing documents.”<sup>42</sup>

## FINANCIAL ISSUES

One community manager, who reported financial mismanagement in both self-managed and professionally managed CIDs, said the problem arises when the same entity both manages and oversees financial issues. This manager recommends that the responsibility for financial issues should be separate from other management responsibilities. It is too tempting to mismanage money when there is no oversight.<sup>43</sup>

Another manager agreed, saying that boards have two functions: leadership and fiduciary responsibility. This manager suggested that these two functions should be separated.<sup>44</sup> Community managers seemed to agree that boards should not focus on administration but on policy and should leave the minutia and finances to professional management. However, managers strongly believe that boards should understand how CIDs work and should be able to oversee community managers.

The areas that cause financial problems or concerns involving boards of directors are:

- Assessments;
- Special Assessments;

- Reserve Funds and Deferred Maintenance, and
- Litigation.

## **Assessments**

Monthly homeowner assessments are used to manage a CID and maintain the common areas of a development. The developer sets the assessment rate when he or she applies to DRE for a subdivision plan. The assessment rate includes funds for both the current and future common area and component upkeep costs. However, it is in the developer's interest to sell the properties as quickly as possible at a profit. There is minimal financial incentive for the developer to set the initial assessment amount at a level that provides adequate maintenance funding and future common area expenses.

Accurately forecasting future common area maintenance costs and repairs over the life of a CID is difficult. DRE assumes that the budget will be accurate for about 18 months.<sup>45</sup> The public report issued by DRE is valid for five years. If the developer has not sold all his property by this time, the report must be updated.

While the developer sets the original rate for assessments, the board is responsible for collecting and adjusting the rate throughout the CID's life. This is one of the more contentious issues in CIDs. One community manager complained that, "Self-management is based on popularity—no one wants to raise dues so they cut dues."<sup>46</sup> A 1987 study commissioned by DRE found that, "In general, boards felt that . . . members objected to assessment increases more than anything else... The boards felt serious tension between their desire to hold costs down and their desire to provide the best possible quality of life in the development."<sup>47</sup>

Boards often bow to homeowner preferences and do not raise annual assessments. This may undermine the long-term financial stability of a CID. Over time, inadequate assessments can result in the physical deterioration of a CID, which can lead to a decline in property values. While the board needs to be responsive to homeowners, some critics are concerned that the hesitancy to adjust assessments can undermine a CID's economic stability and put homeowner investments at risk.

Davis-Stirling tried to address this issue of inadequate assessments and homeowner reticence regarding assessment increases. It allows the board, without homeowner approval, to raise assessment amounts up to 20 percent per year over the previous year's assessment or to lower the rate up to ten percent. Special assessment rates, which are discussed later, are also limited to five percent of the gross association expenses for that year. These amounts may be exceeded by the board in case of an emergency or if approved by a majority vote of a quorum of over 50 percent of the owners.<sup>48</sup>

## ***Foreclosure***

The timely collection of assessments has also become a controversial area in CIDs. Some argue that when homeowners fail to pay their assessments, it can threaten the

financial stability of CIDs.\* Currently, the initiation of a nonjudicial foreclosure proceeding is one of the few effective options associations have to collect overdue assessments. Nonjudicial foreclosure is one of two types of foreclosure proceedings. The other is judicial foreclosure. Judicial foreclosure is processed in the courts. In nonjudicial foreclosure, a private company processes the foreclosure.

Supporters of nonjudicial foreclosure argue that it can be the least expensive method to force homeowners to pay delinquent assessments.<sup>49</sup> According to a fair housing advocate and a foreclosure professional, very few of the foreclosure proceedings that are initiated result in the sale of a home.<sup>50</sup> There is no guarantee that if an association resorts to foreclosure to collect delinquent assessments, that it will recover the money owed.<sup>51†</sup> All other lenders and liens will be paid off first. The association only benefits because a paying owner replaces the owner who was not paying their assessments.

Homeowner advocates and CID professionals argue that foreclosure can be an expensive and inefficient method.<sup>52</sup> For homeowners, a relatively small amount owed can greatly increase because of collection fees and interest. Homeowner advocates also say that associations are too quick to use foreclosure. Boards may feel pressured to foreclose when assessments have not been paid because of their fiduciary duty. Potentially, the board can be sued for not collecting.

### **Special Assessments**

Special assessments—a fee that the board can charge in addition to monthly assessments—are supposed to be for unanticipated costs. Critics complain that HOAs use special assessment to pay for regular maintenance; repair or replacement costs if monthly assessments are too low instead of raising monthly assessments. The DRE 1987 survey of board presidents found that 30 percent of the responding associations voted on special assessments within the previous two years. Of these associations, 25 percent approved the special assessments, though not always on the first attempt. While most regular assessments are under \$1,000 a month per unit, with a median of \$200 per unit,<sup>‡</sup> special assessments can run many thousands of dollars per unit.<sup>53</sup> The study's authors noted that high special assessments were sometimes a source of serious personal tragedies such as forced sales or foreclosures of members' homes.<sup>54</sup> We do not know of any data source that allows us to verify whether forced sales occur or how common they are. At least one source said it is common for special assessments to force people to sell their homes.<sup>55</sup> Seniors on fixed incomes or first time homebuyers, who have purchased in a CID because of affordability, may be especially vulnerable to increased costs from special assessments.<sup>56</sup>

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\* Stephen E. Barton and Carol J. Silverman found that in the previous year 57 percent of surveyed associations reported imposing late fees because of unpaid assessments.

† Stephen E. Barton and Carol J. Silverman, *Common Interest Homeowner's Associations Management Study*, found that 25 percent of surveyed CIDs lost between \$3,000 and \$25,000 because of foreclosures over a two-year period. For five percent of respondents this was five percent of their operating budget.

‡ CAI's National Survey of Community Association Homeowner Satisfaction found that the average monthly fee of those interviewed was \$180. This implies that assessments may have decreased since 1987. Taking inflation into consideration, this decrease is even greater.

## **Reserve Funds**

A percentage of homeowners' monthly assessments are put into a reserve fund, which pays for maintaining an association's property, such as roof replacement, street and parking lot resurfacing, and infrastructure like central heat and air systems. An inadequate reserve fund can result in special assessments when CID assets need to be replaced. Over time, inadequate reserve funds can lead to the physical deterioration of a CID and a decline in property values.

Adequately funded reserve funds allow a CID to:

- Make it easier for homeowners to borrow money for a home purchase because lenders are able to resell the mortgage in secondary mortgage markets;
- Plan for the replacement of major items that deteriorate over time;
- Minimize the need for special assessments;
- Enhance resale values of homeowners' property; and
- Comply with generally accepted accounting and auditing standards for CIDs such as those released by the American Institute of Certified Public Accountants (AICPA) in 1991.<sup>57</sup>

### ***State Reserve Fund Requirements***

In California, the Davis-Stirling Act requires the board of directors to initiate a reserve study every three years to make sure the CID is collecting adequate reserve funds. The reserve study must:

- Identify the major components that the association will need to repair or replace in the next 30 years;
- Identify the remaining useful life of the components;
- Estimate the cost to repair or replace the components during their lifetime, and
- Estimate the total annual contribution necessary to repair or replace each component during and at the end of their lifetime and subtract that amount from existing reserve funds.<sup>58</sup>

Davis-Stirling's reserve fund study requirement is reported to have had an impact on the quality of CID reserve funds. An early study found that two-thirds of the CIDs surveyed had reserve studies. Over half of them had preventative maintenance programs in place.<sup>59</sup> The authors concluded that the reserve study requirement caused CID boards to understand that their fiduciary duties included providing future component replacement costs, as well as immediate maintenance needs. They credited reserve studies with giving boards an argument to convince homeowners to raise assessments.<sup>60</sup>

Currently, CID professionals say it is not enough to require a reserve study. The requirement is not enforced and the law does not define what is required in the reserve

study. There are no guidelines for those conducting the study or for board members who review the studies. There are no standards that determine when a reserve should be considered adequately funded. CIDs are required to review the status of their reserve funds but they are not required by law to have a reserve fund or to have money in their reserve funds.<sup>61</sup>

### **How Big Is the Problem?**

Homeowners are less concerned than professionals with the financial state of their associations.<sup>62</sup> In a 1991 study done for DRE, Ernst & Young found that approximately 80 percent of CID homeowners said that their CID had a reserve study and sufficient funds were being put away for future repairs. In comparison, more than 40 percent of professional managers, real estate attorneys, accountants, and other CIDs professionals felt that insufficient reserve funds were being set aside for future maintenance.<sup>63</sup> Twenty percent questioned the accuracy and completeness of current reserve studies citing the lack of guidelines for putting these studies together.<sup>64</sup>

CID professionals are concerned that many reserve studies do not include enough funds to adequately replace CID components and amenities when they deteriorate. They also question whether or not these studies use realistic estimates of components' projected life and their replacement costs. It is also common practice for HOAs and developers to use DRE's manual to project costs. Some managers say the manual only provides suggested statewide averages that are not accurate for all CIDs.<sup>65</sup> Others point out that by the time the manual is published, the figures are already outdated. When an association takes over a CID, the budget may already be one to three years out of date. This means that an association "starts out behind the eight ball."<sup>66</sup>

Many professionals, and some homeowners, say that homeowners are not aware of their CID's financial situation. Reasons for this include:

- Failure of homeowners to read disclosure documents;<sup>67</sup>
- Inaccurate reporting of financial situation; and
- Lack of disclosure by boards.<sup>68</sup>

The majority of CID homeowners in past surveys seemed to be optimistic about their future economic stability. However, litigation levels show that there are some homeowners who are concerned enough to sue their boards for financial mismanagement. Insurance providers estimate that between 14 and 20 percent of the lawsuits against boards are for financial mismanagement. Of these, the number one issue is lack of reserve funds.<sup>69</sup>

An accountant who specializes in CIDs agrees. He believes that most reserve budgets are too low and not accurate.<sup>70</sup> He says that if reserves are under funded, they become "ticking time bombs" in an economic downturn. A unit's value may decline and homeowners may stop paying their assessments. This can lead to deferred maintenance

and repair, which further devalues the units. There are cases where homeowners with little equity in their properties have walked away from their homes.<sup>71</sup>

Karen Conlon, Executive Director of the California Association of Community Managers (CACM), says that 50 percent of CIDs do not have enough money in their reserve funds. This is especially true of self-managed CIDs whose boards often do not see the benefit of reserve funds. Boards may even borrow money from the reserves for immediate needs and not pay the money back.\* Even professionally managed CIDs have under-funded reserve studies. Conlon points out that a manager can only advise a board. The board does not have to follow a manager's recommendations.<sup>72</sup>

A 1995 California survey of homeowner associations found that, on average, reserves were 59 percent funded.<sup>73</sup> At least one expert believes that CIDs are doing a better job of funding reserves with the current average being closer to 70 percent.<sup>74</sup> This percentage is based on the level of prorated replacement costs at the current point in time. There is some disagreement over the ideal funding level in the literature. Some older studies claim that 75 percent is adequate.<sup>75</sup> Other CID professionals say that reserve funds should be 100 percent funded.<sup>76</sup>

## **Litigation**

Litigation, because of its high cost, has been a financial challenge for CIDs. Boards are sued for both their failure to enforce CC&Rs and for enforcing CC&Rs, architectural issues and financial mismanagement. Boards sue homeowners for noncompliance with CC&Rs and other rules.

### ***How Common is Litigation?***

- Insurance providers estimate that 40 percent of directors are threatened with suits or actually sued during their terms as directors. One insurer said that litigation has increased about 25 percent in the last eight years.<sup>77</sup>
- A 1987 survey of 579 board presidents found that of the 30 percent of boards threatened with lawsuits within the previous year, five percent were actually sued. The same study found that 28 percent of the boards had brought a suit against a homeowner.<sup>78</sup>
- A 1991 survey of 319 CID professionals, board members and homeowners found that over a period of three years, 53 percent of those responding to the survey said their CID had been involved in some sort of litigation. Eighteen percent of these lawsuits were against board members. Of the remaining lawsuits, 28 percent were construction defect litigation suits and 24 percent involved the board suing homeowners for noncompliance.<sup>79</sup>
- Construction defects continue to be the most common reason that a CID is involved in litigation.<sup>80</sup>

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\* While Davis-Stirling does allow the board to borrow from its reserves, it is required to pay the money back according to California Civil Code §1365.5 (c) and (d).

When boards do sue, homeowners can suffer the consequences, such as decreased property values, difficulty reselling their property and assessment increases.

Litigation can also have an impact on a CID's future financial security. Davis-Stirling permits boards to borrow money from the reserve fund to cover budget shortfalls and litigation.<sup>81</sup> The fear is that this encourages litigation and threatens the fiscal stability of a CID.<sup>82</sup>

The authors of DRE's 1991 study write that many lawsuits consist of disagreements over CC&R enforcement that did not "seem particularly worthy of an expensive and time-consuming legal proceeding." Inflexible CC&Rs, homeowners' unrealistic expectations of worry-free living, and unskilled board members result in litigation being used as the first resort rather than the last.<sup>83</sup>

The study cited real estate professionals as saying that litigation is the number one threat to the future viability and market competitiveness of CIDs.<sup>84</sup> Lawsuits have a negative impact on homebuyers and put a financial strain on CIDs, potentially causing assessment increases, special assessments or borrowing from the reserve funds to cover legal fees. Board members in CIDs with construction defects and those in the process of suing developers were more likely to be harassed by homeowners.<sup>85</sup> Some experts claim that construction defect litigation may be a way for board members to transfer homeowner anger from themselves to the developer.<sup>86\*</sup>

Lawsuits may not even be effective. The courts usually do not mandate that homeowners and board members cooperate. They only designate winners and losers. Lawsuits may serve to only increase the tension between members<sup>87</sup> and put a strain on a CID's resources.<sup>88</sup> This further undermines the ability of the CID to function well.

### ***Reducing Litigation in CIDs***

The California Law Revision Commission (CLRC) is currently reviewing CID law. As part of their review, they are examining the use of Alternative Dispute Resolution (ADR) as a way to reduce the high rates of litigation in CIDs. A reduction in conflict or a shift from litigation to ADR could reduce costs to CIDs and homeowners.<sup>89†</sup> Davis-Stirling currently requires those involved in conflicts over CID CC&Rs to consider alternative dispute resolution before they pursue litigation.<sup>90</sup> Current ADR provisions do not address conflicts over management or failure to comply with state law.<sup>91</sup>

The CLRC emphasizes that one of the best ways to deal with conflict in CIDs may be to prevent the conflict from happening.<sup>92</sup> The CLRC is focusing on due process requirements to prevent disputes. Some researchers have found that harassment of the board is more likely when a homeowner believes that his or her rights have been violated.

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\* Quoting David Combs, *Homeowner Associations In Action: A Case Study* (Berkeley: Federation of Homeowners Associations, 1973).

† Litigation can cost between \$5,000 to \$25,000 while mediation can cost as little as \$1,000 to \$5,000.

Studies have shown that when residents are involved in rule making, they are less likely to break the rules.<sup>93</sup> It is possible that increased due process would reduce animosity and CC&R violations in a CID and thereby reduce litigation.

## **PROFESSIONAL MANAGEMENT: IS IT THE SOLUTION?**

CID boards of directors are allowed by law to rely on information from experts and to hire professionals to manage day-to-day CID administration.<sup>94</sup> Comprehensive management can run anywhere from \$11 to \$25 per unit per month with minimums of \$1,500 to 3,000 a month.<sup>95</sup>

Between 70 to 88 percent of CIDs are professionally managed,\* with most managers living off-site.<sup>96†</sup>

Currently, there are 2,000 Certified Community Association Managers (CCAM) registered with the California Association of Community Managers (CACM).<sup>97</sup> A manager must take classes from CACM and meet experience requirements to earn this classification. One person said that CACMs efforts have improved the quality of management.<sup>98</sup>

There may be benefits to hiring professional management, including:

- CID issue expertise;
- Board education;<sup>99</sup>
- Knowledge of CIDs law;
- Financial and physical management expertise;
- Communication skills that may help resolve personality conflicts;
- Ability of CID to qualify for a loan; and
- Less expensive insurance rates for directors and officers liability insurance, which protects the board from errors in judgment, including financial mismanagement.

Hiring professional management does not stop CID financial mismanagement or noncompliance with the law. A mid-1980s survey found that one in 25 CIDs reported significant financial losses in the previous three years because of embezzlement.<sup>100</sup> Davis-Stirling attempts to address some of these issues by prohibiting management companies from commingling funds from different associations.<sup>101</sup> This addressed one of the more common financial abuses, but has not entirely solved the problem.

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\* Figures differ depending on source. It is hard to know exactly how many are professionally managed since there is no comprehensive source for this information. Estimates come from Conlon, October 2001, and Levy & Company, *2001 California Community Association Statistics*.

† The article reported that between 1989 and 1997, the percentage of on-site managers declined from 37 percent to 17 percent.

There are some CIDs experts who believe that the quality of management is improving with time.<sup>102</sup> But an example that shows the difficulty of the issue is the case of a community manager who over the course of 15 years stole an estimated \$800,000 to \$1.5 million from over 50 associations. When an association caught him, he would agree to return the funds if the association signed an agreement that it would not discuss the matter. An association finally sued the manager. The penalty for his conduct is a short jail sentence after which he can return to the community management profession.<sup>103</sup>

Community management professionals believe that because anyone can call himself or herself a manager there is no quality control in the profession. Many managers believe that associations care more about the cost of their management than a manager's qualifications, and will hire a less experienced manager if they charge less. Most managers feel this compromises the quality of their service and the profession as a whole. CACM has been working to have legislation passed that would require the state to license community managers.\* They believe that this could help stop some of the abuses.

While most of the managers advocated that all CIDs be professionally managed, they did qualify this statement. It is not profitable for managers to service smaller CIDs.<sup>104</sup> One alternative is for small associations to hire someone to do only their financial management.<sup>105</sup>

## **WHAT ARE THE IMPACTS OF FINANCIAL PROBLEMS?**

Given the level of concern and the dire predictions regarding the financial state of CIDs, there were only a few horror stories that could be tracked down in California. The Assembly hearing in 1990 mentions two cases of HOA financial failure. Both were caused by internal disputes over assessments.

There is a great deal of talk about CIDs that have deteriorated or are on shaky financial ground. Finding evidence to confirm this situation is more difficult. There are no standards by which to rate financial health in CIDs, nor do we track CIDs that are currently having or have had financial difficulties. Because of this we do not know how many projects might be experiencing financial difficulties. Nor do we know how many individuals may have had to move, borrow money or face other hardships because of poor fiscal management.

## **RENTALS AS INDICATOR SPECIES FOR CID DECLINE**

One of the danger signs that might give a clue to the financial health of a CID is the percentage of units that are rentals. Both the 1987 and 1991 DRE studies found that "there are serious consequences for CIDs" that had between 25-30 percent rental units.<sup>106</sup> Twenty-six percent of those responding to this survey fell into this category.

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\* This year it was Assembly Bill 555.

Large numbers of rentals can have a negative affect on CIDs for many reasons. Renters tend to care less about the development because they are not invested in the property. Absentee owners are more likely to object to increases in assessments that will improve the quality of life in the development.<sup>107</sup> Lenders may have difficulty securing mortgage insurance in developments that have a large numbers of rental units. As a result, some CIDs forbid owners to rent their units.

## **FRANKLIN VILLA-WHEN CIDS GO BAD**

Franklin Villa in Sacramento, California is an example of how a CID can deteriorate when it has poor management, self-serving boards, and absentee homeowners. Franklin Villa was constructed in the 1960s and 70s as a retirement community of 704 two-bedroom, one-bath four-plexes and 253 town homes. By the 1980s, most of the original owners had moved out and were renting their units. Families started moving in because of the affordable rents. Unfortunately, Franklin Villa was designed for retirees with small units and has very few family amenities, such as playgrounds.

By the late 1980s less than ten percent of the units were owner occupied and crime and drugs were becoming major problems. As Franklin Villa declined, it pulled the surrounding neighborhoods down with it.<sup>108</sup> In 1998, the Franklin Villa neighborhood had the highest reported number of violent crimes in the city, the highest number of residential burglaries, the most reports of child and spouse abuses, and the second highest number of assaults.<sup>109</sup> As a result, the Sacramento Housing and Redevelopment Agency (SHRA) became involved in trying to improve the neighborhood. SHRA spent ten years trying to work with Franklin Villa's five HOAs to address the crime issues and improve the neighborhood. They finally determined that the only solution was to purchase the property and dissolve the homeowner associations.

A 1994 Sacramento City staff report to the City Council<sup>110</sup> concluded that Franklin Villa homeowner associations suffered from:

- Financial mismanagement by managers and board members;
- Failure to comply with governing documents and statutes governing meeting and election procedures, and financial disclosures to owners;
- Absence of reserve accounts and failure to collect assessments; and
- Board members who were not paying their assessments.

Staff also reported that the inability of the five homeowner associations to work together made it impossible to address the serious safety issues in the development. For example, the city mandated that the associations pool their money and pay for a security gate. Some of the associations sued and the court ruled against the city.<sup>111</sup>

SHRA is now in the process of purchasing Franklin Villa and providing five full-time security officers. The project is estimated to cost the redevelopment agency between

\$50-60 million and will take several years. SHRA's immediate plans are to rent out the units that they purchase.

## **FRANKLIN VILLA IS NOT THE ONLY ONE**

SHRA is currently working to salvage at least three other CIDs in Sacramento. These developments need less intervention. SHRA money will go towards repairing deferred maintenance and hiring lawyers to rewrite CID bylaws so they are enforceable. These CIDs are adding the authority to do third-party evictions to their bylaws. This allows the homeowner association to evict tenants without the permission of absent unit owners.

Like Franklin Villa, the downfall of these developments resulted from absentee owners. The owners would not assess themselves to maintain the development and would not participate in governing their CID. There are some CIDs that have no one managing them. There are no board members because no one participates<sup>112</sup> and there is no money to hire someone to manage the CID. Even if professional management was hired, there is no one to monitor that person. This would leave these developments vulnerable to financial mismanagement, aggravating the existing problems.

The great majority of CIDs are not blighted. The problem, according to one attorney who sues blighted properties on behalf of cities, is caused by a small amount of developments from the 1960s and 70s. These developments have deteriorated due to inadequate assessments, failure to collect assessments, director mismanagement, and absentee owners. Even though the total number of blighted CIDs is small, because some of them are so large—sometimes up to a thousand units—one bad CID creates an “instant ghetto.”<sup>113</sup> One bad CID can have a tremendous impact on a community.



## **CIDS IN OTHER STATES**

### **UNIFORM COMMON INTEREST OWNERSHIP ACT**

By the 1960s all 50 states had adopted condominium laws. In 1982, the National Conference of Commissioners on Uniform State Laws (NCCUSL) developed the Uniform Common Interest Ownership Act (UCIOA). The UCIOA combined related uniform acts (the Uniform Condominium Act, Uniform Planned Community Act and the Model Real Estate Cooperative Act) in an attempt to provide a comprehensive statute regulating condominiums, cooperatives and other common interest developments. Six states have adopted the UCIOA, including Nevada. Twelve states have adopted some form of the Uniform Condominium Act.<sup>114</sup>

### **RESERVE STUDIES AND FUNDS**

Half of the states (26) do not have laws that specifically address or require reserve funds. Five states require that reserve fund amounts be disclosed in public offering statements related to common interest development or condominium investments. Ten states require that association boards maintain some form of reserve fund or separate account for major repairs and maintenance of common area items. Six states require that owners disclose the status of reserve funds or accounts to prospective buyers.<sup>115</sup> Table 1 sums up these requirements.

<b>Table 1 Reserve Fund Laws</b>	
No Laws Requiring Reserves.	Alabama, Arizona, Arkansas, Colorado, Delaware, Georgia, Idaho, Iowa, Kansas, Louisiana, Maine, Mississippi, Montana, Nebraska, New Jersey, * New Mexico, New York, ** North Carolina, North Dakota, Oklahoma, South Carolina, South Dakota, Tennessee, Utah, Wisconsin, ++ Wyoming
Must disclose status of reserve fund amounts and/or calculations in public offering statements.	Alaska, New Hampshire, Rhode Island, Virginia, West Virginia
Board/association must maintain a reserve fund or separate account for major repairs, maintenance of common area items.	Connecticut, Florida, *** Indiana, Kentucky, Maryland, Massachusetts, Michigan, Minnesota, Oregon, + Washington
Association/Board must conduct full reserve study.	Hawaii, Nevada
Board must provide owners with copy of proposed annual budget that includes reserve funding.	California, Illinois
Owner Must Disclose to Purchaser Reserve Amount Requirements.	California, Pennsylvania, Missouri, Ohio, Vermont, Washington
Board may budget for reserves.	Texas
*Public offering statement must provide for capital items. **Must disclose current cost to replace/repair and estimated life of common improvements; cooperative directors must set aside reasonable sums periodically for reserves. ***May waive maintaining reserve fund by owner majority vote. †May eliminate future reserves if 75 percent of owners approve. ++No reserve fund required per se; future expenses obtained through assessments against unit owners.	
Source: Mitchell H. Frumkin and others, <i>A Complete Guide to Reserve Funding &amp; Reserve Investment Strategies</i> , 5 <sup>th</sup> ed., 2001, Alexandria: Community Associations Press, Appendix B, pp. 36-37.	

Hawaii and Nevada have some of the most comprehensive laws regarding reserve studies and budgeting requirements. Both states require CIDs to conduct reserve studies.

## **Hawaii**

Hawaii requires certain information about reserves and their calculation to be included in the annual operating budget of an association. This includes:

- Estimated revenues and operating expenses;
- Description of how the budget was prepared (cash or accrual basis);
- Total replacement reserves as of the date of the budget;
- Estimated replacement reserves required to maintain property based on a reserve study; and,
- Explanation of how estimated replacement reserves were calculated.<sup>116</sup>

The Hawaii Department of Commerce and Consumer Affairs requires that associations notify owners in writing annually of:

- The purpose of reserves;
- General reserve requirements under Hawaii law;
- Why the association has established certain replacement reserves;
- Whether reserve studies have been prepared for projects; and
- The amount of reserves collected as part of the owners' maintenance fees.<sup>117</sup>

The rules also set forth in detail the criteria to use in order to prepare a reserve study.<sup>118</sup>

## **Nevada**

Nevada mandates that boards conduct reserve studies every five years. The state also has requirements for what the studies must include, and minimum qualifications that must be met by those conducting the studies.<sup>119</sup>

## **California**

California requires reserve study updates to developers' original long-term component replacement estimates but does not require an independent evaluation of the initial study or subsequent updates. California is not specific about how reserves should be calculated, what percentage should be funded, or who should do the reserve updates.

## **CID MANAGERS**

Some states have addressed association management issues by enacting regulating legislation. The laws of Connecticut and Florida are described to show the range of CIDs laws adopted by other states. California has no education or licensing requirements for CID managers.

### **Connecticut**

Connecticut requires managers to register with the Department of Consumer Protection. The registration application provides the applicant's name, home address, business address, and telephone number. There is an application fee of \$60 and registration fee of \$100. Professional or specialized educational qualifications are not required. A manager must obtain a fidelity bond for each community association that he or she manages.<sup>120</sup> The bond protects the HOA from losses caused by any dishonest business practices of the manager.

### **Florida**

Florida's laws are more comprehensive than other states in the regulation of association management and individual community association managers. The state regulates these

services when “substantial specialized knowledge, judgment, and managerial skill” is provided for: (1) remuneration; and (2) associations with at least 50 units or with annual budgets exceeding \$100,000.<sup>121</sup>

The Florida Regulatory Council of Community Association Managers, created by statute, governs managers and enforces related administrative rules. The Regulatory Council consists of seven members appointed by the Governor and confirmed by the Senate. Five members must be licensed managers. Two members must not be connected with the business of community association management. The Council is charged with:

- Adopting rules related to licensure examination and continuing education requirements, and
- Setting providers, fees, and professional practice standards.

Prospective manager licensees apply to the Division of Professions at the Department of Business and Professional Regulation. The application must include any criminal history, which the Division then compares to state criminal records. The applicant must be found to have “good moral character” which means “a personal history of honesty, fairness, and respect for the rights of others and for the laws of [Florida] and the nation.”<sup>122</sup>

All association manager applicants must complete a minimum of 18 classroom hours within 12 months prior to the exam date. Courses must include:

- State/federal laws governing community association operations and state laws governing corporations;
- Procedures for noticing and conducting community association meetings;
- Preparing budgets and finances;
- Insurance issues; and
- Management and maintenance.

Once licensed, a manager must fulfill continuing education requirements. The Council must approve education providers.<sup>123</sup>

## **NEVADA CID PROGRAM**

Like California, CIDs have been an ongoing challenge in Nevada. The Nevada Legislature has passed similar laws to California, including those that require mandatory Alternative Dispute Resolution (ADR) and increase due process requirements. Nevada mandates that prospective community association managers fulfill certification, application and education requirements similar to those in Florida. However, an applicant must also provide information about child support compliance and complete 24 hours of instruction. What is unique about Nevada’s program is its use of an ombudsman to resolve complaints and problems involving CIDs.

## **Ombudsman**

The Nevada Ombudsman's Office was created in 1997 to help CID residents and board members better understand their governing documents and their rights and responsibilities under state law. The law was expanded in 1999 to require the Ombudsman's Office to create an informational database about Nevada CIDs. The law authorizes the ombudsman to obtain records from CIDs and to subpoena witnesses. The office is in the Real Estate Division and is funded by a \$3 annual fee per unit in all associations.<sup>124</sup>

On average, the Ombudsman's Office receives between 1,500-1,600 calls a month. These calls involve between 1,000 to 1,200 individuals. Elden Hardy, the current Ombudsman, believes that one-third of callers' concerns are taken care of immediately because homeowners just want someone to listen and/or explain to them how CIDs work.<sup>125</sup> For example, a caller may be upset about something in the CC&Rs. Explaining to the caller that he or she must follow the CC&Rs is enough to resolve the issue. The office also provides alternative dispute resolution services.

As more people become aware of the ombudsman's office, calls about CIDs to other agencies and departments have decreased from about 100 a month per office to almost none. The Ombudsman's goal is to create an office that homeowners feel is responsive to them and cares about their issues.

## **CID Education**

Nevada Ombudsman Hardy believes that the main reason people call is because homeowners are dissatisfied with their boards' actions in the areas of administering and maintaining CIDs. He estimates that of the calls received, 70 percent involve boards that are not functioning correctly. He gives two reasons for this: personality conflicts and directors' ignorance about how boards function and their legal responsibilities.

In order to address the lack of knowledge, Mr. Hardy has started a popular series of classes for board members and homeowners on CID topics including running and documenting meetings, reserve studies, assessing fines, insurance coverage, and rights and ethical responsibilities. Volunteer CID experts teach these classes. He hopes that these classes will not only educate boards but will help homeowners monitor their boards. The office is working to put information from the classes online so that it will be easily accessible.

## **CID Registration**

CIDs are required to register with the Ombudsman's Office. Before the creation of the Ombudsman's Office, CIDs registered with the Secretary of State's Office as they do in California.

The registration form requires the following information:

- 1) The name, address and telephone number of the association;
- 2) The name of the person engaged in property management for the common-interest community or the name of the person who manages the property at the site of the common-interest community;
- 3) The names, mailing addresses and telephone numbers of the members of the executive board of the association;
- 4) The name of the CID developer;
- 5) The number of units in the common-interest community; and
- 6) The total annual assessment made by the association.<sup>126</sup>

### **Model Reserve Study**

The office anticipates completing a model reserve study created by the University of Nevada in Las Vegas within the next six months. The idea is that any CID will be able to use this reserve study to create a competent study without hiring a professional, potentially saving an association thousands of dollars.

### **Technical Assistance**

The office hopes to have staff members to provide onsite technical assistance to CIDs and serve as impartial observers. Observers would attend meetings and monitor contentious situations. The Ombudsman believes that a neutral third party would help solve a majority of the problems that homeowners report.

### **MONTGOMERY COUNTY, MARYLAND CID PROGRAM**

An estimated one-third of the population in Montgomery County lives in CIDs.<sup>127</sup> The county has developed a program that is similar to Nevada's. While it does not have an ombudsman, the county provides similar services through its Commission on Common Ownership Communities and Office of Common Ownership Communities, both housed in the county's Department of Housing and Community Affairs. Formed in 1991, the Commission is charged with advising the County Council and County Executive on CID issues, promoting public awareness of rights and obligations of living in CIDs, eliminating disputes, and maintaining property values and quality of life in community associations.

All CIDs are required to register annually with the Commission and pay a \$1.50 per unit registration fee. This fee is used to support the Commission's dispute resolution services. Failure to register may result in a \$500 civil fine.

After the parties to a dispute have exhausted all procedures provided in their governing documents, they may file their dispute with the Commission for a fee of \$50. The Commission is made up of 15 members: six residents from self-managed and

professionally managed CIDs, six professional members associated with CIDs such as managers, attorneys or investor-owners, and three real estate sales and development members. There are also six non-voting members from the county council and county departments such as housing and community affairs, public works, and transportation.

The Commission may provide arbitration services or hold a hearing if arbitration is rejected or fails to work. Such a hearing is conducted in the same manner as other county administrative hearings. The panel may resolve the dispute, award damages and/or award costs and attorneys' fees. The hearing panel's decision is binding. However, a party can appeal the decision to the courts if it does not comply with the law, is not supported by the evidence, or is arbitrary and capricious.

## **CALIFORNIA AND A CID OMBUDSPERSON?**

The state of California has ombudspersons in eight areas including mobile homes and long-term care. The California Law Review Commission (CLRC) found general support among stakeholders for a CID ombudsperson.<sup>128</sup> Those who thought that lack of professionalism of managers was the issue did not think that an ombudsperson would solve the problem.

CLRC concluded that there are no reliable statistics on conflict in CIDs. "The best statistics come from the few jurisdictions where there is a governmental entity... elsewhere it is merely anecdotal." They go on to write that in Montgomery County they reported 500 inquires a year for about 100,000 housing units (one complaint per 200 units).

Using the call rates from Montgomery County and Nevada, we can estimate the number of calls that a California ombudsperson might receive. At the more conservative rate of Montgomery County, California is looking at 17,000 inquiries a year, or about 1,400 per month. Estimating California's call level based on Nevada's average of about 1,000 new calls a month, California would experience about 306,000 calls a year or 25,500 calls a month. The huge disparity might be a result of Nevada's program being new, while Montgomery County's is over ten years old. Nevada's call level has already dropped in the last year. Both programs seek to educate CID homeowners, which would hopefully lead to fewer calls over time.

### **California Mobile Home Ombudsman**

California's Mobile Home Ombudsman Program, which started in 1987,<sup>129</sup> is perhaps the state program that is the most similar to a potential CID ombudsman. The Mobile Home Ombudsman Program is housed in the California Department of Housing and Community Development's Division of Codes and Standards.

The Ombudsman's Office has three full-time staff members that handle the bulk of the work. The office has jurisdiction over two types of issues: (1) those involving the selling

of manufactured homes such as fraud, contract violations and product defects and; (2) health and safety issues in manufactured home developments or parks.

The office can force compliance on health and safety issues and purchasing issues and have courts jail violators if necessary. When the office receives a complaint from a homeowner about a development or park issue that is out of their jurisdiction, the office can only respond by sending a letter to the manager or owner of the park. About a quarter of the parks respond to these letters. If the park does not remedy the situation, the homeowner's only option is to sue. This is not common, as homeowners often cannot afford the cost of litigation.<sup>130</sup>

There are approximately 4,795 manufactured home developments or parks in California with approximately 371,000 manufactured homes.<sup>131</sup> The Ombudsman's Office receives 1,000 to 2,600 calls a month.<sup>132</sup> Fifty percent of these calls have nothing to do with manufactured homes and include people looking for information on how to spay their dogs and people who want to complain about their dentist.

Of the 50 percent of calls that are about manufactured homes, 80 percent are about health and safety issues and 20 percent are about the purchase of manufactured homes. Most of the callers just have questions they want answered. Only 40-80 callers a month fill out a formal complaint form.<sup>133</sup>

## **CIDS AND LOCAL GOVERNMENTS**

CIDs privatize some services that many people consider public services, such as, construction, and maintenance of roads, water and waste infrastructure, and landscaping. Often the developer is not held to the same infrastructure standards when he or she is building a CID because the infrastructure is private. This can be because of a less rigid review process or less stringent requirements. Unfortunately, this can result in future maintenance problems for the association. Private streets seem to be especially prone to problems caused by poor construction standards.<sup>134</sup>

Poorly constructed or inadequate infrastructure and buildings can have serious financial impacts on CIDs. A brief survey of local laws related to CIDs found that while most jurisdictions do not have CIDs development standards, they are not uncommon. The most common reason that cities passed specific CID laws seems to be their desire to prevent poor quality projects that could have negative impacts on surrounding neighborhoods and the community. They also enact laws to ensure adequate maintenance and prevent the properties from becoming blighted.

Some CIDs professionals believe that local governments could address these quality issues by doing a better job of inspecting CIDs during construction. Several cities have already responded to construction quality issues by passing laws that have specific development requirements for CIDs, especially condominiums.

### **SAN JOSE**

The City of San Jose passed their 1988 Common Interest Development Ordinance in response to homeowner complaints that CID infrastructure was substandard.<sup>135</sup> The ordinance requires the Departments of Planning and Public Works to review and approve private infrastructure in CIDs, including all paved areas and storm and sanitary sewer systems. Both departments are involved from the initial permitting stage. While San Jose has separate guidelines for CID streets, some cities do not allow private streets or require private streets to follow the same guidelines as public streets.

### **SACRAMENTO**

The City of Sacramento in their municipal code notes that because condominiums are unique forms of housing, they “may lead to conditions of mismanagement, neglect, and blight that impact upon public health, safety, welfare and economic prosperity of the city.”<sup>136</sup>

To prevent this, the city has development standards relating to off-street parking, sewer and water hookups, gas and electricity service, noise insulation, and fire safety.

## **COSTA MESA**

The City of Costa Mesa allows only one homeowner association per development.<sup>137</sup> Working with multiple homeowner associations in a single project has proven problematic for cities in the past.\*

## **FREMONT**

Fremont's code states that its CID laws exist because a CID "presents special land use problems involving potential slum and blight conditions which would be detrimental to the public health, safety, welfare and economic prosperity of the community."<sup>138</sup>

Fremont requires that:

- CIDs with 20 or more units must hire a professional management firm that is accredited as a property management company, or an accredited individual;
- All electrical and mechanical equipment must conform to existing city codes and the development must meet the state's and city's sound transmission standards; and
- There is a one-year warranty on all appliances in each unit, and all electrical, heating, air conditioning, plumbing, ventilation equipment, and elevators.

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\* Sacramento's experience with Franklin Villa is an example of this.

## **COMMON INTEREST DEVELOPMENTS—STRUCTURE AS DESTINY?**

At least one CIDs expert argues that there is too much focus on the board of directors and financial issues as the problems. These issues, the expert argues, do not present as big a problem as most people think. Instead, the root of CID problems is in their structure. This basic flaw plays itself out in a variety of ways that lead to a myriad of finger pointing and the assigning of blame rather than problem solving.<sup>139</sup> These high levels of contention do have financial impacts. They can lead to expensive litigation and a breakdown in the cooperation among homeowners that is needed to sustain a CID.

Legally, a CID is a corporation with its own rules distinct from those of the municipality in which it is located. The individuals living in the CID are essentially shareholders. They have also entered into a private contract to live by the restrictions and rules that the developer has attached to the land on which their homes are built.

In 1985, the Davis-Stirling Act shifted “community association laws away from the corporate model towards a hybrid that draws upon legal concepts developed for public law entities.”<sup>140</sup> By referencing government models in creating Davis-Stirling, the legislature restricted the power that was given to association boards under the Corporations Code and increased the involvement, and potentially, the power of homeowners.<sup>141</sup> Davis-Stirling accomplished this by increasing the due process requirements of CID governance. Appendix B shows the due process requirements of both Davis-Stirling and the Corporations Code.

## **ARE CIDS BUSINESSES, GOVERNMENT OR COMMUNITY?**

Common interest developments are poorly understood not only by residents and prospective buyers but even by many of the people who deal with them professionally. This is not surprising since associations mix elements of government, business and neighborhood organizations yet do not fit the model of any one of them.<sup>142</sup>

Statutory law that combines aspects of business and government is enough to make CID structure seem complex, but there is an additional element. CIDs are made up of people’s homes. The United States has a strong emphasis not only on individual rights, but also on private property rights. The corporate model requires the board of directors to act for the good of the entire community with little input from members. When this model is imposed onto the belief systems that go with private property rights, it can lead to a collision of values and expectations in the most sacred of spaces—the American home.

Developers design a CID’s governing documents to maintain property values. In theory, most homeowners would agree that this is desirable thing. Board members are charged with enforcing the developers’ rules in their roles as managers of the development. At the same time, board members live in a community and their neighbors, who have elected

them, expect them to be good neighbors. Good neighbors help each other out when one of them is having a problem. We do not expect our neighbor to put a lien on our house because we are behind a month on our assessment payment or to fine us when our kids leave their bikes in the driveway. But boards may feel that the well being of their CID demands both these actions.

## **COURTS AND CIDS: CORPORATIONS OR LOCAL GOVERNMENTS?**

In their rulings, the courts have shown some ambiguity as to whether the law should treat CIDs as businesses or governments. Their case decisions have further muddied the definition of CIDs.<sup>143</sup> In many of their decisions, the courts seem to be saying that CIDs must be both corporations and local governments. Homeowners are both stakeholders and citizens.

The courts have asked that associations use fair and reasonable procedures in decision-making and that they follow their own rules and processes.<sup>144</sup> The only requirement is that they must be reasonable and uniformly and predictably enforced.\* The courts have also found that CC&Rs are presumed to be reasonable unless the plaintiff can prove them unreasonable and that CC&Rs are a social covenant to which all residents are committed.

There are some legal scholars who believe that the courts should play a more active role in buffering homeowners from some of the problems found in CIDs. One scholar says that the court could counteract the stifling of participation that results from CIDs' corporate structure by reviewing board procedures for resident involvement.<sup>145</sup> Another argues that the courts and society have established expectations about what it means to be a homeowner. Because of this the courts should protect homebuyers from some of the aspects of CIDs that conflict with these expectations.<sup>146</sup>

## **CIDS AS LOCAL GOVERNMENT**

CIDs take over some of the services and responsibilities that are normally provided by local government. They can contract for fire, security services and road maintenance, and provide recreational facilities, school districts, waste disposal services, and architectural review, to name a few. These powers, along with some of the CID due process requirements, can lead homeowners to think of CIDs as quasi-local or private local governments. When this happens, homeowners can develop expectations about the role of the board that are not accurate.<sup>147</sup>

One of the main differences between the structure of local governments and CIDs is that in a local government, the city mediates as a third party in neighborhood or community disputes.

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\* *Nahrstedt v. Lakeside Village Condominium Association* 8 Cal. 4<sup>th</sup> 361 (1994). Unreasonable is defined as (1) arbitrary, (2) imposing a burden on the individual homeowner that substantially outweighs the benefit to the association as a whole, or (3) violating a fundamental public policy.

In a CID it is just neighbors against neighbors. There may be no disinterested third party and no established rule making or enforcement procedures. This can affect not only due process but also lead to the perception of impropriety. “The board of directors is seen not as trustees of the public interest, but as neighbors with unfair powers over others, and the mixture of political and personal conflict can poison neighbor relations.”<sup>148</sup>

The California Law Revision Commission (CLRC) is currently examining the idea of expanding due process requirements for rule making to help to avoid disputes and misunderstandings and keep them from escalating into litigation.<sup>149</sup> While there are due process requirements for amending and enforcing CC&Rs, there are no such requirements for rules. Rules are created by boards of directors and usually do not require homeowner approval. Studies have found that when associations allow members to be involved in the creation of rules they are less likely to violate them.<sup>150</sup> Rule making due process would face the same challenge as other CID due process requirements: compliance and enforcement.

### **CIDS: BETTER THAN LOCAL GOVERNMENT?**

The CLRC argues that in some ways, there is more direct democratic participation in CID legislative decision-making than in local government. Amendments of governing documents and assessment increases require CID members to vote on the changes. Municipal residents do not have the same input into local decisions.<sup>151</sup>

It is also argued that boards of directors are held to higher standards than local elected officials.<sup>152</sup> They have broad powers but they must exercise them under a strict fiduciary duty to act in the best economic interest of the association as a whole. CID experts caution board members against comparing their responsibilities to those of local elected officials because directors have greater liability.

Critics would point out that while this high standard may apply to corporate officers, California law limits individual liability for CIDs board members. In 1988, the law provided tort immunity for board members. This was increased in 1992 by treating board members like municipal officers. If an association has adequate insurance, directors have immunity for acts performed in the course of their duties if they are done in good faith and without gross negligence<sup>153</sup>

One critic argues that California CIDs exist in limbo between local governments and businesses answering to the responsibilities and checks of neither. He writes that national and state constitutions limit the actions of government especially when it comes to individual civil liberties but:

CIDs currently engage in many activities that would be prohibited if they were viewed by the courts as the equivalent of local governments.... On the other hand businesses are subject to civil liability and are often required to pay damages to those they injure, negligently or intentionally... Either avenue—recognizing constitutional limitations as

governments or civil liability as businesses—would provide a check on the actions of CID boards.<sup>154</sup>

CIDs have strict guidelines that spell out board of directors' financial duties. CC&Rs are explicit about the rules that homeowners must follow. CIDs do not have any provisions for how to be a good neighbor or how to build a sense of community. Living in a community is also about compromise and cooperation as well as rule enforcement and property values.

Some CID professionals think that CID structure needs to change. Governing boards and managers need to be more flexible, responsive, and inclusive when it comes to creating and enforcing rules and CC&Rs.<sup>155</sup>

## WHO MAKES THE RULES FOR CIDS?

### STATE REGULATION

Because CID laws are found in different areas of the California legal code, there are several state entities that are involved with regulating them.

#### The Department of Real Estate

Under the Subdivided Lands Act, Department of Real Estate (DRE) is responsible for regulating the sale of subdivisions, including CIDs, in order to protect the consumer from misrepresentation, deceit, and fraud.<sup>156</sup> DRE reviews materials provided by the developers and then releases a Final Public Report. The developer must have this report before he or she can sell any part of the subdivision. All prospective homebuyers must be given a copy of this report.

As part of the CID public report application process, the developer must submit an association budget—which includes funding for future maintenance—and a copy of the CC&Rs. DRE is responsible for reviewing these documents and for enforcing them until the developer owns less than 25 percent of the development.

As early as 1966, a report on CIDs stated “homeowners’ interests may be just the opposite of the developer’s.”<sup>157</sup> CID governing documents and budgets often reflect developers’ issues. They do not necessarily consider issues that will affect the community or issues that will appear after the CID transitions from the developer to the association. Indeed, the majority of criticisms aimed at developers, after complaints of construction defects, are directed at those who turn over projects with inadequate assessments and incomplete component studies that result in inadequate reserve funds.

If this is the case, CIDs would start out on shaky economic footing. This could create immediate controversy among members as they debate assessment increases. A large number of respondents from one survey reported that inadequate initial budgets forced their associations to pass special assessments to make up for reserve fund shortfalls. Without the additional funds, the homeowners believed that the future viability of their CIDs were threatened.<sup>158</sup>

The DRE review of the public report is supposed to balance the interests of future owners with the developer’s interests. CID studies have found that DRE could improve the financial information provided to homebuyers in their subdivision public report.<sup>159</sup> One expert said that DRE only reviews CID budgets for minimum compliance with their manual.<sup>160</sup> As previously discussed, some experts believe this manual to be inaccurate.

Some CID professionals say that the problem of developers low-balling assessments was more common in the 1970s. DRE now requires developers to disclose if they are subsidizing assessments while the development is under construction. If so, the developer must submit two budgets. One shows the current assessment levels. The

second lets homeowners know what the assessment levels will be when the developer turns the development over to the homeowner association (HOA).<sup>161</sup>

The professionals interviewed for this report pointed to DRE's review of CID governing documents as an area that should be improved. The required governing documents, like the initial budget, are often designed to further the developer's interests and to make the project as marketable as possible. This may cause the CC&Rs to be more restrictive and to limit or forbid anything that might reduce the market appeal of the project.<sup>162</sup>

DRE, by their own testimony, is very careful to make sure that documents are legally accurate.<sup>163</sup> Because of this, lawyers representing developers will often use forms that are previously approved by DRE to expedite the approval process. Or, developers will submit old governing documents for new projects because they have already passed DRE review. One manager estimated that nine out of ten developers use old CC&Rs, which do not always reflect the needs of the current development.<sup>164</sup> One CID legal expert states that the papers submitted by developers, even when they are previously approved, very carefully document all Davis-Stirling requirements including any updates in the law.<sup>165</sup>

### ***Educational Materials***

DRE does produce some materials on living in CIDs and their financial management. Their short brochure called *Living in a California Common Interest Development* provides a brief overview of what a CID is and what homebuyers can expect.<sup>166</sup> (See Appendix C) There were several recommendations in earlier studies that this brochure be mailed or provided to homebuyers and homeowners. The brochure is now available on DRE's web site.

DRE also produces a *Reserve Study Guidelines for Homeowner Association Budgets*, a manual that associations are supposed to be able to use to project costs and assess reserve funds without doing an independent inspection.

### **Secretary of State-Franchise Tax Board**

The Secretary of State oversees corporations. Most CIDs are nonprofit mutual benefit corporations and must file with the Secretary of State. Initial incorporation costs \$30. This information must be updated biannually for a fee of \$20.

The corporation code requires the registering corporation to include the names and addresses of its executive officer, secretary and chief financial officer. In addition, Davis-Stirling requires that a professional manager be listed, if one exists. Often the board officers will use the address of the manager when they submit their information.<sup>167</sup> If the manager leaves, it may be even more difficult for the board to receive information including notices about updating their filing.

Association failure to update their filing can result in a fine, and ultimately in a suspension of a CID's corporate legal benefits. This places the board members at risk of being held individually liable for actions they undertake in their role as board members. The Franchise Tax Board (FTB) can also suspend a CID's corporate status for failure to register or update their tax exemption. Unconfirmed estimates put the number of suspended CIDs at about 25 percent.<sup>168</sup>

### ***Tracking CIDs***

Associations must inform the Secretary of State that they are a CID when they file their incorporation papers. This requirement was added in 1994 in the hope that it would lead to the creation of a fairly comprehensive list of CIDs in California.<sup>169</sup> This is currently not the case. There is no public list of CIDs in California.<sup>170</sup> The Secretary of State does not record in their database when a nonprofit mutual benefit corporation identifies itself as a CID. It is possible to find out if a corporation is a CID if one has the name or its corporate identification number. This would allow someone to get an address a list of officers. However, the address used for filing is often the address of the association manager, making it difficult to contact an association's board. There is no way to get a complete list of existing incorporated CIDs from the Secretary of State or any other state entity without conducting almost prohibitively expensive research.

### **Attorney General**

When a CID is incorporated, the Attorney General does have statutory authority to take legal action against CIDs in certain circumstances. This includes a board of director's failure to:

- Hold regular meetings;
- Allow member access to books and corporate records;
- Provide annual financial reports to members;
- Provide a list of names and addresses of members to other members; and
- Comply with other specific member rights.<sup>171</sup>

The Attorney General's Office receives about 200 complaints a year, not all of which fall in the above categories. If the complaint does fall under the purview of the Attorney General's Office, the Public Inquiry Unit will send a letter to the association notifying them of the violation. This "Notice of Violation" letter requests a response to the charge(s) from the board or its representative in 30 days. Regardless of the response, or whether or not a response is received, the Attorney General does not pursue the matter. According to the Public Inquiry Unit, it is office policy not to intervene in these matters, which are considered private and not within the scope of the Attorney General's functions.<sup>172</sup>

## OTHER INVOLVED ENTITIES

### Professional Service Providers

CIDs have been in existence for over 40 years and common for about 20 years. While many experts feel that CID services are improving over time, it seems that many professionals who provide services to CIDs do not understand their intricacies. One CID professional told the story of a well-known national accounting firm that instructed a large CID in San Diego to pay real income tax, from which incorporated CIDs have certain exemptions. For 26 years, the CID overpaid taxes by about \$100,000 a year. The mistake was discovered when the CID hired a new on-site manager. The development was able to recover four years of their overpaid taxes but suffered a net loss of over \$2 million.<sup>173</sup>

### Homeowners

CID professionals and experts cite the low level of homeowner participation in governance as one of the biggest problems facing CIDs. Most CID managers and professionals believe that if a CID is going to run well, homeowners, like board members, must know about issues such as reserve studies and due process requirements. This allows residents to monitor board members. There were many reasons given for lack of participation: people were too busy to volunteer; people buy CIDs because they are marketed as carefree living; and people just do not care enough to get involved.<sup>174\*</sup> A self-reporting survey of homeowners found that 45 percent of homeowners said that they do not volunteer or volunteer once a year. Thirty-nine percent volunteer once a month or more.<sup>175</sup>

It also might reduce the contention in a CID if everyone understood the rules. Compliance with rules is greater when residents were involved in making the rules.<sup>176</sup> However, those who buy into CIDs often do not know what the rules and requirements are. Even though homebuyers are required to verify that they have received and read the governing documents before purchasing a CID property, up to 90 percent of homebuyers either do not read the information or do not understand it.<sup>177</sup>

CID homeowners are often surprised at the level of participation that is expected from them. When asked what aspects of CIDs living and financial disclosure they did not receive enough information about, homeowners' number one response (40 percent) was that they did not get enough information about the degree of homeowner cooperation required.<sup>178</sup>

One insurance agent, who specializes in CIDs, said that even if buyers read the CC&Rs, they sometimes think that the rules do not apply to them.<sup>179</sup> Homeowners in the United States believe that they should be able to use their property as they like. Even when they

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\* Membership support of boards appears weak: 16 percent of board presidents interviewed in this survey said that they get a lot of support from members, and 39 percent said that members don't care.

understand the concept of CIDs they may not really believe that they will be prohibited from making decisions about their own property.

Critics say that boards will sometimes avoid seeking homeowner participation. When homeowners participate it can be time consuming and can hinder boards from addressing business issues in a timely manner, which they often feel is their first priority.<sup>180</sup> While they disagree with the practice, managers say they understand why this happens especially when CID management is contentious.<sup>181</sup>

### **The Board of Directors**

There is no shortage of homeowner complaints about board members. Homeowners accuse boards of financial mismanagement and violations of CC&Rs and the law. CID professionals interviewed for this study unequivocally said that boards were uninformed. In Nevada, where the state ombudsman tracks calls to his office, most of the complaints received are about board of directors. Callers complain about power plays, personality conflicts, poor management, the board's refusal to respond to homeowners and their concerns, and board member ignorance. The ombudsman believes that in 70 percent of the situations he hears about, the boards are functioning incorrectly.<sup>182</sup>

On the other side are those that argue that homeowners have all the tools they need to control the power of boards. Homeowners can recall board members; and they can run for office or support candidates who share their point of view. In these ways, CID governance is no different than any local municipality. In addition, with the support of five percent of the residents, homeowners can call a special meeting to address issues. Residents can also sue the association if they feel the board has violated its governing documents or state law.

The Davis-Stirling Act contains provisions to improve the governance of CIDs by boards of directors. These include due process and financial requirements, such as mandatory reserve studies and a schedule for updating them. Some homeowner advocates believe that more should be done to curtail the power of boards.

It should be noted that board members are unpaid volunteers with little or no training in CID management. Laws to control boards may have little impact if the directors and homeowners do not understand their responsibilities or are unaware of the laws. Education may do more to address CID issues than additional laws.



## OPTIONS

There are disagreements on how to best address common interest development problems that are repeatedly raised by unhappy homeowners, frustrated boards and worried managers. Some of those involved with CIDs believe that these problems could be solved by improving existing CID laws or by improving governance within the associations. Still others find fault with the professionals involved with CIDs and believe that solutions lie there. Others recommend that the State of California follow the example of states that have created special departments, or positions to handle the issues associated with common interest developments. Still others say that problem CIDs make up a small minority. The majority of CIDs do not have issues that threaten their financial or social stability.

While not necessarily the recommendation of the California Research Bureau, the author or the legislative member requesting this report, the following options reflect the broad range of research on the subject.

## THE ROLE OF THE STATE

Some involved with CIDs claim that CIDs need a government entity to provide oversight. One argument against creating a state CID entity is that CIDs are private property, governed by private contracts, and the state has no role in this relationship.<sup>183</sup> Some experts argue that CIDs became popular because homebuyers felt they could not trust government and they wanted more control over their communities. At least one professional interviewed for this paper argued that if this is true, the majority of homeowners and board members probably do not want to be regulated by the State.<sup>184</sup> The other side of the argument is that CID problems cannot be dismissed entirely by government as private issues because CIDs are often created at the request of local governments.

As one manager pointed out, there are few checks and balances in CIDs, without which people will act in their own self-interest.<sup>185</sup> This includes boards, homeowners, developers, managers, and the other professionals involved with CIDs. One way to deal with CID complaints is for a neutral third party to negotiate the controversies that arise in CIDs. In the past, the courts have often played this role. There are a few problems with the courts as arbitrators for CID issues. Litigation is expensive for associations and often too expensive for individual homeowners. The courts have recently made it clear that they do not want this role. In 1999, the California Supreme Court decided that it is not the Court's place to second-guess homeowner associations.<sup>186</sup>

Those who have tried to promote state oversight of CIDs have found that state entities are not eager to take on the problems associated with the regulation of CIDs.<sup>187</sup> One of the reasons for this hesitancy is that no one knows what level of activity would result from the proposed programs. For example, projections based on the State of Nevada Ombudsman's Office suggest that a California ombudsman or a help line could generate many thousands of calls a month in the beginning.<sup>188</sup>

Many of the states that have entities working with CIDs charge homeowner associations a per unit fee to support the services. Nevada charges associations an annual three dollar a unit fee. If California did the same, it would result in a fund of over \$10 million, costing CID homeowners about 25 cents a month.

Currently Department of Real Estate (DRE), the Secretary of State, and the Attorney General all play roles in some aspect of CIDs. DRE is only involved until the developer relinquishes control, although they do provide some publications on the living in and managing of CIDs. The Secretary of State registers CIDs as nonprofit corporations. The Attorney General has enforcement jurisdiction of aspects of the corporate responsibilities of CIDs, but plays a minor role. Slight expansions of the roles of these entities in the following areas could help address some of the issues confronting CIDs.

The state could play the role of the mediator even without a separate governmental agency. These changes, which are discussed below, could potentially increase Davis-Stirling compliance, improve CID financial soundness, and address some of the other contentious issues in CIDs.

The use of alternative dispute resolution to fulfill the need for a neutral third party has been examined extensively by the California Law Revision Commission<sup>189</sup> and will not be discussed in this report.

## **IMPROVING CURRENT LAWS & REQUIREMENTS**

### **Revising the Davis-Stirling Act**

Most observers agree that there is massive noncompliance with the Davis-Stirling Act. When homeowner associations (HOAs) follow Davis-Stirling, it appears to address some of the problems. Early studies found that the passage of Davis-Stirling resulted in an increase in the number of CIDs with reserve funds and studies.<sup>190</sup> It also provides some governance structure and due process protection for homeowners. One CID professional said, “there is nothing wrong with Davis-Stirling. It really works.” It is the managers who don’t follow the law that create many of the problems.<sup>191</sup>

Some of the managers interviewed for this report would like the state to actively enforce Davis-Stirling. In the absence of enforcement, many would like the law to be changed or repealed as it establishes expectations among homebuyers and homeowners.

Some CID experts believe that the UCIOA provides a more comprehensive framework for CID governance and management.<sup>192</sup> Professor Susan French, in her exploratory paper for the California Law Revision Commission, suggests that the Commission look at repealing Davis-Stirling and replacing it with the Uniform Common Interest Ownership Act (UCIOA). This is not, however, a universally accepted idea.<sup>193</sup>

Proponents contend that the UCIOA is easier to understand for lay people. They also believe that the UCIOA would be more stable because it is more comprehensive and

because the legislature is less likely to amend a uniform act.<sup>194</sup> This would provide a more stable law unlike Davis-Stirling, which has been amended numerous times. UCIOA focuses more on the real estate aspects of CIDs and gives more flexibility to the developer. It also gives more flexibility to owners and associations to move boundaries within the development. UCIOA gives more power to boards in enforcing covenants. It makes it harder for homeowners to amend governing documents and does not have some of the due process requirements that are part of Davis-Stirling. French and other CID experts agree that the best aspects of Davis-Stirling, especially those that address unique aspects of California CIDs, should be integrated into the UCIOA framework.<sup>195</sup>

Enforcement of Davis-Stirling might also address CID litigation issues. One manager believed that the lack of enforcement causes the high level of litigation because either the homeowner or the board must sue to enforce the law.<sup>196</sup> In effect, the individual, the association and the courts have taken over the responsibility for enforcing Davis-Stirling.

Much of the noncompliance is caused by ignorance on the part of CID stakeholders. A casual online poll of homeowner associations conducted by the California Legislation Action Committee of California Community Associations Institute (CLAC-CAI) found that half of the respondents needed help understanding Davis-Stirling and most hire attorneys to help them.<sup>197</sup> At least some of the noncompliance and costly litigation could be reduced through education about the law.

The California Law Revision Commission is in the process of reviewing the Davis-Stirling Act and should have recommendations as to how to improve the law in the next couple of years.

## **CC&Rs**

One of the biggest complaints by homeowners is that they do not understand the responsibilities of CID ownership when they purchase their home. One CID professional who reviews CID disclosure documents for homebuyers said it can be a struggle to get associations to provide all the legally required disclosure documents.<sup>198</sup>

The state could require that the initial disclosure documents tell homebuyers that CC&Rs are binding contracts. This could be accomplished by attaching a “warning label” to the CC&Rs like the one used by the State of Nevada. This information sheet is given to buyers who must initial and date the document. Section titles include among others:

- “1. YOU ARE AGREEING TO RESTRICTIONS ON HOW YOU CAN USE YOUR PROPERTY.” And;
- “3. IF YOU FAIL TO PAY OWNERS’ ASSESSMENTS, YOU COULD LOSE YOUR HOME.”<sup>199</sup>

Another interesting suggestion that might encourage homebuyers to read the CC&Rs is to give the homebuyer a short summary of them. It might convince prospective homebuyers

that they need to read the entire document.<sup>200</sup> At least it would give them some idea of what to expect from living in a CID.

The CID Homeowner Bill of Rights Coalition has proposed a Homeowner Bill of Rights. (See Appendix D) While they are uncertain as to how to inform homeowners that they are entering into a binding contract, they want them to understand that they are agreeing to certain rights and responsibilities when they buy in a CID. The first provision of their Bill of Rights reads:

- I. Since living in a common interest development (CID) requires an individual citizen to enter into a contract with a governing association, the prospective homeowner must give written informed consent to the terms of the association's rules and governing documents, but most especially to the Codes, Covenants and Restrictions (CC&Rs) ten days before close of escrow. The governing documents comprise the contract between the association and the buyer.

Additional suggestions to improve CC&Rs include:

- Creating a standardized form for CC&Rs; and,
- Requiring CC&Rs to specifically allow for enforcement by the board.

### **Assessments and Reserve Funds**

This seemed to be the area of greatest concern among CID professionals although research shows that it is of much less concern to homeowners.<sup>201</sup> There does seem to be a problem with lower income CIDs deteriorating because of deferred maintenance and the inability of homeowners to assess themselves adequately for improvements.<sup>202</sup>

DRE could re-evaluate how developer's budgets are created, how DRE reviews them and how they are disclosed by:

- Requiring an outside review of a development's components and reserve study for accuracy before the developer turns the CID over to the homeowners.<sup>203</sup>
- Reviewing budgets before the developer turns management over to the association to make sure that the figures are updated for inflation and that they include any changes that may have occurred during the development of the project.
- Including a disclosure in the public report and in the CC&Rs that the developer's budget and projections can only be relied on over the short-term and may already be out dated when the HOA take control.

The other problem cited is that even though Davis-Stirling requires reserve study updates, there is no specific requirement to do new reserve studies. There is no standardized computing method for reserve funds or required level of funding.<sup>204</sup> In fact, there is no

requirement to fund the reserves at all. The existence of a reserve fund may cause homeowners to think that they are adequately covered even while the reserve fund is inadequate. Proposed solutions include:

- Amending Davis-Stirling to require new reserve studies on a set schedule;
- Amending Davis-Stirling to include a mandatory level of reserve funding;
- Requiring more information in the annual budget about how reserves are calculated, such as in Hawaii, and
- Providing more accurate guidelines to developers and homeowners for calculating the level of reserves.

Some homeowners are concerned that associations misuse their reserve funds.<sup>205</sup> They feel that this problem will be exacerbated by any mandate that requires full funding. In order to protect against this, Davis-Stirling could be revised to prohibit associations from borrowing from these funds for other purposes.<sup>206</sup>

Common interest developments are often formed because cities do not want to bear the financial costs of maintaining infrastructure. Because cities have a role in forming CIDs, and because they have an interest in ensuring that developments do not become blighted, they could take on the role of conducting reserve studies or infrastructure evaluations for CIDs. This would allow a neutral party to assess reserve fund needs reducing some of the conflict and bias surrounding reserve studies. Cities could charge CIDs a fee to cover the cost of this service.

### **Expanding State Oversight**

CIDs are unlike any other nonprofit mutual benefit corporation, or most other business or nonprofit entities. This is because the developer creates the CID but has a diminishing role and stake in the success of the CID.<sup>207</sup> In order to create some consistency and the availability of expertise throughout the lifetime of a CID, the state could oversee some of the basic aspects of CID management and Davis-Stirling requirements such as:

- Requiring that HOAs review their CC&Rs on a set schedule to make sure they comply with any revisions to the law and meet current homeowner needs. The state could notify CIDs that their CC&Rs must be reviewed. The new CC&Rs would then be submitted to the state with verification that they had been reviewed. The CID also could be required to form a homeowner advisory committee that was involved in the review.
- Notifying CIDs when they need to update their reserve studies, which is required by law every three years. CIDs could be required to send a copy of this study to an oversight agency. Since the quality of these reports is identified as a key problem, a state agency could provide technical assistance to boards of directors on how to comply with these updates.

## **NEW PROGRAMS**

### **Ombudsman**

As discussed, one of the issues in CIDs seems to be the lack of an objective third party to resolve disputes and enforce the rules.

The state could institute an ombudsman's office to provide any combination of the following services:

- Resolve disputes and enforce rules;
- Answer stakeholder questions to clarify the law and rights and responsibilities;
- Alternative dispute resolution services; and
- Education (including classes) and information.

The California Law Review Commission (CLRC) found that there was support among stakeholders for an ombudsperson.<sup>208</sup>

### **Information Clearing House**

To collect more information about CIDs, the CLRC has discussed the idea of a 1-800 number and a web site to serve as a CID clearinghouse. The clearinghouse, like an ombudsman's office, would actively collect information and respond to requests for information. This would include information about the law and the availability of alternation dispute resolution (ADR) processes. The CLRC writes, "It would be relatively inexpensive and quite cost effective to assign a governmental entity with responsibilities in the CID area the task of establishing an information center."<sup>209</sup>

Data collection would help determine a wide range of information about CIDs such as: the real number of CIDs in California, the amount of housing units in CIDs, levels of assessments, and frequency of special assessments. This expanded picture of CIDs housing in California would help the state develop effective CIDs policy.

### **Requiring Professional Management**

Some observers believe that professional financial management increases the financial health of CIDs and Davis-Stirling compliance. As expected, professional managers strongly believe that all CIDs should be professionally managed.

Several managers said the professional management should be required either by Davis-Stirling or in a CID's CC&Rs. Governing documents should also be clear about the role of the manager so they can do their job effectively. Some developers already mandate professional management in their CC&Rs and the City of Fremont requires that CIDs over a certain size have professional management.<sup>210</sup>

Most managers who made this recommendation were clear that this should not apply to small CIDs because professional management would be too expensive for them and may not be necessary since small CIDs are less complex and have fewer amenities.

### *Licensing Community Managers*

Not all managers are well versed in CID issues nor are they all trustworthy. The president of the California Association of Community Managers (CACM) writes that because of the competitiveness of the profession “some manager practitioners have evolved to provide services that are inconsistent or unreliable, and even, unfortunately, fail to conform to federal, state and local laws.”<sup>211</sup>

One way to increase the accountability of managers is for the state to license them. If a manager did not perform well or violated the law, his or her license could be suspended or revoked. For several years there has been a push by managers and some homeowners to require the licensing of managers so there can be some quality control. Many managers interviewed for this report believed that there should be some regulation of the profession and most believed in some sort of continuing education for managers and for board members.

A number of issues would need to be addressed to develop a licensing program. Critics believe that in order for a licensing program to improve the quality of professional management, it must be developed and overseen by a neutral party. License candidates might object to the license and education costs. Homeowners could object to potential service fee costs.

## **EDUCATION & INFORMATION**

The need for increased information and education was the most common recommendation from managers and in the literature. Even those who don't think the state should heavily regulate CIDs, see a state role in providing information and resources. They believe homeowners and boards need an entity to answer their questions.<sup>212</sup> There are several state entities that have been suggested for this role including: the Secretary of State, the Attorney General, the Department of Housing and Community Development, the Department of Real Estate, the Department of Fair Housing, the Department of Consumer Affairs, and the Department of Insurance.

Education needs to be provided at all stages of a CID's lifetime beginning when the first people purchase their homes. Most developers do not put any effort into preparing the board members for taking over governance of a CID. Many board members do not even have the basic knowledge they need to manage a CID, such as how to run meetings, or how to fairly pass rules. Nor do they know what liability they have as a board member.<sup>213</sup> One suggestion was that the developer should be required to fund board education and participation in trade groups before he or she turns over control to the association. This money would also be built into the assessments and mandated in the CC&Rs so that these

practices continued after the association took over.<sup>214</sup> A list of existing resources for CID stakeholders is Appendix E.

## **Possible State Education Actions**

### *Common Interest Development Web Site*

A web site could provide updates on the law and other resources to homeowners and board members, as well as professionals. This site could provide links to other state entities involved with CIDs, as well as other organizations that work with CIDs. For example, DRE's site could provide a link to the Secretary of State's Office, which also has online information about common interest developments and incorporation.

### *Workbook*

The state could develop a workbook that has checklists based on the laws that CIDs need to follow. For example:

- Meeting and due process requirements;
- Budget elements and distribution schedule;
- Records that need to be saved;
- Insurance requirements; and
- Reserve study review and update requirements.

### *Yearly Update*

When an association sends in its incorporation papers to the Secretary of State, it checks a box indicating that they are a common interest development. The Secretary of State could send out a yearly update on law changes or other information to these CIDs.

## **Barriers to Sharing Information**

There is currently no comprehensive list of CIDs readily available. To effectively share information and to better understand CID issues, the state could create a comprehensive list of common interest developments. Such a database would allow the state to send out basic information to associations about state CID requirements and notify associations of changes in the law. Such a list would also provide a basis for surveying homeowners and homeowner associations about potential issues and problems.

There are a few different mechanisms that could be used to put together a list of CIDs in California:

## ***Registering***

Requiring all CIDs to register would also create a list of CIDs. In Montgomery County, Maryland and Nevada, CIDs are charged a per door registration fee to support a variety of services including ADR and educational materials and programs.

The success of any registration requirement depends on the ability to disseminate the information that CIDs need to register. This is already a problematic issue since no list exists. Involving DRE or the Secretary of State's Office, both of which interact with most CIDs at some point, could solve this. DRE must approve all proposed subdivisions and incorporated CIDs must file incorporation papers with the Secretary of State. Either could establish a database that tracks CIDs.

## **A California Example**

The Housing Standards Program in the Department of Housing and Community Development's Division of Codes and Standards permits manufactured home parks. They invoice parks annually and charge a fee that is made up of four components:

- \$25 permit fee;
- \$2 per lot fee;
- \$4 per lot fee for maintenance inspection; and
- \$40 to 1,600 state regulatory fee based on the size of the park.<sup>215</sup>

All parks register with the office when they first open. The office maintains a database on all the parks in California and is supported by the registration fees. The program has inspectors who make sure that parks are registered, as well as making sure that they are being adequately maintained.

## **STRUCTURE**

In the final report for the 1990 Assembly Select Committee on Common interest developments, the authors state that while there is a need for better CID education and information systems, the real problems facing CIDs are systemic "inherent to a system which requires cooperation and involvement but is still a relatively foreign notion in an extremely independent, home-as-castle oriented society."<sup>216</sup>

For the most part, CIDs seem to be as successful as any other local governing structure, such as a city council or a special district. Some of the problems that are unique to CIDs could be addressed by looking at their underlying legal structure. Part of the difficulty arises from the confusion over the definition of CIDs. Homeowners' expectations clash with the corporate law that governs CIDs. They expect their individual concerns to have more weight. Corporate law is not geared towards the individual. Nor does current CID law provide a neutral party to facilitate between the interests of the individual and the community. Instead this task falls to the board of directors.

The governing structure could also be changed. For example, Radburn uses a two-tiered model of governance. There is a board of directors that is elected by the homeowners from candidates selected by the board. There is a separate homeowner association whose president, also elected by homeowners, represents the HOA on the board of directors. The HOA deals with community issues and provides a forum for homeowners to express their concerns. These concerns are then conveyed to the board through the president. This allows the board to focus on business issues. Because all board members must be nominated, it can also be assumed that they have some knowledge that is valuable to the managing of the association. This model has worked for Radburn for almost 75 years. This model could be criticized of further removing homeowners from the decision-making process.

A Florida law office that works with CIDs presents another possible option. They believe that CID governance has already become too removed from residents. “Our current governance models are based on absolutes and generalizations, which . . . result in a perception that the members have no input in the governance of their homes.”<sup>217</sup> They believe that absolute adherence to CC&Rs and the failure of boards to work with residents so that the governing documents meet the needs of the homeowners is giving community associations a bad name.

They recommend much that has been discussed in this paper: educating directors and encouraging residents to participate. They also believe that CC&Rs should be reviewed and altered to fit into the current culture of the association.

The rules that are being overlooked should be reviewed and removed from the books. Rules need to become standards and principles, and emerge from a group participation process, rather than being handed down from above. . . . It is time to move from the rigid covenants, conditions and restrictions paradigm. . . . When a problem arises, we need to look at the best solution, instead of throwing another rule at it.<sup>218</sup>

At least one source recommended that homeowners be required by the CC&Rs to participate either on a committee or as a board member.<sup>219</sup> While most sources did not go that far, it is clear that most professionals and those writing on CIDs believe that homeowners must participate if a CID is to run well both financially and socially. Information about the level of participation required from homeowners should be included in disclosure documents and in homeowner literature, such as the DRE brochure.

## **APPENDIX A: CALIFORNIA CID LEGISLATIVE AND STATE AGENCY FINDINGS**

In the past 26 years the legislature, as well as state departments, have regularly addressed common interest developments issues.

### **LEGISLATIVE HEARINGS**

#### **1983-Assembly Select Committee**

In 1983, an Assembly Select Committee was convened to study common interest developments. At that time CIDs were governed by sections in several different codes and in two different places in the civil code. The committee heard testimony from homeowners, property managers, real estate brokers, lenders, attorneys, and others. It also appointed two task forces: one composed of homeowners, the other of industry representatives with homeowner input.

The result was the 1985 Davis-Stirling Act, which repealed the 1960s Condominium Act, sections of the Business and Professions Code, and the Civil Code and consolidated them into the Civil Code, sections 1350-1372.

In general the Davis-Stirling Act:<sup>220</sup>

- Applies most of the statutory law that had applied to condominiums to all common interest developments including Planned unit developments (PUDs) community apartment projects, and housing stock cooperatives;
- Gives homeowners associations the right to enforce CC&Rs and requires them to manage the CID;
- Allows a majority of the association to amend the associations governing documents;
- Requires the preparation and distribution of financial information to homeowners at specific times throughout the year;
- Limits how the homeowners can raise and collect funds;
- Provides procedures for conducting meetings;
- Identifies who is responsible for maintenance when the governing documents do not specify.

#### **1990-Assembly Select Committee on Common Interest Developments**

The Speaker of the Assembly created the Assembly Select Committee on Common interest developments in January of 1990 to research policy issues related to CIDs.<sup>221</sup> The committee focused on three issues: (1) the problems related to governance of community associations; (2) problems relating to finance and management and, (3) the long-term

social implications of CIDs on housing and communities. The final report states that, despite the horror stories, the committee was reassured that most associations were doing an adequate job of handling their finances.<sup>222</sup>

The report found that:

- According to the experts, five percent of CIDs have serious problems;
- While there maybe a role for the state to play in addressing some of the basic issues raised in the hearings (such as standards for managers, minimum levels for reserve funds, and greater protection of association rights), that “ what is also apparent is that homeowners need to develop greater familiarity with the association process, become more aware and appreciative of the unique nature of relationships within a common interest development, and accept the fact that participation and cooperation are a necessity.”
- There is a need for better education and information systems;
- Some of the problems with CIDs are systemic and will not be solved by creating a state oversight or regulatory agency.

### **1996-Senate Committee on Housing and Land Use Interim Hearing**

In 1994, the Supreme Court decision Nahrstedt v Lakeside Village Condominium Association examined the standards that trial courts should apply when assessing the reasonableness of CC&R restrictions. The court upheld the authority of a CID board to enforce CC&Rs unless they are arbitrary, go against public policy, or impose a burden that far outweighs any benefit. The court determined that CC&Rs would be presumed valid unless they could be proven unreasonable.

In response to Nahrstedt, the Senate Committee on Housing and Land Use decided to revisit CID issues and convened an interim hearing in 1996.<sup>223</sup>

The committee staff identified the following to be the key hearing findings:

- The Davis-Stirling Act is complicated, costly to implement, and unclear making it easy to accidentally violate. Stakeholders support establishing a task force to review the act;
- Community association boards abuse their power resulting in costly litigation by homeowners causing financial hardships to owners and depleted association funds;
- Amendments to the Davis-Stirling Act make CID governing documents outdated so the Board cannot rely on these documents for guidance;
- Smaller CIDs have difficulties hiring professional management so they have a harder time tracking and complying with new laws;
- New laws need to acknowledge that CIDs are not all the same and vary in size and resources;

- CID buyers do not understand how CIDs work and what their rights and responsibilities. The Department of Real Estate brochure on CIDs, “Living in a California Common Interest Development,” brochure should be made available to all CID purchasers before a sale is finalized;
- Given the number of CIDs in the state, there are relatively few legal cases. It was recommended that legislators avoid overreacting to antidotal complaints of wrong doing before passing new laws to solve issues that might be better solved within associations;
- Most CIDs depend on property management companies to comply with the law and to enforce their governing documents. Because of this, property management companies should be licensed by the state, and
- Homeowners want a bill of rights to defend against unjust confiscation of homes, to protect reserve funds, ensure quality services, and safeguard against encroachment on their liberty. Others warned that such a bill should also spell out homeowner’s responsibilities.

## **STATE RESEARCH AND WORKING GROUPS**

### **1987-DRE’s Common Interest Homeowner’s Associations Management Study**

The California Department of Real Estate commissioned two of the most comprehensive studies on CIDs in California. The first in 1987, *Common Interest Homeowner’s Associations Management Study*,<sup>224</sup> surveyed board presidents and conducted in depth case studies of 12 CIDs of varying sizes, most of which were professionally managed.

These are some of the findings and recommendations made by the study:

- The structure of CIDs lead too much of their difficulties. “Clearly common interest developments are a mixture of [management, government and neighborliness], and it is not easy to combine all these things. [They] often conflict with each other.”
- Boards, renters, and buyers need better education and information about the nature of CIDs and their responsibilities and rights. To accomplish this, all board members should attend a basic informational seminars paid for with an increase in the filing fee they pay every year to be incorporated. Community colleges and university extension services should offer courses in the management of CIDs and would include classed for real estate professionals that work with CIDS as well as managers and other association employees.
- Absentee owners affect the efficient management of a CID and the quality of life because they are less likely to support assessment increases. The authors recommended that resident owners have greater authority when it comes to association votes.
- Construction defects are one of the largest problems CIDs face with 37 percent reporting major construction defects. Defects place tremendous stress on the

relationship between the associations and its board and can undermine the effectiveness and the quality of life in a CID. To remedy this, the authors recommend that local government do a better job of inspecting CIDs as they are being built and developers put up a bond to cover defects after the association passed from developer control to homeowner control.

- The reserve study requirement has been very successful in overcoming deferred maintenance problems. This requirement could be further clarified by creating guidelines for what defines an adequate study.
- The state should keep an accurate list of CIDs. To this end, all CIDs should be incorporated.
- Finally, the authors recommend that California review Florida's Board of Condominiums as a possible model to provide education, arbitration services, and to oversee compliance with state laws governing CIDs.

### **1991-Department of Real Estate's Study of the Future Outlook of California Common Interest Developments**

In 1991 the Department of Real Estate commissioned the *Study of the Future Outlook of California Common Interest Developments*<sup>225</sup> to look at the positive and negative factors affecting the future viability and market competitiveness of common interest developments. The study conducted interviews of people involved in housing construction in general, as well as those involved with the construction and financing of CIDs. They also contacted real estate and law professors, CID associations, and CID homeowners. A mail survey of 319 California CID homeowners and association managers, developers and independent CID professionals was also used to collect opinions on the future of CIDs. The study found that:

- CIDs need an active HOA board and an interested HOA membership to continue to function. The authors suggest offering a small stipend to board members;
- CIDs require management expertise and a competent board. Professional management may be too costly for small CIDs to afford. There should be some way to encourage professional quality perhaps through accreditation, certification or licensing;
- CIDs will remain viable in the long run only if the majority of units remain owner occupied;
- The Department of Real Estate should require better initial operating and capital budgets in CIDs' Public Reports submitted by the developer as part of the requirements for a subdivision permit. Budgets should include a line item to purchase additional home warranties;
- Third party inspections should be conducted of projects before they transfer from developer control to the association;

- Formulate clearer requirements for reserve studies and their timelines and make sure they are well funded;
- Require questions about CIDs on the licensing exam for real estate agents;
- Monitor CIDs advertising to make sure that it is not downplaying the responsibilities that go with owning a home in a CID;
- There are a huge amount of lawsuits in CIDs. A number of reasons might contribute to this problem including inflexible CC&Rs and bylaws, expectations by homeowners that they should be able to do what they want to with their property regardless of CC&Rs, lack of understanding of CC&Rs. Litigation poses one of the biggest threats to the future viability of CIDs, according to real estate agents. The study advises against creating a new bureaucracy for solving HOA conflicts. Instead, its authors recommend using mediation as a way to solve conflict and reduce tension in CIDs.
- CIDs may ultimately be a very expensive way to maintain property because all services must be contracted out and paid for at the current labor rate. There is no sweat equity, and
- CIDs are here to stay in California.

### **1998-California Research Bureau Report, Residential Common Interest Developments: An Overview**

One of the outcomes of a 1996 hearing was a request from Senator Byron Sher that the California Research Bureau produce a background paper on CIDs in California. In 1998, the California Research Bureau released the report, *Residential Common Interest Developments: An Overview*. This paper provided an overview of CID structure, historical trends, and governance as well as information on current CID issues and examples of how CIDs were regulated in other states.

The report identified the following as the major policy issues raised by those involved with CIDs:

- Should the Legislature establish an oversight committee for CIDs?
- Should the Legislature license CID professionals?
- Should the Legislature revise the Davis-Stirling Act?
- Should the Legislature pass a “Homeowner’s Bill of Rights?”

The report suggests that there is a lack of up-to-date empirical research on CIDs and that the collection of current information on HOAs and related issues might be useful.<sup>226</sup>

### **1997-1998-Common Interest Development Working Group**

Another outcome from this hearing was the formation of a working group to review the Davis-Stirling Act and make recommendations to the Senate Committee on Housing and

Land Use. The working group met several times and focused on reviewing the Davis-Stirling Act. The 20 members represented a variety of stakeholder groups. Ultimately, they could not reach a consensus on what issues should be addressed or how. Changes in the leadership and focus of the Senate Committee further deterred the success of the working group. Legislative ideas that were considered included requiring a CID seller to provide the buyer with the Department of Real Estate brochure on CIDs and implementing an ombudsperson program to address conflicts in common interest developments.<sup>227</sup>

## **CURRENT STATE ACTIONS**

### **Ongoing-California Law Revision Commission**

After the failure of the working group, interested parties recommended that the California Law Revision Commission (CLRC) initiate a review of CID law for possible reforms.<sup>228</sup> In CLRC's 1998-1999 annual report, which examines potential topics and priorities, the organization agreed with previous examinations of CIDs and determined that the laws governing CIDs are confusing and not enforced. The report states:

The association boards that administer common interest developments, composed of elected unit owners, encounter a statutory framework that is unduly complex; the lay volunteers often make mistakes and violate procedures for conducting hearings, adopting budgets, establishing reserves, enforcing parking, and collecting assessments. The statutes provide no practical enforcement provisions to deter violations. Housing consumers do not readily understand and cannot easily exercise their rights and obligations.<sup>229</sup>

In 1999, the Legislature authorized the CLRC to study common interest development law and focus on:

Whether the law governing common interest housing developments should be revised to clarify the law, eliminate unnecessary or obsolete provisions, consolidate existing statutes in one place in the codes, establish a clear, consistent, and unified policy with regard to formation and management of these developments and transaction of real property interests located within them, and to determine to what extent they should be subject to regulation.<sup>230</sup>

The Commission hired Professor Susan French of UCLA's law school to produce a report on the potential scope and priorities of the Commission's study. *Scope of Study of Laws Affecting Common Interest Developments* was released in November 2000. Professor French notes in her study that Davis-Stirling was not intended to be comprehensive.<sup>231</sup> She also finds that the act "is so unwieldy, disorganized and loaded with micromanagement minutia, that serious consideration should be given to starting over with a new framework on which a more comprehensible and comprehensive law of

common interest developments could be constructed.”<sup>232</sup> She recommends that Uniform Common Interest Ownership Act (UCIOA) as a possible starting point.

Additional recommendations include (1) reviewing the interrelationship between a CIDs governing documents, Davis-Stirling, and the Corporations Code for compatibility and suitability; and (2) finding ways to provide better protection to members of CIDs from deferred maintenance, intrusive regulations, abusive enforcement, and from board violations of due process. She suggests accomplishing this by including a Bill of Rights in CID statute and providing some sort of judicial oversight and dispute resolution.

Professor French points to two camps, those who prefer the micromanagement approach of Davis-Stirling and those who would like a framework that offers CIDs more flexibility in how they comply. She also adds that some homeowner’s groups would like more regulatory oversight either in the form of new entity or an existing agency or department.

The CLRC decided to focus on three areas:

- (1) a comprehensive study of problems and potential solutions;
- (2) the Uniform Common Interest Ownership Act and its applicability to California, and
- (3) nonjudicial dispute resolution including due process for rule and decision-making.<sup>233</sup>

### **2001-Assembly Committee on Housing and Community Development Interim Hearing**

This most recent hearing was held on November 29, 2001 and focused on due process issues as they relate to the relationship between homeowners and homeowner associations. The hearing also heard updates on the ongoing research that is being done on CIDs including the CLRC study and the California Research Bureau report.

### **2002-Current California Research Bureau Report**

This study will give an overview of some of the issues facing CIDs but will focus on the question of the whether or not the current conditions of CID law and practices threaten the financial stability of CIDs.



## APPENDIX B: COMMON INTEREST DEVELOPMENT DUE PROCESS REQUIREMENTS

	<b>Davis-Stirling Act/Civil Code</b>	<b>Corporations Code</b>
<b>Meetings</b>	<ul style="list-style-type: none"> <li>• Any member may attend board meeting (except executive sessions).</li> <li>• Meetings must be conducted in accordance with a recognized system of parliamentary procedure.</li> </ul>	<ul style="list-style-type: none"> <li>• Must hold an annual members meeting.</li> <li>• Special meetings can be called by five percent or more of members.</li> </ul>
<b>Notification</b>	<ul style="list-style-type: none"> <li>• Unless meeting time and place is fixed in the bylaws, members shall be given notice of board meetings.</li> <li>• Members shall be notified in writing that they have a right to copies of board meeting minutes and how they can obtain minutes.</li> </ul>	<ul style="list-style-type: none"> <li>• When members are permitted or required to take action at a meeting, they must be given written notice. This notice shall include topics to be covered.</li> </ul>
<b>Disclosure</b>	<ul style="list-style-type: none"> <li>• Matters discussed in executive sessions must be documented in minutes.</li> <li>• Minutes must be made available to members.</li> <li>• A statement describing association's policy and practice for enforcing lien rights and other legal remedies for assessment nonpayment shall be delivered to members annually.</li> </ul>	<ul style="list-style-type: none"> <li>• Shall keep adequate books and records.</li> <li>• Minutes shall be kept in written form.</li> <li>• Shall keep a record of members and their addresses.</li> <li>• Must furnish results of membership vote if requested.</li> <li>• Accounting books, records, and minutes are open to inspection at written request of members.</li> </ul>
<b>Annual Report/ Financial Information</b>	<p>The association shall prepare and distribute to each member:</p> <ul style="list-style-type: none"> <li>• An operating budget including: <ul style="list-style-type: none"> <li>A. <i>Estimated revenue and expenses</i></li> <li>B. <i>A summary of reserves which lists:</i> <ol style="list-style-type: none"> <li>(1) Estimated replacement costs, remaining life and useful life for each major component.</li> <li>(2) Current estimate of cash</li> </ol> </li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>• An annual report shall be prepared no later than 120 days after close of fiscal year.</li> <li>• Members will be notified and can request a copy.</li> <li>• Report shall include: balance sheet, income statement and statement of any changes in financial situation.</li> </ul>

	<p>reserves necessary to addresses maintenance and repair of major components.</p> <p>(3) Current amount of cash reserves set aside for the above purposes.</p> <ul style="list-style-type: none"> <li>• A professional review of the financial statement (if the association budget is over \$75,000).</li> </ul>	
<b>Membership Participation</b>	<ul style="list-style-type: none"> <li>• The board shall allow any association member to speak at any board meeting.</li> <li>• The board must get membership approval to raise assessments more then 20 percent or levy special assessments over five percent of the gross expenses of the association for that fiscal year.</li> <li>• The board may not amend governing documents without the approval of the members.</li> </ul>	<ul style="list-style-type: none"> <li>• Directors must be elected by quorum of members.</li> </ul>
<b>Disciplinary Actions</b>	<p>Members must be informed if there are monetary penalties for violations of governing documents.</p> <p>Before disciplining a member the board must provide:</p> <p>A. 10 days prior notice of meeting &amp; alleged violation</p> <p>B. Member has a right to attend meeting &amp; address board.</p> <p>C. Disciplining body must notify member within 15 days following action.</p>	<ul style="list-style-type: none"> <li>• Must use procedural due process. May adopt own procedures but the State provides an example of what it considers fair &amp; reasonable: <ul style="list-style-type: none"> <li>A. 15 days prior notice of meeting &amp; alleged violation.</li> <li>B. Opportunity to be heard in orally &amp; in writing at least 5 days before discipline is imposed.</li> <li>C. Disciplining body must notify member in writing of the procedures that will be used in process.</li> </ul> </li> <li>• Enforcement actions must be based on substantive grounds that do not violate contractual or other rights of member.</li> </ul>

# APPENDIX C: CALIFORNIA DEPARTMENT OF REAL ESTATE'S BROCHURE ON LIVING IN A CID

<http://www.dre.ca.gov/cidinfo.htm>

## LIVING IN A CALIFORNIA COMMON INTEREST DEVELOPMENT

**State of California**  
**Department of Real Estate**  
Gray Davis  
*Governor*

Maria Contreras-Sweet  
*Secretary of the Business, Transportation, and Housing Agency*

Paula Reddish Zinnemann  
*Real Estate Commissioner*

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### Preface

There are many questions that homeowners face when planning to purchase a home in a common interest development (CID). The answers to a number of these questions as set forth in this brochure are designed to provide you with general information regarding some of the issues related to living in a CID. We hope this information contributes to your understanding and expectations of home ownership in a common interest development.

Since this brochure does not contain specific legal information or guidance, it should only be used as a general source of information. If you wish to research the subject matter further, you may want to consult with an attorney or an industry professional experienced with CIDs.

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### 1. What is a common interest development (CID)?

A CID is descriptive not only of a certain type of real estate and form of home ownership, but also of a life-style that is becoming more and more common to the American way of life. To understand the concept, it is important to know that there is no one structural type, architectural style, or standard size for CIDs. They come in a variety of types and styles, such as single family detached houses, two story townhouses, garden style units with shared "arty walls," and apartment-like, multi-storied high rises. Currently in California, there are tens of thousands of CIDs, which range in size from a simple two-unit development to a large complex having thousands of homes, many commonly owned facilities, and multiple associations under the auspices of one overall master association. However, despite the wide range of differences that may exist among CIDs, all CIDs are similar in that they allow individual owners the use of common property and facilities and provide for a system of self-governance through an association of the homeowners within the CID.

The most common type of association of homeowners is the nonprofit mutual benefit corporation. This is a corporation in which the members of the corporation vote for a board of directors, which runs the affairs of the corporation. However, some associations, usually the older ones, are unincorporated associations. In many ways, unincorporated associations are treated the same as mutual benefit corporations under California law.

## **2. Do you have to join the association?**

Membership in the association is automatic. When a person buys a lot, home, townhome, or condominium in a common interest development, he/she automatically becomes a member of the association.

## **3. What are Covenants, Conditions and Restrictions (CC&Rs)?**

The Declaration of the Covenants, Conditions and Restrictions, or CC&Rs, contains the ground rules for the operation of the association. This governing document identifies the association's common area and responsibilities, explains the obligation of the association to collect assessments, as well as the obligation of the owners to pay assessments. It also states that the association may sue owners for violations of the rules or failure to pay assessments, and explains what happens if there is any destruction of property in the development as a result of fire or earthquake. Usually, the CC&Rs will also state the duties and obligations of the association to its members, insurance requirements, and architectural control issues.

## **4. How are the CC&Rs enforced?**

California laws allow that either the association or an owner in a common interest development may sue in court and ask the court to enforce the CC&Rs. The law currently requires that, unless an exception applies, prior to the filing of a lawsuit either the owner or the association must offer to engage in some form of alternative dispute resolution process. You may wish to consult with an attorney who specializes in this type of law if you are faced with or contemplating an enforcement matter.

## **5. What is the purpose of the Bylaws?**

As stated above, the CC&Rs generally state how an association is to be operated. In almost every instance the association, through its board of directors, has the ultimate responsibility for managing the association. Since the association is usually a corporation, the Bylaws establish the rules by which the corporation will be run. These usually include such aspects as how members vote for the board of directors, the number and term limit of members of the board of directors, the duties of the board, the duties of the officers, and other incidental provisions.

## **6. Does the Department of Real Estate assist with the enforcement of the Bylaws and CC&Rs?**

CIDs are subject to the Davis-Stirling Common Interest Development Act (California Civil Code Sections 1350 et seq.), which is designed to provide homeowners with a system of self-government and dispute resolution. The Department of Real Estate reviews the legal framework of all new CIDs to ensure compliance with the Subdivided Lands Law through the public report application process prior to the homes being offered for sale to the public. Once sales have commenced, the Department's jurisdiction is limited to the subdivider's obligations under the public report, which does not include intervention in association disputes.

The Attorney General has the authority under Corporations Code Section 8216 to intervene on behalf of members of a non-profit mutual benefit corporation (such as a homeowners association) who are denied certain specified rights. The Attorney General's intervention would be to send a "Notice of Complaint" letter to the board of directors.

If your association has failed to hold regular meetings of members, failed to allow member access to books and records of the corporation, failed to provide annual financial reports to members, failed to provide a list of names and addresses of members, or failed to provide other specified member rights, you may submit a complaint in writing to:

**Office of the Attorney General  
Public Inquiry Unit  
P. O. Box 944255  
Sacramento, CA 94244-2550**

Be sure to include an address for the non-profit corporation (homeowner association) and your own return address. If action is warranted, you will receive a copy of the "Notice of Complaint" letter sent within 30 days of your complaint.

If you want to determine if additional action is possible, you should discuss your problem with your own private attorney.

## **7. Who is in charge of the association?**

The members who own property in the development are in charge of the association. During the annual meeting of the membership, all members are invited to officially meet and vote for all or part of the board of directors, which operates the association. The board of directors' job is to preserve, enhance, and protect the value of the development, but it answers to the members. It is not unusual for the board to contract with a professional management company to run the day-to-day affairs of the association.

## **8. What is the board of directors and how are its members elected?**

The board of directors governs the association. Its members are elected yearly or less frequently, depending upon the terms mandated in the Bylaws of the association. The Bylaws also determine the number of directors. Directors are elected by the members (owners of property) of the association who vote for vacancies as they occur. (Normally, each lot or unit has one vote no matter how many people own it, with the notable exception that the subdivider may, for a time, have up to three votes for each lot or unit he/she owns.)

## **9. How can you serve on the association's board of directors?**

There are two ways to become a member of the board of directors. The first is to request that the association place your name on the election ballot so that other members of the association will have an opportunity to vote for you at the next annual meeting. The second way is to request that the board of directors consider appointing you to any interim vacancy on the board.

## **10. What are the responsibilities of the board of directors?**

The board has the ultimate responsibility for operating the association. That means it makes sure that the association's money is collected, its bills are paid, the association is operated efficiently, and violations of the rules of the association are addressed. For example, the board is responsible for reviewing the association's bank statements, preparing a budget, and distributing the budget (or budget summary) to the members prior to the beginning of the association's fiscal year. The board must also prepare a fiscal year-end financial statement for distribution to the members. There are numerous other things for which the board is responsible, as set forth in the association's CC&Rs, Bylaws, the Corporations Code and the Davis-Stirling Common Interest Development Act (California Civil Code Sections 1350 through 1376).

## **11. Are there other opportunities to volunteer in the association besides the board of directors?**

Usually, an association will have a number of committees that perform valuable functions. For example, the architectural committee oversees requests for modifications to properties in the development and generally attempts to make sure that modifications and other improvements are consistent with the existing architecture of the development. There may be other committees to join, depending on the type of development in which you live. An association may have a landscape committee to oversee landscaping. There may be a welcoming committee or an election committee which addresses the election of the board of directors. The specific number and types of committees are usually determined by the association's Bylaws, CC&Rs, and/or the board of directors.

## **12. How does the association pay its bills?**

Each association has a budget that is prepared, based on the common area obligations of the development, and distributed to all of its members. The budget determines how much money the association is going to need to operate for the following year. The association has the right to bill the members for their fair share of the budgeted amount. This billing is known as an assessment, which may be paid via monthly invoices, coupons supplied by the association, or some alternative method. Ideally, the association collects sufficient money through these assessments and pays the bills for the services and goods contemplated in the budget. If the assessments collected are insufficient to pay the bills, the board of directors is allowed to levy what is known as a special assessment. Without member approval, the total of special assessments in any fiscal year cannot exceed 5 percent of the gross budgeted expenses for that year.

By paying your fair share of the obligations of the association, through the budget and assessment process, you are paying for the current and long term maintenance obligations of the association. Of course, all of the other owners are doing so as well.

## **13. How is the amount of the monthly assessment determined?**

When the budget is prepared, the amounts necessary for the daily operation and long term reserves for maintenance and replacement are determined based on the level of service for which the association is both required and willing to pay. For example, sometimes there are specific items defined in the CC&Rs that require a certain level of maintenance by the association. Once the annual amount is determined, then it must be collected from the members in order for the association to operate. Each member's assessment is usually collected monthly, in 12 equal installments. Some associations collect assessments on a quarterly or annual basis. The CC&Rs will normally indicate the frequency of assessment collections.

## **14. Are there different types of assessments or fees?**

There are several types of assessments that may apply to your association. The California Civil Code defines assessments as either being regular or special. Regular assessments are needed for the operating (day-to-day) and reserve (long-term maintenance) activities of the association.

Special assessments are those levied by the association for major repairs, replacement, or new construction of the common area or for a one-time, unanticipated expense which cannot be covered by the regular assessment (e.g., insurance premiums that unexpectedly "sky rocket").

Note, a special assessment should not be confused with a monetary penalty levied by the association against an individual owner to reimburse the association for an expense such as damage to the common area, or imposed as a disciplinary measure for a violation of the rules and regulations.

Also, some CIDs establish user fees or special charges for uncustomary services and activities. Typically, they are imposed on an owner specifically benefiting from the service, such as an owner who wants to use the common area pool, clubhouse, or tennis courts to entertain private guests. The fees are usually on a pay as you go basis and generally cannot become a lien on the owner's unit or interest.

Some associations have other types of assessments designated as well. For example, an association may have a cable television fee, which is an assessment. Another association may have what is known as a reimbursement assessment which is actually a special assessment levied against an individual owner charging them for damage to the common area that occurs by virtue of an act by the owner or an owner's guest. The best place to look for the different types of assessments which may apply to a development is in the CC&Rs of the association.

## **15. Who can raise the amount of the assessment?**

The board of directors. However, the board must follow certain procedures mandated by California Civil Code Section 1366. Even if the governing documents are more restrictive, the board of directors may not raise the regular assessment more than 20 percent per year, without the approval of the owners. The board must circulate a budget to the membership no less than 45 days but no more than 60 days prior to the beginning of the fiscal year. If the budget indicates that an assessment increase greater than 20 percent is

necessary, a majority of the members of the association must approve the assessment. There are also provisions for a board to increase an assessment more than 20 percent without member approval in cases of emergency such as an extraordinary expense required by order of a court, or for repairs to the common area.

## **16. What happens if you do not pay your assessments?**

Usually, the first thing the association will do is send you a reminder letter. The law is specific in California regarding the due date of assessments and the overall process that an association must follow regarding delinquent assessments. The law states that if an assessment is not paid within 15 days of the due date, a delinquency occurs. At this point, the association can add a charge to your assessment in the form of a late fee in the amount of \$10.00 or ten percent of the monthly assessment amount; whichever is greater, unless the CC&Rs specify a lesser amount. Again, the law covering this area is quite clear and the board must follow these procedures. Once a year, the association will send each owner a copy of the assessment collection policy, which will tell you the amount of the late fee. In addition, if your assessment becomes over 30 days delinquent the association has the right to assess interest up to 12 percent per year on the balance which is owed and unpaid. Furthermore, if you fail to pay your assessments, the matter may be referred to an attorney or foreclosure service. The association has the right to lien your property for the amounts owed as well as other costs such as attorney's fees. Finally, the association can foreclose and take your property for your failure to pay assessments. Additionally, a personal judgment may be entered against you for failure to pay your assessment. As you can see, it is imperative that all owners pay their assessments in a timely manner. Failure by several owners to pay their assessment obligation could place the association in financial difficulty.

## **17. Are there other rules in an association?**

An association's board of directors may establish rules and regulations governing issues ranging from where you can park to what you can place on a balcony or deck. Associations frequently have guidelines and rules which specify the type of landscaping that may be installed or in some instances, not installed. Rules and regulations can be just as enforceable in an association as the CC&Rs, Bylaws and applicable statutes. The most frequent type of miscommunication between an owner and the association usually arises from an owner being unaware of the rules and regulations when the association attempts to enforce them. You can easily prevent such misunderstandings by making certain you have a current copy of the rules and regulations, which may be obtained from the association or the management company.

## **18. Can you make improvements to your home?**

The answer is generally yes, depending on the type of home that you have (condominium, townhome, detached, etc.). However, in addition to the conditions in the CC&Rs, most associations have established rules and regulations (also known as Architectural Guidelines), which must be followed in order to make any alterations or improvements. Generally, associations seek to assist their members who wish to improve their property as long as the improvement is performed in a manner consistent with the CC&Rs and rules and regulations.

## **19. Who do you contact if you are having problems with or questions regarding the home interior? The association common area? Neighbors? Paying assessments?**

The first place to look for answers to your questions is the CC&Rs. Then you should speak to a board member or, if your association has contracted with a management company, they may be able to provide assistance. Problems with the interior of a home normally are the responsibility of the owner. The association's common area is managed by the association, so the appropriate contact is either one of the association's board members or, if applicable, the management company. When there is a dispute between neighbors, sometimes it is best resolved between those owners. Where a dispute involves payment of assessments or an infraction of the association rules or CC&Rs, it would be appropriate to contact the board of directors and/or the management company.

## **20. What is a management company and what does it do?**

A management company is a separate business enterprise usually hired to act as the agent of the association. As an agent for the association, they take their direction specifically from the association's board of directors. Typical contractual responsibilities of the managing agent include a variety of services to the association, such as: collecting assessments, paying the association's bills, taking direction from the board of directors for enforcement of rules infractions, and obtaining various vendors to perform services. The managing agent also helps with the budget process and prepares meeting agendas and minutes for the board of directors. Further, the management company provides assistance to all parties in helping solve problems that can occur in CIDs. They advise the board of directors on how to comply with relevant California Civil Code requirements and assist with appropriate and timely compliance. When contracting with a management firm, it is important that the association be willing to pay for the level of services needed.

## **21. What happens if you rent your home in a common interest development?**

Nothing, as long as your tenant does not create a problem in the development. There is usually no restriction on rentals in a CID. Some CC&Rs require that a rental agreement acknowledge that the tenancy is subject to all of the rules and regulations of the association. Some associations' rules and regulations also require that you provide the association with a copy of the rental agreement. In most associations, the CC&Rs state that the owner of the property being rented is responsible for the conduct of the tenant. Naturally, it is in the best interest of all parties to prevent problem situations between tenants and owners of other units. If your tenant does damage to the common area or creates a nuisance (e.g., loud music or pet problems), the disturbance could become your problem.

## **22. What are your individual responsibilities as an owner living in a CID?**

Primarily, pay your assessments on time and abide by the CC&Rs and all other rules and regulations, which exist for community harmony.

## **23. What are your individual rights as an owner living in a CID?**

You have the right to participate in meetings of the board of directors and to be heard. You have the right to enter into dialogue with your association board of directors with regard to any problem you may perceive in the development. If a dispute arises between you and the association, subject to certain exceptions, you have the right to go through some form of alternative dispute resolution process before the matter reaches the court system. In some instances, you have the right to also go through such a process about your assessment if the association claims that you owe money, which you believe you do not owe.

## **24. Who do I contact when I decide to sell my home?**

You may wish to contact a real estate professional, the board of directors, the professional management company, and/or an escrow company for assistance with the many details. There are a number of documents that an individual owner is legally required to provide to a prospective purchaser of a unit in a CID. You will want to make sure that the buyer is aware of the rules and regulations of the association as well as the assessment obligation so there is not a problem or misunderstanding which could jeopardize the sale of your home.

## **Conclusion**

A successful and viable CID is generally one in which homeowners assume an active role in the association's function, not only by attending meetings, voting, and paying dues, but also by taking an active role in the actual functioning of the association by running for the elected offices, serving on committees, and generally participating in group activities. While the framework of the association is the governing documents, it can certainly be said that the "backbone" of the association is the active and involved membership.

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## APPENDIX D: CALIFORNIA HOMEOWNER BILL OF RIGHTS

*Written by Congress of California Seniors, Older Women's League, Sentinel Fair Housing, Consumers Union, Gray Panthers, Charles Egan Goff, September 21, 2001.*

On September 25<sup>th</sup> we will celebrate the 210<sup>th</sup> anniversary of the ratification of the federal Bill of Rights. To honor this occasion, we the undersigned have ratified ten resolutions comprising a Common Interest Development Homeowner Bill of Rights. Modeled on the Preamble and the Amendments to the U.S. Constitution, this document is meant to inspire public confidence in the concept of the CID, to ensure that this local government institution pursues benevolent goals, and to prevent abuses of power. Any changes to California law governing CIDS must conform to these inviolable principles. We resolve *THAT*,

- I. *Since* living in a common interest development (CID) requires an individual citizen to enter into a contract with a governing association, the prospective homeowner must give written informed consent to the terms of the association's rules and governing documents, but most especially to the Codes, Covenants, and Restrictions (CC&Rs) ten days before close of escrow. The governing documents comprise the contract between the association and the buyer.
- II. *No* CID board shall abridge a citizen's freedom of speech or of the press either through direct order or through intimidation or any kind of public abuse; that no board shall abridge the right of homeowner citizens to assemble peaceably or to petition the board for a speedy redress of grievances. No CID board shall abridge freedom of religion.
- III. *Boards* give a full, true and accurate accounting in writing of all association actions. No actions shall be taken in secret.
- IV. *Homeowner citizens* shall be entitled to speedy access to all association records, particularly to financial records, contracts, and records of governance at any time without exception.
- V. *Homeowner citizens* shall not be deprived of liberty or property, without speedy due process of law. Nor shall private property be taken without just compensation, specifically; there shall be no non-judicial foreclosure.
- VI. *Homeowner citizens* shall have the absolute right to vote on any changes to the terms of the original contract, i.e. changes in rules and amendments to governing documents or fines they are expected to pay. No fine shall exceed the true costs of the remedy.
- VII. *If accused* of violating rules, homeowner citizens are entitled to a speedy and public hearing by an impartial body not selected by the board; the impartial body shall determine the guilt or innocence of the accused and determine what fines, if any, be imposed; that the accused be informed of the nature and cause of the accusation; be confronted with witnesses; and have a compulsory process for obtaining witnesses, records, and advocates. Use of this system does not cancel a citizen's rights of appeal in the courts.

- VIII.** *Residents* shall be treated equally, and not in an arbitrary fashion, without reference to age, race, gender, cultural lifestyle, sexual orientation, national origin, marital status, disability or familial status as established by both state and federal laws and regulations.
- IX.** *Rules* enacted by a CID association and amendments to its governing documents must conform to all state and federal fair housing and health, safety and welfare laws.
- X.** *Elections* shall be in the hands of the homeowner citizens, not the CID board: ballots shall be secret; no homeowner citizen shall be denied the right to vote for failure to pay any fine or tax, including assessments; directors shall serve no more than two terms and be held accountable for their decisions; the makeup of the board shall reflect the makeup of the association membership.

## **APPENDIX E: CID RESOURCES**

### **PROFESSIONAL ASSOCIATIONS**

#### **Community Associations Institutes (CAI)**

<http://caionline.org>

In 1973 the Urban Land Institute (ULI) and the National Association of Homebuilders (NAHB) formed CAI to promote homeowner associations by providing builders, managers and homeowners with educational materials. Today CAI, a nonprofit organization, has 58 chapters in the U.S. and internationally. As of 1999 CAI represented approximately 16,500 CID stakeholders<sup>234</sup> from the following groups:

- Developers and builders;
- Community managers and management firms;
- Associations and individual homeowners;
- Public officials; and,
- Attorneys, accountants, reserve specialists, and other CID service providers.

CAI has a research component, the Community Associations Research Foundation (CAI-RF) which supports and conducts CIDs research.

The organization provides a variety of education opportunities for its members including:

- Books and newsletters;
- Conferences;
- Classes;
- Legal and political resources;
- Networking and advocate opportunities; and
- Certification programs for community association managers, lawyers, and reserve study specialists.

There are eight Chapters of CAI in California.

#### **California Legislation Action Committee (CLAC)**

<http://www.clac.org>

CLAC is the legislative advocacy group for the California chapters of CAI. It is based in Sacramento.

### **California Association of Community Managers (CACM)**

<http://www.cacm.org/>

CACM membership is made up of community association managers and CID professionals.

It provides education, training and encourages the professionalism of community association managers. The organization offers classes on a variety of topics of interest to community managers, which can lead to manager certification. CACM also is involved in the legislative process.

### **Executive Council of Homeowners (ECHO)**

<http://www.echo-ca.org>

ECHO was founded in 1972 by five San Jose based homeowners associations as a nonprofit corporation dedicated to assisting California HOAs. Its membership consists of 1,400 homeowner associations.

ECHO provides education to HOAs on financial and legal issues, insurance, maintenance, and management through the following forums:

- Newsletter;
- Publications;
- Conferences;
- Trade shows; and
- Seminars.

ECHO is also involved in legislative advocacy.

## **HOMEOWNER ADVOCACY GROUPS**

### **American Homeowners Resource Center**

<http://www.ahrc.com>

This organization's stated mission is to:

- Help preserve the constitutional and legal rights of homeowners,
- Provide information to homeowners on those rights,
- Help homeowners to protect and preserve those rights,
- Publicize violations of those rights, and
- Remedy abuses of those rights by education, mediation, legislation, litigation, and elections.

The website includes homeowner discussions, an extensive database of articles related to CID issues, and a directory of recommended service providers.

### **CID Homeowner Bill of Rights Coalition**

[writzy@aol.com](mailto:writzy@aol.com)

Phone 916.442.4474

The Coalition works to ensure CID homeowner civil rights by providing information and support in asserting these rights. They are active in introducing new California legislation to protect homeowner rights. The Coalition's founding members include the Congress of California Seniors, Consumers Union, Gray Panthers, Sentinel Fair Housing, the Older Women's League, Charles Egan Goff, and individual CID homeowners.

### **Homeowners Supporting Homeowners in Associations**

<http://www.hshia.org>

This is a grassroots site in Arizona. Its symbol is a flamingo in defiance of the restrictions in most CIDs that prohibit lawn decoration of this type. The site provides a posting site where homeowners can tell their stories and share their association-related frustrations.

### **Privatopia.Info**

<http://www.privatopia.info/>

News, analysis, commentary, and publications on the privatization of local government.

## **STATE RESOURCES**

### **Department of Real Estate**

The DRE provides the following publications for ten dollars a piece.

- *Operating Cost Manual for Homeowners Associations* Contains guidelines and worksheets for budget preparation and calculation of reserves and assessments.
- *Reserve Study Guidelines for Homeowner Association Budgets* Explains how to determine sufficient reserve funds.
- *Subdivision Public Report Application Guide* Provides instructions and explains what is required to apply for a subdivision public report.

## **STATE ONLINE INFORMATION**

### **Attorney General**

Nonprofit Mutual Benefit Corporations Complaint Information

<http://www.ag.ca.gov/consumers/complaints/npmb.htm>

## **Department of Real Estate**

*Frequently Asked Questions about Common Interest Developments*

[http://www.dre.ca.gov/faqs\\_cid.htm](http://www.dre.ca.gov/faqs_cid.htm)

*Living in a Common Interest Development-Brochure*

<http://www.dre.ca.gov/cidinfo.htm>

*Disclosures in Real Property Transactions*

<http://www.dre.cahwnet.gov/disclosures.htm#delivery%20of>

## **Secretary of State's Office**

*Organization of California Common Interest Development Corporations*

[http://www.ss.ca.gov/business/corp/corp\\_artscidinf.htm](http://www.ss.ca.gov/business/corp/corp_artscidinf.htm)

*California Corporations Code for Nonprofit Mutual Benefit Corporations*

<http://www.leginfo.ca.gov/cgi-bin/calawquery?codesection=corp&codebody=&hits=All>

## **PRIVATE INFORMATION SOURCES**

There are a number of publications that are available in the market place on a variety of HOA and CID topics. In addition many CID professionals and vendors produce publications and educational materials. Much of this information is on the web.

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- <sup>122</sup> Florida Administrative Code Annotated 61-20.503.
- <sup>123</sup> Florida Administrative Code Annotated 61-20.5081.
- <sup>124</sup> Nevada Revised Statutes Chapter 116.
- <sup>125</sup> Elden Hardy, Common Interest Development Ombudsman, State of Nevada, personal communication, November 2001.
- <sup>126</sup> Nevada Revised Statutes Chapter 116.1116.
- <sup>127</sup> Evan McKenzie, *Privatopia*, p. 132.
- <sup>128</sup> California Law Revision Commission, Study H-851, Memorandum 2001-31.
- <sup>129</sup> California Health and Safety Codes §§18150-18153.
- <sup>130</sup> George Macias, Administrator, California Mobile Home Ombudsman Program, personal communication, February 27, 2002.
- <sup>131</sup> Chris Anderson, Manager, Housing Standards Program, California Department of Housing and Community Development, personal communication, February 28, 2002.
- <sup>132</sup> George Macias, February 2002.
- <sup>133</sup> *Ibid.*
- <sup>134</sup> James L. Winokur. "Choice, Consent, and Citizenship in Common Interest Communities" in Stephen E. Barton and Carol J. Silverman, eds., *Common Interest Communities: Private Government and the Public Interest* (Berkeley: Institute of Governmental Studies Press, 1994), p. 89.
- <sup>135</sup> City of San Jose Department of Planning, Building, and Code Enforcement, *Staff Report*, file number PD 01-03-041, August 8, 2001.
- <sup>136</sup> Sacramento City Municipal Code §17.192.010.
- <sup>137</sup> City of Costa Mesa Municipal Code, Title 13, Chapter V, Article 2, §13-41 (d).
- <sup>138</sup> City of Fremont Municipal Code, Title VIII, Chapter 2, Article 21.3, §8-22135 (b) (1).
- <sup>139</sup> Carol Silverman, personal communication, October 2001.
- <sup>140</sup> Curtis C. Sproul, "Common Interest Community Associations, and Their Management Structure."
- <sup>141</sup> *Ibid.*
- <sup>142</sup> Stephen E. Barton and Carol J. Silverman, *Common Interest Homeowners' Associations Management Study*, p. 27.
- <sup>143</sup> Curtis C. Sproul, "Common Interest Community Associations, and Their Management Structure."
- <sup>144</sup> California Law Revision Commission, Study H-851, Memorandum 2001-55, p. 16.
- <sup>145</sup> David C. Drewes, "Putting the 'Community' Back in Common Interest Communities: A Proposal for Participation-Enhancing Procedural Review," *Columbia Law Review*, Vol 101, No. 2, March 2001, pp. 314-350.
- <sup>146</sup> Patrick A. Randolph, Jr., "Symposium: Common Interest Development Communities: Part II: Changing the Rules: Should Courts Limit the Power of Common Interest Communities to Alter Unit Owners' Privileges in the Face of Vested Expectations?" *Santa Clara Law Review*, Vol. 38, No. 4 (1998), pp.1082-1083.
- <sup>147</sup> Geri Kennedy, Community Financial Services, personal communication, September 27, 2001. Curtis C. Sproul, "Is California's Mutual Benefit Corporation Law the Appropriate Domicile for Community Associations?" *University of San Francisco Law Review*, Vol. 18, Summer 1984.
- <sup>148</sup> Stephen E. Barton and Carol J. Silverman, "Common Interest Communities: Private Government and the Public Interest Revisited," in Barton and Silverman, eds., *Common Interest Communities: Private Governments and the Public Interest*, p. 38.
- <sup>149</sup> California Law Revision Commission, Study H-851, Memorandum 2001-55.
- <sup>150</sup> Stephen E. Barton and Carol J. Silverman, *Common Interest Homeowners' Associations Management Study*.

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- <sup>151</sup> California Law Revision Commission, Study H-851, Memorandum 2001-55.
- <sup>152</sup> Curtis C. Sproul, "Common Interest Community Associations and Their Management Structure," p. 6.
- <sup>153</sup> California Civil Code § 1365.7
- <sup>154</sup> Evan McKenzie, *Privatopia*, p. 154.
- <sup>155</sup> Wayne S. Hyatt, "Putting the Community Back in Community Associations: An Action Plan" in *Community First!*, Bill Overton, PCAM, ed. (Alexandria, VA: Community Association Institute, 1999), p. 104.
- <sup>156</sup> California Business and Professions Code §11000, et. seq.
- <sup>157</sup> Stanley Scott, "The Homes Association: Will 'Private Government' Serve the Public Interest?" in Stephen E. Barton and Carol J. Silverman, eds., *Common Interest Communities: Private Governments and the Public Interest* (Berkeley: Institute of Governmental Studies Press, 1994), p. 24.
- <sup>158</sup> California Department of Real Estate, *Study of the Future Outlook of California Common Interest Developments*, p. V-18.
- <sup>159</sup> *Ibid.*, p. VI-5.
- <sup>160</sup> David Levy, personal communication, May 22, 2002.
- <sup>161</sup> Curtis C. Sproul, May 13, 2002.
- <sup>162</sup> Stephen E. Barton and Carol J. Silverman, *Common Interest Homeowners' Associations Management Study*, p. 5.
- <sup>163</sup> Sam Perrotti, Assistant Commissioner of Subdivisions, Department of Real Estate testifying at the Assembly Committee on Housing and Community Development, interim hearing: *Common Interest Developments: The Relationship Between Homeowners and Homeowner Associations*, November 29, 2001.
- <sup>164</sup> Patricia Arnold, October 2001.
- <sup>165</sup> Curtis C. Sproul, May 13, 2002.
- <sup>166</sup> Available from the California Department of Real Estate on-line at <http://www.dre.ca.gov/cidinfor.htm>.
- <sup>167</sup> Guy Puccio, Legislative Advocate, Executive Council of Homeowners (ECHO), personal communication, March 4, 2002.
- <sup>168</sup> Jacquie Berry, February 2002.
- <sup>169</sup> Robyn Boyer Stewart, October 2001.
- <sup>170</sup> David Levy, December 2001.
- <sup>171</sup> California Corporations Code §8216.
- <sup>172</sup> Mike Raymer, Attorney General's Public Inquiry Unit, and personal communication, Fall 2001.
- <sup>173</sup> David Levy, December 2001.
- <sup>174</sup> Stephen E. Barton and Carol J. Silverman, *Common Interest Homeowners' Associations Management Study*, p. 13.
- <sup>175</sup> The Gallup Organization, *National Survey of Community Association Homeowner Satisfaction*.
- <sup>176</sup> Stephen E. Barton and Carol J. Silverman, *Common Interest Homeowners' Associations Management Study*.
- <sup>177</sup> California Department of Real Estate, *Study of the Future Outlook of California Common Interest Developments*, p. V-3.
- <sup>178</sup> *Ibid.*
- <sup>179</sup> Kevin Davis, October 23, 2001.
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- <sup>182</sup> Elden Hardy, November 2001.
- <sup>183</sup> Robyn Boyer Stewart, October 2001.
- <sup>184</sup> Karen Conlon, October 2001.
- <sup>185</sup> Doug Christison, September 27, 2001.
- <sup>186</sup> Joel M. Kriger, "California Supreme Court Sets Standards for Judicial Review of Homeowner Association Board Decisions," *Community Association & Construction Defect Law Quarterly Newsletter*, Anderson & Kriger, fourth quarter, 1999, citing *Lamden v. La Jolla Shores Clubdominium Homeowners*. <http://www.a-k.com/q41999.pdf>
- <sup>187</sup> Karen Conlon, October 2001 and Boyer Stewart, October 2001.
- <sup>188</sup> Based on conversations with the Nevada Ombudsman's Office, November 2001 and the California Law Revision Commission, Study H-851, Memorandum 2002-10.
- <sup>189</sup> California Law Revision Commission, Study H-851, <<http://www.clrc.ca.gov/status.html>>.
- <sup>190</sup> Stephen E. Barton and Carol J. Silverman, *Common Interest Homeowners' Associations Management Study*.
- <sup>191</sup> Jacquie Berry, February 2002.
- <sup>192</sup> Katherine Rosenberry and Curtis C. Sproul, "Symposium: Common Interest Development Communities: Part I: A Comparison of California Common Interest Development Law and the Uniform Common Interest Ownership Act," *Santa Clara Law Review*, Vol. 38., No. 4 (1998), pp. 1009-1080.
- <sup>193</sup> For a longer discussion on this issue see California Law Revision Commission Study H-850, *Common Interest Development Law: Scope of Project (Background Study)*, Memorandum 2001-19, January 22, 2001, by Professor Susan French.
- <sup>194</sup> Ibid.
- <sup>195</sup> Ibid.
- <sup>196</sup> Doug Prehoda, October 3, 2001.
- <sup>197</sup> See the CLAC Web site under poll results <<http://www.clac.org/2-5.htm>>.
- <sup>198</sup> Jacquie Berry, February 2002.
- <sup>199</sup> Nevada Revised Statutes 116.41095.
- <sup>200</sup> Elden Hardy, November 2001.
- <sup>201</sup> California Department of Real Estate, *Study of the Future Outlook of California Common Interest Developments*.
- <sup>202</sup> Chris Pahule, January 2002, Stephen Young, Community Development Director, Sacramento Housing and Redevelopment Agency, personal communication, February 2002.
- <sup>203</sup> Jacquie Berry, February 2002.
- <sup>204</sup> David Levy, October 2001.
- <sup>205</sup> Mary Horton, May 22, 2002.
- <sup>206</sup> The section that allows the HOA to borrow from the reserve funds for other purposes is California Civil Code §1365.5 (c)(d).
- <sup>207</sup> Curtis C. Sproul, "Is California's Mutual Benefit Corporation Law the Appropriate Domicile for Community Associations?" *University of San Francisco Law Review*, Vol. 18, No. 4, Summer 1984, pp. 695-748.
- <sup>208</sup> California Law Revision Commission, Study H-850, Memorandum 2001-31.
- <sup>209</sup> Ibid.
- <sup>210</sup> City of Fremont Municipal Code §8-22135.
- <sup>211</sup> Karen Conlon, "Manager Certification. Do We Need It?" *Community Association & Construction Defect Law Quarterly Newsletter*, Anderson & Kriger, first quarter 2001 <<http://www.a-k.com/q12001.pdf>>.
- <sup>212</sup> Karen Conlon, October 2001.

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- <sup>214</sup> Robyn Boyer Stewart, October 2001.
- <sup>215</sup> California Health and Safety Code §18502.
- <sup>216</sup> California Assembly Select Committee on Common Interest Developments, *1990 Final Report* (California State Assembly, Sacramento, CA) p. 31.
- <sup>217</sup> Alan S. Becker & Gary A. Poliakoff, P.A., "Trends in Community Associations for the 21<sup>st</sup> Century," *Community Update*, January 2001. [http://becker-poliakoff.com/publications/newsletters/cu/jan01/trends\\_in\\_community.htm](http://becker-poliakoff.com/publications/newsletters/cu/jan01/trends_in_community.htm)
- <sup>218</sup> *Ibid.*
- <sup>219</sup> David Drewes, "Putting the 'Community' Back in Common Interest Communities."
- <sup>220</sup> Professor Katharine Rosenberry, written testimony, *Common Interest Development Issues after Nahrstedt: The Summary Report for the Interim Hearing of the Senate Committee on Housing and Land Use*, (Sacramento: The Committee, November 12, 1996) p. 30.
- <sup>221</sup> California Assembly Select Committee on Common Interest Subdivisions, *Final Report*, (Sacramento: The Committee, 1990).
- <sup>222</sup> *Ibid.*, p. 39.
- <sup>223</sup> California Senate Committee on Housing and Land Use, *Common Interest Development Issues after Nahrstedt: The Summary Report for the Interim Hearing of the Senate Committee on Housing and Land Use*, (Sacramento: The Committee, November 12, 1996).
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- <sup>225</sup> California Department of Real Estate, *Study of the Future Outlook of California Common Interest Developments*.
- <sup>226</sup> Helen E. Roland, *Residential Common Interest Developments: An Overview*, (Sacramento: California Research Bureau, 1998) < <http://www.library.ca.gov/CRB/98/06/98006.pdf> >.
- <sup>227</sup> Howard Yee, former consultant to the California Senate Committee on Housing and Land Use and staff for the Common Interest Development Working Group, personal communication, January 7, 2002.
- <sup>228</sup> Correspondence to the CLRC dated October 5, 1999 from Fredrick Pilot, President of Common Interest Consumer Project (CICP). Mr. Pilot states that CICP recommended a review of CID law to the CLRC based on the working groups failure. Nathaniel Sterling, Executive Secretary of CLRC, in his cover sheet to Mr. Pilot's correspondence—*First Supplement to Memorandum 99-58*, October 8, 1999—credits Mr. Pilot as "instrumental in getting the Commission to request authority to study common interest development law."
- <sup>229</sup> California Law Revision Commission, *1998-1999 Annual Report*, 28 Cal. L. Revision Comm'n Reports 679, 693-94 (1998).
- <sup>230</sup> California Resolution Chapter 81 of the Statutes of 1999 (ACR 17 1999).
- <sup>231</sup> Susan F. French, pp. 2-3.
- <sup>232</sup> *Ibid.*, p. 6.
- <sup>233</sup> California Law Revision Commission, Study H-851, Memorandum 2001-31.
- <sup>234</sup> Community Associations Institute, *Community Associations Factbook* (Alexandria, VA: The Institute, 1999).