

## Board Member Duties & Responsibilities

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### A. BOARD MEMBER OF A COMMUNITY ASSOCIATION

#### *What is a community association?*

A community association is a "common interest development". The California State Legislature first used this term with the adoption of the Davis-Stirling Common Interest Development Act in 1985. These housing developments are defined as condominium projects, planned developments, stock cooperative or community apartment projects. Each of these types of developments have "separate interests" wherein each owner has the exclusive right of ownership, use and occupancy of their "unit" as well as shared ownership in one or more "common areas". The separate interest in a planned development usually includes a separately owned lot or parcel of land. In a condominium project all land including the parcel lots and common area are commonly owned and the separate interest only includes the air space within the boundaries of the separate interest.

Use restrictions are an inherent part of any community association and are crucial to a stable planned environment. Restrictions on the use of the property in a community association may limit activities conducted in both the common area and the units. Use restrictions typically relate to things such as alteration to a building exterior, parking of vehicles and recreational equipment, the keeping of pets, and whether persons can conduct a business on the premises.

Use restrictions are not the only characteristic of common interest ownership. Ownership usually requires mandatory membership in an owners' association who elects a Board of Directors to run the association. This board is empowered to enforce the use restrictions as well as enact new rules governing the use and occupancy in the project. Because of the considerable power granted the board in the governing documents there is a potential for abuse of that power. Subordination of individual property rights to the collective judgment of the owners' association together with restrictions on the use of real property comprise the chief attributes of owning property in a common interest development. A court decision noted **"inherent in the condominium concept is the principle that to promote the health, happiness, and peace of mind of the majority of the unit owners since they are living in such close proximity and using facilities in common, each unit owner must give up a certain degree of freedom of choice which he or she might otherwise enjoy in separate, privately owned property."** Though the term used here is condominium, this concept would apply for any common interest development.

#### *How are community associations managed?*

Most associations are formed as non-profit mutual benefit corporations. In order to manage the business affairs of the association, the governing documents provide for the election of a Board of

Directors. The governing documents establish the number of directors to be elected. The number is usually odd (to prevent tie votes), with the number of members typically ranging from three to seven. An association can change the number of directors, but this will require an amendment of the documents, usually the By-Laws, but sometimes the CC&Rs also if they specify a number. In order to amend the documents you will need to review the governing documents. The number and percentage of votes necessary to amend the By-Laws is typically less than the CC&Rs. An amendment to the CC&Rs is not valid until it is recorded. The members elect the directors and the directors elect the officers. In small boards some of the positions are typically dual positions. In a three member board the offices of secretary and treasurer is usually held by the same director. The other two officers would be the President and the Vice-President. The governing documents will outline the duties of each office and specify the term. Most terms are either one or two years. In an association where the term is two years, the terms are many times staggered, allowing for only some terms to come up for election each year. This helps provide continuity on the board.

Board members are volunteers, performing their duties without the benefit of a salary. They can be reimbursed for expenses they incur in the course of carrying out their duties, however. The association should carry an insurance policy called a "D&O" policy to provide coverage for the board members in the event of a claim. A member is expected to act in the best interests of the association at all times. There will be times when a decision to do something which benefits the membership as a whole will conflict with what is best for you personally.

***Can we hire a manager to handle the association rather than the board?***

Your board may choose to hire a professional manager. The manager is not a substitute for a Board. The board may delegate duties to the manager, however the activities and affairs of the Association shall be under the ultimate direction of the Board of Directors. The manager is not a voting member of the association or the Board.

***Do Board members require special training? What are they expected to do?***

Many board members have never served on a board before and most have no special skills. The primary duties of a board member are:

1. To remain informed about the association's business at all times;
2. To attend meetings on a consistent basis. If you miss a meeting, obtain a copy of the draft minutes as soon as they are available. Talk to one of the other board members about the meeting;
3. Vote against actions, which you disagree with and have the minutes reflect your vote;
4. Have complete copies of the governing documents (CC&Rs, By-Laws, Articles of Incorporation, Rules & Regulations, if any). Read them thoroughly. Re-read them periodically;
5. Exercise diligence in carrying out and following through on responsibilities assumed or assigned to you.

Board members are not expected to be specialists or experts. To help you meet the expectations of the governing documents you should:

1. Consider a membership in a professional organization such as ECHO (The Executive Council of Homeowners) or CAI (Community Associations Institute). ECHO is a California based organization with its headquarters in San Jose. CAI is a national organization with a Bay Area Chapter in Oakland. ECHO and CAI have many excellent publications available for purchase in addition to their monthly newsletter, which you receive as part of your membership.
2. Purchase a copy of the statutes affecting associations. Some boards believe they only need to be concerned about what is in their documents. New laws and changes to existing ones are enacted annually. These laws are statutory and affect your association even if you have not yet amended your documents to reflect them.
3. Attend educational seminars. Many are geared specifically towards the new board member. In addition, ECHO holds an annual event each summer that offers a specific course curriculum for the new board member.
4. Hire experts to help you in the preparation of your budget, financial reports, reserve study and funding plan, as well as the preparation and distribution of the annual disclosures to your membership as required under the governing documents and California Civil Code. Seek the advise of an attorney who specializes in community association law. Select an insurance broker who specializes in community associations. He or she will advise you of insurance requirements under the state laws as well as your governing documents.
5. Resist the temptation to be a "popular board member". Prepare a realistic budget that addresses proper maintenance of the common areas as well as adequate funding of the reserve account. Do not reduce the annual funding to reserves to fund increased operating expenses.
6. Remember to run your association like the **multi-million business it is!**

#### **B. Legal Duties and Responsibilities:**

The Board has several legal obligations with respect to their role in running the Association's business and protecting and preserving the Association's assets. The Association's assets not only include the upkeep of the physical structures, but also the Association's operating and reserve funds, as well as properly planning and funding for future reserve expenditures. For almost two decades, all California common interest developments (meaning either condominiums or planned developments) have been required to obtain, maintain and update reserve studies. The reserve study must be reviewed annually as well as the proforma budget. In addition, the Board must disclose to the membership how the board intends to fund the unfunded liabilities.

### **Fiduciary Duty:**

The Board of Directors of any homeowners association owes a fiduciary duty to the membership to maintain and preserve the assets of the corporation. In a common interest development the assets of the corporation are the funds in the Association's account and the physical plant, e.g. the buildings, grounds and improvements.

In summary, the board of directors of a common interest development must make prudent business decisions that can withstand the scrutiny of comparison to other similar associations. It is not possible to make decision based upon how "we have always made decisions", but rather those decisions must be made in light of the standards of how other similar associations make decisions. Ignorance of the law or errors in judgment can bring claims of the board breaching its fiduciary duty. In order to avoid such claims, the board must follow the mandates of California law as they pertain to common interest developments and the board must make prudent business decisions that will withstand the scrutiny of how other associations make similar decisions.

### **Statutory Obligations:**

The Board of Directors of a common interest development is bound by all of the corporations code provisions pertaining to Mutual Benefit Corporations (Corporations Code § 7110-8817). In addition, over the past fifteen years, an entire section of the California Civil Code has been created to deal with common interest developments (Civil Code §1350-1376). This section of the Civil Code is commonly referred to as the "Davis Stirling Act".

Some of the "duties" under the Davis Stirling Act include the following:

1. **Maintenance of Common Area:** The Association, acting through the board of directors, is obligated to repair, maintain and replace the common area. (C.C. §1364)
2. **Assessments:** The Association, acting through the board, is obligated to "levy regular and special assessments sufficient to perform the Association's obligations under the governing documents". (C.C. §1366)
3. **Enforcement of Governing Documents:** The board has the duty to enforce the governing documents. (C.C. §1354)
4. **Reserve Study:** At least once every three years the Board must make a study of the reserve requirements of the development. This study must also be reviewed by the Board on an annual basis and adjusted at one year intervals as required. (C.C. §1365.5d)
5. **Proforma Budget:** On an annual basis (and within maximum and minimum time periods) the Board must prepare and distribute to the members detailed budgets, annual financial reports and annual required disclosures. (C.C. §1365)
6. **Quarterly Financial Review:** On a quarterly basis the Board must review a reconciliation of the association's actual financial performance to the performance forecasted in the budget. (C.C. § 1365.5)

In addition to the above, the Davis Stirling Act mandates that the Association, acting through its board of directors, distribute certain documents to the membership. Some of those requirements including the following:

1. **Proforma Budget:** 45 to 60 days prior to beginning of the fiscal year, the Association must distribute a proforma operating budget or a summary of the proforma budget. (C.C. §1365a&c)

2. **Collection Policy:** The Association, acting through the board, must deliver to the members, on an annual basis, a statement describing the association's policies and practices in enforcing lien rights and other legal remedies to collect delinquent assessments. This disclosure must be done within 60 days before the start of the fiscal year. (C.C. § 1365d) Also, effective January 1, 2003, the Board must deliver a Notice to all owners at least sixty days prior to the commencement of the fiscal year. The notice must be printed in 12-point font and has to provide specific language as stated in the statute (C.C. § 1365.1)

3. **Insurance:** The amounts of General Liability Insurance and Directors and Officers Liability insurance coverage maintained by the Association must be distributed upon issuance or renewal of policies, but no less than annually. (C.C. §1365.9c)

4. **Transfer of Reserve Funds:** If any reserve funds are "borrowed" or used to pay for operating expenses or expenses not designated in the reserve study, the Association must notify the membership at the next available meeting and they must provide a plan for the repayment of those funds within a twelve month period, or provide a justification as to why the funds can not be fully repaid in that time period. (C.C. §1365.5)

5. **Fine policy:** At the time that a fine policy is adopted or revised, the policy must be distributed to the membership in order to be effective. The fine policy, if it has not been revised, should be distributed annually. (C.C. §1363i)

6. **Alternative Dispute Resolution Requirements:** 45 to 60 days prior to beginning of the fiscal year, or in any general membership mailing during the year, the Association must distribute a summary of the requirements of this code section which mandates that an attempt be made to conduct some form of alternative dispute resolution prior to the filing of a claim to enforce the Declaration. (C.C. §1354i)

7. **New Buyer Disclosures:** The Association, acting through its managerial personnel, is obligated to furnish selling owners with copies of governing documents and financial information so that the seller can provide this information to prospective purchasers. A reasonable charge for compiling this information is allowable. It is generally good practice to disclose any material information that could impact the financial condition of the association. The board has a duty to disclose financial matters, such as borrowing from the reserves, or underfunded reserves, as well as to disclose known defect or problems in the common area. In addition, the Association must disclose any change in regular assessments or an anticipated special assessment, which the board has approved but not yet due and

payable. The Association is also allowed to disclose any outstanding violations of the CC&Rs or governing documents effecting the unit and/or the unit owner that is in escrow. (C.C. §1368)

Further, the membership is allowed to review the annual financial report and the corporations minutes. Under **Corporations Code § 8333, the books and records** of the association, including the written minutes, must be open to inspection by any member at any reasonable time for a purpose reasonably related to a member's interests as a member of the Association. Additionally, the minutes must be made available to the members within 30 days of the meeting and that upon the member's request for and upon reimbursement of reasonable cost for making copies, the requested minutes shall be made available. Owners must be notified, at least annually, of their right to have copies of the minutes of the board of directors' meetings and how and where the minutes may be obtained.

The right to review records is expanding on January 1, 2004. AB 104 was introduced to clarify the inspection rights of owners, but failed to define "accounting books and records" and "minutes of proceedings". Based upon experience, there is no clear guideline as to what is included in "accounting books and records". Does it include copies of cancelled checks? Some say "yes", other lawyers say it is not that broad. Portions of documents can be withheld (redacted) if they are private or privileged information, however, compensation of employees must be disclosed. The Association can obtain an injunction if an owner is abusing the process, but the statute also provides that the Association will pay for the recovery of the owner's attorney's fees and civil penalties if it unlawfully withholds records.

**Civil Code §1363.05, the "Common Interest Development Open Meeting Act"** also governs how meetings must be conducted. In summary, this section requires that all meetings of the board of directors be open to the membership, excepting executive session and unless the bylaws provide the date and time of meetings, or a longer notice period, that the members be provided at least four days notice of time and place of a meeting (excepting emergency meetings). The board must also provide for a portion of the meeting to allow member comments in an open forum context. The time can be limited by the board, it must be part of every meeting.

In addition to the above, **Civil Code §1352.5** requires all homeowners associations, including its managing agent, to attach a cover sheet to any governing document distributed from January 1, 2000 forward. That law was modified in the year 2000, yet it still mandates that a cover sheet must contain certain language. This law also has other requirements expanding the area of prohibited discrimination to include a new protective class of persons based upon "source of income". This was primarily generated to preclude any limitation on renting to people using Section 8 vouchers, but it could have more far-reaching implications.

**Civil Code Section 1363, Discipline of Members.** This law mandates certain procedures that associations must use with regard to imposing fines on members. This law requires that the Board of Directors notify a member of a hearing at least fifteen (15) days prior to the meeting/hearing. It therefore **REQUIRES** that there be a "hearing" **BEFORE** a fine can be imposed. The notification is required to contain the date, time and place of the meeting/hearing, the nature of the alleged violation for which the member is being disciplined and a statement that the member has the right to attend and address the board at the meeting/hearing.

If the Board imposes ANY disciplinary action at the meeting/hearing, it MUST notify the member by personal delivery or first class mail within ten (10) days following the action. Unless the Board of Directors meets the requirements of this provision, the disciplinary action is not effective and can not be enforced. It also requires that any outstanding fines be disclosed in connection with any escrow disclosures. The real implication is the need to follow the notice requirements, both before and after the hearing, and to preserve a paper trail (including proof of mailing) if the Association intends to be able to collect the fine at close of escrow. The main things to remember is that absent the proof that the hearing notice was provided at least fifteen days before the hearing and that notice of action was mailed within ten days of the board's decision, the fine is not enforceable.

**Pet policies.** A new "pet law" that impacts common interest developments and mobile home parks became effective in January of 2001. If the Association's documents prohibit pets all together, such a provision is enforceable UNTIL the Association makes any changes/revisions to it "governing documents". This means that if a "rule" is changed, then the prohibition is no longer enforceable and the Association shall be required to allow no more than ONE pet per household. Association's with poundage limitations and other such restrictions may want to re-visit their pet restrictions in light of this new law as it may be helpful in "fine-tuning" a previously ambiguous regulation.

**Non-Commercial Signs.** AB 1525 was signed into law and will go into effect on January 1, 2004. It will prohibit associations from regulating any non-commercial signs, posters, or banners on an owners lot, or unit, except for health and safety reasons. It expressly over-rides provisions in private covenants (CC&Rs) prohibiting signs, other than for sale and rent signs. The size can be up to nine square feet, and non commercial flags and banners may be up to 15 sq. ft.

**Rules.** New legislation, effective January 1, 2004, defines "operating rules" and makes it defines the procedure that the association must follow in order to adopt and/or enforce such rules. "Operating Rules" relate to rules governing management and operation of the common interest development, or the conduct of the business affairs of the association. An operating rule will only be valid, and enforceable if the following is satisfied:

- (a) The rule is in writing;
- (b) The rule is within the Board's authority, as conferred by law or the governing documents;
- (c) The rule is not inconsistent with governing law and/or the governing documents;
- (d) The rule is adopted in good faith; and,
- (e) The rule is reasonable.

The proposed rule must be distributed, in writing, to all owners at least 30 days before making the rule change. The notice to owners must include the text of the proposed rule change and a description of the purpose and effect of the proposed rule change. The rule change must be made at a meeting of the board of directors, and must allow public comment from owners. Once

approved by the board, and as soon as possible, but no more than 15 days after the meeting at which the rule change was approved, the board shall deliver notice of the rule change to all owners.

**Board Action.** It is not always the case that the Board will vote unanimously for any particular action. However, once a motion is made by the board, and passed by the appropriate vote, the entire board should support that decision as the Association's decision. Publicly undercutting, and criticizing of board decision by Board members is a potential breach of fiduciary duty and should be addressed by the Board. If a Board member objects to the Board action, the member should vote "NO". The minutes should accurately reflect the votes of the Board member.

An Association is generally a corporation which will have ongoing liability for the business decisions which any or all of its Board of Directors make. Therefore, it is critical to properly document the decisions of the Board and, once the decisions are made, for each individual Board members to support the decisions of the whole. The California Supreme Court in the case, *Lamden v. La Jolla Shores Clubdominium Association (1999)*, set out the new "deferential standard" for reviewing board decisions. The court in *Lamden* said that courts should defer to a board's authority and presumed expertise in discretionary decisions regarding the maintenance and repair of common interest development, provided that the decisions are based upon reasonable investigation, made in good faith and with regard to the best interest of the association, and are within the scope of authority granted to the board under the governing documents and relevant statutes.

Personal liability for individual Board members is not very common because most decisions are made within the scope and responsibility of the Board, which provides the individuals with a right to indemnification. However, if a Board member acts outside the scope of the Board's authority, or in disregard of Board action, then the cover of protection may be lifted from the individual.

**Insurance coverage for Associations.** It is becoming increasingly more difficult for Associations to obtain coverage for property damage, liability claims and protection for officers and directors. The number of different insurance companies that will cover such claims is rapidly diminishing in California. Many Associations are either being cancelled or their coverage will only renewed if the insurance deductible is significantly increased. It was quite common that most common interest development policies carried a \$1,000 deductible on any property damage claim.

Typically, the Association would have an Association rule or policy that provides that the unit owner of the unit damaged pays for the deductible. Such a policy is increasingly more important because most deductibles are being increased from \$1,000 to \$2,500, \$5,000 and I know of one Association that could only find coverage if it agreed to a \$10,000 deductible. This means that only those large claims, such as a fire, will be covered by the Association's master policy.

As a result, a clearly communicated policy to all owners must be drafted to ensure that the Association doesn't have to specially assess every time there is a burst pipe, toilet overflow or roof leak. It should be anticipated that most, if not all, of those claims, will not be covered by the Association's Master Policy.