SWEDELSON GOTTLIEB
Community Association Attorneys

NEW DAVIS-STIRLING ACT EXPLAINED
FROM THE COMMUNITY ASSOCIATION ATTORNEYS AT SWEDELSONGOTTLIEB

As Carole King famously sang about the earth moving under her feet in *Tapestry,* one of the best selling albums of all time, the ground under the feet of many California community association board members, managers, lawyers and others who live in or work with California community associations is going to shift on January 1st, 2014. Unless you're Rip Van Winkle, you know that the business of operating and managing California condominiums, planned developments and stock cooperatives will be dealt with under a new set of laws after January 1st. This "earthquake" (we are in California) is thanks to Assembly Bill 805, signed into law by Governor Brown in late 2012, delaying enactment until January 1, 2014, giving us a year to get ready) which revised and reorganized the Davis-Stirling Common Interest Development Act (the "Act"). This redo of the original 1985 Act (the "old Act") and the patch job of more than fifty amendments the Legislature has passed along the way has been a long time coming and was sorely needed.

The intent of the new Act is to simplify, clarify, and remedy inconsistencies. It provides helpful new definitions and standardized terms. Similar issues are grouped together in shorter sections instead of scattered as they were in the old Act. And there are no sub-sections in the new Act, making it easier to find what section you may be looking for.

Below is a summary of some of the more important changes and new provisions. To help you navigate through all of the specific changes, SwedelsonGottlieb has prepared a Conversion Table that compares the old and new sections of the Act. You may visit lawforhoas.com to view the Table online or contact our office for a laminated hard copy. The on-line version of the Conversion Table provides the sections from the old Act with the corresponding section of the new Act as well as a description of the subject matter and in many cases a link to the new Act section.

The new Act applies to residential community associations only; non-residential, commercial and industrial associations now have their own act. So nothing in this article applies to a non-residential association.

HIERARCHY OF GOVERNING DOCUMENTS

The old Act never addressed the hierarchy of the Governing Documents and this led to some confusion and disputes. New Civil Code §4205 states explicitly that the governing documents may not include provisions that are inconsistent with California law, and that if there is any inconsistency between the governing documents and the law, California law controls. This should eliminate divergent opinions on these matters.

The new Act also states that if there are any inconsistencies between the articles of incorporation and the CC&Rs, the CC&Rs

will control. If there is an inconsistency between the Bylaws and the Articles of Incorporation, the Articles of Incorporation will control. The new Act specifically provides that an association's operating rules cannot have a provision that is inconsistent with the declaration, articles of incorporation, or bylaws. But the new Act does not address the Condominium Plan and whether it controls over inconsistencies with the CC&Rs. And sometimes, despite the best of intentions, there are inconsistencies.

AMENDING GOVERNING DOCUMENTS TO CONFORM TO THE NEW ACT

The Board of Directors is authorized to amend the governing documents to correct cross-references to the old Act. The new Act addresses the fact that many associations' Governing Documents refer to sections of the old Act (and sometimes older sections of the Civil Code) that as of January 2014 will be repealed and no longer exist. To avoid confusion (and there will be confusion), the new Act allows a board to amend the Governing Documents for the sole purpose of correcting cross-references to the repealed sections of the former Act by adopting a board resolution that shows the correction. The new Act also provides for the "correction" of the CC&Rs to show the new statutory cross-references, but only so long as a copy of the board's resolution authorizing the correction is recorded along with the restated declaration. While the board of directors has the power to make these amendments without the vote of the owners, we suggest that boards work with the association's legal counsel to ensure that the process is handled properly. And, for the record, there is no requirement that an association amend its CCRs. References to the old Act do not invalidate the CC&Rs. But amending the CC&Rs to change the Code sections will likely eliminate some confusion.

"Governing Documents" Is Now Added to Association Records

The old Act, at Civil Code §1365.2, provides the list of records to which an owner is entitled on demand, but that list does not include the Governing Documents. Pursuant to the new Act §5200(a)(11), Governing Documents are now included.

ANNUAL POLICY STATEMENT AND ANNUAL BUDGET REPORT

The new Act stipulates that associations must create two important new documents, **t**he **ANNUAL BUDGET REPORT** (Civil Code §5300) and the **ANNUAL POLICY STATEMENT** (Civil Code §5310).

The new Act requires community associations to prepare and deliver to owners these two new documents, much of which includes material and disclosures associations were previously required to send out as part of the year-end mailing to the members. These take the place of the requirement under old Act §1365 and §1365.5 for the distribution of financial and reserve information, and Annual Disclosures, such as the collection policy, summary of insurance, architectural review procedures, fines and discipline policies, etc., some of which are found in various sections of the old Act. These disclosures or a summary of same, under the new Act, are required to be delivered to the owners

within 30 to 90 days before the end of the fiscal year. Delivery is to be by "individual delivery" pursuant to new Civil Code §4040.

As with the old Act, which allows the association/board to decide whether to send homeowners a complete summary of the Pro Forma Operating Budget—the "Annual Budget Report," under the new Act—the board/association can opt to send a summary of both the Annual Budget Report and the Annual Policy Statement, although members may request the complete document.

COMMUNICATION AND NOTICES

The new Act now defines an **"INDIVIDUAL NOTICE"** as a notice that an association provides to a specific owner when the Act or an association's Governing Documents require it. **Individual Notice** can be delivered by:

- **"Snail" Mail, U.S. Post Office**
  First-class mail, postage prepaid.
  Registered mail.
  Certified mail.
  Express mail.
- **Overnight Mail, Express Service Carrier**
  For example, FedEx, UPS
- **Email, Facsimile, or Other Electronic Means**
  The recipient must consent *in writing* to this method of delivery.

We expect that many associations will be asking owners to consent to email notifications. Without such written consent, in all cases, any **Individual Notice** must be addressed (and sent by first-class mail) to the recipient at the address last shown on the books of the association. It must also be sent to a secondary address if the member has requested it.

"GENERAL NOTICES" are defined by the new Act as notices from the association to the entire membership. A **General Notice** can be delivered:

- By **Posting** the printed document in a prominent location that is accessible to all owners, if the location has been designated for posting of General Notices by the association in the **Annual Policy Statement.** Pursuant to new Civil Code §5310(a)(3), an association can include within its **Annual Policy Statement** the location, if any, designated for posting of General Notices to the membership. See "Annual Policy Statement."
- In a **Billing Statement**.
- In a **Newsletter**.
- Via **Television**, if the association broadcasts television programs for the purpose of distributing information from the association to its members.

"**DELIVERED TO AN ASSOCIATION**" is a new definition. It means that any document that can be delivered to an association must be delivered to the person designated in the **Annual Policy Statement**. If such person is not designated in the Annual Policy Statement, the statute defaults to the association president or treasurer for the entire year.

ELECTIONS

Text of Proposed Document Amendments

The new Act adds a requirement that when members vote on a proposed amendment to the governing documents, the association must provide them with the actual text of the proposed amendment. Although this was not required previously, most attorneys provided this information to the board to send to the members. Now it is required.

Reversal of Operating Rule Changes

Under the old Act, members of an association could request a special meeting to vote on whether to reverse an operating rule recently enacted by the board. This authority was actually enacted before major changes to the election law were added to the old Act. The new Act, now Civil Code §4365, clears up that provision by replacing confusing references to the Corporations Code with references to the secret ballot two-envelope procedure that is required for most community association elections.

Majority of A Quorum

"Majority of a quorum" is now defined as "a majority of those [owners] voting in a vote wherein at least a quorum of the owners participate." This definition is in new Civil Code §4070, which makes it consistent with Corporations Code §5034.

The new provision regarding homeowners' reversal of a rule change (new Civil Code §4365) is one of many in the new Act that require the affirmative vote of a "majority of a quorum" of the members/owners. "Majority of a quorum" has historically been a confusing term. So hopefully this new definition will help eliminate confusion.

Application of Secret Ballot Process/Procedure

Under the old Act, the secret ballot process, which includes utilizing two envelopes, had to be used for votes or elections dealing with assessments or special assessments where a vote was required, for the election and removal of directors, for amendments to the governing documents, or relating to the grant of exclusive use of a common area. Other decisions made by a vote of the owners did not require the secret ballot process. However, the new Act allows associations to choose to use the two-envelope secret ballot process for other types of votes or elections, *but only if the association includes this requirement in its election rules.*

Notice of Election Results

The old Act requires that the results of an election or a vote of the owners be "publicized" in a "communication directed to all members." New Civil Code §5120(b) eliminates the ambiguity in the old Act by providing a definition for a writing, and establishes that such notice can be sent by General Notice.

Custody of Ballots

The new Act removes the conflict between the old Act §1363.09, and Corporations Code §7527 regarding how long, after an election, the ballots should be held in case the election is challenged. The old Act required the inspector of election to retain

custody of the ballots for 9 months after the election, although members could contest the election for 12 months. The new Act removes the conflict by requiring that the ballots be retained by the inspector of elections for the 12-month period of time to challenge the election. After that, the inspector of election turns the ballot materials over to the association, which is not required to keep the record for longer than the 1-year period.

Campaign Communications
Under the old Act, association moneys could not be used for campaign communications. The old Act defines "campaign communications" as expressly advocating the election or defeat of any candidate who is on the ballot, or including the photograph or prominently featuring the name of any candidate on a communication from the association or board, except in the ballot and ballot materials, within thirty days of the election. The new Act creates an exception. Now the inclusion of a candidate's name or photograph in a communication that is required to be provided to owners would not be considered a violation of the Act. A good example of this would be the meeting Minutes, which would not be prohibited because Minutes include the name of a candidate in an election.

COMMON AREA: Right of Access, Use, and Modification of the Separate interests and Grant of Exclusive Use

Right of Access to Separate Interest
Under the old Act, under most circumstances, associations were prohibited from denying an owner physical access to the owner's separate interest of their unit or property. New Civil Code §4510 provides that residents, owners, and occupants have the same right to access their separate interest (unit, home, etc.) as well as rights to use the common areas (pool, gym, other recreational facilities).

Restrictions on Certain Uses of An Owner's Property
The new Act still prohibits associations from restricting certain homeowner's rights, such as the right to display a flag or post a sign (subject to statutory restrictions), even if these activities are prohibited by the association's Governing Documents. Under new Civil Code §4700, these prohibitions will remain. They will just be easier to find. Previously, they were scattered throughout the Code. Now they are together in one section. In addition, new Civil Code Section 4700 refers to other Code sections applicable to community associations and related to property use that are not included in the new Act, including Code sections relating to signs, solar energy systems, day care, etc.

Owner Modifications of Separate Interest
Under the existing Act, a condominium owner is entitled to make changes to their separate interest, which is their unit, subject to certain limitations. The Civil Code also allows owners to make modifications necessary to accommodate their disability. Under the old Act, these provisions referenced changes to a "unit" in a condominium project. New Civil Code §4760 revises these sections of the Act so that they apply to a separate interest in any

type of community association. As with the old Act, the new Act carries over the requirement that associations make "reasonable accommodations" for handicapped or disabled residents, which is a requirement of both state and federal housing laws. The new Act makes it clear that these accommodations are made at the owner's and not the association's expense. This should be helpful when dealing with an owner who insists their association modify the common area at the association's expense to accommodate their disability.

Grant of Exclusive Use of Common Area
Under the old Act, under most circumstances, associations had to obtain the approval of at least 67% of the association's membership before the board would grant an individual owner the right to exclusive use of a portion of the common area. New Civil Code §4600 clarifies that this requirement applies to *both* the common area owned by the association, as well as the common area owned by the members as tenants in common. The new Act makes it clear that it applies to an association's grant of exclusive use of a common area, no matter how the common area is owned; i.e., tenants in common or owned by the association.

The new Act provides additional exceptions for when an association may grant access to common areas, *but only if the CC&Rs expressly provide for this assignment.* These include, but are not limited to, grants:

- Necessary to accommodate a resident's disability.
- Required by law.
- Dealing with assignment of a parking space.
- Dealing with assignment of a storage unit.
- Dealing with other amenities.

CHANGES RELATING TO BOARD OF DIRECTORS MEETINGS AND CONFLICTS OF INTEREST

Notice of Board Meetings
Corporations Code §7211(a) provides that if a corporation's bylaws specify a date, time, and place for a board meeting, no further notice is required. This conflicts with the old Act's requirements regarding notice and agenda for board meetings. To address this conflict, new Civil Code §4920 provides that with the exception of an executive session or emergency board meetings, all regular session board meeting should be noticed at least four days before the meeting. Emergency board meetings are not required to be noticed to the members.

When it comes to giving notice of the board meeting, the old Act required that the notice be posted in the common area. New Civil Code §4920(b)(c) changes this and provides that notice be given by "general delivery." New Civil Code §4045 defines General Notice as including personal notice (new Civil Code §4040) as well as including the notice in the billing statement, newsletter, posting it in an area of general accessibility, in a place designated for that purpose in the Annual Policy Statement, and/or on association-generated television programming. Civil Code §4045(b) provides that owners who have requested individual

delivery are still entitled to receive notice in that fashion.

Definition of "Meeting."
The new Act (Civil Code Section 4090) changes the definition of a "board meeting." Instead of defining a board meeting as a congregation at the same time and place, of "a majority of the members of the board," the new Act defines a board meeting as the congregation of a sufficient "number of directors to establish a quorum."

Conflicts of Interest
We've all been in this situation: a director or community member with a conflict of interest refused to acknowledge it or disqualify him/herself, and there was nothing the association could do because it wasn't covered by the Act. Now it is. New Civil Code §5350 lists six matters on which a director or a member of a committee is not allowed to vote:

(1) Discipline of the director/community member.

(2) Issues relating to an assessment levied against the director or committee member for damages to the common area/facilities.

(3) A request from or by a director/community member for a payment plan for unpaid assessments.

(4) A vote on the decision as to whether to foreclose on a lien on a separate interest of a director/community member.

(5) Proposed architectural modifications to the separate interest of the director/ community member.

(6) A grant of exclusive use of the common area to the director/community member.

The inclusion of a committee member in this section is also helpful and would obviously only apply to committees where the member has the authority to decide on any of the listed issues. This would certainly apply, for example, to a member of an architectural committee whose own application has been submitted for consideration by the committee.

Previously, because the Act did not deal with conflicts and disqualification, we had to make do with Corporations Code §7223 and §7224. However, the language in those sections did not really apply directly to community associations. It said that disqualification depended on whether the director has "a material financial interest" in the transaction or subject to be decided upon. The new Act should help associations.

CHANGES RELATING TO RECORDS AND NOTICES

Written Request for Documents
As with the old Act, new Civil Code §5260 provides that a request from an owner to inspect an association's documents or records must be in writing and delivered to the association. What's new is Civil Code §4035, which designates who has to receive the request: the "person designated in the Annual Policy Statement . . . to receive documents on behalf of the association. If no person has been designated to receive documents, the document shall be

delivered to the president or secretary of the association."

The documents an association is required to deliver pursuant to new Civil Code §4035 are:

- Request to change information on the membership list.
- Request to add or remove a secondary address for delivery of Individual Notices to the member.
- Request for individual delivery, or to cancel a prior request for individual delivery.
- Request to opt out of having the owner's name and contact information included on the membership list.
- Request to receive a full copy of the specified Annual Budget Report or Annual Policy Statement.
- Request to receive all reports in full.

ASSESSMENTS AND DELINQUENT ASSESSMENT COLLECTION

Increases in Assessments
Under the old Act, an association could increase assessments pursuant to the procedures set out in either the Governing Documents or the old Act. Most associations choose to rely on the Civil Code, which allows for increases up to 20% over the prior year's assessment. However, the old Act required that the association timely send out the Pro Forma Operating Budget with all of the requisite notices and disclosures in order to take advantage of the ability to increase the assessments by 20%.

The new Act changes this and allows for an annual increase in regular assessments, but only if the board/association has complied and distributed the Annual Budget Report. No longer can an association merely comply with the requirements in the Governing Documents. In reality, the requirements of the Annual Budget Report are not very different from the requirements for the Pro Forma Operating Budget, so this change should not create problems for most associations.

Vote of Owners to Obtain Approval Before Increasing Regular Assessments By More Than 20% or Imposing A Special Assessment That Is More Than 5% of the Association's Budgeted Gross Expenses For the Fiscal Year.
The new Act clarifies that the secret ballot two-envelope process must be used to obtain owner approval for increasing regular assessments by more than 20%, or special assessments that are in excess of 5% of the association's budgeted gross expenses. While some suggest that this is a clarification, most of us already thought that the secret ballot process applied to that vote.

As with the old Act, the new Act also provides that associations are required to identify a mailing address for overnight payment of assessments. Under the new Act, this is to be set out in the Annual Policy Statement.

Accounting for Reserve Fund Expenditures For Construction Defect Litigation
Under the old Act, Civil Code §1365.5(d) when the board expends reserve funds for

construction defect litigation, the board is required to notify the owners of the decision and of the availability of an accounting of those expenses by the next general mailing to the owners. Pursuant to new Civil Code §5200(a)(12), this document is to be part of the "association records" and new Civil Code §5520 provides "General Notice" to the owners. That notice is to be sent by any of the methods set forth in new Civil Code §4045. The new Act provides more options of providing notice to the owners and this includes providing notices with billing statements, postings, in common areas, newsletters, association television, etc.

ENFORCEMENT AND DISPUTE RESOLUTION

Schedule of Monetary Penalties
The old Act required that the association had to deliver to the members a schedule outlining monetary fines for violating the governing documents, but it did not have to be on an annual basis. The new Act, new Civil Code §5850, simplifies delivery of the fine schedule: the policy regarding fines has to be included in the Annual Policy Statement. If the schedule of fines is amended, it must be delivered to the members pursuant to the General Notice provisions of the new Act. The new Act also references violations by tenants which was not referenced in the old Act.

Due Process/Opportunity to Be Heard
Before an association can impose discipline (a penalty or fine) on a member for a violation of the Governing Documents, the board/association must provide the owner with notice of the alleged violation and an opportunity to be heard by the board. This is called "due process"; it is a right guaranteed under our nation's Constitution. Under the new Act, the notice of hearing must be provided to an owner by Individual Notice. The new law clarifies that this notice also applies when the association seeks to impose a monetary charge on an owner to reimburse the association for damage to common area facilities caused by the owner or the member's guest or tenant.

Alternative Dispute Resolution
Under the old Act, Alternative Dispute Resolution ("ADR") must be offered to an owner before a civil action is filed by or against an association to enforce the Governing Documents, the Act, or a provision of the Corporations Code. The party that receives the ADR request, whether it is the association or the owner, is not required to accept the offer. However, if the ADR offer is not accepted, then, in an action in which fees and costs may be awarded, the court may consider the refusal to engage in ADR when determining the amount of the fee award. Under the old Act, this only applied in an action to enforce the Governing Documents. Under the new Act, this would apply to any action to which fees and costs may be awarded, which may include actions to enforce the Governing Documents or certain sections of the Civil Code.

WHO SPONSORED THE ACT AND WHY
The California Law Revision Commission (the "CLRC") sponsored the new Act. The CLRC's role is to revise laws that they have determined need revising. The old Act, which was first adopted in 1985, has had

over fifty amendments, and many of the code sections were lengthy and confusing and not necessarily in proper order. The CLRC felt that it would be appropriate to organize the Act better, to make it easier to understand. No one can dispute their reasoning.

Although the CLRC said that new Act was intended to clarify and simplify common interest law, it will take some time and effort for all of us to fully understand the reorganized new Act and to be able to locate the sections of the Act that we used to reference on a regular basis.

The CLRC also indicated that because more than 50% of all California community associations have 50 units or less, and that these smaller associations are typically operated without professional management or legal assistance, which is likely true, these smaller associations would not be as invested in the old Act (at least not like those of us who review and cite the Act daily) and that the small associations and their board members would benefit from a law that is better organized and easier to use.

Is it everything we hoped for? In a word: No. But it is a big step in the right direction.

There are several sections of the new Act that are not consistent or are confusing and should be changed. And since the new Act is so different from the old Act that then-legislators Davis and Stirling made into law in 1985, why not just call it the Common Interest Development Act, which is really what it is.

For more information relating to the new Act or California law relating to community associations, we invite you to visit our hoalawblog.com or the firm's website at lawforhoas.com.