NEW LEGISLATION FOR 2017 & CASE LAW REVIEW FROM 2016

PRESENTED BY

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A PROFESSIONAL LAW CORPORATION

I. Federal Laws

A. H.R. 1301 – Amateur Radio Parity Act of 2016 Introduced March 4, 2015, passed House on September 12, 2016

This federal legislation has not yet been enacted. As currently written it directs the Federal Communications Commission (FCC) to amend station antenna structure regulations to prohibit a private land use restriction from applying to amateur radio stations if the restriction:

- Precludes communications in an amateur radio service,
- Fails to permit a licensee of amateur radio service to install and maintain an effective outdoor antenna on property under its exclusive use or control, or
- Is not the minimum restriction which may be practicable to accomplish the lawful purposes of a community association seeking to enforce the restriction.

Before installing an outdoor antenna, however, an amateur radio licensee must obtain a community association's prior approval. A community association may: (1) prohibit installations on common property not under the exclusive control of the licensee, and (2) establish installation rules for amateur radio antennas and support structures.

This Bill passed the House of Representatives as amended on September 1, 2016. It is awaiting action by the Senate.

B. H.R. 3700 – Housing Opportunity Through Modernization Act of 2016

The Housing Opportunity Through Modernization Act of 2016 (HOTMA) became public Law No. 114-201 on July 29, 2016. It requires the Federal Housing Administration (FHA) to modify its certification requirements to make recertifications substantially less burdensome than original certification processes. In response to the legislation, the FHA released a mortgagee letter on the owner occupancy issue (see below) and issued proposed new regulations for public comment. The proposed regulations include reinstating single unit approvals and extending the certification period from two years to three years.

II. Federal Regulations

A. HUD/FHA Regulations

Per the H.R. 3700 requirements discussed above, HUD issued Mortgagee Letter 2016-15 on October 26, 2016 which provided guidance on the percentage of owner occupied units required to obtain project approval. The FHA retained the current 50% owner occupancy requirement for existing projects and 30% for proposed projects. FHA may approve an owner occupancy percentage as low as 35% under certain circumstances. The conditions for approval with this lower occupancy ratio are as follows:

- Projects must be approved through HUD – the HRAP process – not a lender
- 20% of the budget must go to fund reserves
- No more than 10% of units may be more than 60 days delinquent in assessments
- 3 years of "acceptable" financial documents must be provided

The owner occupancy ratio must be documented through sales agreements, developer information, or, for existing projects, "Evidence that units have closed and are occupied by the owner." The letter does not say what evidence is acceptable.

Relaxing the owner occupancy requirements will make it easier for projects which are financially sound but for some reason have a low owner occupancy ratio to obtain project approval.

B. HUD Regulations on Quid Pro Quo and Hostile Environment Discrimination – Amendments to 24 CFR Part 100 – 81 FR 63054 – Effective October 14, 2016

The Federal Department of Housing and Urban Development (HUD) has now finalized its rules amending the Fair Housing Regulations to add new standards for investigation and prosecution of harassment on the basis of race, color, religion, national origin, sex, familial status, or disability. Specifically, the new Regulations will define and provide examples of quid pro quo (this for that) and hostile environment harassment under the Fair Housing Act.

The Regulations became effective October 14, 2016. See 24 CFR 100. 81 Federal Register 178 (September 14, 2016)

The California Department of Fair Employment and Housing (DFEH) will now be adopting similar, if not identical, regulations.

III. California State Legislation

A. Amendments and New Additions to the Davis-Stirling Common Interest Development Act

1. S.B. 918 (Vidak) - Notices

S.B. 918 adds new Civil Code § 4041 to the Davis–Stirling Common Interest Development Act (the "Act"), requiring owners to provide associations with the following information on an annual basis:

a. The address or addresses to which notices from the association are to be delivered.

b. An alternate or secondary address to which notices from the association are to be delivered.

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

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

Associations will be required to seek this information from the owners and update their records at least 30 days prior to sending out the association's annual disclosures. If an owner does not provide the association with the address or alternate/secondary address, the association can send notices to the property address.

2. A.B. 2362 (Chu) – Pesticides

Adds new Civil Code Section 4777 to the Act which requires as follows:

a. An association or its authorized agent that applies any pesticide to a separate interest or to the common area without a licensed pest control operator shall provide the owner or tenant of an affected separate interest with the notice set out in the statute.

b. In addition, if the association is making broadcast applications, or using total release foggers or aerosol sprays, and the owner or tenant in an adjacent separate interest that could reasonably be impacted by the pesticide use must also be given the written notice.

c. The written notice must contain the following statements and information, using words with common and everyday meaning:

i. The pest or pests to be controlled.

ii. The name and brand of the pesticide product proposed to be used.

iii. "State law requires that you be given the following information:

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

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

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

iv. The approximate date, time, and frequency with which the pesticide will be applied.

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

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

e. Giving Notice:

i. At least 48 hours prior to application of the pesticide to a common area, the association or its authorized agent shall, if practicable, post the written notice described above in a conspicuous place in or around the common area in which the pesticide is to be applied. Otherwise, if not practicable, the association or its authorized agent shall provide individual notice to the owner or tenants of the separate interest that is adjacent to the common area.

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

f. Notice to tenants of separate interests shall be provided, in at least one of the following ways:

i. First-class mail.

ii. Personal delivery to a tenant 18 years of age or older.

iii. Electronic delivery, if an electronic mailing address has been provided by the tenant.

g. Immediate Application:

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

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

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

i. If any owner or tenant of a separate interest or an owner or tenant of an adjacent separate interest is also required to be notified, the association or authorized agent shall provide that person with this notice as soon as practicable after the oral agreement is made authorizing immediate pesticide application, but in no case later than commencement of application of the pesticide.

j. A copy of a written notice described in the statute shall be attached to the minutes of the board meeting immediately following the application of the pesticide.

k. The following definitions apply to the new statute:

(1) "Adjacent separate interest" means a separate interest that is directly beside, above, or below a particular separate interest or the common area.

(2) "Authorized agent" means an individual, organization, or other entity that has entered into an agreement with the association to act on the association's behalf.

(3) "Broadcast application" means spreading pesticide over an area greater than two square feet.

(4) "Electronic delivery" means delivery of a document by electronic means to the electronic address at, or through which, an owner of a separate interest has authorized electronic delivery.

(5) "Licensed pest control operator" means anyone licensed by the state to apply pesticides.

(6) "Pest" means a living organism that causes damage to property or economic loss, or transmits or produces diseases.

(7) "Pesticide" means any substance, or mixture of substances, that is intended to be used for controlling, destroying, repelling, or mitigating any pest or organism, excluding antimicrobial pesticides as defined by the Federal Insecticide, Fungicide, and Rodenticide Act (7 U.S.C. Sec. 136(mm)).

3. S.B. 944 (Senate Housing and Transportation Committee – Omnibus Bill) – S.B. 944 makes numerous changes to many State Codes, as "clean up" legislation, including amendments to the Act, Civil Code Sections 4270, 4750.10, and 5570

a. Civil Code Section 4270: the Bill clarifies that the exceptions to the general requirements for amending a declaration include the alternative procedures specified in the Act

The amended Section will provide as follows:

4270(a) A declaration may be amended pursuant to the declaration or this act. Except where an alternative process for approving, certifying, or recording an amendment is provided in Section 4225, 4230, 4235, or 4275, an amendment is effective after all of the following requirements have been met …

b. Civil Code Section 4750.10: the Bill renumbers Civil Code Section 4750.10 as 4753.

c. Civil Code Section 5570: the Bill corrects an incorrect statutory reference for the definition of "major component."

The amended section will now provide as follows:
5570. …

(b) For the purposes of preparing a summary pursuant to this section:…

(2) "Major component" has the meaning used in Section 5550…

4. A.B. 1963 (Calderon) – Defects

A.B. 1963 will continue the current provisions of the Act, Civil Code Section 6000, regarding the requirements for design and construction defect claims. The existing law ends on July 1, 2017, and this Bill extends Civil Code Section 6000 until July 1, 2024, and would repeal the new Section effective January 1, 2025.

Note: The Commercial and Industrial Common Interest Development Act ("Commercial CID Act") was not amended to extend Civil Code Section 6870, which is virtually identical to Section 6000. Presumably, this is an oversight by the Legislature which will be corrected by a Bill prior to the sunset date of July 1, 2017.

B. Other California Legislation

1. S.B. 1005 (Jackson) – Marriage - Amends numerous sections of several Codes relating to marriage.

Under S.B. 1005, the terms "husband," "wife," "spouses," "married persons," or other comparable term is replaced with "spouse" and/or "spouses." The term spouse is to include "registered domestic partner." S.B. 1005 also changes gender specific language to gender-neutral language and expands the definition of spouse to include registered domestic partnerships to be more inclusive of nontraditional partnerships.

a. Civil Code Section 51.3, which is part of the Unruh Civil Rights Act relating to housing for senior citizens, is changed to now define cohabitants as persons who live together as spouses or persons who are domestic partners under the meaning of §297 of the Family Code.

b. The language of Corporations Code Sections 5612 and 7612 regarding "husband and wife as community property" now reads "spouses as community property."

2. S.B. 269 (Roth) – Disability Access - Amends the Civil Code and Government Code

The Construction-Related Accessibility Standards Compliance Act establishes standards for making new construction and existing facilities accessible to people with disabilities. A disabled person who encounters a violation of the accessibility standards which causes difficulty, discomfort, or embarrassment can recover actual and statutory damages.

Previously, the law only required that the plaintiff encounter a violation in order for statutory damages to be awarded, not that the plaintiff prove that he/she was in fact damaged. This Bill tightens the requirements for proving statutory damages by creating a rebuttable presumption that certain technical violations do not cause a plaintiff to experience difficulty, discomfort, or embarrassment.

Situations where the rebuttable presumption limits the statutory damages include:

- Any small business with 50 employees or fewer that was inspected by an approved Certified Access Specialist within the last 120 days.

- Any small business with 25 employees or fewer with less than $3,500,000.00 in annual receipts over the prior three years if they corrected the violations within 15 days from the date of written notice or service of a complaint for violations including:

    - Outside and inside signage issues – identifying accessible places
    - Parking lot paint stripes and condition – color and visibility
    - Detectable warning surfaces on accessibility ramps

The stated intent of this Bill is to make it more difficult to sue for ADA violations. As this law applies to places of public accommodation, it would only apply to associations which have spaces that are open to the public, such as event arenas or rental spaces and to commercial CIDs.

This Bill also requires expedited review of applications to correct construction related violations of the disability laws. This would, theoretically, make it easier to more swiftly remedy any violations so that additional people are not injured.

3. S.B. 945 (Monning) – Pet Boarding Facilities

This Bill establishes operating guidelines for pet boarding facilities and responsibilities of pet boarding facility operators. It also authorizes cities and counties to adopt ordinances establishing additional standards. Any violation of these guidelines or responsibilities is a new criminal infraction.

"Pet Boarding Facility" - "means any lot, building, structure, enclosure, or premises, or a portion thereof, whereupon four or more dogs, cats, or other pets in any combination are boarded at the request of, and in exchange for compensation provided by, their owner…[excluding animal control, humane society, registered veterinary facilities, and ASPCA]."

"Pet Boarding Facility Operator" - "means a person who owns or operates, or both, a pet boarding facility."

New requirements include animal care standards such as checking on the animal at least once every 24 hour period, feeding the animals "nutritious food," and maintaining either a fire suppression sprinkler system or a fire alarm that is connected to the central reporting station.

The operator is responsible for compliance with all requirements and may be fined up to $250.00 for the first violation and up to $1,000.00 for each subsequent violation.

With the rise of home pet boarding operations through sites like Rover.com, (Airbnb for dogs) S.B. 945 gives associations definitions to reference when enforcing commercial business restrictions against these types of facilities. If a homeowner or tenant has been cited for an infraction, it can provide the association with a determination by the city or county that a pet boarding business exists.

4. S.B. 1069 (Wieckowski)/A.B. 2299 (Bloom) – Accessory Dwelling Units

Two related Bills were passed related to accessory dwelling units ("ADUs"). The Bills clarify existing law which already permits accessory dwelling units, which were formerly referred to in the statutes as second units, and are commonly called "granny flats."

These Bills were proposed to address what the authors perceived to be a massive housing shortage. The idea is to promote the creation of affordable housing in high-priced markets, including the Bay Area, and Malibu, which are the areas where the Bills' authors are from. The proponents asserted that although the law allowed ADUs, few were built because of excessive fees and restrictions imposed by the local governments. Combined, the Bills amend Government Code Section 65852.2, which provides that local governments are required to accept, and approve or disapprove an application for an ADU ministerially without discretionary review, within 120 days after receiving the application, if it meets the requirements set forth in the statute:

- The statute provides that an ADU that conforms to the statute shall be deemed to be an accessory use or an accessory building and shall not be considered to exceed the allowable density for the lot upon which it is located, and shall be deemed to be a residential use that is consistent with the existing general plan and zoning designations for the lot.

Although these two Bills do not directly regulate homeowners associations, because ADUs are allowable residential uses, associations will not be able to prohibit ADUs as a commercial use, even if built for rental purposes. However, associations can still establish and enforce architectural provisions which may restrict or prohibit accessory structures.

5. A.B. 1732 (Ting) - Single-user Restrooms

Effective March 1, 2017, A.B. 1732 amends the Health and Safety Code to require any single-user restroom facility in any business establishment or place of public accommodation to be identified as an "all gender" facility. According to the Assembly Floor Analysis, this legislation will require business with single user restrooms to be universally accessible regardless of a person's gender designation.

While the Health and Safety Code does not provide a definition of a business establishment, there are other statutes that consider homeowner associations to be business establishments.

If a clubhouse or other association facility includes a single-user restroom facility, the prudent step would be to have "all gender" signage that meets the Title 24 requirements by March 1, 2017.

The Health and Safety Code will be amended to read as follows:

Single User Restroom

118600.

(a) All single-user toilet facilities in any business establishment, place of public accommodation, or state or local government agency shall be identified as all-gender toilet facilities by signage that complies with Title 24 of the California Code of Regulations, and designated for use by no more than one occupant at a time or for family or assisted use.

(b) During any inspection of a business or a place of public accommodation by an inspector, building official, or other local official responsible for code enforcement, the inspector or official may inspect for compliance with this section.

(c) For the purposes of this section, “single-user toilet facility” means a toilet facility with no more than one water closet and one urinal with a locking mechanism controlled by the user.

(d) This section shall become operative on March 1, 2017.

6. S.B. 1092 (Monning) – Advertising – Private Residence Rental Listing

This Bill:

- Amends Business and Professions Code Section 22592 to add subsection (b) to require online short-term rental sites, such as Airbnb and VRBO, referred to in the Bill as "hosting platforms," to provide notice to homeowners and tenants who are listing their residences for short-term rental to review their insurance policies for appropriate insurance coverage prior to participating.

- Clarifies definition of "residence" in language in Business and Professional Code Section 22592 (a) to also include mobilehomes. Section 22592 (a) requires tenants who list their residences for short-term rental to check their lease or contract for any restrictions on short-term rentals.

The purpose of the Bill is to require homeowners or tenants who are listing their properties on Airbnb or the like to review their insurance policies and obtain an understanding of what their insurance covers and whether it will protect them in the event of a loss arising out the short-term rental.

When a loss arises in connection with a short-term rental, it will be harder for a homeowner/ tenant to argue that he/she/they did not know or think to check the extent of their insurance coverage. For example, residential insurance policies often exclude coverage for commercial activities, which can include claims arising in connection with short-term rentals. By advising homeowners/tenants to check their insurance coverage, the incidents of an owner or tenant assuming the risk of renting without carrying appropriate insurance coverage will hopefully be reduced.

7. S.B. 7 (Wolk) - Housing - Water Meters: Multiunit Structures

This Bill was proposed to encourage the conservation of water in multifamily residential rental buildings and to establish practices involving submetering of dwelling units. The Bill also includes appropriate safeguards regarding landlords and tenants. The Bill defines a “landlord” as an owner of residential rental property, and specifically excludes common interest developments (as defined in Civil Code Section 4100) from being considered landlords.

This Bill applies to all dwelling units offered for rent or rented where submeters are required by Health and Safety Code Section 17922.14 or to units where submeters are used to charge tenants separately for water usage.

If a landlord chooses to bill tenants separately for water usage, the landlord must have that spelled out in the rental agreement, state the approximate cost, explain that the water usage charges are separate from the rent and include the due dates and billing procedures for the water usage costs.

Although most CIDs are not considered landlords, if the CID is using submeters and a property within the association is being used as a rental property, the owner of the property will need access to the information from the submeters. Under this Bill, landlords are required to keep accurate records of all of the following:

1. The date submeters are inspected, tested and verified and the date it will be reinspected;

2. Any fixed fees the water purveyor charges and the usage charges for the property;

3. The number of dwelling units if multiple units are being charged in the last billing cycle;

4. The per unit charges for volumetric water usage;

5. The formula used to calculate the charges for the tenant;

6. Physical location of the submeter.

This Bill will take effect January 1, 2018.

8. A.B. 1978 (Gonzalez) – Employment; property Service Workers

This is the "Justice for Janitors" Bill which would require every employer of janitors now meet new specific requirements concerning registration, records, and sexual harassment training.

Any company that hires workers to perform janitorial services, including independent contractors or employees must follow the requirements of this Bill.

The Bill would require every employer of janitors, effective July 1, 2018, to register annually with the Labor Commissioner in accordance with prescribed procedures. The Bill would prohibit an employer from conducting any business without registration as required by the Bill and would authorize the commissioner to revoke a registration under certain circumstances. The Bill would set application fees of $500 and renewal fees of $500 annually for registration.

The Bill would require an employer to include specific information in the registration application. The Bill would prohibit the Division from granting registration under specific circumstances. The Bill would require the commissioner to maintain on the department's Internet Web site a public database of registered property service employers.

The Bill would require the division, by January 1, 2019, to establish a biennial in-person sexual violence and harassment prevention training requirement for employees and employers. Until the division establishes that training requirement, employers must provide employees with a pamphlet of the Department of Fair Employment and Housing on sexual harassment.

Associations which hire janitorial companies should be aware of these requirements, and in contracts, require that the companies comply with all laws concerning registration, training and other requirements of the Labor Code. Associations which hire janitors directly may also be subject to these new laws.

9. S.B. 3 (Leno) - Minimum Wage/Sick Leave

On and after July 1, 2014, existing law requires the minimum wage for all industries to be not less than $9 per hour. On and after January 1, 2016, existing law requires the minimum wage for all industries to be not less than $10 per hour.

This Bill would require the minimum wage for all industries to not be less than specified amounts to be increased from January 1, 2017, to January 1, 2022, inclusive, for employers employing 26 or more employees and from January 1, 2018, to January 1, 2023, inclusive, for employers employing 25 or fewer employees. The Governor can temporarily suspend increases based on certain determinations. The Bill would also require the Director of Finance, after the last scheduled minimum wage increase, to annually adjust the minimum wage under a specified formula.

On or before July 28, 2017, and on or before every July 28 thereafter until the minimum wage is a specified amount for employers employing 26 or more employees, the Bill would require the Director of Finance to annually determine, based on certain factors, whether economic conditions can support a scheduled minimum wage increase and certify that determination to the Governor and the Legislature.

On or before July 28, 2017, and on or before every July 28 thereafter until the minimum wage is a specified amount for employers employing 26 or more employees, in order to ensure that the General Fund can support the next scheduled minimum wage increase, the Bill would also require the Director of Finance to annually determine and certify to the Governor and the Legislature

whether the General Fund would be in a deficit in the current fiscal year, or in either of the following 2 fiscal years.

CALIFORNIA'S MINIMUM WAGE

Scheduled Wage Increases (If No Increases Are Paused)

Wage	26 Employees or More	25 Employees or Less
$10.50/hour	January 1, 2017	January 1, 2018
$11/hour	January 1, 2018	January 1, 2019
$12/hour	January 1, 2019	January 1, 2020
$13/hour	January 1, 2020	January 1, 2021
$14/hour	January 1, 2021	January 1, 2022
$15/hour	January 1, 2022	January 1, 2023

10. S.B. 814 (Hill) - Water

This Bill declares that during prescribed periods excessive water use by a residential customer in a single-family residence or by a customer in a multiunit housing complex, as specified, is prohibited.

This Bill, during prescribed periods, requires each urban retail water supplier to establish a method to identify and discourage excessive water use. This Bill would authorize as a method to identify and discourage excessive water use the establishment of a rate structure that includes block tiers, water budgets, or rate surcharges over and above base rates for excessive water use by residential customers. This Bill authorizes an ordinance, rule, or tariff condition that includes a definition of or procedure to identify and address excessive water use, as prescribed, and makes a violation of this excessive water use ordinance, rule, or tariff condition an infraction or administrative civil penalty and authorizes the penalty for a violation to be based on conditions identified by the urban retail water supplier. By creating a new infraction, this Bill imposes a state-mandated local program.

C. Vetoed Bill

1. A.B. 2724 (Gatto) – Drones - Vetoed by the Governor

A.B. 2724, had the Governor signed it, would have created the DRONE Act, requiring manufacturers of drones to provide information about FAA safety and licensing, and requiring drones equipped with GPS to also be equipped with geofencing technology to prevent the drone from flying into an area prohibited by law. It would also have required drone owners to have insurance in an amount to be determined by the Department of Insurance.

In his veto message, the Governor said the Bill would create a patchwork of regulatory requirements and the geofencing provision would probably be preempted by the Federal government. "Piecemeal is not the way to go."

D. State Regulations

1. DFEH Regulations – by the California Department of Fair Employment and Housing (DFEH) through its Fair Employment and Housing Council – on Harassment, Retaliation, Disability and Assistance Animals – Amendments to Title 2 of the California Code of Regulations

The DFEH is currently in the process of drafting Regulations that would parallel many of the federal disability and discrimination regulations.

The DFEH is also creating specific regulations on Assistance Animals.

On November 11, 2016 the Council issued its proposed rulemaking and issued the proposed Regulations for public commentary until January 10, 2017, and are available to view on the State DFEH website at www.dfeh.ca.gov.

2. California Law Revision Commission (CLRC) – CIDs and Mechanics Liens – Draft Recommendations of CLRC re Notice of Claim of Liens and Lien Release Bonds as of October 4, 2016

The CLRC has been studying both CIDs and Mechanics Liens. They will propose legislation to address issues with mechanics liens in CIDs. On October 4, 2016, the CLRC issued its draft recommendation in Memorandum 2016-55.

The CLRC proposes changes to both the Davis-Stirling Act and the Commercial CID Act to provide notice to the "owner" of the common area by making the Association the owner's agent for receipt of notices, including preliminary notices by contractors. Delivery of the notice to the Association would be considered notice to the "owner." The CLRC thinks this would eliminate confusion about who owns the common area, and because the Association generally maintains the

common area, it would typically be the entity having the work done on the common area.

In addition, current law provides for a prohibition on recording of mechanics and other liens on common areas in a condominium project for work performed by one owner, unless other owners of the "property" have consented. Also, current law allows an owner in a condominium project to pay off the lien claimant the fraction of the total sum secured by the lien (e.g. percentage of common area owned by that unit) and obtain a release of the mechanics or other lien as to that unit. (See Civil Code Section 4615). The CLRC proposes to expand this to include all types of CIDs not just condo projects.

E. Reminder of Existing Law: Civil Code Section 4775 – Maintain, Repair And Replace Exclusive Use Common Area

Effective January 1, **2017**, the Davis-Stirling Common Interest Development Act ("Davis-Stirling" or "Act") changes the legal presumption for "exclusive use common area" maintenance, repair and replacement. Civil Code Section 4775 will provide that the owner is responsible for "**maintaining**" his/her exclusive use common area and the Association is responsible for "**repairing and replacing**" the exclusive use common area **unless the CC&Rs provide otherwise**.

The Act does not change the presumption as to who is responsible for maintaining, repairing and replacing common area (the association) or for maintaining, repairing and replacing separate-interest property (the owner of each separate interest).

But, beginning in January 2017, there will be an important distinction regarding exclusive use common area maintenance, repair and replacement. The owner of the appurtenant separate interest will "**maintain**" the exclusive use common area and the association will be responsible for **repair and replacement** unless the CC&Rs provide otherwise.

The difference between maintaining and repairing an exclusive use common area component is not clear or defined in the new Code Section. For example, Black's Law Dictionary defines "maintain" as to "care for (property) . . . to engage in general repair and upkeep." (8th ed. 2009, at p. 1039) If the duty to maintain requires "general repair," confusion will result regarding where a homeowner's duty to maintain ends and an association's duty to repair begins.

Associations with exclusive use common area still have time to investigate and evaluate the potential impact of this statutory change before the January 1, 2017, effective date for this change in the law. Depending on the circumstances, both as to the existing association governing documents, and the physical components of the project, associations may need to consider:

- A CC&R amendment, e.g., to overcome the statutory presumption and to make repair and replacement of exclusive use common area the obligation of the owner of the appurtenant separate interest.

- Adding exclusive use common areas to the association's reserve study for repair and replacement.

- Proposing a special assessment or implementing regular assessment increases to fund reserves for repair and replacement of exclusive use common areas.

- Adopting rule changes to define maintenance obligations applicable to various exclusive use common area components.

Depending on the age of a community, the existence and nature of exclusive use common area improvements, as well as the association's financial resources, the changes to Civil Code Section 4775 could have a significant impact.

IV. Case Law

A. Published Cases

1. Palm Springs Villas II HOA v. Parth (June 21, 2016) 248 Cal. App. 4th 268 (As modified on denial of rehearing July 14, 2016, review denied October 12, 2016)

Board President, Erna Parth, took a variety of actions, including authorizing contracts, hiring an unlicensed contractor, signing promissory notes, and terminating the management company without Board approval. She also signed a contract with a security company even though the Board had voted to obtain bids from security companies. After the Board learned she had signed the contract, they refused to ratify the contract. The security company then sued the Association, and the Association filed a cross complaint against Parth for breach of fiduciary duty, and breach of the CC&Rs/Bylaws. Parth demurred to the breach of fiduciary duty cause of action, which was sustained. After discovery, Parth brought a motion for summary judgment on the basis that she was protected by the Business Judgment Rule and the provisions of the CC&Rs which protected directors from liability. The trial court granted the Motion and found that Parth had provided sufficient evidence that she had followed the Business Judgment Rule: 1) She was disinterested, 2) acted in good faith, without intentional misconduct and 3) based on the information she possessed. The Association appealed. On appeal the Court of Appeal found that Parth had committed a variety of wrongdoing, and that the Business Judgment Rule does not protect directors who do not act as ordinarily prudent persons, and who fail to make reasonable inquiry under the circumstances presented. The Court of Appeal found Parth had failed to investigate the companies she contracted with, failed to determine if she

had the authority to take certain actions, failed to determine the requirements of the Governing Documents for promissory notes, and filed to exercise reasonable due diligence to ascertain the extent of her authority as a Director and as President.

The Court of Appeal remanded the case back to the trial court for further proceedings.

In summary, this case exemplifies what may happen to those Directors who take matters into their own hands and do not consider the limitations of the Governing Documents. The Business Judgment Rule will not protect directors who do not act in a reasonable manner, and who do not perform the minimal investigation needed into their legal authority and who act in a unilateral manner.

See Article attached from the *Orange County Lawyer* magazine by attorney Nathan P. Bettenhausen, *Going Rogue*.

2. Rancho Mirage Country Club HOA v. Hazelbaker (August 9, 2016) 2 Cal. App. 5th 252

The issue in this case relates to the ability of the Association to recover attorney's fees incurred in enforcing a settlement agreement reached during mediation pursuant to the Davis-Stirling Common Interest Development Act. ("Act") The appellate court affirmed the trial court's granting of attorney's fees, as follows:

Defendants and appellants Thomas B. Hazelbaker and Lynn G. Hazelbaker own, through their family trust, a condominium in the Rancho Mirage Country Club development. Defendants made improvements to an exterior patio, which plaintiff and respondent Rancho Mirage Country Club Homeowners Association (Association) contended were in violation of the applicable covenants, conditions and restrictions (CC & Rs). The parties mediated the dispute pursuant to the Act. The mediation resulted in a written agreement, executed by Thomas, but not by Lynn, which included an attorneys fee provision for the award of attorney's fees to the prevailing party in any action to enforce the agreement. Subsequently, the Association filed a lawsuit, alleging that defendants had failed to comply with their obligations under the mediation agreement to modify the property in certain ways.

While the lawsuit was pending, defendants made modifications to the patio to the satisfaction of the Association. Nevertheless, the parties could not reach agreement regarding attorney fees, which the Association asserted it was entitled to receive as the prevailing party.

The Association filed a motion for attorney fees and costs, seeking an award of $31,970 in attorney fees and $572 in costs. The trial court granted the motion in part, awarding the Association $18,991 in attorney fees and $572 in costs. Defendants argued on appeal that the trial court's award, as well as its subsequent denial of a motion to reconsider the issue, were erroneous in various respects.

This case presents the question of whether the Act, and particularly the fee-shifting provision of section 5975, subdivision (c), applies to an action to enforce a settlement agreement arising out of a mediation conducted pursuant to the mandatory alternative dispute resolution requirements of the Act. The Court of Appeal found it does apply in at least some circumstances.

The Act is intended, among other things, to encourage parties to resolve their disputes without resort to litigation, by effectively mandating pre-litigation ADR. (See § 5930(a) [enforcement action in civil court may not be filed until parties have "endeavored to submit their dispute" to ADR; § 5960 [in determining amount of fee and cost award, court "may consider whether a party's refusal to participate in [ADR] before commencement of the action was reasonable"].].)

The Court held that narrowly construing the phrase "action to enforce the governing documents" to exclude actions to enforce agreements arising out of that mandatory ADR process would discourage settlement during ADR, and encourage gamesmanship. For example, a party might agree to a settlement in mediation without any intention of fulfilling its settlement obligations, simply to escape the cost-shifting provisions of the Act.

The Association's lawsuit was based on the failure of defendants to take certain steps to bring their property into compliance with the applicable CC & Rs. The relief sought by the Association was an order requiring defendants to take those steps, and a declaration of the parties' respective rights and responsibilities. The fact that it took a mediation and an agreement for defendants to take steps to bring the property into compliance with CC & Rs, does not change the underlying nature of the dispute between the parties, or the nature of the relief sought by the Association. The Court found nothing in the that suggests a court should give more weight to a lawsuit than to a mediation agreement—rather the court needed to determine whether an action is one "to enforce the governing documents" in the meaning of section 5975.

The Court also held that the trial court did not abuse its discretion in finding that the Association was the prevailing party. The objective of the Association's enforcement action, including the pre-litigation ADR process, was to force defendants to bring their property into compliance with the CC&Rs. It was successful in achieving that goal.

The Court also concluded that the award of attorney's fees against Lynn, who did not sign the settlement agreement, was appropriate, as the action was one to enforce the CC&Rs, which did not require resorting to the provision of the settlement agreement.

3. Almanor Lakeside Villas Owners Association v. Carson (April 19, 2016) 246 Cal App. 4th 761

Almanor Lakeside Villas Owners Association is the homeowners association in which appellants James and Kimberly Carson own The Kokanee Lodge and Carson Chalets – properties they purchased for use as short-term vacation rentals. The properties are subject to the CC&Rs of the Almanor development. Section 4.01 of the CC&Rs designates certain lots, including the Carson properties, that can be utilized for commercial or residential purposes. Section 4.09 of the CC&Rs prohibits owners from using their lots "for transient or hotel purposes or renting for "any period less than 30 days." In 2010 the Almanor Board of Directors began to develop regulations to enforce the CC&Rs; the Carsons believed their properties were exempt from the use restrictions of the CC&Rs, they also believed that various rules adopted by the board did not apply to their properties. The Almanor Association began to issue fines to the Carsons for a wide range of CC&R violations; the Carsons disputed these fines. Additionally, the Carsons failed to pay the Association's assessments for approximately two years. In June 2012, the Carsons paid $14,752.35 to the Association with the strict instructions that the payment was to be applied to unpaid assessments and not towards any of the disputed fines; according to the Carsons, Almanor improperly applied $1,160 of the payment towards disputed fines.

Almanor insisted that the lump sum payment from the Carsons did not satisfy the account balance and brought an action against them arguing that the Carsons owed $54,000 in dues, fees, fines and interest. The Carsons filed a cross-complaint arguing that the CC&Rs did not contemplate the commercial businesses and that the commercial lots are exempt from the rental prohibition.

The Trial Court found that Section 4.01 and 4.09 were in direct conflict with each other and that it would be unreasonable to strictly enforce the absolute use restrictions (Section 4.09) against the Carsons. The Trial Court further found that the Association could impose reasonable use restrictions consistent with their right to use their lots for commercial lodging purposes. It further found that of the fines imposed in 2010, 2011, and 2012, only the fines pertaining to the non-use of Almanor's boat decals were reasonable, which totaled $6,620, including late fees and interest. Both parties claimed to be the prevailing party in the lawsuit, and both parties sought attorneys' fees and costs under the Civil Code Section 5975. The Trial Court found that Association was the prevailing party and awarded $101,803.15 in attorneys' fees and costs to the Association, in addition to the $6,620 in damages.

The Carsons appealed the Trial Court's decision. The Court of Appeal upheld all decisions of the Trial Court. Particularly, the Court found that Civil Code Section 5975 provides that in an action to enforce the governing documents, the prevailing party **shall be awarded reasonable attorneys' fees**. The Court of Appeals noted that reviewing courts have found that this section of the Davis-Stirling act reflects Legislative intent that the prevailing party receive attorneys' fees as a matter of right and that the trial court is therefore obligated to award attorneys' fees whenever the statutory conditions are satisfied. The Davis-Stirling Act does not define "prevailing party" and California courts have reasoned that the prevailing party is the party who achieves its main litigation objectives.

The Carsons argued that the amount of the award of attorneys' fees was unreasonable, but failed to provide case law or other authoritative support. The Court found that Civil Code 5975 is not discretionary, but rather mandatory.

4. Nellie Gail Ranch Owners Association v. Mc Mullin (2016 WL 571912) Filed October 3, 2016

The Association filed an action to quiet title to a portion of the common area and compel the Defendants to remove unauthorized improvements. The Defendants built a retaining wall and other improvements which occupy 6,000 square feet of the Association's common area.

The trial court ruled in favor of the Association and granted a mandatory injunction authorizing the Association to remove the improvements at the Defendants' expense. The Appellate Court affirmed the trial court's decision.

The Defendants attempted to argue that the Association was equitably estopped from attempting to quiet title as the Association had told them that it would not pursue the wall as a violation of the CC&Rs. Equitable estoppel requires that the party asserting it be ignorant of the true facts and that they justifiably relied on the conduct or statements of another who has knowledge of those facts.

At the time that the Association had informed the Defendants of that decision, the Association was aware that the Defendants had completed unauthorized improvements to the Defendants' property, but the Association was not aware that those improvements had intruded into the Association's common area. Prior to beginning the work, the Defendants had sought and been denied approval repeatedly as their lot map did not reflect all easements and property lines. Each time they resubmitted the application they failed to remedy that problem.

Because the Defendants knew the Association was unaware of the intrusion, they could not justifiably rely on the assertions made by management.

The Defendants also argued that they were entitled to keep the property under the doctrine of adverse possession. However, a California specific requirement for adverse possession is that the alleged possessor must pay taxes on the property or show that the property is not subject to tax. Here, the Court found that the common area in question has a value that is included in the taxes which are assessed and paid by all of the homeowners equally.

The Court also found that trial court was correct in awarding the injunction, as"a property owner generally is entitled to a mandatory injunction requiring an adjacent owner to remove an encroachment, but a trial court has discretion to deny an injunction and grant an equitable easement if the encroacher acted innocently and the balancing of the hardships greatly factor the encroacher."

In the present case the Defendants were not innocent, so the court was correct in granting the injunction.

5. City of San Diego v. San Diegans for Open Government (September 22, 2016) 3 Cal. App. 5th 568 (As modified on denial of rehearing October 17, 2016)

The City of San Diego ("City") filed a Validation Action against all interested parties to allow the City to levy a special tax to finance the expansion of the San Diego Convention Center. Attorney Melvin Shapiro filed an answer as an interested party and the San Diegans for Open Government ("SDOG") also filed an answer verifying it was an interested party. The trial court found in favor of the City and SDOG and Shapiro appealed. On appeal, the Court of Appeal reversed the trial court's judgment and remanded the matter back to the trial court with directions to enter the decision in favor of SDOG and Shapiro and to resolve ancillary proceedings.

A joint motion for attorneys' fees was filed by SDOG and Shapiro seeking $862,404.92. The City opposed the motion on the grounds that SDOG's corporate status at the time they filed their answer was suspended by the Secretary of State. The City provided evidence that the attorneys for SDOG knew the corporation's status was suspended, but still proceeded with the filing of the answer, along with the filing of at least five other lawsuits while SDOG was suspended. The City filed a motion to strike SDOG's answer and a motion for attorneys' fees.

The superior court denied the City's motion and allowed for partial attorneys' fees that were incurred after the corporation revived its corporate status. However, the court found that had the City raised a statute of limitations defense, it probably would have been successful. SDOG was eventually awarded $258,629.89 in attorney's fees. The City appealed.

On appeal the City argued SDOG was not entitled to any attorney fees under Section 1021.5, also known as the private attorney general doctrine. The Court of

Appeal pointed out that the private attorney general doctrine operates as a financial incentive for attorneys to protect the public against certain government encroachment and missteps, but should not be such a "carrot" as to promote an attorney to act unethically or unprofessionally, which is what happened in this case.

SDOG and their attorneys did not deny that the corporation was suspended. SDOG and their attorneys did not disclose the status of the corporation to the City or the Court. Furthermore, they raised no defense, except to claim the status was "widely known". The court pointed out that a corporation that is suspended lacks legal capacity to prosecute or defend a civil action and cannot sell, transfer or exchange real property in California and any contract entered into during the time of suspension are voidable.

Since SDOG lacked the capacity to appear in the Validation Action, under Section 1021.5, it was also not entitled to any attorney fees. SDOG argued that its' corporate status was revived and that should validate otherwise invalid prior proceedings. But the Court of Appeal distinguished between procedural steps taken on behalf of a suspended corporation while under supervision, and substantive defenses that accrue during the time of suspension. Since, the Validation Action had a strict deadline, the timely answer from the suspended corporation was invalid as the corporate status was not revived until months after the deadline had passed.

Important that all associations and managers recognize the perils of corporate suspension, not only for the Association but in the event of litigation.

6. Lee v. Silveira (December 5, 2016) 2016 WL 7048004 (ordered certified for publication on 12/8/2016)

Three members of the Board of Friar's Village HOA FVHOA sued six other Board Members and the manager, after the Board signed a management contract with Stos-Robinson Management, but didn't sue the FVHOA.

FVHOA is a 440 unit townhome project in San Diego. The Association signed a contract with Stos-Robinson, dba ARK Management, in March 2011 to provide financial management services, manage common areas, etc. In October 2013, ARK LLC was formed and, in November 2013, ARK LLC acquired Stos-Robinson (Stos-ARK). On March 13, 2014, the Board signed a new management contract with Stos-ARK which had an "evergreen" automatic roll over renewal provision which required that unless notice was given at least 60 days prior to the annual expiration date of the contract, that the contract would automatically renew for another year.

At the February 7, 2015 Board Meeting, the plaintiff directors requested the Board seek additional bids for management, but the defendant directors believed the Board should renew the Stos-ARK contract for another year because the extensive renovation project taking place at the Association and that it would be difficult for a new management company to step in.

Defendant Silveira made the motion to renew the contract, subject to the advice of counsel, defendant Durst seconded the motion, and the motion passed 6 to 3, with the three plaintiff directors voting no.

Plaintiff directors sued only for "Declaratory Relief" alleging:

- Defendants failed to follow proper bid procedures on the contract by not obtaining sufficient bids to ensure FVHOA paid the best price for its manager
- Violation of wage and hour laws
- Increased insurance premiums based on a settlement negotiated by the manager
- Adoption of policies in violation of rights of directors
- Board rubber stamping of the manager's recommendations
- Escalation of the roofing contract beyond the initial contact levels without competitive bidding
- Retaliation by defendant directors against plaintiff directors who raised certain issues
- Refusal to allow taking of verbatim transcripts of board meetings
- Allowing management to take minutes instead of the secretary
- Allowing management to impose onerous default fees on HOA member

Defendants filed a special motion to strike the complaint as a strategic lawsuit against public participation (SLAPP) under CCP Section 425.16 (anti SLAPP motion). This law allows a motion to strike the complaint on the basis that a lawsuit claim that arises from any act in furtherance of the person's right of petition or free speech under the US or California Constitution in connection with a public issue, unless the court finds the plaintiff has established that there is a probability that the plaintiff will prevail on the claim.

Defendants argued the complaint was based on decisions and statements made in duly noticed board meetings while conducting board business, and therefore involved acts or activities in furtherance of constitutionally protected activity within the meaning of the anti-SLAPP law. The trial court found the complaint was not a model of clarity, but denied the motion and found that the only relief sought by the plaintiffs was a determination of what was required under the governing documents and did not arise out of speech/petition rights.

Defendants appealed and the Court of Appeal reversed the Trial Court.

Court of Appeal found there is a two step analysis in determining whether complaint should be stricken under anti-SLAPP laws:

1) Defendant must show that the claim arises out of an act in furtherance of the person's right of petition or free speech, which includes any written or oral statement or writing made in a place open to the public or a public forum in connection with an issue of public interest or any other conduct in furtherance of the constitutional right of petition or free speech in connection with a public issue or an issue of public interest.

2) If defendant meets this burden, the burden then shifts to plaintiff to establish there is a probability that the plaintiff will prevail on the claim.

The Court of appeal found that the "public forum" included a board meeting of a homeowners association because it serves a function similar to a governmental body. The FVHOA Board promulgated and enforced policies and rules, and voted on and approved projects that directly affected the lives of FVHOA members who lived in the 440 units. The Defendant Directors statements were made and alleged "wrongful conduct" was done at Board Meetings, and thus the Court of Appeal found that the Board Meetings constituted a "public forum" under the anti-SLAPP law.

The Court of Appeal determined that a matter of "public interest" includes activities of private entities, like associations, that impact a broad segment of society and/or that affects a community in a manner similar to that of a governmental entity. The Court found that the Board's decision making process and debate in approving the roofing contract, which affected multiple buildings, and the management contract which affected the day to day operations of the FVHOA community impacted a broad segment, if not all, FVHOA members. Thus, these actions were matters of "public interest."

The Court found that the Director Defendants acts of voting at board meetings on contracts were acts in furtherance to their right of free speech made in connection with a public issue and therefore were protected under the anti-SLAPP law.

The Court further noted that the Plaintiffs' tactic in not naming the FVHOA and only naming the Directors supported its conclusion that the defendants were sued for exercising their First Amendment Rights as a result of how they voted on matters pending before the Board.

The Court also found plaintiffs failed to meet their burden to show they would prevail on the merits of their lawsuit.

This case confirms the trend by Courts since 2000 to find that associations are quasi-governmental entities for purposes of SLAPP actions, and that the Board meetings and communications constitute public forums. The decisions made by Boards may also be matters of public interest when those decisions involve all or most of the membership.

B. Unpublished Cases

1. In re Warren (Case No 15-cv-03655) U.S.D.C. Northern District of California – Order Affirming Bankruptcy Court determination.

The 5810-5816-5818 Mission Street Homeowners Association ("Association" or "Claimant") appealed an order from the Bankruptcy Court in a Chapter 11 Bankruptcy Petition which denied the Association's motion for relief. The Bankruptcy Court found that the Association was only entitled to an allowed secured claim for amounts actually stated in the notice of delinquent assessments/lien, and not after accrued amounts.

Association had recorded the lien, per Civil Code Section 5650(b) in September 2008 and stated the amounts of assessment, late charges, interest and other fees which had been incurred as of that time. The lien also stated that it constituted a charge for any and all other assessments and other amounts which may become due subsequent to the filing of the lien. After the homeowner, Deloris Warren filed a Ch. 13 Bankruptcy in August 2014, and later converted it to a Chapter 7 Bankruptcy in October 2014, the Association filed a claim for the amount of lien, plus all after accrued assessments, late charges, interests, costs, attorney's fees, etc. for all amounts due between December 2007 and August 2014.

The US Bankruptcy Court ignored the California Case precedent, including Edwards v. Bear Creek Master Association case and found that the Association should have filed multiple liens to keep updating the amounts owed as stated in the lien. The Association could not rely on the initial lien to secure subsequent unpaid amount.

Since this is an unpublished opinion by a Federal Court, which did not correctly construe California law, many attorneys believe that this opinion has no precedent. Currently, most Bankruptcy Courts do not follow this reasoning, and regularly award associations the amounts that accrue after the filing of the lien, and consider such amounts as secured by the lien.

Going Rogue: The New Perils that Await Directors Who Negligently Take Matters into Their Own Hands

By Nathan P. Bettenhausen, Esq.

Historically, the business judgment rule "set up a presumption that directors' decisions are made in good faith and are based upon sound and informed business judgment." *Lee v. Interinsurance Exchange* (1996) 50 Cal.App.4th 694, 715. Under this rule, a director is not liable for mistaken corporate action that is made in good faith, in what the director believes to be in the best interest of the corporation, and where no conflict of interest exists. *See Gaillard v. Natomas Co*. (1989) 208 Cal.App.3d 1250, 1263. However, the recent decision in *Palm Springs Villas II Homeowners Association, Inc. v. Parth* (2016) 248 Cal.App.4th 268 serves as a warning that the rule may only shield directors who first demonstrate that they meet a standard of reasonable diligence. Such an approach will likely have unintended consequences, the principal ones being that the business judgment rule may be unavailable for negligent directors and it may now be entirely ineffective at the summary judgment stage.

The *Parth* Case:

In *Parth*, the Board of Directors for the Palm Springs Villas II Homeowners Association, Inc. ("Association") derived its authority from the Association's governing documents, which included the Declaration of Covenants, Conditions and Restrictions ("CC&Rs") and the Bylaws. Although the governing documents empowered the Board to enter into contracts and to borrow money, they expressly limited the Board's ability to enter into contracts longer than one year in duration without the approval of a majority of the condominium owners. Notably, the CC&Rs also contained an exculpatory provision that protected Directors from personal liability so long as their corporate conduct was made in good faith and without willful or intentional misconduct.

After the condominium owners voted against the Board's request to levy a special assessment to offset costs connected with needed roof repairs, Parth, as President of the Board, pressed forward on her own to hire a roofing company. A contractor referred her to a roofer, but Parth neglected to investigate whether the company was licensed, failed to obtain a bid from the roofer, and was confused as to which company was ultimately hired. Nonetheless, the Board ultimately approved the retention of the roofing company. However, the Association's expert opined that the roofer's invoices were atypical and inflated, and that the work performed was deficient and required significant repairs.

To further complicate matters, Parth unknowingly exceeded her authority by hiring a new management company without Board approval, signing a promissory note without the approval of the condominium owners, signing a contract with a security company without Board approval, and entering into a five-year contract with a landscape company without the approval of the condominium owners. In her defense, Parth claimed that she didn't understand the authority she was granted under the governing documents, but sincerely believed in her authority and in her need to act.

When the Board refused to ratify the security company contract, the company sued for breach of contract and the Association cross-complained against Parth alleging breach of fiduciary duty and breach of the governing documents. In her summary judgment motion, Parth successfully argued that the breach of fiduciary duty claim was barred by the business judgment rule and the exculpatory provision in the CC&Rs. The trial court found that Parth was disinterested, and acted, upon information she possessed, in good faith and without willful or intentional misconduct. As for the existence of bad faith, the trial court found that there was a triable issue as to whether Parth violated the governing documents, but concluded that such a violation was insufficient to overcome the business judgment rule or the exculpatory provision.

On appeal, the *Parth* court reversed and held that there were material issues of fact as to whether Parth acted on an informed basis and with reasonable diligence, thereby precluding the protection of the business judgment rule on a summary judgment motion. In so doing, the Court of Appeal explained that "whether a director exercised reasonable diligence is one of the 'factual prerequisites' to application of the business judgment rule." *Id*. at 280. By characterizing "reasonable diligence" as a prerequisite to the rule, the *Parth* court suggests that the business judgment rule will only apply if directors can first demonstrate that they did not engage in negligent conduct. This would effectively remove a host of protections for directors who are merely misinformed, misguided, and honestly mistaken. *See Biren v. Equality Emergency Medical Group, Inc.* (2002) 102 Cal.App.4th 125, 137. Similarly, it may now become virtually impossible to successfully invoke the rule at the summary judgment stage since any conduct suggestive of negligence would raise a material issue of fact.

While the business judgment rule previously protected directors from liability for corporate actions that were unknowingly outside the scope of their authority, this ruling suggests that such a violation of the governing documents will, at least on summary judgment, bar the protection of the rule. As for the availability of the rule at trial, the *Parth* court leaves that very much in doubt. *Parth, supra,* at 284. At the very least, directors will now need to demonstrate that they attempted to ascertain the scope of their authority before conducting corporate business.

Best Practices for Directors:

To avoid personal liability and to come under the protection of the business judgment rule, prudent directors should follow best practices even during emergency situations. In situations when it's impractical to follow corporate formalities strictly, a director should immediately thereafter apprise the board of recent developments and the basis for the director's actions, and seek retroactive approval from the board for the actions taken.

In order to demonstrate that reasonable diligence was exercised, board meeting minutes should also carefully reflect the rationale behind corporate decisions and should document the decision-making process. Since directors will be required to affirmatively prove, in a lawsuit, that they employed reasonable diligence before taking corporate action, board meeting minutes are a valuable opportunity for them to create a written record. *See*, e.g., Corporations Code Section 314 (corporate minutes are prima facie evidence of the matters stated therein). And while the *Parth* court may have abrogated some of the protections afforded by the business judgment rule,

it also reaffirmed the important role expert consultants and legal counsel play in the corporate decision-making process. *See* Corporations Code Section 309(b)(2) (directors are entitled to rely on the information, reports, and opinions provided by counsel and experts.) But as a cautionary tale, *Parth* should give pause to rogue directors: the business judgment rule isn't what it used to be.

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