Community Association Management *Insider*®

AUGUST 2011

INSIDE THIS ISSUE

Census: Home-Based Businesses Booming

The most recent U.S. Census reports that there has been a sharp increase in the number of home-based businesses across the country. According to Census statistics, 51.6 percent of the country's businesses are operated within homes or other noncommercial spaces.

The Census revealed that businesses with certain characteristics tend to be based at home more often than at commercial locations. For example, 58.2 percent of women-owned businesses, 54.4 percent of non-minority-owned businesses, and 55.4 percent of firms owned by military veterans are home-based. The vast majority of home-based businesses are small businesses.

For a discussion of how home-based businesses can affect community associations, see last month's feature, "Controlling Owners' Business Use of Their Units," *Insider,* July 2011, p. 1.

PRODUCED IN CONSULTATION WITH

community ASSOCIATIONS INSTITUTE

FEATURE

How to Allocate Budgetary Surpluses

The financial health of a community association is one of the most important things that an association manager must constantly monitor. Without enough funds, the association's board of directors may struggle to cover costs, and may eventually have to increase assessments. Since the downturn in the economy, many associations have felt the stress of budgetary shortfalls. But as the economy improves, some are getting a pleasant surprise: They have a budgetary *surplus,* rather than a shortfall.

If you've discovered a surplus, you must make sure that the board allocates that amount appropriately to benefit the community association and owners. Budgetary surpluses are rarer now than in the past, but how you handle yours is still of the utmost importance.

Set Priorities for Extra Funds

After a board initially determines that there's a surplus, its decision about allocation should depend on the association's needs and the tax consequences of that decision, says Virginia attorney Robert M. Dia-

(continued on p. 2)

BEST PRACTICES

Set Sexual Harassment Complaint Procedure to Protect Community from Liability

Association managers need to be concerned about their community's procedures for handling sexual harassment complaints by employees against their supervisors, warns New Orleans employment attorney Charles F. Seemann III. That's because an employer can be held responsible if one of its supervising employees violates federal or state laws that prohibit sexual harassment—even if the employer was unaware of the violation. If you're sued for a supervisor's misconduct, you could end up owing the victim back pay, emotional distress damages, and a penalty amount of up to $300,000 or more, depending on what state you do business in.

What can you do to protect yourself from being held liable if one of your supervisors sexually harasses an employee? You should already have a policy prohibiting sexual harassment and explaining

(continued on p. 5)

Community Association Management Insider (ISSN 1537-1093) is published by Vendome Group, LLC, 149 Fifth Avenue, New York, NY 10010-6823.

Volume 11, Issue 1

Subscriptions/Customer Service: To subscribe or for assistance with your subscription, call 1-800-519-3692 or go to our Web site, *www.vendomegrp.com*. Subscription rate: $469 for 12 issues (plus $17 shipping/handling). **To Contact the Editor:** email *epurcell@vendomegrp.com*. Call: Elizabeth Purcell at (212) 812-8434. Fax: (212) 228-1308.

To Place an Advertisement, Please email Sharon Conley, *sconley@vendomegrp.com,* or call (216) 373-1217.

Budgetary Surpluses (continued from p. 1)

mond. Boards will normally look at their needs and wants to determine what project, if anything, they might use the funds for, such as adding the funds to a contingency or replacement reserve, says Honolulu-based attorney Richard S. Ekimoto.

"I don't think that there's a 'one size fits all' rule for surpluses," says Ekimoto. Diamond agrees that there's no rule for where surplus money should be allocated. And there shouldn't be one, he stresses. "The board should have the flexibility to apply the funds where needed, which will vary from association to association and from time to time depending on the association's financial and physical needs," Diamond warns.

"Normally, the biggest issue is whether the funds should be returned to the owners and if so, how you would do it," says Ekimoto. "The answer to this is probably going to vary from state to state and depend on the governing documents," he adds.

Often, the funds may need to be returned to the current owners even if the surplus is due to a settlement to reimburse the association for repair expenses. "Some might want the prior owners to get a share of the reimbursement," he says. In that case, the board should get legal advice on what it can do with the funds, Ekimoto suggests. "It's difficult to rebate surpluses because owners move—so the recipient of the rebate may not have paid the money that generated the surplus," notes Diamond, who adds that a board could also choose to prepay future expenses to eliminate the surplus.

Don't Restrict Board's Ability to Allocate

Generally, policies help guide the board as it tries to comply with the law and make things run smoothly within the community. But in the case of a surplus, you shouldn't draft a policy for how these funds will be allocated—or *not* allocated—or ask the board to implement such a policy. That's because a policy governing the allocation of a surplus could restrict the flexibility the board needs when making allocation decisions.

The items that could use an extra boost from more funding vary from year to year. And a policy that locks the board into allocating some or all of a surplus to a certain item that doesn't need more money every year could mean that other items that need attention are ignored—even though the association has extra funds.

For example, a surplus allocation policy that requires all or a certain percentage of any surplus to be put into the reserve fund for capital improvements is impractical because each year there could be various items in the community that desperately need attention, while a capital improvement isn't even on the horizon. And it's especially impractical if owners are forced to pay increased assessments to fix an item that needs immediate attention because money has been allocated to a project that won't take place anytime soon.

"It's constraining to have a policy, but there should be a procedure by which the board analyzes the budget to determine the reason for the surplus and appropriate options to consider for the use of the funds," suggests Ekimoto.

"Instead of a policy, a board should use its discretion and rely on advice from the association's accountant and manager," says Diamond. Because you field complaints and suggestions from owners, and you are the most familiar with the community's needs, strengths, and weaknesses, you have good judgment as to which items need a financial boost now and which can wait. You can advise the board about which items are a financial priority.

If the surplus wasn't expected, the board should look into how it happened, but not with suspicion. Rather, an investigation should be done to find out where the savings were achieved or whether something that was budgeted had not yet been done, notes Diamond.

Although a surplus could indicate that assessments are too high, that's rarely the case. More often, a surplus results from a time difference—for example, you budgeted for a new copier in December, but you didn't buy it until January. It can also be caused by an unpredictable variance—for example, you save on plowing during a year when it doesn't snow as much as usual.

Generally, associations budget too thinly, so surpluses rarely occur. But when they do, the best approach is to maintain assessment levels and apply the surplus to reserves or additional resident services or enhancements to the community, suggests Diamond. Only if a surplus continues for more than one or two years and reserves are adequate and fully funded should an association consider reducing assessments, he advises.

"Surpluses are normal accounting and financial events that should be dealt with in due course," points out Diamond. He cautions managers not to overreact. If there are large surpluses, look to see if necessary expenditures for maintenance and services are being made and paid for. "If so, then surpluses should be viewed as a pleasant surprise—and far preferable to deficits," he adds.

Insider Sources

Robert M. Diamond, Esq.: Reed Smith LLP, 3110 Fairview Park Dr., Ste. 1400, Falls Church, VA 22042-4536; *rdiamond@reedsmith.com.*

Richard S. Ekimoto, Esq.: Ekimoto & Morris, LLLC, 1001 Bishop St., Ste. 780, Honolulu, HI 96813; *www.hawaiicondolaw.com.*

RECENT COURT RULINGS

➤ Association's Boat Prohibitions Can Be Enforced

Facts: A homeowner bought a lakefront lot in a community association. Before the purchase, he received and reviewed the community association's covenants and rules. Shortly after moving in, the owner began storing a pontoon boat along the water's edge, which was part of the community's "green belt" area—that is, property around the lake and between the shoreline and the property of individual owners. In its governing documents, the community association noted that the green belt area "is for all members to use and enjoy and must be retained and maintained for this purpose."

The community association notified the owner that he was violating the covenants and rules against storing boats in the green belt area and that he would be fined if he didn't comply with the boat storage regulations. A week later, the owner was notified that he would be fined $25 a day for his continued violations and that he could request a hearing before the community association's board of directors.

At the owner's request, two hearings were held, after which the community association's board of directors concluded that the owner had continued to violate the covenants regarding the storage of his boat in the green belt area and would continue to be penalized.

The owner sued the community association, claiming that its restrictive covenants were "vague and unenforceable." He asked the trial court for a judgment in his favor without a trial. The trial court ruled in favor of the association. The owner appealed.

Decision: The appeals court upheld the trial court's decision in favor of the community association.

Reasoning: On appeal, the owner contended that the restrictive covenants don't prohibit the storage of boats in the green belt area. The appeals court disagreed. It decided that the terms of the covenants and rules prohibiting the storage of boats there were "clear and unambiguous."

(continued on p. 4)

Recent Court Rulings (continued from p. 3)

The appeals court noted that the governing documents stated: "No boat shall be permitted on any lot except in an enclosed garage or such other location approved by the Architectural Committee if screened so as not to be visible from any other lot." Under the governing documents, boats had to be located on the *owner's* property and not on the *Green Belt.*

Not only do the governing documents clearly show that the unambiguous terms of the covenants and rules prohibit the storage of boats on the green belt area, but the owner had been given and reviewed those covenants and rules before purchasing his home, said the appeals court. Moreover, the owner had violated the prohibition by storing his pontoon boat on the green belt area, he was twice notified in writing of the violations, and two board hearings on the matter had been held, the court noted. The owner had been put on notice of the policy and was properly notified of his violations, it added.

■ Crouch v. Bent Tree Community, Inc., June 2011

IN THE NEWS

➤ Retired Marine Wins Battle Over Flagpole

Retired Marine Mike Merola can now fly his flag on the 20-foot flagpole he erected on his property at the Lakeland Village Community Association in Houston, Texas. In December, Lakeland claimed that Merola was in violation of the community's design rules and ordered him to take down the flagpole. When Merola refused, the association sued.

The case hasn't been formally dismissed yet, but the two sides came to an agreement. Merola may keep the pole and fly his flag—as long as he abides by the new guidelines and regulations that Lakeland puts in place. Lakeland is expected to issue a stipulation that Merola must move the pole away from the property line, but isn't expected to take any further action. Merola's court fees and fines, which had reached $20,000 by April 1, have been dropped.

On June 16, Texas Gov. Rick Perry signed a bill into law that protects homeowners' right to fly United States, Texas, or any military branch flags. While the law, prompted by Merola's case, guarantees homeowners the right to mount a flagpole of up to 20 feet on their property, it allows homeowners associations to stipulate the size and location of the flagpole, the flag size, and other details.

Lakeland is expected to draft the new guidelines concerning the flagpole by the end of July. Once those regulations have been adopted, the case will be dismissed.

According to the *Houston Chronicle,* Merola says that many of his neighbors have told him that they plan to put up their own 20-foot flagpoles as soon as his case is dropped.

➤ Augusta HOA Denies Housing for Disabled Veteran

Knob Hill Property Owner's Association in Augusta, Ga., recently denied housing to a retired, paralyzed African-American war veteran. The association claimed that the home would require specialized accommodations and that those accommodations would ultimately lower the overall property value of Knob Hill.

Sgt. 1st Class Sean Gittens and his family were working with Homes for Our Troops, an organization dedicated to providing homes free of charge for disabled veterans, in order to find an affordable place to live in Georgia. During a press conference held by the organization on June 28 to address the issue, the founder, John Gonsalves, expressed regret at the association's decision. However, he asserted that the decision in no way reflected the community of Knob Hill and the people who live there.

Gonsalves went on to explain that this is the first time construction has been blocked by a homeowners association. Homes for Our Troops has built over 100 homes. It's now committed to getting a design approved within Knob Hill for the Gittens family, Gonsalves said, but he emphasized that the decision to stay in the subdivision was ultimately up to the Gittens, who had rented a house with no accommodations in Knob Hill, but planned to move out because they didn't feel welcome anymore.

➤ Florida Adopts New HOA and Condo Laws

New legislation in Florida, effective July 1, will have a major impact on both condominium and homeowners associations within the state. The legislation will primarily affect procedural and operational issues of the associations. Cooperative associations were, as they have been in the past, excluded from the bill.

The law, House Bill 1195, will amend current laws concerning owner privacy rights, employee salary information, and closed board meetings, among other things.

Regarding owner privacy rights, the new law permits owners to publish "personal indentifying information," such as emails and telephone numbers—as long as the owners authorize publication with a signed waiver.

Also, under the new law, employee salary information has been made accessible to unit owners. The law states that an employee's salary information and written employment agreement are now classified as "official records" and are available for owner examination. However, anything classified as "personnel records" is still protected from inspection.

Concerning closed board meetings, the legislature shaped the statute to mirror Florida's Homeowner's Association Act. As of July 1, under both laws, a board may hold closed meetings pertaining to "personnel matters."

Other issues covered under HB 1195 include board term limits, the owner's right to speak at HOA board meetings, and board eligibility.

But the law addresses board term limits only for condominium associations, stating that term limits for directors are valid as long as the term limits are spelled out in the association's bylaws.

All restrictions have been removed regarding an owner's right to speak at an HOA board meeting. An owner may speak at meetings in relation to "all designated items." However, there is no stipulation that the HOA board must publish an agenda, which could complicate the definition of "designated items."

Finally, the law amends the condominium statute for board eligibility. A board candidate must be eligible to serve on the board at the time of the deadline for submitting a notice of intent. If this requirement isn't met, the candidate's name will not appear on the ballot. The new law sets the deadline for submitting a notice of intent at 40 days prior to the election.

Best Practices (continued from p. 1)

what sexual harassment is. But you also need to make sure you have an effective sexual harassment complaint procedure that makes it easy for employees to come forward and report harassment so that you can stop the harassment before it becomes "severe" or "pervasive"—and before the employee sues. And if an employee does sue, a well-written and effectively enforced complaint procedure may convince a court that you took reasonable steps to prevent and correct the behavior.

We'll give you a Model Procedure: Encourage Employees to Complain About Harassment, based on the U.S. Equal Employment Opportunity Commission's (EEOC) guidelines, which you can distribute to your employees along with a copy of your community's policy prohibiting sexual harassment.

Sexual Harassment Law Basics

The Supreme Court has ruled that an employer is always liable for a supervisor's harassment if the harassment "significantly affects" the victim's employment status—for example, by causing the employee to lose a promotion or be demoted or terminated. If the sexual harassment doesn't significantly affect the victim's employment status but creates a hostile or offensive environment, the employer may be able to avoid liability or limit damages. The employer can do this by showing both:

- That it exercised reasonable care to prevent and promptly correct any harassment; and
- That the harassed employee unreasonably failed to take advantage of any preventive or corrective opportunities the employer provided (for example, the employee did not use the employer's complaint procedure to report the harassment) or failed otherwise to avoid harm.

After two landmark Supreme Court decisions, the EEOC published enforcement guidance on an employer's liability for unlawful

(continued on p. 6)

Best Practices

(continued from p. 5)

harassment by supervisors [Burlington Industries, Inc. v. Ellerth; Faragher v. City of Boca Raton]. These guidelines set out what an employer should do to prevent unlawful harassment. And they stress the importance of having a policy *and* complaint procedure on sexual harassment, and distributing both to all employees.

What Complaint Procedure Should Do

Your complaint procedure should encourage employees to report sexual harassment as soon as possible. In part, this means making sure a harassed employee won't encounter any unreasonable obstacles to making a complaint. For example, requiring harassed employees to write out complaints might discourage complaints and open the door to lawsuits.

Like our Model Procedure, your procedure should:

Encourage victims to make complaints. "Encourage your employees to come forward as soon as possible," says Seemann. Isolated incidents of sexual harassment generally don't violate the law. But a pattern of such incidents may be unlawful. If the victim doesn't complain before the harassment becomes a pattern, you can defend yourself by showing that the employee didn't take advantage of your company's established procedure before the harassment became severe enough to violate the law, says Seemann. This makes it difficult for an employee to get a court to award damages.

But if you fail to encourage employees to complain before harassment becomes severe or pervasive, it will be difficult to establish this defense [Proc., par. 1].

Encourage all employees to report observations. Don't just encourage victims to report harassment. Also encourage anyone who witnesses sexual harassment to report it. "That way, you'll have an easier time uncovering harassment and getting rid of it from your workplace," says Seemann. By asking witnesses of harassment to report it, you also make clear to all your employees that you're trying to prevent and promptly correct sexual harassment [Proc., par. 2].

Give employees easy ways to complain. "For your complaint procedure to be effective, you need to make it as easy as possible for employees to report sexual harassment," says Seemann. That means you need to give employees a choice of accessible individuals to complain to. A complaint procedure that requires employees to complain first to their supervisors isn't always effective against sexual harassment because the supervisor may be the harasser. So tell employees that they can complain not only to their supervisors but also to any management-level employee.

Also, designate at least one official outside the employee's chain of command to take harassment complaints. If you have a director of human resources, designate him or her. Otherwise, designate a person in a senior management position, such as a vice president. By allowing an employee to bypass the chain of command, you make it easier for the complaint to be handled impartially. An employee who reports harassment by his or her supervisor may feel that an official within the chain of command will more readily believe the supervisor's version of events [Proc., par. 3].

> **PRACTICAL POINTER:** Require all managers and supervisors to report sexual harassment complaints to appropriate officials right away. Even if the victim wants to keep a complaint confidential, managers and supervisors should understand that they have a duty to report harassment complaints. Otherwise, you could be liable for failing to act on the complaint.

Assure Confidentiality of Complaints

In your complaint procedure, assure your employees that you'll protect the confidentiality of their complaints *to the greatest extent possible.* That way, they'll be more willing to come forward [Proc., par. 4]. On the other hand, never promise *complete* confidentiality—you won't be able to conduct an effective investigation without revealing certain information to the accused harasser and potential witnesses.

Make sure that you share information about harassment accusations only with people who need to know it. Tell people who receive and investigate complaints that they must keep the information confidential. You need to protect the privacy of both the victim and the harasser. If you don't, either of them may file a defamation or invasion of privacy claim against you, warns Seemann.

Assure protection against retaliation. To be effective, your complaint procedure should assure employees that there will be no retaliation against employees for reporting sexual harassment or giving information about harass-

ment in good faith, says Seemann [Proc., par. 5].

That means you should take measures to prevent retaliation. For example, when investigating a complaint, remind the harasser and the witnesses about the prohibition against retaliation. You should also scrutinize employment decisions affecting the complaining employee during and after the investigation to ensure that no one retaliates against the employee.

Although you don't want to discourage your employees from making complaints or reporting violations, it's okay to include the term "good faith" to remind them to exercise good faith when they make a complaint. These words send a signal to your employees that they should consider their motivation when they make a complaint and that the complaint procedure isn't a tool to use inappropriately—for example, to get even with a supervisor who gave them a poor job evaluation, says Seemann.

PRACTICAL POINTER: Be sure you also have a written procedure spelling out how you'll investigate sexual harassment complaints.

Have Employees Acknowledge Procedure

Distribute the new complaint procedure to all your employees—including temporary employees, day laborers, and anyone who gets a paycheck from you. Also, have employees sign an acknowledgment saying that they've read and that they understand the policy and complaint procedure. That way, you'll have a record showing that an employee was aware of your community's policy to encourage victims and other employees to report sexual harassment. And remember to post the complaint procedure in central locations and to include it in your employee handbook.

MODEL PROCEDURE

Encourage Employees to Complain About Harassment

Here's an example of a sexual harassment complaint procedure, developed with the help of employment attorney Charles F. Seemann III and based on the U.S. Equal Employment Opportunity Commission's guidelines, which you can give to your employees. In keeping with suggestions in the guidelines, the procedure encourages employees who are victims of harassment to complain, asks employees who observe harassment to report it, gives harassed employees a choice of accessible individuals to whom they can complain, says that any complaints or reports will be kept confidential to the greatest extent possible, and takes a stand against retaliation.

Check with your attorney about adapting this procedure at your community.

SEXUAL HARASSMENT COMPLAINT PROCEDURE

If you are the victim of sexual harassment, ABC Community strongly encourages you to tell us about the problem by making a complaint.

1. **Do not wait to complain.** You should not wait until harassment becomes severe or persistent to bring a complaint. If you complain right away, we can stop the harassment before it gets worse.
2. **Report sexual harassment of fellow employees.** If you see another employee being sexually harassed, please report this to the director of human resources or to any other management-level employee, including the president.
3. **Where to complain.** You may complain directly to your supervisor, the director of human resources, or any other management-level employee, including the president. You do not have to complain first to the person who is harassing you.
4. **Confidentiality of complaints and reports.** If you make a complaint or report the harassment of another employee, we will protect the confidentiality of your complaint or report to the greatest extent possible.
5. **No retaliation for good-faith complaints or reports.** No reprisal, retaliation, or other adverse actions will be taken against any employee for making in good faith a complaint or report of sexual harassment, or for assisting in good faith in the investigation of any such complaint or report. If you suspect someone is engaging in retaliation or intimidation, report it immediately to human resources or a manager.

Insider Source

Charles F. Seemann III, Esq.: Special Counsel—ERISA Litigation, Proskauer Rose LLP, 650 Poydras St., Ste. 1800, New Orleans, LA 70130; *www.proskauer.com.*

www.communityassociationinsider.com

Search Our Web Site by Key Words: sexual harassment; complaint procedure; retaliation

Community Association Management *Insider*

VENDOME GROUP LLC 149 FIFTH AVE NY NY 10010

Presorted Standard
U.S. Postage
PAID
Permit No. 1906
Southern, MD

Open to Read Your Latest Issue