Community Association Management *Insider*®

AUGUST 2014

INSIDE THIS ISSUE

HOA Flags Member Over Patriotic Display

A more than two-year battle over an American flag display in a Jacksonville, Fla., homeowners association has led to more than $8,000 in fines and a lien on a member's home in that community. A Florida veteran has been fighting with the association about what he asserts is his right to keep the flag in a flower pot in his front yard.

The member reached an out-of-court settlement with the HOA after a lawsuit last year, and he agreed to display the flag in compliance with the association documents. But the association has rewritten its rules since then. According to the HOA, homeowners can fly a flag inside a flagpole on the side of the building, but they can't place the flag elsewhere, like inside a potted plant.

A lawyer from the firm that's representing the HOA said that foreclosure proceedings on the member's home can begin soon if payment isn't made. ♦

PRODUCED IN CONSULTATION WITH

community ASSOCIATIONS INSTITUTE

FEATURE

Reduce Risk of Social Media Threats from Employees and Members

While social media can be used to positively promote your management company and the associations it manages, there are also two inherent dangers in this type of communication. First, social media may be used improperly by your employees, leading to liability for the company. Second, the association's members may use it as an outlet for complaints, leaving the board and manager to undo the damage—undesirable impressions of the community that negative comments have created.

It's very difficult to police the personal social media channels of your employees and community members, and doing so has the potential to tread on privacy and free speech rights. But you don't have to let social media run amok. Use a two-step plan to harness the power of social media and use it in your favor.

(continued on p. 2)

Q&A

Using Reserve Account Funds Appropriately

Q I'm a new board member on my community association's board of directors, and I'm getting up to speed on association issues. There has been some discussion about whether it's appropriate to borrow from our reserve account. What is a reserve account, and what are some guidelines for using its funds?

A A reserve account is an account specifically designed to pay for common elements for which a useful life can be estimated—for example, the replacement of an existing swimming pool, tennis court, or clubhouse roof. It's not intended to fund everyday needs that are covered by the community's general operating account. Reserve account funds are part of any association's long-term financial plan, which helps to strengthen the community's fiscal health and increase the homes' market values, and allows boards to fulfill their fiduciary responsibilities.

A well-funded reserve account clearly signifies that a community association is equipped to deal with its long-range needs. Without a

(continued on p. 7)

Community Association Management Insider [ISSN 1537-1093 (PRINT), 1938-3088 (ONLINE)] is published by Vendome Group, LLC, 216 East 45th St., 6th Fl., New York, NY 10017.

Volume 14, 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.vendomerealestatemedia.com*. Subscription rate: $370 for 12 issues. **To Contact the Editor:** Email *egibney@vendomegrp.com*. Call: Elizabeth Purcell-Gibney at (212) 812-8434. Fax: (212) 228-1308.

To Place an Advertisement, Please email Erin Tyler, *etyler@vendomegrp.com*, or call (216) 373-1217.

Social Media Threats (continued from p. 1)

Step #1: Establish Social Media Policy for Workplace

The rampant use of social media during the workday by employees results in an unrealized amount of time being wasted, warns community association management expert Paul D. Grucza. He says that his company has established a social media policy to ensure productivity, but also to prevent employees from posting opinions and issues pertaining to the company or its community association clients that could negatively color people's impressions of the company or a community. The policy has worked; Grucza credits the rules—which are disseminated and explained to new employees at an orientation—for resulting in a spotless track record for his workers.

The policy that you create for your employees will be company-specific, but it should have some basic elements. It should:

Ban use of social media on company equipment. "We can't stop employees from using social media on their personal cell phones during the day, especially during breaks," says Grucza. But we do suggest that they exercise prudence about the comments that they make personally. We make the policy clear, but we don't constantly hammer staff with warnings. I think that, as a result, our staff has been very professional in how they use Facebook, Twitter, and other channels," he says.

Emphasize social media as a valuable professional tool. For example, Grucza uses it to reach out to industry connections and stay up to date with industry developments. Stressing the value of social media to employees and teaching them to monitor themselves minimizes the dangers inherent in the workplace, advises Grucza.

Clearly state the consequences of improper use. Grucza's policy mirrors the company's computer usage and privacy policies. He says that it's understandable if, from time to time, social media misjudgments are made, but there's a distinction between an accidental post and an employee's trolling the Internet to post content on message boards that are unrelated to the job or reflect badly on the employer.

If a "reasonable person" could've made the mistake, managers could consider just giving a warning. But purposeful misuse of technology is certainly grounds for discipline or even termination, says Grucza, whose policy dictates a written warning for the first violation and termination for a repeat offense.

Grucza notes that getting compliance through "acceptance of policy" is a good strategy. He has found that when employees understand the ramifications of social media abuse for the company they usually are more willing to follow it. "But where there's an absence of guidelines, problems develop. If you have guidelines in place, you have a greater chance of compliance," he adds.

Have employees sign acknowledgment. After reviewing the company's policy with employees, put a note in their file that they were counseled on the effective use of social media. Documenting the fact that employees know about the policy is useful, in case a violation of the policy leads to disciplinary action.

Step #2: Educate Members

Social media, and particularly chat groups, can be problematic from the association's perspective, says Grucza. Problems can stem from three sources:

Association website. Many associations have the ability to either create an online discussion group or comment section on the community's website.

"In this age, where everything can be scrutinized and analyzed, by and large, most associations are careful with their content and make appropriate representations while distributing material that is informational, non-incendiary, non-opinionated, and engaging to the community," Grucza observes. He says that in the overwhelming majority of situations, these types of website-based discussion/comment sections work very well. If your association's website has this feature, the association's "webmaster" should monitor the activity daily and have the ability to delete inappropriate comments and block users who repeatedly make such posts.

Social media group/page. If an association wants to start, say, a Facebook page for its community, trouble can crop up if the association doesn't have a social media policy and a social media charter in place. This is a gray area where inappropriate "venting" by disgruntled members who don't want to take the time to contact the manager or a board member with their concerns can do serious damage: Unregulated posts not only allow members to make false claims and sully the reputation of the community, management, or board members, but they also deprive the management staff of the opportunity to resolve legitimate issues when members choose to use social media rather than lodge a formal complaint that can be dealt with.

So, if the association sets up, say, a Facebook page, a board member or manager should be given the responsibility of managing and monitoring it, just as someone is responsible for maintaining the association's website. And guidelines about what posts will be considered inappropriate and blocked or deleted should be distributed to all members.

Unaffiliated chat rooms. Chat rooms that have been set up personally by owners and have no official ties to the association can become an avenue for complaints that the management company or board may be completely unaware of, says Grucza. "It's frustrating because if we don't know about a problem, we can't fix it," he points out.

Can an association control the abuse of social media among its members? Surprisingly, the answer is yes. The board can attempt to control a threatening social media blitz through education, says Grucza.

"Our association clients are constantly reminding members about the power of social media and the good it can do for the community—and the repercussions of using it the wrong way," he notes. This can be done through meetings, reminders on the association's website, and even through forming a social media and technology committee. Grucza says that there's a high "engagement rate" using this technique, meaning that owners respect and embrace the guidelines that have been set up.

"As with many association initiatives, our best tool is education," he emphasizes. "We remind members that social media sites should be of value to the community, not just outlets for frustration or complaints."

The world of social media is fast-growing and ever-changing, so the rules you create today regarding its use by members may be obsolete in a few months, Grucza says. He recommends that the association's communications committee not only monitor the use of social media by members for potential issues, it should also be vigilant about keeping up with changing technology so it's aware of the methods that members may be using to dispense information. "Staying ahead of the technology curve is crucial," he says. ♦

Insider Source

Paul D. Grucza, CMCA, AMS, PCAM: Director of Education & Client Engagement, The CWD Group, Inc. AAMC, 2800 Thorndyke Ave. West, Seattle, WA 98199; *www.cwdgroup.com.*

RECENT COURT RULINGS

➤ Association Couldn't Enforce Lien Against Bankrupt Homeowner

Facts: An association filed a lien on a homeowner's property after she didn't pay dues or assessments for several years. It filed the lien under the Pennsylvania Uniform Planned Community Act (UPCA). In order to recoup the past-due amount, the association arranged for a sheriff's sale of the homeowner's property. But two days before the sale, the homeowner filed for bankruptcy, which meant that the association couldn't sell her property at the sale. The sale was cancelled, but the association sought to enforce its lien.

The homeowner argued that her bankruptcy filing precluded the association from pursuing the lien, and that the association had three years within which to enforce the lien and hadn't, therefore, giving up its right to do so. The association claimed that the sheriff's sale was an "action in debt" that constituted enforcing the lien.

A bankruptcy court and district court ruled in favor of the association. The homeowner appealed.

Decision: A Pennsylvania appeals court vacated the decision of the lower courts.

Reasoning: The appeals court determined that the association didn't have a valid statutory lien on the debtor's property pursuant to the UPCA, so the homeowner could avoid the association's claims. That was because an action in debt, such as the sheriff's sale, didn't constitute a "proper method to enforce a statutory lien under the UPCA." Thus, any portion of the lien representing assessments due three years before the date of the homeowner's bankruptcy petition had been extinguished, said the appeals court.

- In re Makowka, June 2014

➤ Homeowners Bound by Vague Restrictive Covenants

Facts: Homeowners installed landscaping on their property without receiving approval from their association's architectural review committee (ARC), which was required by restrictive covenants in the community's governing documents. The homeowners refused to remove the landscaping after they were informed by the association's manager that it conflicted with the appearance of the community and was prohibited. They argued that the restrictive covenants were vague and ambiguous as to what outdoor improvements could be made by homeowners. A trial court ruled in favor of the association, and the homeowners appealed.

Decision: A Tennessee appeals court upheld the trial court's decision.

Reasoning: The appeals court agreed with the trial court that the association was entitled to enforce its restrictive covenants requiring homeowners in the community to apply for and receive permission to make landscaping changes to their yards. The ARC had acted within its discretion in ordering the homeowners to remove the improvements that it found to be inconsistent with other homes in the neighborhood—despite the fact that it agreed that the restrictive covenants are vague and that their enforcement is very subjective.

The appeals court found that the covenants are enforceable as long as the homeowners are on notice of the board's general authority and the board then follows its own appropriate procedures in enforcing the covenants.

The appeals court pointed out that, although the covenants were vague in some areas, they also clearly define what an improvement is and state that it specifically includes landscaping. Also, when the homeowners signed and purchased into the community and accepted the part of the deed regarding restrictive covenants, they acknowledged that they may have to get permission for any improvement made that would be incompatible with the rest of the neighborhood.

- Avalon Sections 4 v. Chaudhuri, June 2014

➤ Board Could Unilaterally Increase Regular Assessment

Facts: An association's governing documents granted the board the authority to levy a special assessment if the regular assessment is inadequate. The board raised the regular assessment from $100 per quarter to $130 per quarter. Notice was sent to the homeowners. This increase was discussed at the annual association meeting, which included the presence of a

quorum of the membership. However, the members didn't vote on the assessment increase.

Two years later, the homeowners and the other members were also charged a $50 special assessment, but there was no evidence the required 10-day notice was given.

The homeowners continued to make only $100 payments for another year, but then paid no assessments. The governing documents state that the association may charge a late fee and 18 percent interest on payments that are over 20 days late, which it did for the homeowners. The association later sued the homeowners when they refused to pay.

A magistrate court ruled in favor of the association as to the regular assessment payments, but concluded the special assessment didn't properly comply with the notice requirement in the governing documents. The homeowners appealed, arguing that the governing documents provided that the regular assessment couldn't be changed by the board without approval by members, including the homeowners, at a meeting.

A district court upheld the decision in favor of the association. The homeowners appealed again.

Decision: An Idaho appeals court upheld the decision of the lower courts.

Reasoning: The appeals court noted that the magistrate had established that, as residents in the community, the homeowners are subject to the association's governing documents, including the rules regarding regular assessments to pay for the association's costs and expenses. And it agreed that the governing documents provide only for written notice in the event any meeting may be held to allow a membership vote in connection with an increase in the regular assessment. But they didn't require a meeting for the fixing and levying of assessments, and, indeed, other provisions place that responsibility with the board.

- Eagle Springs Homeowners' Assn. v. Herren, June 2014

➤ No Damages Awarded for Homeowners Who Filled in Excavation Site

Facts: Homeowners bought an empty lot in a planned development and hired an architect and contractor to build a three-story, single-family home there. Prior to building the lot, an association member with an adjacent lot asked the homeowners if they would like to jointly buy with him an empty lot that each of their properties had in common so that they could each have more space between their properties. The homeowners declined the offer and went ahead with plans to build on only their purchased lot. The member then filled an empty seat on the association's board of directors. Other neighbors in the community decided to buy the empty adjacent lot and built a house on it.

Shortly thereafter, the neighbors asked a court for an injunction—that is, an order from the court—preventing the homeowners from building their home as planned because it would violate the driveway easement the neighbors claimed they had on the homeowners' empty property.

After a series of communications with the board, including the member who had originally wanted to make sure that the homes surrounding his weren't overbuilt to the edge of their lots, the homeowners were told that they would have to stop construction and rework their plans. They spent $150,000 filling in the excavation site to avoid legal action the board had threatened.

In the meantime, however, city officials contacted the board to let them know that an easement didn't, in fact, exist. Therefore, the homeowners would have been entitled to build their home as planned. When the homeowners learned that they had unnecessarily spent $150,000 while the board knew that an easement—the reason they were told to fill in the excavation site—didn't actually exist, they sued the association for breach of fiduciary duty. They also asked the court for a declaration that a driveway easement didn't exist. A district court ruled in favor of the homeowners by issuing the declaration that the easement didn't exist, but it ruled in favor of the association as to the breach of fiduciary duty claims. The homeowners appealed.

Decision: An Illinois appeals court upheld the decision of the trial court.

Reasoning: The appeals court agreed with the trial court that one of the central issues in the case—whether a driveway easement actually exists or not—had been resolved. The city, which was the final authority on whether official easements existed, had sent documentation that it didn't. The neighbors claimed that the easement had been given to them through a casual arrangement with the original builder of the development. But personal agreements for easements for land couldn't be honored in this situ-

(continued on p. 6)

Recent Court Rulings (continued from p. 5)

ation. For the easement to be real, the builder would have had to record it with the city, which he never did.

Although the homeowners asserted that the board member had improperly influenced the board to prevent the homeowners from building as planned, and was motivated by self-interest because the claimed driveway easement would provide more light and air, and less density, to the rear of his home and would increase his property's value, the appeals court found no actual evidence. The association's attorney had advised the board member to recuse himself from all board decisions regarding the homeowners' construction and the easement, which he did.

The appeals court agreed with the trial court that the association hadn't breached its fiduciary duties by not immediately informing the homeowners that the board wouldn't be pursuing legal action against them due to the fact that the easement had been proven to be fictitious, even though it unfortunately resulted in $150,000 in damages to fill in the excavation site. ♦

- Feliciano v. Geneva Terrace Estates Homeowners Assn., June 2014

IN THE NEWS

➤ Calif. Design Defects Case Falls in Favor of HOAs

In a unanimous decision, California's Supreme Court has ruled that the principal architects for a condominium project may be sued directly by a condominium homeowners association for design defects. In that case, units in a condominium project in San Francisco allegedly developed several defects including water infiltration, structural cracks, and overheating that made units virtually uninhabitable at times. The association sued the architects, alleging that these defects were caused by negligent design.

The architects claimed that they were not in a direct contractual relationship with the eventual buyers and, therefore, owed a duty only to the developer who had hired them. The trial court dismissed the complaint. However, the California Supreme Court reinstated the suit, holding that the architects did owe a duty to the eventual unit owners. The Court noted that the importance of contractual "privity" has diminished over time and liability to foreseeable third parties has been extended in many circumstances.

In deciding that the architects owed a duty of care to the ultimate owners, the Court highlighted three factors: (1) the closeness of the connection between the architects' conduct and the plaintiffs' injuries; (2) the limited and predictable class of potential plaintiffs; and (3) the absence of options for the owners in obtaining design services on their own—that is, that ultimately the owners are forced to rely on the skill of the developer's architects.

The Court concluded that an architect owes a duty of care to future homeowners where the architect is the principal architect on the project—that is, the architect, in providing design services, is not subordinate to any other design professional—even if the architect doesn't actually build the project or exercise ultimate control over construction decisions. The ruling indicates that, even though, on most projects, the developer has the final say on design choices, the architect who makes recommendations on the design cannot escape liability [Beacon Residential Community Association v. Skidmore, Owings & Merrill, LLP, July 2014].

➤ HOA Policy Aims to Protect Members from Bears

A Central Florida neighborhood has created a policy aimed at protecting homeowners from bears. The homeowners association voted for the unprecedented change in an attempt to try to prevent another bear attack after a resident was recently mauled. The attack is considered the worst bear attack in state history. Officials have maintained that bears can be kept out of neighborhoods by limiting their food supply—like open trash cans.

That's why the association voted unanimously for a new policy that requires all homeowners to use "bear-resistant" trash cans that have locks on them. It also banned beekeeping and feeding of wild animals. Warning letters and fines may be issued to members who fail to comply. However, the association has decided to pay for the cost of these new "bear-resistant" trash cans for the first year. ♦

Q&A (continued from p. 1)

well-funded reserve account, an association's only option to pay for repair needs that arise may be to impose a special assessment, which some members may feel is unfair because it penalizes those members who happen to live in the community when these predictable expenses become due.

There are several proper uses of reserve account funds. For example, with the proper establishment of a reserve account, income taxes can be reduced and an association can assure that every present and future member pays a fair share of required future capital expenditures. To determine how much to fund a reserve account, the board should hire an engineer to prepare a replacement study that will project the repair and replacement needs and costs of the association's common elements.

Once funded, the reserve account should generally be tapped only to pay for items listed in the replacement study—with certain exceptions. To use the reserve account appropriately, follow these guidelines:

Guideline #1: Charge capital items from most recent replacement study to reserve account. If an item's actual cost is significantly greater, or the useful life is shorter, than estimated, then the engineer should be consulted to update the replacement study as quickly as possible to reflect this transaction's impact. The updated study should be integrated into the coming year's budget.

Guideline #2: Charge capital items excluded from replacement study to reserve account. Since engineering studies only estimate the common elements' replacement costs, certain items may have been missed during the preparation of the engineer's report, or the costs and conditions of an item's replacement may have changed over time. An association should recoup both the element's replacement cost and the deficit created by the unexpected expenditure through an increased replacement contribution level.

Guideline #3: Don't charge minor repairs to reserve account. These should be funded through the operating budget. Associations should define thresholds for "minor" and "major" repairs with their managing agent and accountant.

Guideline #4: Don't charge maintenance costs to reserve account; establish separate fund. A deferred maintenance fund should provide for the periodic maintenance of items, such as painting, caulking, and power washing. It would be inappropriate to use the reserve account for these types of maintenance expenditures. Boards should establish a deferred maintenance fund for the maintenance of items that don't recur annually.

Guideline #5: Charge developer transition-related items to reserve account. During the initial years of an association's existence there may be situations in which a developer is responsible for various replacements to the common elements. However, due to transition litigation, the developer may refuse to perform the necessary repairs or replacements. These types of expenditures can be charged to the reserve account, and any money subsequently received should reimburse the account. If there is no settlement, the engineer should be consulted to determine the impact on the association's reserve account, and the association's future funding policy.

Guideline #6: Charge income taxes to reserve account. Many associations choose to allocate any interest or investment income earned by the reserve account back to the fund. Such income may be contributed net of the federal income taxes, because associations must pay tax on such income.

Guideline #7: Charge interest expense to reserve account. If applicable, interest expense may be charged to the fund. Many associations have authorized major capital replacement projects only to discover that they are unable to fund all of the planned replacements. Absent a special assessment, many associations seek assistance from lending institutions to close these funding gaps. Proper practice is to include the expenditure, debt service, and the future assessments required for debt repayment in the reserve account budget.

Guideline #8: Don't borrow from reserve account. Borrowing could create negative tax implications and may ultimately lead the association down the road to financial ruin. To avoid this, an association should regularly monitor its operating budget to ensure that each year's deficit, if any, is addressed in the subsequent year. ♦