



Community Association Management Insider®

Helping You Run Your Condo or Homeowners Association Legally and Efficiently

FEBRUARY 2015

FEATURE

We'll give you nine tips for improving decision-making — and avoiding board-related lawsuits.

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Comply with Fiduciary Duty by Improving Board's Decision-Making Process

While board members have what's known as a "fiduciary duty" to the association, some members—especially those who are at odds with choices the association has made—mistakenly think that the board should serve their particular interests. That goes squarely against the concept of fiduciary duty—that is, a legal obligation imposed on all board members to be loyal to the association.

Members might also suspect that board members are acting in their own interests. A member might even sue the association over a decision he or she thinks is in the interest of individuals on the board and not in the best interest of the association. Your association's board is often called upon to make judgments about important community issues and the threat of a lawsuit shouldn't affect the board's ability to operate. But it still should be cautious when making decisions.

Focus on improving your board's decision-making process. Doing so will increase the likelihood that courts will defer to your board's judgment and decrease the chance of members suing board members for breaching their fiduciary duties.

Follow Nine Tips to Avoid Litigation

Generally speaking, a fiduciary is someone who transacts business, or handles money or property, on behalf of others. Because of the nature of the relationship, being a fiduciary entails a duty of loyalty, care, and good faith. In the community association context, board members must act in good faith and use the same degree of care that a reasonably prudent person would use. Keep the following points in mind when making decisions as a board.

Tip #1: Give proper notice of meetings. When planning board meetings or meetings of the members, make sure you follow any notice requirements set in your association's governing documents and your state law. This is a fundamental requirement that must be observed with respect to all association meetings. So check whether

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your state law or governing documents have such requirements and work closely with your board and attorney to follow any notice requirements.

Tip #2: Don't make decisions or take actions unless a quorum is present.

Before making any decisions or taking any actions at a meeting, make sure a quorum is present. A quorum is the number of people who must be present for the board to take any official actions. Your association's governing documents and/or your state law will explain how many people make up a quorum. Some board members mistakenly believe that a meeting can proceed without a quorum present as long as no one objects. But, with very few exceptions, actions taken at meetings where a quorum isn't present are invalid.

If a quorum isn't present at a meeting, either take steps to get more people to attend the meeting—for example, you could take a 30-minute recess and call people to try to get them to join the meeting—or meet at some other time. Keep in mind, however, that some states' laws let associations continue a meeting that had a quorum when it began but lost it as the meeting progressed because people left. Consult your attorney to find out what your state law says.

Tip #3: Don't serve alcohol at meetings. Some boards hold board meetings at directors' units, often accompanied by beer or wine. This is a very bad idea. It's common knowledge that alcohol impairs decision-making. And while one drink at a meeting might seem harmless, it could potentially cause trouble if there's ever a lawsuit and a court must decide whether to defer to the judgments the board made during that meeting. So if you want to increase the likelihood that courts will defer to your board's judgments, don't serve alcohol at meetings.

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Tip #4: Allow sufficient discussion at meetings. Let those present at meetings contribute to the discussion of the matters at hand. If a court sees that your board didn't consider other people's points of view, it may be less likely to defer to your board's judgments. Certainly, boards have the authority to place reasonable limits on the length of time each participant can speak during a meeting and on the total time afforded for discussion. But any attempt to prevent discussion and railroad issues to conclusion will be looked at skeptically by courts.

Tip #5: Discuss important matters at two meetings. For important matters—unless you're faced with an emergency situation—don't make hasty decisions. Instead, discuss such matters at no fewer than two meetings before drawing any conclusions. Do this even for matters that seem to have pretty obvious solutions, but have a potential to be controversial in the community. When a board can show that it took its time making a decision and weighed all of the pluses and minuses of various courses of action, a court will be more likely to defer to its judgment.

Tip #6: Form committees. A good way to show that your board invited others' input and considered alternatives before deciding on a course of action is to appoint a committee of members to brainstorm solutions to problems. A committee of members can help the board by making recommendations to it, ranking them in order of preference, and explaining why certain solutions are better than others. That doesn't mean that the board should cede its decision-making responsibility to such committees though. Indeed, boards should make clear to any committee they appoint that the board is seeking information and recommendations, but that the final decision will be the board's. As the only elected body in the community, the board should always make the final decision.

Tip #7: Get professionals' advice. Getting the advice of appropriate professionals, such as attorneys, engineers, and architects, can help show that your board made an informed and reasonable judgment. Your board should do this when it's dealing with an issue that's clearly outside board members' expertise, such as a structural problem with the physical components of your community. Although doing so can be costly, if the matter ends up in court, it will be money well spent. It's more difficult for anyone to accuse a board of acting unreasonably if it followed the advice of a competent professional.

Tip #8: Choose least intrusive solution. Whenever your board is faced with more than one viable solution to a problem, it should choose the one that's least intrusive on members' rights. Boards often get into trouble when they take actions that trample on members' rights. But when a board can show that it chose the solution that had the least effect on members, a court will be more likely to defer to its judgment.

Tip #9: Explain rationale in meeting minutes. Courts will often read the meeting minutes to get a feel for the board's decision-making process and rationale for the decision in question. If the minutes reflect little discussion—or just a motion and second for the motion—before a decision was made, a court will be less likely to defer to the board's judgment. Concise minutes are generally desirable, but when an important decision is being made, it doesn't hurt to explain the basis for it in the minutes.

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Your meeting minutes should also include important procedural details about the meeting, such as the date and location of the meeting, the attendees, that there was a quorum present, and the wording of any motions passed or defeated. Including this information in the minutes will help show that the board went about its business in an orderly, legitimate way.

Court: Association Had No Fiduciary Duty to Member

When a member doesn't understand that the board's fiduciary duty is to the association first and foremost, it unfortunately can result in a drawn-out lawsuit. This is especially true in situations involving money—specifically, when a member thinks she isn't obligated to pay for something. If a member thinks that she isn't required to pay for an item or repair costs, you may have to defend your actions. A recent Kentucky case demonstrates how far this can go. Happily for the association in that case, it prevailed against a litigious member of the community.

There, a member noticed a window leak in her two-story penthouse unit. For several years after, the member reported that and other water leakage problems to the association's board. The association eventually waterproofed the exterior masonry, which resolved the problem. But a dispute arose over the need to replace the unit's wall of windows and over who should bear the cost of replacement.

The association contended that members owned the windows in their units and were personally responsible for replacement costs. The member claimed that her wall of windows didn't need to be replaced, but that the association should be responsible for any replacement costs because windows are a "common element." She sued the association, arguing that any need for replacement was caused by the association's alleged failure to maintain the exterior of the building as required by the governing documents—a failure that was a breach of its fiduciary duty to members.

After a jury trial, a trial court ruled in the member's favor. It determined that the windows needed to be replaced and replacement was necessary because the association hadn't exercised reasonable care in maintaining the building's exterior. It found that the association breached its duty to exercise "good faith and loyalty" in making decisions with respect to members. It awarded \$54,000 to the member.

The association appealed. An appeals court reversed. The member appealed again. The Supreme Court of Kentucky determined that the association hadn't breached its fiduciary duty, and thus upheld the appeals court's reversal. It concluded that the association didn't have a fiduciary duty to individual owners. The association was a nonprofit corporation, which in Kentucky doesn't have a fiduciary duty. Rather, said the court, the officers and directors have a fiduciary duty, but that duty is to the *nonprofit corporation*, not the *owners* of individual units.

Because the association was contractually obligated to maintain the exterior of the building, the jury could have determined that its failure to do so breached its general contractual duty to act in good faith. But a jury's finding of failure to act in good faith isn't necessarily equivalent to a finding of a breach of fiduciary

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duty. The court noted that, in a fiduciary relationship, the fiduciary—here, the association—must make every effort to avoid having its own interests conflict with those of the principal—here, the member.

“When conflict is unavoidable, the fiduciary must place the interests of the principal above his own,” the court said. “A fiduciary duty requires more than the generalized business obligation of good faith and fair dealing,” it explained. Because the jury awarded \$54,000 in damages as a result of a breach of fiduciary duty and not breach of contract, the court upheld the appeals court’s reversal. The trial court should’ve dismissed the fiduciary duty claim [Ballard v. 1400 Willow Council of Co-Owners, Inc., November 2013]. ♦

RECENT COURT RULINGS

➤ **Association Didn’t Respond Properly to Flag Complaint**

FACTS: A homeowner flew the American flag on a flagpole in front of his house. The association sued the homeowner to enjoin him from displaying the flag. The homeowner asked a trial court for a judgment in his favor without a trial. The trial court ruled in favor of the homeowner without specifying the grounds upon which it made the decision. The association appealed.

DECISION: A Texas appeals court upheld the lower court’s decision.

REASONING: The homeowner contended that the association may not prevent him from displaying his flag under the federal Freedom to Display the American Flag Act, as well as the Texas state law. The Flag Act says that a condominium association, cooperative association, or residential real estate management association may not adopt or enforce any policy, or enter into any agreement, that would restrict or prevent a member of the association from displaying the flag of the United States on residential property within the association with respect to which such a member has a separate ownership interest or a right to exclusive possession or use.

According to the homeowner, the association is prohibited from restricting his display of the flag because: (1) the association qualifies as a “condominium association,” “cooperative association,” or “residential real estate management association” as those terms are defined by the act; (2) the homeowner is a “member” of the association, as that term is defined by the act; and (3) he displays his flag on residential property for which he “has a separate ownership interest or a right to exclusive possession or use.” The member conceded that the Flag Act allows the association to place “reasonable restrictions” on displaying the American flag “necessary to protect a substantial interest of the association.”

The homeowner flew the flag from a flagpole suspended above his front yard (the association’s property). The flagpole is attached to a beam anchored (but not affixed) to his front porch (the homeowner’s private property). The association contended that this display doesn’t meet the “separate ownership interest or a right to exclusive possession or use” requirement. It also argued that the flag-

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pole was a safety hazard, and thus the association was acting to protect the safety of its residents.

The appeals court said that it didn't need to decide whether the Flag Act bars the association from enforcing its guideline regarding flag display because the association failed to challenge the homeowner's motion for summary judgment—that is, a judgment in his favor without a trial—under the Flag Act in its response to the motion. “When the trial court does not specify the basis for its summary judgment, the appealing party must show it is error to base it on any ground asserted in the motion,” the appeals court noted. The appeals court stressed that, when summary judgment may have been rendered by a trial court—properly or improperly—on a ground not challenged by the party appealing the ruling, the trial court's ruling must be affirmed.

Here, the appeals court concluded that the homeowner's motion sufficiently raised the Flag Act as a possible ground for a judgment in his favor without a trial. While it was true that the trial court didn't specify on which grounds it granted summary judgment, the association failed to challenge the court's grounds.

- Forrest Lake Townhouse Assn. v. Martin, January 2015

► Federal Court Couldn't Rule on Homeowners' State Claims

FACTS: Two homeowners sued the association. They asked for a temporary restraining order to stop the association from locking them out of their home due to the foreclosure on their home. They claimed that the president of the association began harassing one of the homeowners due to her nationality and language barrier.

According to the homeowners, the association wouldn't accept their payments beginning in 2010 and wouldn't allow them or their children to attend association meetings. The homeowners also claimed that the president and association fraudulently foreclosed on the property while one of the homeowners was under Chapter 7 bankruptcy protection, which constituted elder abuse and was carried out in violation of various California laws relating to foreclosure. The homeowners stated that they were never given an opportunity to correct matters related to the foreclosure or payments.

The homeowners sued the president of the association and the association in federal court, believing that the court had jurisdiction over their case. They cited violations of their due process rights, freedom of religion rights, and the Homeowners Bill of Rights in their lawsuit.

DECISION: A federal court ruled in favor of the president and the association.

REASONING: The district court noted that the crux of each of the homeowners' claims for relief was events leading up to foreclosure and allegedly wrongful foreclosure in violation of various California laws. Foreclosure activity carried out by private entities, such as homeowners associations, pursuant to state law doesn't implicate constitutional interests—which are decided in federal, not state

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court—the federal court noted. Therefore, the homeowners' lawsuit should be dismissed for lack of subject matter jurisdiction, said the federal court.

The federal court also denied the homeowners' request for a temporary restraining order that would bar the association from locking the homeowners out of their home. It asserted that it couldn't grant any relief at this stage in the proceedings. That was because federal courts—unlike state courts—are courts of limited jurisdiction; they lack inherent or general subject matter jurisdiction. Federal courts can adjudicate only those cases that the United States Constitution and Congress authorize them to adjudicate. That doesn't include cases like the homeowners' case here. The homeowners weren't able to adequately allege a basis for subject matter jurisdiction by the federal court, so it couldn't give them a temporary restraining order. ♦

- *Bozorgi v. Wood Crest Hills Home Owners Assns.*, January 2015

RISK MANAGEMENT

Recognize Warning Signs, Get Help for Elderly Members

Although many elderly members in your community are capable of living independently, sooner or later you may have an elderly member who has trouble coping with day-to-day concerns, such as managing money or keeping his unit tidy. An elderly member who has trouble coping may neglect normal upkeep in his unit. Oversights can lead to property damage and safety concerns. For example, the member may eventually stop cleaning, let his bathtub overflow, or leave the gas range on—putting himself, other members, and your condominium building at risk. You can help avoid disaster by looking for six warning signs that an elderly member's situation might become serious.

Heed Warning Signals

If a mishap occurs that affects the safety of other members or the condition of the building—such as an elderly member's overflowing sink—you would probably talk to the member and ask him to be more careful. But you can act promptly, before other members are put at risk, if you are aware of the following signs or triggers that should cause an association or building staff to pay more attention to an elderly member and that an appropriate social service agency should be notified.

Signal #1: Repeated questions or requests. An elderly member may ask a staff member several times a day whether the mail has come in yet. This may possibly be a sign of dementia or it may just mean that the member is lonely. If a member asks repeated questions, monitor the situation for other signs or triggers. An elderly member may make repeated calls for things she no longer can do, such as opening jars. This is an indication of physical frailty or arthritis, and means that nobody else is around to help and additional assistance may be needed for the member at home.

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Signal #2: Wandering. You may find your member wandering around your building. It is common for a person with dementia to wander and become lost, and many do, repeatedly. In fact, over 60 percent of those with dementia will wander at some point.

Signal #3: Inappropriate dressing. This could be dressing in heavy gloves and an overcoat in 90 degree weather or going outside without shoes when it's snowing. Associated with this is any uncharacteristic action or deterioration of personal habits, such as infrequent bathing and shampooing.

Signal #4: Substance abuse. A member may ask your staff to buy him alcohol, or may slur, which may indicate a substance abuse problem, or it may mean that he is overmedicated. Overdosing on medication may indicate confusion, forgetfulness, or a misunderstanding of a doctor's instructions.

Signal #5: Compulsive hoarding. Compulsive hoarding was once categorized as an obsessive-compulsive disorder. But recent studies are showing that it is a mental illness of its own. Building staff usually become aware of hoarding behavior through maintenance visits or complaints from neighbors about smells or pests originating in the member's apartment. Hoarding can be dangerous for the member if one of his collected items were to fall on him.

Signal #6: Frequent visits from strangers. Frequent unrelated visitors may indicate the possibility of exploitation. Elderly members may start to bring unrelated individuals into their homes because the members are lonely or confused, and these people may be exploiting them financially. These strangers may start walking off with the elderly member's personal property and valuables.

Assist Member in Need

Fortunately, there are local and state agencies that assist elderly members. Programs are available, regardless of income, to those who are mentally or physically impaired and unable to carry out daily chores or protect themselves from neglect without assistance, and who have no one available to assist them responsibly. If the member is better able to care for himself and his unit with the help of these agencies, your building will benefit, too.

Your search for agencies can start with a public service of the U.S. Administration on Aging called the Eldercare Locator, which is celebrating 20 years of connecting the elderly and their families or caretakers with community resources and services. Visit www.eldercare.gov for more information.

Keep two things in mind when calling one of the agencies provided by the Eldercare Locator. First, describe the danger to the member—for example, a member who leaves gas jets on may asphyxiate himself or die in a fire. Don't describe the danger to your building. Social services are interested in the welfare of the elderly member; they're not interested in your building.

Second, let the agency decide how to help. Don't try to diagnose the member's problem or tell the agency what kind of help is needed. You may think he needs to be in a hospital, but you should stick with the facts—for example, the member leaves faucets running and gas jets turned on. Let the agency decide what help is called for. ♦

Q&A***Purchasing Property at Foreclosure Sales***

Q A home in our community has been foreclosed on by the association after the owner failed to pay assessments for a long period of time. The association wants to buy the foreclosed lot. Is there a rule regarding how much money an association is allowed to spend buying a foreclosed lot? There also are past-due real estate taxes on this lot. How much can an association spend paying the past-due real estate taxes owed on a lot if obtained in its own foreclosure action?

A A situation like this is state-specific. For example, in Florida, the Florida Homeowners' Association Act states that an association may purchase a parcel at its foreclosure sale, and hold, lease, mortgage, or convey the parcel, says Fort Myers, Fla., attorney Joseph E. Adams. Like statutes in some other states, the Florida statute does not provide a rule about the amount of money that can be spent. But some states may have different rules that you must follow. This is why it's crucial to check with your association's attorney before taking action.

However, it's rare for an association to bid more than its "judgment credit," meaning that the association would normally stop bidding when a third-party bidder exceeds the amount of the association's judgment, and the association would be paid in full for its unpaid assessments, notes Adams. There may be rare cases where a different approach may be justified—for example, bidding more than the judgment credit amount. In such cases, the association's attorney should be consulted in advance to determine if there are any limitations on acquiring title to a parcel in the community outside of the normal foreclosure process, he stresses.

The payment of taxes in this situation is also state-specific. The Florida statute is silent on the point. "It seems self-evident that any corporation has the power to expend its resources to protect and preserve any asset it owns, which would include paying delinquent taxes on a foreclosed parcel," says Adams, who doesn't believe he has ever seen governing documents that would limit the authority of an association to pay taxes on property it owns. Adams notes that a strictly drafted expenditure limit could possibly come in to play. Your association's attorney should also review this matter in the context of your specific situation, he emphasizes. ♦

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