

SOUTH COAST HOMEOWNERS ASSOCIATION

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INSPECTION OF RECORDS IN AN HOMEOWNERS ASSOCIATION

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Editor's Note: This article appeared in the November 1999 issue of the *ECHO Journal*, the monthly publication of the Executive Council of Homeowners, a Northern California HOA organization and is reproduced here with their permission. Mr. Fier is in private law practice in San Mateo. He can be reached at 650-572-1900.

The matter of inspection of records comes up in almost every homeowners association. Some of the most frequent questions are:

- What are the inspection rights of members who want to review the records of the association?
- What are the limits on this inspection right?
- Who pays for the costs involved?
- What are the inspection rights of directors

These questions, as well as other questions dealing with the inspection rights within an association, are addressed in this article.

MEMBER INSPECTION RIGHTS

1. *What can be inspected by a member?* Section 1363(f) of the Civil Code (Davis-Stirling Act) requires that association members be given access to association records in accordance with the Corporations Code. Records must be maintained in written form (Corp Code 8320(b)). A request to inspect is not complied with unless and until the corporation makes the records available in written form at its expense (i.e. computer records must be printed out as well as e-mail messages, and tape recorded messages

must be transcribed).

2. *Who can inspect?* The requesting person or an agent or attorney. The law only allows one person to inspect and there can be no limitation on inspection rights (Corp Code 8313).
3. *Who should pay for the copies?* The right to inspect also includes the right to make copies and extracts (Corp Code 8311). Who pays for the copies is a matter of association policy, but if a charge is made, it should be reasonable. If the association is managed, the charge for copying should not exceed what the management company charges the association.
4. *Can the association or management company charge an inspection fee?* The law prohibits any limitation on a member's rights. Therefore, an inspection fee should not be charged because it could be viewed as an attempt to limit this inspection right.
5. *What records are required to be kept?* The association is required to keep records, which include, but are not limited to, all governing documents; adequate and correct books and records of account; minutes of the proceeding of its members, board and committees; and members' names, addresses and classes of membership.
6. *What constitutes accurate and correct books and records of account?* "Books" is defined in Webster's as a business record or register. "Record" is defined as an account in written or other permanent form. The custom and practice of the association should be given weight in this situation.
7. *What if a member demands to see all invoices and checks?* A member **does not** have the right to inspect these documents. They are backup information used to form the association's books and records. If an audit or review has been performed by the association's CPA, and the results were distributed to members, this would be a duplication of work already done. A director, however, could obtain access to this information.
8. *What are the restrictions on a member's right to inspect?* The purpose for inspection must be reasonably related to a member's interest. The demand for inspection must be in writing and request a reasonable time (Corp Code 8333). A membership list can be obtained, but it cannot be used to solicit money or property for a commercial purpose, sold to or purchased by anyone; for sale to any person; or for any purpose which the demanding member does not reasonably and in good faith believe will benefit the corporation. If the association feels that the membership list will be misused, it can refuse the demand or sue to restrain its misuse. If a member fraudulently or maliciously violates the law regarding the use of the membership list, he or she may be held liable for any damages suffered by the association, may be required to forfeit or repay any profit derived from the violation, and may be liable for punitive damages and reasonable costs and expenses, including attorney fees.

**PLEASE FEEL FREE TO MAKE COPIES FOR YOUR BOARD MEMBERS
SHARE THIS NEWSLETTER WITH YOUR ENTIRE BOARD OF DIRECTORS**

DIRECTOR'S INSPECTION RIGHTS

A director's inspection rights are absolute. (Corp Code 8334). Not only can a director inspect and copy all books, records and documents, but a director can inspect the physical properties of the association. The law does not require a written demand and no statement regarding the director's purpose need be presented. A director has fiduciary duties that he or she must perform in good faith and with the best interest of the association in mind.

The only limitation on these broad inspection rights is that this right must be balanced against the constitutional rights of members. In the case of *Chantiles vs. Lake Forest II* (1995), a director wanted to inspect the proxy ballots of an election. The court denied this request and said a board member's request must be balanced with a member's reasonable expectation of privacy in his/her ballots.

Can a member's right of inspection be limited? If it is believed that the director is seeking information for an improper purpose, then the demand can be denied. If the situation winds up in court, then the court has the power to balance the competing demands and limit the inspection. Consider a couple example situations:

What if a committee investigating embezzlement by a board member has developed working papers and the board member being investigated demands to see these papers before the committee issues the final report? Should a director be given access to documents if a disclosure is contrary to the board's fiduciary duty to the corporation?

What if a board member demands to see the bids for a painting contract, before the bids are closed, because his brother-in-law is bidding on the job? Should a director be given access to documents if a conflict of interest exists?

In these situations, a denial might be appropriate. Alternatively, the association might condition the right to inspect on adherence to certain ground rules, i.e. the nondisclosure of the contents of the inspection to others.

LEGAL REQUIREMENTS

There is a legal requirement that proper records be kept. Directors and officers of an association can be found guilty of a misdemeanor if they act in any of the following ways:

1. Knowingly make or publish any material, false report or statement about the financial condition of the corporation;
2. Willingly or fraudulently exaggerate the financial conditions of the corporation;
3. Act with the intent to defraud, destroy, alter, mutilate or falsify any of the corporation's documents.

If board members deliberately manipulate the books to keep assessments artificially low or withhold a reserve study that shows the association to be underfunded, the board could be found to be criminally liable.

RELATED RIGHTS

- 1. Disclosures-Construction Defects** – A preliminary list of defects must be provided to each member of the association (Civil Code 1375); this list can then be passed on to buyers
- 2. Minutes of board meetings** – Must be made available within 30 days of the meeting. When requested by a member, the minutes or a summary must be provided (Civil Code 1363.05) At the time the association distributes its annual budget, members must be advised, in writing, of the right to obtain copies of minutes of the board of directors meetings. (Civil Code 1363).

CONCLUSION

Inspection rights are different for members and for directors. Directors have a broader right than members. A checklist of frequently requested documents is shown in the accompanying table.

When members or directors ask to inspect association records, the best policy is to be open and honest; but if any improper motive is suspected, be cautious. For special situations, consult with your association attorney.

CALIFORNIA LEGISLATION INTRODUCED - 2000

Some observers thought that this year would be a quiet one on the legislative front; the reason being that the Davis-Stirling Act is currently being reviewed by a legislative commission and its findings and recommendations for changes are due last this year or sometime next year. A number of bills were introduced in the legislature earlier this year. Some have made substantial progress towards passage and would yield fundamental changes to the Davis-Stirling Act if passed and signed by Governor Davis. Here is a brief summary of what is happening in Sacramento.

SB 453 (O'Connell) – signed by Governor – 5/23/00 and effective immediately – Makes technical changes to the Subdivision Map Act and the Davis-Stirling Act to facilitate the conversion of community apartment projects and stock cooperatives to condominiums. The proponents of this bill state that by removing inconsistencies in California law relating to conversions, it will make it easier for these projects to convert to condominiums and by converting, more conventional financing options will be available to buyers which should enhance property values.

AB 1859 (McClintock) – passed Assembly – 5/22/00 and now in the Senate – This bill, if passed, would revise Civil Code Section 1366 pertaining to assessments. Existing law requires the board of directors to levy assessments sufficient to meet its obligations. The bill would exempt regular assessments from owners from execution by a judgement creditor of the association to the extent necessary for the association to perform its obligations under the governing documents. The exemption would extend only to “essential services” (such as utilities or insurance) as determined by the court.

The bill is the result of a fiscal disaster that befell Le Parc Homeowners Association in Simi Valley. Following the Northridge Earthquake, Le Parc contracted with ZM Corporation to repair its common interest development. When a dispute arose between the HOA and its contractor, the contractor sued the HOA for the work performed under the contract, trade libel and slander and for damaging the company's perspective business advantage. In 1998, Le Parc was ordered to pay a \$6.6 million judgement to ZM (plus 10% interest).

The association members refused to approve an increased assessment to pay the judgement. The association's insurance company refused to pay the judgement. The association tried to file a Chapter 11 bankruptcy case but it was dismissed because the contractor would not agree to it. The judge deemed this to be an emergency situation under Civil Code 1366 and impose a special assessment. (\$25,000 per unit – 264 units). A receiver was appointed by the court to collect both the regular and special assessments. During this time, the receiver did not maintain the property or keep up with utility payments. The county health inspector closed the pool last August. The association's attorney says that the property values have declined so much that Ventura County has lost a half million dollars in property taxes.

SB 1882 – Construction Defects – passed Senate 5/25/00 – on to Assembly – This bill would require the California Research Bureau to conduct a study by December 2001 to examine whether large scale construction in the 1980s had an adverse effect on the quality of construction and whether overbuilding and the end of favorable tax treatment for rental housing were responsible for the end of the boom in condominium construction. Also, whether condominium prices were depressed in the early 90s due to consumers preferring single family homes; whether construction defect recoveries by homeowner associations have improved the quality of current construction and the impact of insurance availability and cost to developers and contractors. Also, how the price of land contributes to the lack of affordable housing in California.

Perhaps some of these issues are geographical. Here in South Santa Barbara County, developers are “falling over one another” trying to build housing projects. Land costs, governmental costs and regulation, planning issues and public opposition all play a major role here. It’s not because no one wants to build.

AB 1893 – Manager’s Licensing – passed Assembly 5/25/00 – in Senate – This bill would establish a program within the California Department of Consumer Affairs to regulate providers of management services to common interest developments. Real estate brokers would be exempt from these requirements. As the bill is currently amended, it would be unlawful for any individual to act in the capacity of a common interest development manager without first obtaining a certificate under from the Department of Consumer Affairs. Those who hold the CCAM Certificate from the California Association of Community Managers (CACM) or the PCAM Certificate from the Community Associations Institute (CAI) would not have to obtain the certificate from the state.

Requirements to obtain state certification would include the payment of fees including renewal fees, be a high school graduate, two year’s experience in managing CID units, 16 hours of instruction in California law pertaining to CIDs, 14 hours of instruction in finance, contracts, maintenance, risk management, professional conduct and other areas of instruction pertinent to CID Management. Certificates would be valid for three years. 15 hours of continuing education would be required at renewal.

The bill anticipates that the cost of the program would be \$300,000 annually which would be borne by those obtaining and maintaining certificates. The bill’s sponsor, the California Association of Community Managers, has indicated to the legislature that there are many untrained and unqualified individuals who seek employment as CID managers. They state that there have been many instances of unqualified managers improperly mishandling HOA funds and that such incidents have resulted in financial losses and subsequent disrepair of the CIDs.

CAI is opposing the bill at this time. Issues they have raised include no testing for certification, not knowing what the actual costs will be to certificate holders and the management companies, managers being held responsible for board actions, fidelity insurance requirements, etc.

This bill would have far-reaching impacts, if passed. Associations that have on-site managers would have to get them certified. Management companies would have to get all their managers qualified, not just the owner of the business.

AB 1493 – Restrictive Covenants – passed Assembly – Senate Committee hearing 6/6/00 – would amend last year’s law on amending documents with restrictive or racial covenants to limit amendments to those who have an ownership interest in the property and the amendment could only apply to blatant racial covenants.

AB 1823 – Disciplinary Actions – passed Assembly – Senate Committee hearing 6/6/00 – this bill would clarify disclosures required of the association about unresolved CC&R violations with a member when a member places his unit for sale. Strengthens notification requirements for disciplinary action against a member (due process, hearings, etc.)

AB 2031 – Inspection of HOA Records – passed Assembly – on to Senate – this bill would expand the association records that a member can inspect (see page 1 for what the current law is). The association would have to maintain the following documents for at least seven years: proposals, contractual agreements, correspondence, tax filings, receipts, checks, cancelled checks, ledgers, accounting books, ballots and other voting instruments, and voting records. The board of directors shall provide all members of the association with the same access to these documents as members of the board, including the right to copy and inspect such records. Documents would have to be made available within 10 days of receipt of the member’s written request. If the documents requested contain personal information about homeowners, including contact information such as telephone numbers and names, financial information and medical information and information relating to the makeup of a household, including the number of people in a household and whether they are related to each other, the board of directors shall, before providing the documents to the member, redact that information. If a member suffers an economic loss because of an association’s violation of this law, the member may recover compensatory damages of up to \$5,000.

According to the Assembly’s bill analysis, “Many individuals wrote in support of this bill”. These boards rig votes, destroy documents and perform a myriad of other secretive acts that they know will go unchallenged by residential owners because of the lack of law to assert their rights. Some HOA groups oppose the bill since existing law provides for some records inspection, some documents are protected under executive session meeting rules (Contracts, personnel and litigation).

Think about when a member has a complaint and you tell them to “put it in writing”. Another member could inspect that correspondence. If the member knew that his correspondence could be reviewed by the “offending member”, even if sections were blacked out, wouldn’t that give the member concern that he could not communicate with the board in confidence? How much time will it take for a board, or its manager, to review requested correspondence and delete identifying information? Who will pay for these services?

This bill has a lot of support in the legislature. It passed the Assembly 75-2.

Other bills have been introduced on senior citizens housing and home warranties.

This is shaping up as a potentially major year for change in the Davis-Stirling Act and laws affecting homeowner associations. If you would like a copy of any of these bills, you can call your Assembly member or State Senator's office. Or you can access them on the Internet at www.leginfo.ca.gov. Information including all versions of the bill, votes, analyses, pending actions, etc. are available here.

UPCOMING MEETINGS

June 2-3 – Executive Council of Homeowners (ECHO) conducts its annual two-day educational seminar at the Santa Clara Convention Center in San Jose. Call Mike Gartzke for additional information – 964-7806.

September 16 – Community Association Institute, Channel Islands Chapter Trade Faire – Ventura

September 30 – Community Association Institute, Mid-California Chapter Trade Show – San Luis Obispo

South Coast Meetings – We hope to have a legal meeting with Beth Grimm at some point this summer but no date has been set. We also will have a budget session in August-September. Hopefully we will have these dates set by the next newsletter.

PUBLICATIONS AVAILABLE FROM SOUTH COAST HOA

2000 Condominium Bluebook – A compilation of laws and other useful information to assist in association administration. \$14.00 postpaid

Operating Cost Manual for Homeowners Associations – a useful guide when developing your association budget, published by the California Department of Real Estate - \$ 5.00 postpaid.

Extra Copies of the South Coast Newsletter – Can be added to an existing membership for only \$10 per year. This would allow an extra copy to be sent to another address within the association. Copies of the Bluebook or other publications distributed by South Coast are not included in this subscription.