Study H-851 October 23, 2002

Memorandum 2002-58

**Nonjudicial Dispute Resolution Under CID Law:
Alternative Dispute Resolution**

BACKGROUND

In its study of common interest development law, the Commission has been giving priority to nonjudicial dispute resolution. This memorandum presents a staff draft implementing decisions made to date concerning alternative dispute resolution. The memorandum also presents a few outstanding issues for Commission resolution. Our objective is to develop a tentative recommendation that can be circulated to interested persons for comment.

CIVIL CODE SECTION 1354 — ADR PROCESS

The existing Davis-Stirling alternative dispute resolution process is found at Civil Code Section 1354. We have fixed up defects in the existing statute (e.g., manner of service of request for resolution, tolling statute of limitations, etc.) and redrafted the statute for clarity, pursuant to Commission decisions at the July 2002 meeting. The redrafted statute is set out at Exhibit pp. 1-8 as Civil Code Sections 1369.510-1369.590 (alternative dispute resolution).

There remains an issue concerning the existing procedure on which the Commission requested further information. When a claim for money damages is involved, why is the procedure limited to cases under $5,000? Doesn't this just allow a party who wishes to avoid the ADR requirement to do so simply by making a claim of $5,001?

The existing statute requires the parties to attempt to engage in ADR where the dispute involves declaratory or injunctive relief, but not generally where a claim for money damages is involved. As redrafted, the provision reads:

> **§ 1369.520. ADR prerequisite to enforcement action**
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> 1369.520. (a) An association or an owner or a member of a common interest development may not file an enforcement action

unless the parties have endeavored to submit their dispute to alternative dispute resolution.

(b) This section applies only to an enforcement action that is solely for declaratory, injunctive, or writ relief, or for that relief in conjunction with a claim for monetary damages not in excess of five thousand dollars ($5,000). Except as provided in Section 1366.3, this section does not apply to an action for association assessments.

The legislative history of this measure indicates that the bill as introduced was limited to declaratory and injunctive relief; it did not require ADR for damage claims at all. Judiciary Committee analyses pointed out that the scope was too limited — the bill was intended to divert smaller CID disputes out of the court system, but many disputes involve minor damages (such as the cost of repainting or relandscaping).

A proposal to include actions for monetary damages within the scope of the ADR requirement met with organized opposition from plaintiffs' attorneys, who argued that personal injury actions should be excluded from the ADR requirement. The compromise that came out of this dialogue was that any type of claim for monetary damages would be covered by the ADR requirement, so long as it was small ($5,000 or less) and so long as it was joined with a declaratory or injunctive relief claim. The $5,000 figure was undoubtedly selected as an arbitrary but convenient number because it corresponds with the small claims jurisdiction.

Should we be concerned that a person who wishes to avoid the ADR requirement can game the system by including a damage claim for $5001? The staff is not sure it's worth trying to address the problem. If a person wants to avoid ADR and fiddles with the damage claim in order to do so, the person is unlikely to be open to settlement, and the ADR exercise is apt to be unfruitful anyway. **The staff is not inclined to disturb the compromise that was negotiated in 1993.**

Pursuant to a Commission decision in July, we have included in the Comments a note that the ADR requirement is inapplicable to an action brought in small claims court. This is necessarily the case under existing Section 1354, since it is limited to actions for declaratory and injunctive relief, which are beyond small claims jurisdiction. However, because Section 1366.3 incorporates the alternative dispute resolution provisions of Section 1354 for assessment disputes, and because assessment disputes may well be within small claims jurisdictional limits, the waters are somewhat muddy. **The staff believes it**

would be helpful to include in the statute an express provision that the ADR procedures are not prerequisite to a small claims action:

> 1369.520. (a) An association or an owner or a member of a common interest development may not file an enforcement action unless the parties have endeavored to submit their dispute to alternative dispute resolution.
>
> (b) This section applies only to an enforcement action that is solely for declaratory, injunctive, or writ relief, or for that relief in conjunction with a claim for monetary damages not in excess of five thousand dollars ($5,000). Except as provided in Section 1366.3, this section does not apply to an action for association assessments. This section does not apply to a small claims action.
>
> **Comment.**
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> ...
>
> Subdivision (b) makes clear that a dispute resolution effort is not a prerequisite to a small claims action. The small claims action itself satisfies key functions of alternative dispute resolution — it provides a quick and inexpensive means of resolving a dispute within the jurisdiction of the small claims division of the superior court.

ASSOCIATION PROCEDURES

Formal alternative dispute resolution involves a neutral in the resolution process. However, a neutral costs money, and many of the types of disputes that surface in a common interest development are not monetary disputes. A person should be able to resolve a dispute involving ordinary day to day living arrangements without having to take a lot of time and pay a lot of money.

For this reason, the Commission has asked the staff to develop a requirement that every association must offer an internal dispute resolution mechanism at no cost to the parties. A homeowner would not be required to participate in that process, but on demand of a homeowner, the association would be required to participate in that process. This would supplement the regular Civil Code Section 1354 dispute resolution procedure involving use of a neutral.

Under the Commission's concept, if an association fails to provide such an internal dispute resolution mechanism, the statute would provide a default mechanism that would apply. As an initial approach, the statute might provide a meet and confer process, in which a board member is delegated authority to deal with the homeowner and settle the matter on behalf of the board.

There is an existing model in New Jersey law, which mandates that planned real estate developments "shall provide a fair and efficient procedure for the resolution of disputes between individual unit owners and the association, and between unit owners, which shall be readily available as an alternative to litigation." N.J.S.A. 45:22A-44(c). The problem with New Jersey law is that it is not clear whether a particular process adopted by an association is "fair and efficient"; the law provides no safe harbor or default procedure. If we impose such a requirement, we will need to do better than that.

The staff suggests something along the following lines for California:

Article 5. Dispute Resolution Procedure

§ 1363.810. Scope of article

1363.810. (a) This article applies to a dispute between an association and a member, or between members of an association, involving their rights, duties, or liabilities under this title, under the Nonprofit Mutual Benefit Corporation Law, or under the governing documents of the common interest development or association.

(b) This article supplements, and does not replace, Article 2 (commencing with Section 1369.510) of Chapter 7, relating to alternative dispute resolution as a prerequisite to an enforcement action.

Comment. Article 5 (commencing with Section 1363.810) is intended to provide a simple and efficient intra-association dispute resolution procedure at no cost to the parties. This is distinct from the alternative dispute resolution process involving a neutral that is required by Article 2 (commencing with Section 1369.510) of Chapter 7 as a prerequisite to litigation to resolve the dispute.

The Nonprofit Mutual Benefit Corporation Law is found at Part 3 (commencing with Section 7110) of Division 2 of Title 1 of the Corporations Code.

§ 1363.820. Fair, reasonable, and expeditious dispute resolution procedure required

1363.820. (a) An association shall provide a fair, reasonable, and expeditious procedure for resolving a dispute within the scope of this article.

(b) A dispute resolution procedure provided by an association is presumed to be fair, reasonable, and expeditious. The presumption created by this subdivision may be rebutted by a showing of bad faith in the adoption or implementation of the dispute resolution procedure.

Comment. Subdivision (a) of Section 1363.820 establishes the requirement, and prescribes the standard, for an association's internal dispute resolution procedure. For a description of disputes covered by the requirement, see Section 1363.810 (scope of article).

Although an association is required to provide a fair, reasonable, and expeditious dispute resolution procedure, its failure to do so is not subject to judicial mandate by writ or injunction and is not otherwise actionable. Pursuant to Section 1363.840(a) (default meet and confer procedure), inaction by an association is deemed to be adoption of the default procedure provided in that section.

The standard of "fair, reasonable, and expeditious" prescribed in Section 1363.820 is not an objective standard, and will vary from association to association, depending on such factors as size, involvement of membership, etc. A larger association might, for example, make use of a "covenants committee" composed of disinterested association members to hear and resolve disputes with binding effect on the board, whereas in a smaller association such a procedure might well be impossible because every member of the association could have an interest in the dispute.

Subdivision (b) implements the policy of this article to avoid squabbles over procedural details and instead focus on the substance of the dispute to be resolved. It should be noted that an association that has an existing internal dispute resolution procedure need not re-adopt it for the purposes of this article; the existing procedure is presumed to satisfy the requirements of this article.

The minimum requirements for an association's internal dispute resolution procedure are prescribed in Section 1363.830. The default meet and confer procedure applicable if an association fails to adopt a fair, reasonable, and expeditious procedure is prescribed in Section 1363.840.

§ 1363.830. Minimum requirements of association procedure

1363.830. A fair, reasonable, and expeditious dispute resolution procedure shall at a minimum satisfy all of the following requirements:

(a) The procedure may be invoked by any party to the dispute, including an association.

(b) If the procedure is invoked by a member in a dispute with the association, the association shall participate in, and is bound by any resolution of the dispute pursuant to, the procedure.

(c) If the procedure is invoked by a member in a dispute with another member, or by the association in a dispute with a member, the member may elect not to participate in the procedure. If the member participates but the dispute is resolved other than by

agreement of the member, the member shall have a right of appeal to the board of directors of the association.

(d) An agreement reached pursuant to the procedure binds the parties and is judicially enforceable.

(e) The procedure shall be provided by the association without cost to the participants.

Comment. Section 1363.830 prescribes the standards for an association's fair, reasonable, and expeditious internal dispute resolution procedure. If an association fails to provide a fair, reasonable, and expeditious procedure, the default dispute resolution procedure provided in Section 1363.840 is applicable.

§ 1363.840. Default meet and confer procedure

1363.840. (a) This section does not apply in an association that otherwise provides a fair, reasonable, and expeditious dispute resolution procedure. An association that does not otherwise provide a fair, reasonable, and expeditious dispute resolution procedure is deemed to have provided the procedure prescribed in this section. The procedure provided in this section is fair, reasonable, and expeditious, within the meaning of this article, subject to good faith implementation by an association.

(b) Any party to a dispute may invoke the following procedure:

(1) The party may request another party to meet and confer in an effort to resolve the dispute. The request may be oral or written, by whatever means appears to the party appropriate to communicate the request.

(2) A member of an association may refuse a request to meet and confer. The association may not refuse a request to meet and confer.

(3) If the association is a party to the dispute, the board of directors shall designate a member of the board to meet and confer. If the association is not a party to the dispute, but the parties request participation of the association, the board of directors shall designate a member of the board to participate.

(4) The parties shall meet promptly at a mutually convenient time and place, explain their positions to each other, and confer in an effort to resolve the dispute. If the association is not a party but participates on request of the parties, the board designee shall seek to facilitate resolution of the dispute.

(5) A resolution of the dispute agreed to by the parties shall be memorialized in writing and signed by the parties, including any board designee on behalf of the association. An agreement that is not in conflict with law or the governing documents of the common interest development or association binds the parties and is judicially enforceable.

Comment. Section 1363.840 provides a default dispute resolution procedure based on a "meet and confer" model. See, e.g., Gov't Code § 3505 ("Meet and confer in good faith" means that the parties have the mutual obligation personally to meet and confer promptly upon request by either party and continue for a reasonable period of time in order to exchange freely information, opinions, and proposals, and to endeavor to reach agreement ...")

An agreement reached pursuant to the meet and confer procedure prescribed in subdivision (b) binds the parties, provided it is not inconsistent with law or the governing documents. Thus, for example, a dispute could not legally be resolved by an agreement to a change in operating rules; operating rules may only be changed by appropriate association action. But an agreement could involve a commitment to bring the proposed rule change before the board with a favorable recommendation for board action.

ASSESSMENT DISPUTES

The mandatory ADR provisions of existing Section 1354 do not by their terms apply to assessment disputes. However, they may be invoked by a homeowner who pays under protest the amount of the assessment plus late charges, interest, delinquency costs. See Section 1366.3. This procedure may not be used by the homeowner more than twice a year nor more than thrice in five years.

The assessment dispute provision has been roundly criticized because it is largely ineffective. Assessments generally cannot be compromised out. All that is achieved by the homeowner invoking ADR after paying an assessment under protest is to run up costs, which ultimately are borne by the homeowner, and delay the homeowner from getting into court.

Perhaps the major benefit to the section is that, by incorporating Section 1354, it picks up the attorney's fee provisions of Section 1354 for the prevailing party. Whether a homeowner will often prevail in an assessment dispute case, however, is questionable. It appears to the staff more likely that attorney's fee provision will work to the homeowner's disadvantage.

Use of small claims procedures for enforcement of assessment disputes is considered to be good practice. See Sproul & Rosenberry, *Advising California Condominium and Homeowners Associations* § 4.19 at 170-71 (Cal. Cont. Ed. Bar 1991):

> To save associations the time and expense of bringing a civil action in [superior] court, their attorneys usually recommend that

> associations themselves bring actions on delinquent assessments in small claims court, if they are below the jurisdictional limits for small claims court ($5000 as of January 1, 1991 (CC §116.220)). A small claims action brought under CCP §§116.110-116.950 is often the fastest and most cost-effective method of collecting a delinquent assessment. In fact, because the small claims jurisdictional limits are likely to be well in excess of the amount of a regular assessment, a need to file a [superior] court action is probably indicative of negligence on the association's part in pursuing delinquent accounts.

See also, Batchelder, *Mandatory ADR in Common Interest Developments: Oxymoronic or Just Moronic?*, 23 Thom. Jeff. L. Rev. 227, 240 (2001) ("The small claims system affords inexpensive and speedy justice and, although not preferable to a more peaceful solution as through mediation, at least avoids the costly game playing that can result from forced ADR.").

The Commission has considered the possibility of requiring that assessment disputes be enforceable only in small claims court. The Commission rejected that approach for various reasons, including restrictive jurisdictional limits applicable in small claims court.

If small claims jurisdiction is invoked, ADR procedures should be inapplicable — small claims court provides the same function of an informal and inexpensive forum for dispute resolution. The staff draft notes this in the Comment to Section 1366.3. However, the staff thinks an express statutory provision would be preferable. See discussion of Section 1354, above.

The Commission felt that a more fruitful approach for assessment disputes might involve looking into the assessment lien process to see whether any improvements could be made from an ADR perspective. Interestingly, legislation enacted this session and operative January 1, 2003, seeks to address this matter, New Civil Code Section 1367.1 requires the board to give an owner 30 days' notice of an assessment delinquency and provides the owner an opportunity to attempt to work out a resolution via a "meet and confer" type of process:

> (c)(1) An owner may dispute the debt noticed pursuant to subdivision (a) by submitting to the board a written explanation of the reasons for his or her dispute. The board shall respond in writing to the owner within 15 days of the date of the postmark of the explanation, if the explanation is mailed within 15 days of the postmark of the notice.
>
> (2) An owner, other than an owner of any interest that is described in Section 11003.5 of the Business and Professions Code,

> may submit a written request to meet with the board to discuss a payment plan for the debt noticed pursuant to subdivision (a). The association shall provide the owners the standards for payment plans, if any exist. The board shall meet with the owner in executive session within 45 days of the postmark of the request, if the request is mailed within 15 days of the date of the postmark of the notice, unless there is no regularly scheduled board meeting within that period, in which case the board may designate a committee of one or more members to meet with the owner.

The staff believes **the Commission should monitor experience under this provision before seeking any further revision of the law** on the subject.

DISPUTE RESOLUTION INFORMATION CENTER

The Commission has felt that it would be helpful to all parties concerned if there were somewhere people could turn to for advice on dispute resolution in the CID context. We have envisioned a state agency that could provide contacts for mediation and other locally available dispute resolution programs. We have also envisioned that the state agency could serve as an information center where people could learn about their rights and responsibilities by obtaining a copy of the Davis-Stirling Act and other governing laws.

We have anticipated that this could be done quite inexpensively by maintaining a website with relevant information and by providing a toll-free phone number with automated information. There are a number of possible agencies that would be logical choices to serve as an information center. They include:

(1) **Department of Justice** (has existing enforcement authority under the Nonprofit Mutual Benefit Corporation Law).

(2) **Department of Consumer Affairs** (administers the Dispute Resolution Programs Act).

(3) **Department of Housing and Community Development** ("As California's principal housing agency, the mission of HCD is to provide leadership, policies and programs to expand and preserve safe and affordable housing opportunities and promote strong communities for all Californians.").

(4) **Department of Real Estate** (regulates development, but not operation, of CIDs).

(5) **Administrative Office of the Courts** (could coordinate with court clerk's office in each county).

To this should be added a new candidate that we have not previously considered — (6) **Secretary of State**. Under legislation operative January 1, 2003, every CID must register biennially with the Secretary of State, and the Secretary of State must make the registration data available as public information. The Secretary of State may impose a filing fee of up to $30 per registration.

The staff believes the Secretary of State would be ideal for our purposes. Its function as central statewide repository for CID information will quickly become known. The Secretary of State already maintains an excellent and heavily-used website. And perhaps most important, a mechanism now exists for funding the information function — the biennial registration fees of CIDs (which the staff estimates could generate as much as $500,000 annually). This is significant since the staff anticipates agency opposition to any new functions in the present environment of budget constraints.

The staff suggests addition of a provision along the following lines:

> **Civ. Code § 1363.7 (added). Common interest development information center**
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> 1363.7. (a) The Secretary of State shall maintain a common interest development information center. The information maintained in the center shall be accessible to the public by means of both an internet website and a toll-free automated answering system, and by any other means the Secretary of State determines is feasible and appropriate.
>
> (b) The common interest development information center shall include all of the following information:
>
> (1) The text of, or directions for how to obtain the text of, this title, the Nonprofit Mutual Benefit Corporation Act, and any other statute or regulation the Secretary of State determines would be relevant to the operation of common interest developments and the rights and duties of associations and members or owners.
>
> (2) Information concerning nonjudicial resolution of disputes that may arise within a common interest development, including contacts for locally available alternative dispute resolution resources. The information may include appropriate links to existing resources, such as the Dispute Resolution Programs Act.
>
> (3) Any other information the Secretary of State determines would be useful to common interest developments, associations, members owners, and the public, concerning common interest developments.
>
> (c) The determinations made by the Secretary of State under this section are within the Secretary of State's discretion. The Secretary of State may make the determinations by any procedure the

Secretary of State deems appropriate; the determinations are not subject to the rulemaking requirements of the Administrative Procedure Act.

(d) The Secretary of State shall fund the cost of maintaining the common interest information center from the filing fee provided for in Section 1363.6.

Comment. Section 1363.7 establishes a statewide information center for common interest developments. The section builds on the Secretary of State's function to maintain a common interest development registry under Section 1363.6.

Subdivision (a) requires the common interest development information center to be accessible via the internet and by a toll-free phone response system. However, nothing precludes the Secretary of State from providing for a more extensive information center, including paper copies of information, a response staff, etc., if feasible within funding constraints.

The key information required by subdivision (b) relates to rights and duties within a common interest development, and procedures for resolving disputes within a common interest development. However, depending on available resources, the Secretary of State may wish to expand the functions of the information center to include other relevant matters, such as contacts for common interest development management, homeowner rights organizations, and the like. This, and other, determinations of the Secretary of State authorized by this section concerning the information center, are within the discretion of the Secretary of State. Subdivision (c).

Subdivision (d) provides the funding mechanism for the common interest development information center. The Secretary of State should set the fee authorized by Section 1363.6 (common interest development registry) at a level sufficient to maintain both the information center and the registry.

ENFORCEMENT OF BYLAWS AND OPERATING RULES

Subdivision (a) of Section 1354 is unrelated to the ADR material in the rest of the section. Subdivision (a) provides:

> (a) The covenants and restrictions in the declaration shall be enforceable equitable servitudes, unless unreasonable, and shall inure to the benefit of and bind all owners of separate interests in the development. Unless the declaration states otherwise, these servitudes may be enforced by any owner of a separate interest or by the association, or by both.

The Commission has asked whether this section requires revision to make clear that an association member is entitled to enforce bylaws, operating rules, and other governing documents. As currently written, there may be a negative implication derived from the provision's limitation to enforcement of CC&Rs.

This concern is certainly real. A leading text on CID law states:

> Some attorneys prefer to put the restrictions in an association's internal rules or bylaws because these documents are easier to amend. This practice is not recommended, however, because rules and bylaws are seldom recorded, and restrictions are enforceable under CC § 1354 only if they are set forth in a recorded declaration.

Sproul & Rosenberry, Advising California Condominium and Homeowners Associations, § 7.1 (Cal. Cont. Ed. Bar 1991).

The staff thinks that both an association and its members would be surprised to find that what appears to be a valid restriction in the bylaws or operating rules is in fact unenforceable if not contained in recorded CC&Rs. However, there is little case law directly on point. Perhaps that is attributable to associations' following "best practices" and putting their restrictions in CC&Rs, or perhaps it does not occur to people to challenge enforcement of a bylaw or operating rule restriction on the basis of lack of authority. Most challenges to enforcement of a restriction appear to address the reasonableness of the restriction, rather than enforcement authority. That having been said, there are a few cases that do address enforcement of unrecorded restrictions adopted by an association; these are discussed below.

The concept that a restriction in the bylaws or operating rules may be unenforceable is derived by negative implication from the fact that a restriction in CC&Rs is enforceable because recorded, giving constructive notice of the restriction to purchasers of the property. The theory of enforceability is explained by the California Supreme Court in *Nahrstedt v. Lakeside Village Condominium Ass'n*, 8 Cal. 4th 377, 33 Cal. Rptr. 63, 70-71 (1994):

> One significant factor in the continued popularity of the common interest form of property ownership is the ability of homeowners to enforce restrictive CC&R's against other owners (including future purchasers) of project units. (Natelson, Law of Property Owners Associations, *supra*, § 1.3.2.1, p. 19; Note, *Business Judgment, supra*, 64 Chi.-Kent L.Rev. at p. 673.) Generally, however, such enforcement is possible only if the restriction that is sought to be enforced meets the requirements of equitable servitudes or of covenants running with the land. (Cal. Condominium and Planned

> Development Practice, supra, §§ 8.42-8.44, pp. 666-668; Note, *Covenants and Equitable Servitudes in California* (1978) 29 Hastings L.J. 545, 553-573.)
>
> Restrictive covenants will run with the land, and thus bind successive owners, if the deed or other instrument containing the restrictive covenant particularly describes the lands to be benefited and burdened by the restriction and expressly provides that successors in interest of the covenantor's land will be bound for the benefit of the covenantee's land. Moreover, restrictions must relate to use, repair, maintenance, or improvement of the property, or to payment of taxes or assessments, and the instrument containing the restrictions must be recorded. (See § 1468; Advising Cal. Condominium and Homeowners Associations (Cont. Ed. Bar 1991) § 7.33, p. 342.)
>
> Restrictions that do not meet the requirements of covenants running with the land may be enforceable as equitable servitudes provided the person bound by the restrictions had notice of their existence. (*Riley v. Bear Creek Planning Committee* (1976) 17 Cal.3d 500, 507 [131 Cal.Rptr. 381, 551 P.2d 1213]; Cal. Condominium and Planned Development Practice, supra, § 8.44, pp. 667-668.)

A restriction that is recorded is enforceable because a purchaser of property subject to the restriction has notice of it. But does it necessarily follow that an unrecorded restriction is unenforceable?

Nahrstedt itself refers to enforceability of association rules (33 Cal. Rptr. 2d at 69-70):

> Restrictions on property use are not the only characteristic of common interest ownership. Ordinarily, such ownership also entails mandatory membership in an owners association, which, through an elected board of directors, is empowered to enforce any use restrictions contained in the project's declaration or master deed and to enact new rules governing the use and occupancy of property within the project. (Cal. Condominium and Planned Development Practice (Cont. Ed. Bar 1984) § 1.7, p. 13; Note, *Business Judgment, supra*, 64 Chi.-Kent L.Rev. at p. 653; Natelson, Law of Property Owners Associations, *supra*, § 3.2.2, p. 71 et seq.) Because of its considerable power in managing and regulating a common interest development, the governing board of an owners association must guard against the potential for the abuse of that power. [FN6] As Professor Natelson observes, owners associations "can be a powerful force for good or for ill" in their members' lives. (Natelson, *Consent, Coercion, and "Reasonableness," supra*, 51 Ohio St. L.J. at p. 43.) Therefore, anyone who buys a unit in a common interest development with knowledge of its owners association's

> discretionary power accepts "the risk that the power may be used in a way that benefits the commonality but harms the individual." (*Id*. at p. 67.) Generally, courts will uphold decisions made by the governing board of an owners association so long as they represent good faith efforts to further the purposes of the common interest development, are consistent with the development's governing documents, and comply with public policy. (*Id*. at p. 43.)
>
> FN6 The power to regulate pertains to a "wide spectrum of activities," such as the volume of playing music, hours of social gatherings, use of patio furniture and barbecues, and rental of units. (Note, *Business Judgment, supra*, 64 Chi.-Kent L.Rev. at p. 669.)

At least two cases deal head on with enforceability of restrictions found in unrecorded rules adopted by an association pursuant to CC&Rs. Both cases concern restrictions on use of the association's tennis courts by a nonresident owner. The cases reach opposite results on the facts, but appear to be consistent with respect to the principle that restrictions contained in rules are enforceable if not inconsistent with the CC&Rs.

In *MaJOR v. Miraverde Homeowners Ass'n*, 7 Cal. App. 4th 626, 9 Cal. Rptr. 2d 237 (1992), the court found that the association's rule limiting use of common facilities by a nonresident owner was unenforceable by the board. The rule was inconsistent with CC&Rs that granted every member a right to enjoyment of the common areas. "Where the association exceeds its scope of authority, any rule or decision resulting from such an ultra vires act is invalid whether or not it is a 'reasonable' response to a particular circumstance. Where a circumstance arises which is not adequately covered by the CC&R's, the remedy is to amend the CC&R's." 9 Cal. Rptr. 2d at 243.

Liebler v. Point Loma Tennis Club, 40 Cal. App. 4th 1609, 47 Cal. Rptr. 2d 783 (1995), distinguishes *MaJOR* and upholds the enforceability of an association rule, including fines, against use of the common facilities by a nonresident owner. In *Liebler* the court concluded that the rule was consistent with CC&Rs that precluded an owner from severing the owner's separate interest from the owner's undivided interest in the common area. The court cited *Nahrstedt*, which accords a restriction contained in recorded CC&Rs a presumption of validity. "In this case, the challenged rule is clearly within the contemplation of the relevant presumptively valid provisions of [the CC&Rs]. Because we hold the challenged rule is a proper implementation of the relevant sections of the CC&Rs, Liebler's argument that the rule is not permitted by the CC&Rs must fail." 47 Cal. Rptr. 2d at 788. The court made a similar analysis with respect to the fine schedule adopted by the association for enforcement of the rule. 47 Cal. Rptr. 2d at 790.

The staff concludes from all this that a restriction in an association's governing documents, even though not recorded as part of the CC&Rs, is enforceable provided it is consistent with the CC&Rs (and is not unreasonable, and is adopted following appropriate procedures, and is not discriminatory, etc.). Given the relative sparsity of direct authority on the point, **it probably would be worthwhile to clear the matter up by statute**.

Section 1354(a) could be revised to read:

> (a) The covenants and restrictions in the declaration shall be enforceable equitable servitudes, unless unreasonable, and shall inure to the benefit of and bind all owners of separate interests in the development. Unless the declaration states otherwise, these servitudes and governing documents adopted pursuant to them may be enforced by any owner of a separate interest or by the association, or by both.
>
> **Comment**. Subdivision (a) of Section 1354 is amended to make clear that documents governing the operation of a common interest development or association, such as bylaws, operating rules, and articles of incorporation or association, are enforceable to the same extent as the declaration. See Section 1351(j) ("governing documents defined). Governing documents are enforceable under this section only if consistent with the declaration, if reasonable and nondiscriminatory, and if adopted with proper authority and procedures, including any required notice.

The bare statute language gives no hint of the many constraints limiting enforceability of the governing documents — proper adoption, reasonableness, etc. Rather than attempting to spell all this out in the statute, we have made reference to these constraints in the Comment.

Note that the draft is limited to a governing document adopted "pursuant to" the CC&Rs. The enforcement authority is thus dependent on existing CC&R authority of some type. The authority could arguably be as general as "the board shall promulgate and enforce bylaws and operational rules governing use of separate interests and common areas."

Note also that at least one commentator has raised the possibility that the presumption of reasonableness afforded a declaration of CC&Rs in *Nahrstedt* might not extend to other governing documents. See Bernhardt, California Real Estate Cases § 4.2 at p. 314 (Cal. Cont. Ed. Bar 1992) ("It is uncertain whether the same standard of reasonableness will be applied to ... similar restrictions found in the association's rules or bylaws, rather than in the CC&Rs."). The staff does

not believe anything in the proposed Comment would prejudice the determination of that issue one way or the other. It is perhaps noteworthy, though, that Prof. Bernhardt assumes enforceability of restrictions not contained in the CC&Rs.

Respectfully submitted,

Nathaniel Sterling
Executive Secretary

Exhibit

ALTERNATIVE DISPUTE RESOLUTION

TITLE 6. COMMON INTEREST DEVELOPMENTS

☞ **Note.** The following chapter and article headings assume enactment of the Commission's recommendation regarding the structure of the Davis-Stirling Common Interest Development Act.

CHAPTER 2. GOVERNING DOCUMENTS

Article 2. Enforcement

Civ. Code § 1354 (amended). Enforcement of covenants and restrictions

SEC. 1. Section 1354 of the Civil Code is amended, to read:

1354. ~~(a)~~ The covenants and restrictions in the declaration shall be enforceable equitable servitudes, unless unreasonable, and shall inure to the benefit of and bind all owners of separate interests in the development. Unless the declaration states otherwise, these servitudes may be enforced by any owner of a separate interest or by the association, or by both.

~~(b) Unless the applicable time limitation for commencing the action would run within 120 days, prior to the filing of a civil action by either an association or an owner or a member of a common interest development solely for declaratory relief or injunctive relief, or for declaratory relief or injunctive relief in conjunction with a claim for monetary damages, other than association assessments, not in excess of five thousand dollars ($5,000), related to the enforcement of the governing documents, the parties shall endeavor, as provided in this subdivision, to submit their dispute to a form of alternative dispute resolution such as mediation or arbitration. The form of alternative dispute resolution chosen may be binding or nonbinding at the option of the parties. Any party to such a dispute may initiate this process by serving on another party to the dispute a Request for Resolution. The Request for Resolution shall include (1) a brief description of the dispute between the parties, (2) a request for alternative dispute resolution, and (3) a notice that the party receiving the Request for Resolution is required to respond thereto within 30 days of receipt or it will be deemed rejected. Service of the Request for Resolution shall be in the same manner as prescribed for service in a small claims action as provided in Section 116.340 of the Code of Civil Procedure. Parties receiving a Request for Resolution shall have 30 days following service of the Request for Resolution to accept or reject alternative dispute resolution and, if not~~

~~accepted within the 30-day period by a party, shall be deemed rejected by that party. If alternative dispute resolution is accepted by the party upon whom the Request for Resolution is served, the alternative dispute resolution shall be completed within 90 days of receipt of the acceptance by the party initiating the Request for Resolution, unless extended by written stipulation signed by both parties. The costs of the alternative dispute resolution shall be borne by the parties.~~

~~(c) At the time of filing a civil action by either an association or an owner or a member of a common interest development solely for declaratory relief or injunctive relief, or for declaratory relief or injunctive relief in conjunction with a claim for monetary damages not in excess of five thousand dollars ($5,000), related to the enforcement of the governing documents, the party filing the action shall file with the complaint a certificate stating that alternative dispute resolution has been completed in compliance with subdivision (b). The failure to file a certificate as required by subdivision (b) shall be grounds for a demurrer pursuant to Section 430.10 of the Code of Civil Procedure or a motion to strike pursuant to Section 435 of the Code of Civil Procedure unless the filing party certifies in writing that one of the other parties to the dispute refused alternative dispute resolution prior to the filing of the complaint, that preliminary or temporary injunctive relief is necessary, or that alternative dispute resolution is not required by subdivision (b), because the limitation period for bringing the action would have run within the 120-day period next following the filing of the action, or the court finds that dismissal of the action for failure to comply with subdivision (b) would result in substantial prejudice to one of the parties.~~

~~(d) Once a civil action specified in subdivision (a) to enforce the governing documents has been filed by either an association or an owner or member of a common interest development, upon written stipulation of the parties the matter may be referred to alternative dispute resolution and stayed. The costs of the alternative dispute resolution shall be borne by the parties. During this referral, the action shall not be subject to the rules implementing subdivision (c) of Section 68603 of the Government Code.~~

~~(e) The requirements of subdivisions (b) and (c) shall not apply to the filing of a cross-complaint.~~

~~(f) In any action specified in subdivision (a) to enforce the governing documents, the prevailing party shall be awarded reasonable attorney's fees and costs. Upon motion by any party for attorney's fees and costs to be awarded to the prevailing party in these actions, the court, in determining the amount of the award, may consider a party's refusal to participate in alternative dispute resolution prior to the filing of the action.~~

~~(g) Unless consented to by both parties to alternative dispute resolution that is initiated by a Request for Resolution under subdivision (b), evidence of anything said or of admissions made in the course of the alternative dispute resolution process shall not be admissible in evidence, and testimony or disclosure of such a~~

~~statement or admission may not be compelled, in any civil action in which, pursuant to law, testimony can be compelled to be given.~~

~~(h) Unless consented to by both parties to alternative dispute resolution that is initiated by a Request for Resolution under subdivision (b), documents prepared for the purpose or in the course of, or pursuant to, the alternative dispute resolution shall not be admissible in evidence, and disclosure of these documents may not be compelled, in any civil action in which, pursuant to law, testimony can be compelled to be given.~~

~~(i) Members of the association shall annually be provided a summary of the provisions of this section, which specifically references this section. The summary shall include the following language:~~

~~"Failure by any member of the association to comply with the prefiling requirements of Section 1354 of the Civil Code may result in the loss of your rights to sue the association or another member of the association regarding enforcement of the governing documents."~~

~~The summary shall be provided either at the time the pro forma budget required by Section 1365 is distributed or in the manner specified in Section 5016 of the Corporations Code.~~

~~(j) Any Request for Resolution sent to the owner of a separate interest pursuant to subdivision (b) shall include a copy of this section.~~

Comment. Section 1354 is amended to remove subdivisions (b)-(j), relating to alternative dispute resolution. Those provisions are relocated and revised as Sections 1369.510-1369.590 (alternative dispute resolution). See the Comments to those sections for details of the disposition and revision of former subdivisions (b)-(j).

Civ. Code § 1366.3 (amended). Alternative dispute resolution for assessments

1366.3. (a) The exception for disputes related to association assessments in ~~subdivision (b) of Section 1354~~ Article 2 (commencing with Section 1369.510) of Chapter 7 shall not apply if, in a dispute between the owner of a separate interest and the association regarding the assessments imposed by the association, the owner of the separate interest chooses to pay in full to the association all of the charges listed in paragraphs (1) to (4), inclusive, and states by written notice that the amount is paid under protest, and the written notice is mailed by certified mail not more than 30 days from the recording of a notice of delinquent assessment in accordance with Section 1367 or 1367.1; and in those instances, the association shall inform the owner that the owner may resolve the dispute through alternative dispute resolution as set forth in ~~Section 1354~~ Article 2 (commencing with Section 1369.510) of Chapter 7, civil action, and any other procedures to resolve the dispute that may be available through the association.

(1) The amount of the assessment in dispute.

(2) Late charges.

(3) Interest.

(4) All reasonable fees and costs associated with the preparation and filing of a notice of delinquent assessment, including all mailing costs, and including reasonable attorney's fees not to exceed four hundred twenty-five dollars ($425).

(b) The right of any owner of a separate interest to utilize alternative dispute resolution under this section may not be exercised more than two times in any single calendar year, and not more than three times within any five calendar years. Nothing within this section shall preclude any owner of a separate interest and the association, upon mutual agreement, from entering into alternative dispute resolution for a number of times in excess of the limits set forth in this section. The owner of a separate interest may request and be awarded through alternative dispute resolution reasonable interest to be paid by the association on the total amount paid under paragraphs (1) to (4), inclusive, of subdivision (a), if it is determined through alternative dispute resolution that the assessment levied by the association was not correctly levied.

Comment. Section 1366.3 is amended to correct section references.

[The "other procedures to resolve the dispute that may be available through the association" referred to in subdivision (a) would include the internal dispute resolution procedure required by Sections 1363.810-1363.840 (dispute resolution procedure).]

It should be noted that an association may elect to enforce a delinquent assessment in small claims court. Cf. Sproul & Rosenberry, *Advising California Condominium and Homeowners Associations* § 4.19 at 170-71 (Cal. Cont. Ed. Bar 1991) (small claims procedure preferred). In that case, ADR provisions would be inapplicable, since the small claims procedure satisfies the same functions. [See Section 1369.520 & Comment (ADR prerequisite to enforcement action.]

CHAPTER 7. CIVIL ACTIONS AND LIENS

Civ. Code § 1368.4-1369 (article heading). Miscellaneous provisions

SEC. 2. An article heading is added immediately preceding Section 1368.4 of the Civil Code, to read:

Article 1. Miscellaneous Provisions

Civ. Code § 1369.510-1369.590. Alternative dispute resolution

SEC. 3. Article 2 (commencing with Section 1369.510) is added to Chapter 7 of Title 6 of Part 4 of Division 2 of the Civil Code, to read:

Article 2. Alternative Dispute Resolution

§ 1369.510. Definitions

1369.510. As used in this article:

(a) "Alternative dispute resolution" means mediation, arbitration, conciliation, or other nonjudicial procedure that involves a neutral party in the decisionmaking process. The form of alternative dispute resolution chosen pursuant to this article may be binding or nonbinding at the option of the parties.

(b) "Enforcement action" means a civil action or proceeding, other than a cross-complaint, for any of the following purposes:

(1) Enforcement of this title.

(2) Enforcement of the Nonprofit Mutual Benefit Corporation Law.

(3) Enforcement of the governing documents of a common interest development.

Comment. The first sentence of subdivision (a) of Section 1369.510 continues the substance of a portion of the first sentence of former Section 1354(b), and broadens it to include conciliation and other nonjudicial processes that involve a neutral in dispute resolution. The second sentence of subdivision (b) continues the substance of the second sentence of former Section 1354(b).

Subdivision (b) supersedes the portion of the first sentence of former Section 1354(b) that limited the alternative dispute resolution process to enforcement of governing documents. Under this section, an enforcement proceeding may involve enforcement of rights under this title and under the Nonprofit Mutual Benefit Corporations Law as well. See also Section 1351(j) ("governing documents" defined). The Nonprofit Mutual Benefit Corporations Law is found at Part 3 (commencing with Section 7110) of Division 2 Title 1 of the Corporations Code.

Subdivision (b) continues the exemption of cross-complaints formerly found in Section 1354(e).

§ 1369.520. ADR prerequisite to enforcement action

1369.520. (a) An association or an owner or a member of a common interest development may not file an enforcement action unless the parties have endeavored to submit their dispute to alternative dispute resolution.

(b) This section applies only to an enforcement action that is solely for declaratory, injunctive, or writ relief, or for that relief in conjunction with a claim for monetary damages not in excess of five thousand dollars ($5,000). Except as provided in Section 1366.3, this section does not apply to an action for association assessments.

Comment. Subdivision (a) of Section 1369.520 continues the substance of the first sentence of former Section 1354(b). See also Section 1369.510 ("alternative dispute resolution" and "enforcement action" defined). Subdivision (a) does not continue the exclusion for matters as to which the applicable time limitation for commencing the action would run within 120 days. Instead, action under this subdivision tolls a statute of limitations that would run within 120 days. See Section 1369.550.

Subdivision (b) expands the provision of the first sentence of former Section 1354(b) governing the types of enforcement actions to which the section applies, to include writ relief. [It should be noted that because the alternative dispute resolution requirement is limited to actions for declaratory, injunctive, or writ relief (or those types of relief joined with a damage claim not exceeding $5,000), the requirement necessarily is inapplicable to small claims proceedings. Cf. Code Civ. Proc. § 116.220 (limited jurisdiction of small claims court).]

Subdivision (b) is also revised to include an explicit cross-reference to Section 1366.3 (alternative dispute resolution for assessments). Although the alternative dispute resolution requirement does not by its terms apply to assessment disputes, the requirement may be made applicable pursuant to the procedure provided in Section 1366.3.

§ 1369.530. Request for resolution

1369.530. (a) Any party to a dispute may initiate the process required by Section 1369.520 by serving on another party to the dispute a Request for Resolution. The Request for Resolution shall include all of the following:

(1) A brief description of the dispute between the parties.

(2) A request for alternative dispute resolution.

(3) A notice that the party receiving the Request for Resolution is required to respond within 30 days of receipt or the request will be deemed rejected.

(4) If the party on whom the request is served is the owner of a separate interest, a copy of this article.

(b) Service of the Request for Resolution shall be by personal delivery, first class mail, express mail, facsimile transmission, or other means reasonably calculated to provide the party on whom the request is served actual notice of the request.

(c) A party on whom a Request for Resolution is served has 30 days following service to accept or reject the request. If a party does not accept the request within that period, the request is deemed rejected by the party.

Comment. Subdivision (a)(1)-(3) of Section 1369.530 continue the substance of the third and fourth sentences of former Section 1354(b). Subdivision (a)(4) continues the substance of former Section 1354(j).

Subdivision (b) supersedes the fifth sentence of former Section 1354(b). It expands the permissible manner of service of the Request for Resolution, consistent with general provisions for notice of motion in civil proceedings.

Subdivision (c) continues the substance of the sixth sentence of former Section 1354(b).

☞ **Staff Note.** The Commission intends to consider the question whether ADR should be mandatory rather than optional when results of pilot projects involving mandatory mediation in Los Angeles County are available for evaluation.

§ 1369.540. ADR process

1369.540. (a) If the party on whom a Request for Resolution is served accepts the request, the parties shall complete the alternative dispute resolution within 90 days after the party initiating the request receives the acceptance, unless extended by written stipulation signed by both parties.

(b) Chapter 2 (commencing with Section 1115) of Division 9 of the Evidence Code applies to any form of alternative dispute resolution initiated by a Request for Resolution under this article, other than arbitration.

(c) The costs of the alternative dispute resolution shall be borne by the parties.

Comment. Subdivision (a) of Section 1369.540 continues the substance of the seventh sentence of former Section 1354(b).

Subdivision (b) supersedes former Section 1354(g)-(h). It replaces the former provisions with a reference to the general mediation confidentiality statute, but precludes application of that statute to arbitration proceedings pursuant to this article. See also Section 1269.510(a) ("alternative dispute resolution" defined).

Subdivision (c) continues the eighth sentence of former Section 1354(b).

The parties to an agreement reached pursuant to alternative dispute resolution may include in the agreement provisions for its enforcement in case of breach, such as a stipulation for entry of judgment or for injunctive relief.

§ 1369.550. Tolling of statute of limitations

1369.550. If the applicable time limitation for commencing an enforcement action would run within 120 days after service of a Request for Resolution, the

time limitation is extended to the 120th day after service. If the parties have stipulated to an extension of the alternative dispute resolution period beyond the 120th day after service of a Request for Resolution pursuant to Section 1369.540, a time limitation that would expire during the alternative dispute resolution period is extended to the end of the stipulated period.

Comment. Section 1369.550 supersedes the first clause of former Section 1354(b), which excepted actions in which the applicable time limitation would run within 120 days. Under Section 1369.550, a Request for Resolution is required even if the statute of limitations would expire within 120 days of the request. Instead, if the statute of limitations would run within 120 days after service of the request, the statute is tolled until the 120th day after service of the request.

§ 1369.560. Certification of efforts to resolve dispute

1369.560. (a) At the time of commencement of an enforcement action, the party commencing the action shall file with the initial pleading a certificate stating that alternative dispute resolution has been completed in compliance with this article.

(b) Failure to file a certificate pursuant to subdivision (a) is grounds for a demurrer or a motion to strike unless one of the following conditions is satisfied:

(1) The party commencing the action certifies in writing that one of the other parties to the dispute refused alternative dispute resolution before commencement of the action, or that preliminary or temporary injunctive relief is necessary

(2) The court finds that dismissal of the action for failure to comply with this article would result in substantial prejudice to one of the parties.

Comment. Subdivision (a) of Section 1369.560 continues the substance of the first sentence of former Section 1354(c) and broadens its application to include writ proceedings and proceedings for enforcement of this title and the Nonprofit Mutual Benefit Corporation Law as well as the association's governing documents. See Sections 1369.510(b) ("enforcement action" defined), 1369.520 (ADR prerequisite to enforcement action).

Subdivision (b) continues the substance of the second sentence of former Section 1354(c), but eliminates as an excuse from compliance that the statute of limitations would run within 120 days after filing. Cf. Section 1369.550 & Comment (tolling of statute of limitations). See also Code Civ. Proc. §§ 430.10 (demurrer), 435 (motion to strike).

The requirement of this section does not apply to the filing of a cross-complaint. See Section 1369.510(b) ("enforcement action" defined).

§ 1369.570. Stay of litigation for dispute resolution

1369.570. (a) After an enforcement action is commenced, on written stipulation of the parties the matter may be referred to alternative dispute resolution and stayed.

(b) The costs of the alternative dispute resolution shall be borne by the parties.

(c) During a referral, the action is not subject to the rules implementing subdivision (c) of Section 68603 of the Government Code.

Comment. Section 1369.570 continues the substance of former Section 1354(d) but expands its application beyond actions for enforcement of covenants and restrictions. See Section 1369.510(b) ("enforcement action" defined).

§ 1369.580. Attorneys fees

1369.580. The prevailing party in an enforcement action shall be awarded reasonable attorney's fees and costs. On motion for attorney's fees and costs, the court, in determining the amount of the award, may consider a party's refusal to participate in alternative dispute resolution before commencement of the action.

Comment. Section 1369.580 continues the substance of former Section 1354(f) but expands its application beyond actions for enforcement of covenants and restrictions. See Section 1369.510(b) ("enforcement action" defined). This is consistent with existing law. See, e.g., Kaplan v. Fairway Oaks Homeowners Ass'n, 98 Cal. App. 4th 715, 120 Cal. Rptr. 2d 158 (2002) ("The Legislature obviously intended to broaden the availability of attorney fee awards by authorizing attorney fees in an action to enforce the governing documents rather than just the declaration.")

§ 1369.590. Member information

1369.590. (a) An association shall annually provide its members a summary of the provisions of this article, that specifically references this article. The summary shall include the following language:

> Failure of a member of the association to comply with the prefiling requirements of Section 1369.520 of the Civil Code may result in the loss of your right to sue the association or another member of the association regarding enforcement of the governing documents or the applicable law.

(b) The summary shall be provided either at the time the pro forma budget required by Section 1365 is distributed or in the manner prescribed in Section 5016 of the Corporations Code.

Comment. Subdivision (a) of Section 1369.590 continues the substance of the first and second paragraphs of former Section 1354(i). Subdivision (a) makes clear that it is the duty of the association to provide the summary.

Subdivision (b) continues the third paragraph of former Section 1354(i).