Study H-856 December 8, 2008

# First Supplement to Memorandum 2008-63

## Common Interest Development Law: Nonresidential Associations (Scope and Methodology of Study)

The Commission has received several comments on CLRC Memorandum 2008-63:

*Exhibit p.*

- Skip Daum, Community Associations Institute – California Legislative Action Committee (12/03/08) . . . . . 1
- Steve Dyer, Monterey, CA (12/03/08) . . . . . 2
- Terry Farris (12/03/08) . . . . . 3
- Tina Rasnow, Ventura County Superior Court (12/03/08) . . . . . 4
- Craig Stevens, Commercial Property Owners Association (12/03/08) . . . . 6

### INTEREST IN STUDY

Craig Stevens, a representative of the Community Property Owners Association, which Mr. Stevens indicates includes 2000 "building owners/CID members," welcomes this study. Exhibit p. 6. He states that he is putting together a "task force" consisting of management companies, attorneys, developers, trade groups, brokerage companies, and building owners, and will be compiling recommendations on the study for submission to the Commission.

Skip Daum, a lobbyist for the Community Associations Institute – California Legislative Action Committee, indicates that his group is particularly interested in how the study will treat the election provisions in the Davis-Stirling Act. Exhibit p. 1.

### OVERARCHING COMMENT RELATING TO RESIDENTIAL CIDS

Tina Rasnow, a coordinator with the Ventura County Superior Court Self-Help Legal Access Center, believes that many owners in nonresidential CIDs are small business owners or sole proprietors, who need many of the same consumer protection provisions as homeowners. Exhibit p. 4. Ms. Rasnow

indicates that her eleven years running the Self-Help Legal Access Center has caused her to recognize that many business owners, despite incorporating their businesses and owning commercial property, may have neither the funds nor the legal sophistication to protect themselves from mismanagement of the development in which that property is located.

## MIXED USE DEVELOPMENTS

Three commenters have inquired whether this study will consider the application of the Davis-Stirling Act to "mixed use" common interest developments, i.e., CIDs in which the separate interests are a mix of both residential *and* commercial units. Exhibit pp. 1, 2, 3. Examples of such developments might be a commercial office park with a residential loft over one of the offices, a residential development containing a coffee shop, or anything in between.

**The Commission welcomes information from any interested person on the number of mixed use CIDs in California, any trend toward such developments, or the most common composition of such developments** (i.e., the percentage of residential vs. nonresidential units within a development)**.**

### Existing Law

Under Civil Code Section 1373, CIDs that are limited *solely* to commercial or industrial uses (either by a zoning requirement or by the development's recorded declaration) are exempted from selected provisions of the Davis-Stirling Act. Civ. Code § 1373(a). Therefore, under existing law, the existence of even a single residential unit within a CID makes any of the exemption provisions within Section 1373 inapplicable to all units in that CID.

### Policy Considerations

In Section 1373(b), the Legislature expressly found that some provisions of the Davis-Stirling Act are appropriate to protect residential owners, but may also impose "unnecessary burdens and costs" on nonresidential owners.

Applying that reasoning to a mixed use development, the provisions of the Davis-Stirling Act that the Legislature listed in Section 1373 should be applicable to the residential owners in the development, but may constitute an unneeded

burden on the commercial or industrial owners in the development. How should a proposed revision treat these conflicting policy considerations?

*Treat Mixed Use Development as Residential Community*

A revision in this matter could treat a mixed use CID in the same way as a purely residential community. Under this formulation, which is the approach taken by existing Section 1373, all provisions of the Davis-Stirling Act would apply to *all* units in a mixed use CID, both residential and nonresidential. That formulation would preserve existing protections for residential owners in a mixed use development, but would also continue any existing burdens created by those same provisions on the nonresidential owners in the development.

*Treat Mixed Use Development as Commercial Development*

Or, the revision could treat a mixed use CID in the same way as a purely *nonresidential* community. Under this formulation, *all* units in a mixed use CID — including residential units — would be exempted from whichever provisions of the Davis-Stirling Act do not apply to nonresidential CIDs generally. That formulation would remove all unnecessary regulatory burdens on nonresidential owners in a mixed use CID, but would deprive the residential owners in the development of the benefits that those same provisions were intended to confer on them.

This formulation would constitute a significant change in both general policy and existing law.

*Special Statutory Treatment for Mixed Use Development*

A third alternative would be to explicitly recognize and provide special statutory treatment for mixed use developments, either by (1) specially defining a mixed use development based on a formula relating to the ratio of residential to nonresidential units, or by some other criteria, or (2) setting forth a special set of Davis-Stirling Act provisions intended to be either applicable or inapplicable only to mixed use CIDs.

Either of these approaches could be very complicated. Both would likely require the assistance of experts on the issue, or at minimum significant input from knowledgeable practitioners.

*Distinct Treatment Based on Ownership Interest in a Mixed Use CID*

Another theoretical alternative would be to identify the provisions of the Davis-Stirling Act that specifically address rights or responsibilities of owners in a CID, and then provide dual versions of those provisions, one set applicable to residential owners in a mixed use CID, and one set applicable to the nonresidential owners in the CID.

The staff views this alternative as very unlikely to be a satisfactory solution. First, the policy considerations underlying many of the "owner" provisions in the Davis-Stirling Act are to some extent based on a homogeneous development. For example, provisions specifying how owners must vote can only be workable if equally applicable to *all* owners in a development.

In addition, many of the provisions in the Davis-Stirling Act are "governance" provisions, regulating the association in charge of the development, rather than individual owners (e.g., budget or record keeping requirements). Based on the inherent nature of a mixed use CID (i.e., one association governing two different types of owners), it would be impossible to modify these provisions to satisfy both groups of owners at the same time.

*Mixed Use Developments with Master Association*

Stephen Dyer points out that there are some developments that consist of multiple, separate CIDs, all under the umbrella of a master association. See Exhibit p. 3. It is possible that one component CID will consist entirely of nonresidential units, while another component CID consists entirely of residential units. In this scenario, the overall development is mixed use, but the individual CIDs that make it up are not.

In that situation, it would seem that Section 1373 would apply to the entirely nonresidential CID, exempting that CID from some provisions of the Davis-Stirling Act. It would not apply to the residential CID. If the master association is also classified as a CID, it would have both residential and nonresidential members and would therefore be a mixed use association of the type discussed above.

We should keep this sort of development in mind when considering the proper treatment of mixed use communities. **The staff invites comment from interested persons if there are other unusual development configurations that**

**might bear on the issue of mixed use communities, or if the description of the "master planned community" set out above omits or misrepresents any details.**

*Timing of Decision on Mixed Use Developments*

In CLRC Memorandum 2008-63, the staff has recommended a methodology for this revision that begins with the Commission deciding whether each existing provision of the Davis-Stirling Act should be applicable or inapplicable to nonresidential CIDs.

If the Commission follows this methodology, these individual decisions might in some cases be affected by whether the category of "nonresidential CIDs" includes mixed use developments. This suggests that the Commission should not begin its consideration of the applicability of individual provisions of the Davis-Stirling Act to nonresidential CIDs until it first decides how the revision should treat mixed use CIDs.

However, the Commission may not yet have sufficient information to decide how to treat mixed use CIDs in this study.

An alternative approach would be to draft a proposed revision based solely on consideration of the application of the Davis-Stirling Act to purely nonresidential CIDs, and then modify that draft if necessary at a later time, to accommodate treatment of mixed use CIDs. However, this approach would add significantly to the Commission's workload, as each previous applicability decision would have to be revisited based on a consideration of the decision's impact on mixed use CIDs.

*Recommendation*

The conservative approach to the treatment of mixed use developments would be to stick with the approach taken by the Legislature in enacting Section 1373. By limiting the application of Section 1373 to purely commercial or industrial developments, the Legislature decided that a mixed use development should be treated in the same way as a residential CID.

Maintaining that approach in a proposed revision would preserve the policy balance struck by the Legislature in 1988. That said, **the staff invites interested persons to comment on this question.** It may be that there are good arguments for changing approaches on this issue.

The staff recommends that **the Commission defer a decision on how a proposed revision in this study should treat mixed use CIDs, until the**

**Commission's February meeting.** In the interim, the staff will gather more information from commenters, and then make a recommendation on the issue in a memorandum to be presented before the February meeting.

Respectfully submitted,

Steve Cohen
Staff Counsel

# EMAIL FROM SKIP DAUM, COMMUNITY ASSOCIATIONS INSTITUTE – CALIFORNIA LEGISLATIVE ACTION COMMITTEE (DECEMBER 3, 2008)

Brian... I haven't read the docs yet, but are you considering mixed use CIDs in the "non-residential" project? Or, in the regular CID project?

We're particularly interested in the election law provisions.

Respectfully,
Skip Daum
Administrator/ Advocate
Community Associations Institute-
California Legislative Action Committee
(916) 791- 4750
(916) 772- 3781

## EMAIL FROM STEVE DYER, MONTEREY, CA
## (DECEMBER 3, 2008)

Brian -

Thank you for forwarding Memorandum 2008-63.

I believe support the Commission's decision to study whether there are provisions within the Davis-Stirling Act which should not be applied to nonresidential commercial/industrial developments.

In that regard, there are two comments that I would like to offer.

1 - Suppose a development is a mixed use project with a separate set of CC&Rs for the residential element, a parallel set of CC&s for the commercial/industrial segment and a master Declaration for the entire project. How will the Commission's study treat that type of development?

2 - Last Fall I wrote to you about the Commission's common interest development project. My letter, a copy of which is attached, pointed out there were a number of provisions in the Davis-Stirling Act that caused a significant burden to residential developments in which there were no significant common area improvements as well as to associations that had a very limited function (e.g., road maintenance associations, well sharing associations) that fall within the statutory definition of a "common interest development". I suspect that many of those associations which have a limited function do not recognize that they be subject to the Act or have chosen not to comply with it. I realize the application of the Act to these associations is not within the scope of Memorandum 2008-63, but I believe the Commission should look at this issue as well.

Steve

Stephen W. Dyer
HORAN, LLOYD, KARACHALE, DYER, SCHWARTZ,
LAW & COOK, INCORPORATED
499 Van Buren Street
P. O. Box 3350
Monterey, CA 93942-3350
Telephone (831) 373-4131
Facsimile (831) 373-8302
Email: sdyer@horanlegal.com

## EMAIL FROM TERRY FARRIS
## (DECEMBER 3, 2008)

Just an observation/question regarding section 1373(a) - your proposed study of exempting nonresidential CIDs from unnecessary regulation under the Davis-Sterling Act does not sound like it takes into account the mixed-use zoning designation( i.e. a zoning designation that typically combines commercial and residential uses) that exists in many cities and counties. This oversight brings up equity issues for commercial/industrial owners vs homeowners. Who shall bear the financial burden of this regulation? Thank you for this opportunity to comment.

Terry Farris, AICP

# EMAIL FROM TINA RASNOW, VENTURA COUNTY SUPERIOR COURT (DECEMBER 3, 2008)

Thanks for the update. I did not read the entire text yet (only about half of it), but I have some concern about protection for small business owners who purchase an office condo and who may face many of the same problems homeowners face when the developer failed to set aside enough money in reserves to cover maintenance; when power and control remain with the developer until most of the units are sold; when mismanagement of assets causes depletion of reserves and resulting costly special assessments, etc.

While it is true that many provisions of Davis-Stirling are particularly directed to homeowners, I think consumer protection needs to be in place for non-residential CID's because many are owned by sole proprietors and small business owners who do not have the expertise or bargaining power that large businesses have. The fact that they may be set up as corporations or LLC's does not necessarily mean they have legal counsel or sophistication. Unfortunately, many small business owners fall prey to the seminars and websites promising personal immunity or protection from lawsuits by incorporating, when in fact they function for all intents and purposes, as a dba. We see them regularly in our self-help center at the court when they get embroiled in a dispute and we explain that because of their corporate status they must be represented by an attorney, yet they do not have the money to hire one.

The eleven years I have run the Self-Help Legal Access (SHLA) Center at the Ventura Superior Court has caused me to rethink many of my previous views about business owners, their access to legal counsel, and their sophistication. They, like many members of the general public, are easy victims of scam artists looking to get rich by selling false promises, and with legal costs such as they are, many are simply unable to afford good legal counsel which they desperately need.

I think it is important to get input from small business owners who own office condos, perhaps through the Chambers of Commerce, or other small business groups, or from attorneys who represent the small business owner, to determine what types of protections need to be in place for this population. I would be reluctant to gut existing protections, without having some alternative in place.

Thanks for considering my comments.

"Our lives begin to end the day we become silent about things that matter." ---Dr. Martin Luther King, Jr.

Tina Rasnow, Coordinator
Self-Help Legal Access Center
Superior Court, County of Ventura
800 South Victoria Avenue
Ventura, California 93009
(805) 654-3879
FAX (805) 654-3560
email: tina.rasnow@ventura.courts.ca.gov

# EMAIL FROM CRAIG STEVENS, COMMERCIAL PROPERTY OWNERS ASSOCIATION (DECEMBER 3, 2008)

Brian,

This is wonderful! Thank you so much for revisiting this topic.

I have already been pulling together a task force of Commercial Property Owners Association "stakeholders" consisting of; management companies, attorneys, developers, trade groups (CACM, CAI, BIA, BOMA, NAIOP, IREM and possibly CAR), brokerage companies and building owners.

I have already personally reviewed every word of the Davis-Stirling Act again, and am compiling my recommendations for the task force and then collectively to the CLRC.

Maybe something good will emerge ultimately from all of your teams hard work on the CID agenda.

Thanks again, on behalf of my 30 team members, 70 developers and 2000 building owners/CID Members and the emerging niche of Commercial Property Owners Association formation and management.

Craig Stevens
(714) 322-8993