NEWS LETTER

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Unintended Consequences of Association Action in the Context of Violation Hearing

The law of unintended consequences is an adage that actions of people and governments always have effects that are unanticipated and often undesirable. The law of unintended consequences is always at work and everywhere, even in community associations.

The Florida Statutes governing condominiums under Chapter 718 and homeowners associations under Chapter 720 both allow an association to impose fines against owners (their tenants, guests, and invitees, if applicable) and to suspend the right to use common areas after at least 14 days written notice and an opportunity for a hearing before an independent committee ("violation hearings").

We recently encountered a situation where an association adopted a long list of burdensome policies and procedures in addition to the minimum requirements of Florida law for conducting violation hearings. Particularly noteworthy were the requirements to have an independent mediator preside over the hearing and enforcement of the Florida Rules of Evidence. Presumably, these policies and procedures were enacted to ensure fairness to all parties. Instead of fostering fair and efficient hearings, however, the real consequences of these additional policies and procedures were delays, inefficiencies, and a board hesitant to conduct hearings due to confusion over what evidence was admissible at the hearing. Rules of evidence can be difficult for laymen without any legal background to understand. It is certainly understandable why the association adopted these policies and procedures since fairness to all parties in violation hearings is of critical importance. However, this is an example of the law of unintended consequences at play. The unanticipated outcomes were not the ones intended by the association's purposeful actions.

In spite of the above example, fines and the suspension of common area use rights can be a useful tool to compel compliance with your association's governing documents. In many cases, the offending owner will respond to the notice and attend the hearing before the association's violations hearing committee. Although the association should demonstrate fairness, the association serves not only the role of prosecutor and judge, but also the jury. It is important to keep in mind that a violation hearing is not a formal court of law where all rules of evidence and procedure are strictly applied, nor is there a requirement that an association hire an independent mediator to preside over the hearing. In fact, one of the strong benefits an association has is the ability to fine and suspend in a tribunal without being burdened by the technical rules as to the admissibility of evidence. Florida law affords associations this advantage and your association

should be careful not to take any action that may complicate or unintentionally burden the process of conducting a fining or suspension hearing.

There are few statutory rules to be followed in the actual process of conducting fining or suspension hearings. This is a good thing. The legislature, in crafting the law, recognized the ability of associations to conduct hearings without having to comply with a complex set of rules. It is our opinion that it would be neither wise nor prudent to impose any additional rules or restrictions which could cause unintended burdens on your association. Our office can provide your association with guidance to ensure that your violation hearings are conducted properly, efficiently and in accordance with Florida law.

Developer's Unilateral Amendment To a Community's Declaration – How Far Is Too Far?

A Florida appellate court recently noted limitations on a developer's right to unilaterally amend a community's declaration of covenants, even if the developer reserved amendment rights in the original document, and reviewed the constitutionality of retroactively applying the financial reporting requirements of Section 720.3086, Florida Statutes, to an association established before the statute took effect.

In *Flescher v. Oak Run Associates, Ltd.*, Case Nos. 5D12-2575 & 5D12-3254 before the Fifth District Court of Appeal, the developer recorded declarations of covenants in 25 single-family home neighborhoods, each providing that the developer would use assessments collected from homeowners for various expenses, including landscaping and lawn maintenance, utilities, security service, and garbage collection. The developer, who had the sole and absolute right to amend each declaration, later amended all of the declarations to: 1) remove provisions requiring that assessments be used for these specific purposes; 2) limit the use of the assessments to the common and recreational areas; and 3) allow the developer to retain any unused assessments. In combination, these provisions effectively shifted the burden of what used to be required assessment expenses to the homeowners and barred the creation of any reserves.

The appellate court reiterated that the developer has the right to amend, alter, modify, or change a declaration if the right is reserved in the original declaration and that the reserved right is reasonably exercised. As outlined by the appellate court, an unreasonable exercise of a developer's amendment rights is an amendment that destroys the general plan under which the community operates and either materially changes the character of the community or materially changes the financial burden on the existing homeowners. The exception to this rule would be if the original declaration had indicated to homeowners that the developer may unilaterally alter the financial burdens on the homeowners by an amendment to the declaration.

Although the appellate court did not find that the developer's amendment in *Flescher* resulted in material changes to the character of the development, it did determine that the developer's amendment:

> *…operated to relieve the developer of his express burden to use the funds collected for maintaining the lawns and landscaped areas of the common areas and recreation areas and for all utility costs…, garbage and trash collection,…security service, cable television reception service, an exclusive closed-circuit…television channel, and for the road and drainage facilities, repair, and maintenance.*

In light of the foregoing, the appellate court held that the amendment was an improper exercise of the developer's amendment power to the extent that it altered the financial burdens of the homeowners and the homeowners were not put on notice that these burdens could be altered since the developer's right to do so was not expressly reserved in the original declarations.

Accordingly, it is important to remember that even where a developer has the unilateral right to amend the declaration of covenants, a developer's exercise of its right to amend is not without limits and courts will not enforce developer initiated amendments that change the character of the development or alter the economic burdens of the homeowners.

Property Managers Are Not Debt Collectors?

On December 12, 2012, the Eleventh Circuit Court of Appeals filed a decision in the matter of *Harris v. Liberty Community Management, Inc*. (Case No. 11-144362*)*, holding that Liberty was not covered by the Fair Debt Collection Practices Act (FDCPA). This is good news but management companies would be mistaken in concluding that this means that they are categorically exempt from the Federal law.

The FDCPA, in pertinent part, specifically excludes as a debt collector:

> "Any person collecting or attempting to collect any debt owed or due or asserted to be owed or due another to the extent such activity (i) is incidental to a bona fide fiduciary obligation…".

The key to the decision in the *Harris* case was the Court's factual finding that debt collection was only an incidental part of the company's business. This may not be true if a management company has a group of employees spending all or most of their time working on collection matters or derives a substantial percentage of its revenues from collection work regardless of how it is organized.

Law firms are in the same situation. The exclusion only protects them if they do not regularly engage in debt collection. For instance, in *Cook v. Hamrick*, 278 F. Supp.2d 1202 (D. Colorado 2003) the Court recognized that pursuing a claim for attorney's fees on an eviction case did not make the lawyer a debt collector. Lawyers who only pursue foreclosure of liens, but not money judgments, may also escape coverage. See *Williams v. Trott*, 822 F.Supp. 1266 (E.D.Mich.1993). The same is not true for law firms that regularly foreclose mortgages and provide payoffs and reinstatement figures for a bank. See *Sandlin v. Shapiro & Fishman*, 919 F. Supp. 1564 (M.D. Florida 1996).

Whether debt collection is "incidental" or a substantial part of the business is a fine line. Another problem in making a definitive self-diagnosis of debt collector status is the dynamics of the situation. In good times, collection work for a property management company doing work for Associations may only be occasional. In bad times it may become the biggest generator of revenue. The addition of one client with many collection matters could also move a management company out of "incidental" involvement in collection work.

Compliance begins with labeling yourself as a debtor in each piece of correspondence to the debtor. There are no points for partial compliance. Good faith is also no defense. If you are covered by the statute, then you are liable for any violation. Management companies that have significant income from collection work still need to be very concerned about the FDCPA and the Florida Consumer Collection Practices Act (CCPA) which can also apply.

Court Addressed Insurance Coverage Confusion

A Florida Appellate Court has again been required to explain what conflicting insurance policy provisions mean in light of Florida's Condominium Act.

In *Citizens Property Insurance Corporation v. River Manor Condominium Association, Inc.*, filed on April 4, 2013, the issue was whether the Florida Condominium Act overrode an exclusion in the Citizens Property Insurance policy for elements of the property that the Association had an obligation to insure. In a 13-page decision, the Court ruled that it did not.

Section 718.111(11)(b), Florida Statutes states: "The Association shall exercise its best efforts to obtain and maintain insurance as described…". However, as the Court explained, there is no "reciprocal statute" that requires insurance carriers to provide the insurance. The Court reiterated the general rule that, under the Condominium Act, the Association is the insurer of any damage that the Association is required to insure. This is true even when the insurance is not available. This is the same principle that applies when the loss falls within the deductible. This is well understood but the confusion created by a standard policy provision amending the policy in case of conflict with the law was enough to confuse even the Judge in the lower court.

In another recent case, *Cheetham v. Southern Oak Insurance Company*, ___ So.2d ___, 2013 WL, 1222942 (Fla. App. 3 Dist.), 38 Fla.L.Weekly D694, the issue was damage caused by a backup caused by the failure of a pipe running from the main drain from the house due to age. The Court explained that the exclusion for damage from deterioration absolved the insurance company from paying to replace the old pipe but not the damage caused by the backup. The Court also held that the backup from the homeowner's own sewer line did not fall within what is commonly called the "flood exclusion". The confusion that caused the error in the lower court is that the flood exclusion applies only to external sources of water or sewage. While many insurance policies do have exclusions that apply to damage caused by broken, leaking or clogged pipes, the policy in this case did not have that type of exclusion. However, the fact that the broken pipe was in the yard and not the house was enough to create an argument that led to the litigation all the way to the appellate division.

To Preserve or Not to Preserve

Unlike condominium associations, the board of directors of a homeowners association is eventually required to address the issue of whether or not to preserve its recorded restrictions. In 1963, the Florida Legislature passed the Marketable Record Titles to Real Property Act ("MRTA"). MRTA's purpose is a laudable one, i.e. facilitate and simplify land transactions by improving marketable title. However, MRTA also has unintended consequences. In particular, it has adversely impacted certain deed restricted communities by extinguishing the communities' deed restrictions as to some lots.

When title is conveyed to a condominium unit, the legal description must cite the recording information for the condominium declaration in the instrument of conveyance (deed). The requirement in the condominium statute ensures that every time a condominium unit is conveyed that the conveyance references the recorded declaration of condominium. There is no corollary statutory requirement for communities governed by homeowners associations to recite the recording information for the restrictions in a deed. Rather, in a homeowners association setting, the deed rarely refers to the lot in a subdivision plat and merely makes a broad reference that the property is subject to restrictions of record. The reference to the restrictions of record does not satisfy MRTA's specificity requirement.

Once a restriction is deemed extinguished under MRTA, the right to enforce the restriction is lost unless the restriction is revived. When restrictions of record are extinguished under MRTA, the consequences can be devastating to a community because the loss of the restrictions can affect property values as the homeowners association and other property owners lose the ability to enforce the extinguished restrictions. Deed restrictions are generally recorded to preserve a community's architectural and aesthetic standards.

To address the unintended consequences that MRTA has had or may continue to have on deed restricted communities, Florida's legislature amended MRTA to provide a method under which a homeowners association's board of directors may take action to preserve its community's restrictions before they expire. However, the statute currently does not require a homeowners association's board of directors to do so. Until recently, an unanswered question existed regarding whether a property

could sue its homeowners association for an injunction to force its board of directors to take action to preserve the community's restrictions.

Florida's Fourth District Court of Appeals answered the unknown question in the affirmative. *Southfields of Palm Beach Polo and Country Club Homeowners Association, Inc., et al. v. Victoria D. McCullough*, Nos. 4D-11-1130 and 4D11-4659 (Fla. 4th DCA April 17, 2013). Based upon the holding in *McCullough*, a homeowner association's board of directors does have a duty to preserve its community's restrictions (at least in the Fourth District). Why? According to the Fourth District Court of Appeals, the trial court said it best when it stated: "[i]f parcels were to drop out piecemeal without the requisite votes required by the [governing] documents, the Association would begin to resemble a piece of Swiss cheese, with portions of Southfields covered by the restrictions and other portions … not covered by the restrictions."

Under MRTA, it behooves any association (other than a condominium association) to be aware of MRTA and to consult with legal counsel regarding whether the association should take action to preserve its restrictions.

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This newsletter is provided as a courtesy and is intended for the general information of the matters discussed herein above and should not be relied upon as legal advice. Christopher J. Shields (christophershields@paveselaw.com) is a Florida Bar Certified Real Estate Lawyer and Partner in the Pavese Law Firm and heads the Community Law Section for the Firm. Christina Harris Schwinn (christinaschwinn@paveselaw.com) is a Partner in the Pavese Law Firm. Ms. Schwinn also specializes in Labor/Employment Law. Susan M. McLaughlin (susanmclaughlin@paveselaw.com) is a Partner in the Pavese Law Firm. Keith Hagman (keithhagman@paveselaw.com) is a Partner in the Pavese Law Firm. Charles B. Capps (charles capps@paveselaw.com), is an Associate with the Pavese Law Firm. Kathleen Oppenheimer Berkey (kathleenberkey@paveselaw.com) is an Associate with the Pavese Law Firm. Matthew P. Gordon, Esq. (matthewgordon@paveselaw.com) is an Associate with the Pavese Law Firm. Christopher L. Pope (christopherpope@paveselaw.com) is an Associate with Pavese Law Firm. Mr. Capps, Ms. Berkey, Mr. Gordon and Mr. Pope handle all aspects of Community Association law for the Firm. Brooke N. Martinez (brookemartinez@paveselaw. com) is an Associate with the Pavese Law Firm. Each attorney is well versed and capable of handling all aspects of community association law, including but not limited to governing document interpretation, covenant enforceability, collection of assessments, lien foreclosures and general litigation. Please feel free to contact them via the e-mail addresses listed above.

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