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2008 Legislative Changes Affecting Community Associations: An Analysis of HB 516

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The 2008 legislative session saw the General Assembly adopt legislation that constitutes the most comprehensive and sweeping changes to Virginia community association law this decade. Specifically, effective July 1, 2008, House Bill 516 will become law (although certain provisions will not be implemented until later).

The bill has a wide-ranging scope; which includes the creation of a new regulatory Board, the establishment of manager licensing requirements, changes to the existing procedures for association disclosure packages, the creation of an Ombudsman with the authority to hear complaints made by association members, and the creation of a limitation on a Property Owners' Association's authority to impose fees on its members.

I. Creation of Common Interest Community Board

HB 516 transfers the regulatory authority over community associations to a newly created Common Interest Community

Board. The CICB will consist of three community managers, an attorney, a certified public accountant, two real estate developers, one citizen who serves on an association Board, and two citizens who reside in a community association. The CICB will have the responsibility for overseeing the licensing and certification requirements for property managers, which is discussed in detail below. Among the responsibilities of the CICB will be to establish regulations governing the licensing and certification of managers, regulating the complaint process created through the Office of the Ombudsman, as well as handling the registration of condominiums and annual reports for community associations currently handled by the Real Estate Board.

In addition, the CICB will be responsible for administering the Common Interest Community Management Information Fund, which was previously handled by Real Estate Board. The CICB will charge management companies an annual licensing fee of the lesser of \$1,000 or .02 percent of

the company's gross receipts, and also be the recipient of community association's annual registration fees, which will increase to the lesser of lesser of \$1,000 or .02 percent of the association's gross assessment income for the prior fiscal year.

Among the CICB's regulatory functions will be to receive complaints relating to the misconduct of management companies that are subject to the licensing requirements of the new Act. Community associations that believe that there has been a mishandling of their business operations or their funds now will have the option of submitting a complaint to the Director of the CICB. As part of this regulatory effort, the CICB will also administer a Common Interest Community Management Recovery Fund (CICMRF), which will be funded by community associations and property management companies through an annual assessment of \$25 each. By July 1, 2011, the CICMRF must have at least \$150,000. The CICMRF will be available to associations as reimbursement for any funds misappropriated by their management company provided that the CICB finds that there was sufficient evidence to substantiate the association's claim of malfeasance.

The CICB shall also have the power to issue cease and desist orders and seek injunctions against any person or company in violation of the licensing statute. The CICB may also seek an injunction against any person or company. In addition, the CICB will have jurisdiction over violations of the Condominium Act or Property Owners' Association Act committed by any person or company, and may issue civil fines of up to \$1,000 for each such violation.

II. Licensing Requirements

a. Licensing and Certification

The New Section 54.1-2346 of the Virginia Code requires any person, partnership, corporation, or other entity offering management services to a common interest community to be licensed, effective January 1, 2009.

Exemptions to this requirement are set forth in Section 54.1-2347.

The definition of a "common interest community" is as follows:

Real estate located within the Commonwealth subject to a declaration which contains lots, at least some of which are residential or occupied for recreational purposes, and common areas to which a person, by virtue of his ownership of a lot, is a member of an association and is obligated to pay assessments provided for in a declaration.

The term "management services" is defined to include the following:

(i) acting with the authority of an association in its business, legal, financial, or other transactions with association members and nonmembers; (ii) executing the resolutions and decisions of an association or, with the authority of the association, enforcing the rights of the association secured by statute, contract, covenant, rule, or bylaw; (iii) collecting, disbursing, or otherwise exercising dominion or control over money or other property belonging to an association; (iv) preparing budgets, financial statements, or

other financial reports for an association; (v) arranging, conducting, or coordinating meetings of an association or the governing body of an association; (vi) negotiating contracts or otherwise coordinating or arranging for services or the purchase of property and goods for or on behalf of an association; or (vii) offering or soliciting to perform any of the aforesaid acts or services on behalf of an association.

Section 54.1-2347(A) sets forth the various exemptions from the licensing requirements. They are as follows:

1. An employee of a duly licensed common interest community manager providing management services within the scope of the employee's employment by the duly licensed common interest community manager;
2. An employee of an association providing management services for that association's common interest community;
3. A resident of a common interest community acting without compensation providing management services for that common interest community;
4. A member of the governing board of an association acting without compensation providing management services for that association's common interest community;
5. A person acting as a receiver or trustee in bankruptcy in the performance of his duties as such or any person acting under order of any court providing management services for a common interest community;

6. A duly licensed attorney-at-law representing an association or a common interest community manager in any business that constitutes the practice of law;

7. A duly licensed certified public accountant providing bookkeeping or accounting services to an association or a common interest community manager;

8. A duly licensed real estate broker or agent selling, leasing, renting, or managing lots within a common interest community; and

9. An association, exchange agent, exchange company, managing agent, or managing entity of a time-share project registered pursuant to the Virginia Real Estate Time-Share Act (§ 55-360 et seq.) providing management services for such time-share project.

These provisions will require management companies to be licensed by the newly-created CICB and also will require property managers employed by management companies to obtain an individual certification by July 1, 2011, per Section 54.1-2346(C). Managers that are employed directly by a community association are not subject to the licensing or certification requirements set forth in HB 516.

Section 54.1-2346 requires all employees on a management company who have "principal responsibility for management services" or who have "supervisory responsibility for employees who participate directly in the provision of management services" to obtain a certificate issued by the CIC Board which certifies that the employee "possesses the character and minimum skills

to engage properly in the provision of management services to a common interest community.”

The legislation requires the CIC Board to adopt regulations to establish certification criteria; however, we also anticipate that existing CAI and other management certifications such as a CMCA or PCAM will be sufficient to allow a property manager to be deemed “certified” by the CIC Board.

b. Additional Requirements of Licensed Management Companies

In order to obtain and maintain its license, a property management company must comply with several other provisions of the Bill that relate to the duties and responsibilities of a fiduciary managing the property of another.

Section 54.1-2346(D) of the new statute requires property management companies to obtain and maintain a blanket fidelity bond or employee dishonesty insurance policy that performs two functions: a) protects community associations against losses of its money resulting from theft or dishonesty committed by the officers, directors, and employees of the association or management company where appropriate, and b) protects an Association against losses of its money resulting from theft or dishonesty committed by individuals employed by the association or management company.

The amount of the coverage must be at least equal to the lesser of \$2 million or the highest aggregate amount of the operating and reserve balances of under the custodial

control of the management company or association in the appropriate case, but in no case less than \$10,000.00.

Section 54.1-2346(E) also imposes several other requirements upon the property management companies, as a condition of obtaining its license and renewal. Those requirements include:

1. The management company must be in good standing and authorized to transact business in Virginia;
2. The management company must establish a Code of Conduct for its officers, directors, and employees to protect against conflicts of interest;
3. The management company provides all management services pursuant to a written contract;
4. The management company must establish a system of internal accounting controls to manage the risk of fraud or illegal acts; and
5. The management company retains an independent certified public accountant to review or audit the financial statements prepared by the management company at least annually in accordance with standards established by the American Institute of Certified Public Accountants or by any successor standard-setting authorities.

Section 54.1-2353(A) of the Bill establishes additional fiduciary duties owed by the management company to their community association clients when handling its financial affairs:

1. All funds deposited by the management company on behalf of a community association shall be handled in a fiduciary capacity, kept in a separate account or accounts, and in an FDIC-insured financial institution separate from the management company's accounts;

2. The funds shall be the property of the community association and shall be segregated for each depository in the records maintained by a management company in a manner that permits the funds to be identified as owned by a particular association;

3. The management company must retain records of community associations and may dispose of them only in accord with a written policy contained in a contract between a management company and their association clients;

4. The management company must return all of an association's original records that are in the possession of the management company within a reasonable time after termination of the contract with the community association without additional cost to the community association. Any failure by a management company to obtain the required license or comply with the other requirements of the licensing laws may subject the manager or company to criminal (as a misdemeanor) and civil penalties, as set forth in Section 54.1-111 of the Virginia Code.

Management companies may qualify for a provisional license provided they apply for a provisional license *before* the deadline of January 1, 2009. Any such provisional license would expire after June 30, 2011,

and would not be subject to renewal. At that time, the management company would have to obtain a full and regular license.

III. Disclosure Packets

House Bill 516 contains several provisions that relate to the delivery of the disclosure packets, including who may receive and request them and when.

The Bill also sets restrictions on the fees that a management company may charge for its preparation of the disclosure packets and prohibits it from charging any other fees not expressly authorized in the Property Owners' Association Act or Condominium Act.

Further, the Bill eliminates a management company's or association's ability to **require** anyone to pay the fees for the disclosure packet prior to the issuance of the packet and instead requires the management company or association to make arrangements to collect the payment of these fees from the settlement agent. If settlement does not occur within ninety (90) days of the delivery of the disclosure packet, the management company or association may assess the fee against the lot owner for which it prepared the disclosure packet and this fee shall become an assessment against the member's lot.

a. Substance of Disclosure Packet

For the most part, House Bill 516 mirrors the existing Code regarding the information that an association is required to disclose in the disclosure packets. The only major change is contained in Section 55-509.5(A)(13) (see condo) which requires an association to include a “copy of any approved minutes of the board of directors and association meetings for the six calendar months preceding the request for the disclosure packet.” This revised language clarifies that the association has an affirmative obligation to disclose in the disclosure packet whether or not the lot or unit is currently in violation of the association’s governing documents.

b. Delivery of Disclosure Packet

Section 55-509.5(C) contains changes relating to whom the management company or association must deliver the packet. House Bill 516 now requires associations or management companies to deliver the packet in accordance with the written request and instructions of the seller or his authorized agent. This written request must specify the complete contact information for the parties to whom the association or management company shall deliver the disclosure packet.

In addition to changes relating to who may receive the packet, House Bill 516 also elaborates on the methods of transmitting the packet by providing detailed requirements relating to electronic transmission. Section 55-509.5(C) provides that the seller or authorized agent may

request the management company or association to provide the disclosure packet in hard copy or in electronic form. If the seller does not request a particular method of transmission, the management company or association may choose the method, but must comply with any in-person requests of the seller at the management company or association’s principal place of business to provide a hard copy of the packet. The management company or association cannot charge a seller an extra fee to use its electronic network or system if the seller requests an electronic transmission. In addition, the seller may designate: (1) in condominiums, up to two additional recipients; but (2) for property owners associations, one additional recipient, to receive the electronic disclosure packet at no charge.

In addition to changes to whom and how the management company or association must provide disclosure packets, House Bill 516 also changes when the management company or association must provide the packet.

Effective July 1, Section 55-509.5(A) will require the management company or association to deliver the disclosure packet within fourteen (14) days after receipt of the written request. The requirement to deliver the packet may not be conditioned upon receipt of payment. Section 55-509.6(B) will not allow the management company or association to **require** cash, check, certified funds or credit card payments at the time a party makes the request for a disclosure packet; however, Section 55-509.7 is silent on a similar restriction with respect to self managed associations. Section 55-509.6(D) requires the management company to collect

any fees at the time of settlement on the sale of the lot. If settlement does not occur within 90 days of the delivery of the disclosure packet, or funds are not collected at settlement and disbursed to the association or the management company, all fees, including those costs that would have otherwise been the responsibility of the purchaser or settlement agent, shall be assessed against the lot owner and shall be the personal obligation of the lot owner and shall be an assessment against the lot and collectible as any other assessment in accordance with the provisions of the declaration and § [55-516](#). The seller may pay the association by cash, check, certified funds, or credit card, if credit card payment is an option offered by the association.

c. Disclosure Packet Fees

In addition to those changes set forth above, House Bill 516 also revamps the types and amounts of fees that the management company may charge. Section 55-509.6(B) provides that the management company, may charge a “reasonable” fee for the following services and subject to these limitations:

1. The inspection of the exterior of the dwelling unit and the lot, as authorized in the declaration and as required to prepare the association disclosure packet, a fee not to exceed \$100;

2. The preparation and delivery of the disclosure packet in (i) paper format, a fee not to exceed \$150 for no more than two hard copies or (ii) electronic format, a fee not to exceed \$125 for no more than two electronic copies. Only one fee shall be

charged for the preparation and delivery of the disclosure packet;

3. At the option of the seller or his authorized agent, expediting the inspection, preparation and delivery of the disclosure packet, an additional expedite fee not to exceed \$50.

4. At the option of the seller or his authorized agent, an additional hard copy of the disclosure packet, a fee not to exceed \$25 per hard copy, for each hard copy requested in addition to a hard or electronic copy already issued or to be issued to the seller, purchaser, or the settlement agent;

5. At the option of the seller or his authorized agent, a fee not to exceed an amount equal to the actual cost paid to a third-party commercial delivery service for hand delivery or overnight delivery of the association disclosure packet; and

6. A newly recognized post-closing fee to the purchaser for the purpose of establishing the purchaser as the owner of the property in the records of the association, a fee not to exceed \$50 and collected at settlement. No such fee is recognized in the existing Code.

In addition, the Association is required to disclose any fees it charges for the preparation of a disclosure package against a subsequent purchaser in the event settlement does not occur within 90 days. This disclosure must be included in the line item addressing the statement of account for the lot or unit.

For self managed Associations, the fee structure remains unchanged.

d. Disclosure Packet Updates

House Bill 516 also contains several changes to the requirements concerning requests for updates of an already issued disclosure packet.

The resale provisions in both the Condominium Act and POA provides that now both the *purchaser* and the *seller* may request an update of a disclosure packet for the same fee of no more than \$50.00 and within the same ten (10) day time frame. The requester cannot be required to pay in cash, by credit card, check or certified funds at the time the request is made, and the requestor may request that the update be provided in either hard copy or electronic funds.

In addition, Section 55-509.6(G) and Section 55-509.7(C) allows the settlement agent to require a community association managed to provide a written statement concerning any outstanding fees within three (3) days of the written request at a fee of no more than \$50.00. This type of update is distinct from the resale disclosure update mentioned above and is not recognized in the existing Code.

In addition, the purchaser or his agent may also request that a community association to perform an updated inspection of the lot and related report for a fee not to exceed \$100.00.

The same delivery methods for the original disclosure packet apply to the update.

IV. Complaint Process- The Office of the Common Interest Community Ombudsman

Section 55-530(B) establishes the Office of the Common Interest Community Ombudsman (“the Office”). Ostensibly, this Office will serve as an informational resource to members of associations and help them understand their rights and the processes available to them according to their associations’ legal documents, as well as Virginia law.

According to Section 55-530(C)(7), the Office has the authority to issue nonbinding explanations of laws or regulations governing common interest communities or interpretations thereof by the CIC Board.

In short, the goal of the Office is to reduce and resolve conflicts among associations and their membership; however, we suspect the actual role the Office will be different, as we more fully explain below.

The Office will have jurisdiction to investigate and adjudicate complaints initiated by members against community associations.

a. Internal Association Complaint Process

Section 55-530(E) provides that the CIC Board shall establish by regulation a requirement that each association shall create reasonable procedures for the resolution of written complaints from the members of the association and other citizens. These complaint procedures must include the following:

1. A record of each complaint shall be maintained for no less than one (1) year after the association acts upon the complaint.

2. Each association shall provide complaint forms or written procedures to be given to persons who wish to register written complaints. The forms or procedures shall include the address and telephone number of the association or its common interest community manager to which complaints shall be directed and the mailing address, telephone number, and electronic mail address of the Office of the Common Interest Community Ombudsman. The forms and written procedures shall include a clear and understandable description of the complainant's right to give notice of adverse decisions to the Office.

In addition to any procedures set forth in a community association's legal documents for the resolution of complaints, the Conservancy must ensure that it complies with the requirements of this section once the CIC Board adopts its implementing regulations. Once this happens, we will let you know.

b. CIC Complaint Process

Irrespective of whether the CIC Board adopts any regulations in the future, House Bill 516 provides members of community associations with the right to file complaints with the CIC Board against their community association effective July 1.

Section 55-530(F) provides that the complainant must merely submit the notice

of complaint in writing, along with copies of all pertinent records, and pay a \$25 fee (which the CIC Board may waive in its discretion, if the complainant pleads undue financial hardship.)

Section 55-530(G) requires a community association to respond to the complaint within a reasonable time, if the CIC Board requests such.

We hope we're wrong, but we expect that this procedure will result in a lot more complaints against community associations in general, as it eliminates the burden of cost that litigation requires of a litigant.

It is too soon to tell whether the CIC Board will be a paper tiger or a quasi-court.

The Bill is silent on whether the CIC Board can levy penalties, monetary or injunctive, in connection with its rulings, and, therefore, there will be serious legal questions if it tries to do so through authority that it arrogates to itself through its regulations.

As the Bill currently reads, the CIC Board's decisions are final, but not binding upon the parties. Therefore, rather than insulating a community association from litigation and mandating an alternative dispute resolution process, the Bill provides yet another forum for members to lodge complaints.

V. New Restriction on Fees Charged by Associations

HB 516 amends the POA by creating a new Section 55-509.3, which prohibits a property owners' association from levying any charges or assessments unless such charge or assessment is expressly authorized by the POA, the Association's Declaration, or otherwise by law with the exception of any charge or assessment is related to services provided by or through the association or related to the use of common area – which are allowed regardless of whether originally authorized by the POA or the Declaration or other law. This provision was designed to invalidate certain fees or charges that are created strictly by resolution of the Board. Examples of charges that may now be invalid include transfer fees, new construction fees, bounced check fees and leasing fees.

Please contact any of our community association attorney if you have any questions relating the application of this law to your association.