Baker & Hostetler LLP

303 East 17th Avenue
Suite 1100
Denver, CO 80203-1264

T 303.861.0600
F 303.861.7805
www.bakerlaw.com

David B. Waller
direct dial: 303.764.4093
dwaller@bakerlaw.com

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HAND DELIVERY

Business, Labor and Technology Committee
Colorado Senate

Re: HB09-1359

Dear Members of the Committee:

I am a partner in the Denver office of Baker Hostetler. I spend a great deal of my time working with community associations regulated under the Colorado Common Interest Ownership Act ("CCIOA"), both with respect to formation and operations. Having had the opportunity to review HB09-1359, I would like to submit the following comments with respect to the proposed additions of 38-33.3-209.5(1)(b)(IX) (**reserve studies**) and 38-33.3-303(1)(b) (**executive board disclosures**).

Reserve Studies

I fully support the efforts of the bill's sponsors, Representative Kerr and Senator Boyd, to emphasize reserve studies. These studies are an integral part of the management process, and their use avoids preventable funding emergencies. I am particularly happy with the balance struck by proposed 38-33.3-209.5(1)(b)(IX), which encourages disclosure and unit owner understanding of important details regarding the study, while also allowing management companies and HOA boards the flexibility to undertake studies relevant to the particulars of the property.

My only concern here has to do with the practice of HOAs to undertake interim reserve studies that update the financial analysis portion of the reserve study. These interim studies are useful when financial assumptions change, but don't necessarily require new physical inspections. In order to clarify that these interim studies remain permissible, and to ensure that HOAs are not discouraged from running financial "stress tests" when circumstances require, I suggest the following minor revision to proposed Section 38-33.3-209.5(1)(b)(IX):

WHEN THE ASSOCIATION HAS A RESERVE STUDY PREPARED FOR THE PORTIONS OF THE COMMUNITY MAINTAINED, REPAIRED, REPLACED, AND IMPROVED BY THE ASSOCIATION AND WHETHER THERE IS A FUNDING PLAN, PROJECTED SOURCES OF FUNDING, AND WHETHER THE RESERVE STUDY IS BASED ON A

PHYSICAL ANALYSIS, ~~AND~~ A FINANCIAL ANALYSIS, OR BOTH. FOR THE PURPOSES OF THIS SUBPARAGRAPH (IX), AN INTERNALLY CONDUCTED RESERVE STUDY SHALL BE SUFFICIENT.

Executive Board Disclosures

Proposed Section 38-33.3-303(1)(b) states as follows:

NOTWITHSTANDING ANY PROVISION OF THE DECLARATION OR BYLAWS TO THE CONTRARY, ALL MEMBERS OF THE EXECUTIVE BOARD **SHALL HAVE AVAILABLE TO THEM ALL INFORMATION RELATED TO THE RESPONSIBILITIES AND OPERATION OF THE ASSOCIATION OBTAINED BY ANY OTHER MEMBER OF THE EXECUTIVE BOARD**. THIS INFORMATION SHALL INCLUDE, BUT IS NOT NECESSARILY LIMITED TO, REPORTS OF DETAILED MONTHLY EXPENDITURES, CONTRACTS TO WHICH THE ASSOCIATION IS A PARTY, AND COPIES OF COMMUNICATIONS, REPORTS, AND OPINIONS TO AND FROM ANY MEMBER OF THE EXECUTIVE BOARD OR ANY MANAGING AGENT, ATTORNEY, OR ACCOUNTANT EMPLOYED OR ENGAGED BY THE EXECUTIVE BOARD TO WHOM THE EXECUTIVE BOARD DELEGATES RESPONSIBILITIES UNDER THIS ARTICLE.

We presume that proposed Section 38-33.3-303(1)(b) is intended to create a more transparent HOA decision-making process. However, we think this approach creates at least three significant problems.

- The underlined portion of proposed Section 38-33.3-303(1)(b) above is not quantifiable, and thus raises concerns with respect to both enforcement and abuse. Regarding enforcement, the provision does not, and practically cannot, adequately empower the executive board members to require informative disclosures of the type of information described. This flaw, however, does create the likelihood for abuse, as a minority of executive board members could use the provision to bring HOA business to a standstill through allegations of non-disclosure. This strategy could be used on an "after-the-fact" basis, even in the event the information not disclosed was immaterial to the challenged action.

- This provision likely creates an enhanced "duty of loyalty" that would apply to HOAs but not similarly-situated corporate entities.[1] As this enhanced obligation is not part of the analytical framework established by existing case law or common law, it should be expected that the judiciary would be called upon to define its parameters. Those decisions would almost assuredly create a significant degree of uncertainty, especially with respect to the liability waiver applicable to directors not appointed by the developer

[1] *See* CRS §7-108-401(1), which requires each director of a corporation to discharge their duties in good faith and in a manner reasonably believed to be in the best interests of the corporation. This duty of loyalty can not be eliminated or limited in the corporations documents. *See* CRS §7-108-402(1). These provisions also apply to nonprofit corporations pursuant to CRS §§7-128-401 & 402.

pursuant to CRS §38-33.3-303(2)(b). This, in turn, will adversely impact HOA management and operations. For example, a broad interpretation of the proposed provision that increase the risk of director liability would make it difficult to acquire D&O insurance at a reasonable cost or upon reasonable terms.

- Proposed Section 38-33.3-303(1)(b) does not appreciably enhance transparency, as it significantly overlaps with existing provisions intended to protect unit owners from overreaching by an executive board. For example:

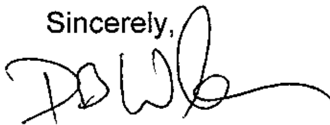
  - Pursuant to CRS §38-33.3-310.5, individual members of the executive board are currently subject to the conflict-of-interest provisions applicable to nonprofit corporations at CRS §7-128-501. Those existing provisions would require the executive board member to disclose any "contract, transaction or other financial relationship" between the HOA and the executive board member or a party related to the executive board member. Failure to disclose the conflict of interest would render the action "void or voidable."

  - Most, if not all, of the types of documents described in the provision are arguably already available to all unit owners (including executive board members) under CRS §38-33.3-317(1) and (2).[2] Because all unit owners are also allowed to attend and speak at all executive board meeting pursuant to CRS §38-33.3-308(2.5)(a) and (b), these two provisions combine to create a real check on executive board actions.

Notwithstanding our above-listed concerns, we understand that the Committee may be intending to curb a particular type of abuse of which it has become aware. If that is the case, we believe that the remedy may be more narrowly targeted through a revision to CRS §38-33.3-317(5) that would supplement the types of documents available for unit owner review.

We thank you for the opportunity to address the Committee.

Sincerely,



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[2] There is no reason why these documents would not be available to all unit owners, including executive board members, following the expiration of the Declarant control period as CRS §38-33.3-303(9)(a) through (m) lists a full roster of documents the Declarant is required to turn over to the association.