What needs to be fixed in Texas' HOA and deed restriction laws?

A Whirlwind of Legislation: Since 1985, the Texas Legislature has engaged in a whirlwind of activity relating to HOAs and deed restrictions. Only one session (1993) failed to enact or amend these laws. Each active session has added to the power of HOAs -- specifically HOAs primarily in the Houston area. In fact, the legislation has been so quick in coming and apparently so unintegrated, that the 1999 Legislature enacted three separate Property Code Chapters numbered 207!

The current work of the Senate Subcommittee on Property Owners' Associations will, I hope, bring some reason and integration to this area. In particular, I hope that the subcommittee produces a new law that protects homeowners -- a protection that is missing in the current law.

Until the 2001 legislative session, the new legislation has been focused almost exclusively on strengthening HOA powers without addressing or balancing those powers with homeowner rights. The 2001 session enacted new Property Code Chapter 209 which on its face claimed to offer homeowners protection. That facial claim is untrue. Chapter 209, on balance, strengthens HOAs at the expense of homeowners.[1]

The problems: What we need now is an integrated law that addresses the problems that have arisen under the last two decades of legislation. The protections needed should apply to all homes -- **including condominiums and town homes.**

The problems include at least the following:

- **No Bill of Rights:** The absence of any homeowner bill of rights.[2] At the very least, homeowners need guarantees of free speech,[3] due process,[4] and the right to vote.[5]
- **Foreclosure power**
  - The current right of HOAs to foreclose on homesteads.[6]
  - The current right of HOAs to foreclose on homesteads for trivial amounts of debt.
  - The current practice of HOAs foreclosing on neighbors without a vote of the owners.
  - The current practice of HOAs foreclosing on neighbors in relative secret, at least as concerns the overall subdivision.
  - The use of Chapter 204 to expand the HOA's foreclosure right.[7] The Texas Supreme Court, in *Inwood*, limited HOA foreclosures to assessments that touch or concern the land (in that case for maintenance of common areas). HOAs have used Chapter 204 improperly to allow foreclosure based on any unpaid assessment.
- **Assessments**
  - The current practice of HOA boards accumulating unnecessary savings and continuing to charge assessments.[8]

- The absence of statutory protections against unilateral use of large sums of HOA funds
- The inherent power under Chapter 204 to accumulate increases in assessment for decades.

- **Fines**
  - The current right of HOAs to assess fines.[9]
  - The lack of any clear, objective, and limited standards for HOA fines.
  - The lack of due process protections with respect to fines.
  - The lack of reasonable limits on fines.
  - The failure of Chapter 209 to include any meaningful prohibition of foreclosures based on fines[10]
- **Voting**
  - The current practice of HOAs "disqualifying" owners from voting.[11]
  - The current practice of HOA boards refusing to abide by majority resolutions or votes
  - The lack of clear standards for determining a percent of votes in a subdivision.[12]
  - The lack of clear rules and safeguards for conducting HOA elections.[13]
  - The current law that permits passage of new assessments by only a majority of those voting rather than a majority or other percentage of all owners.[14]
  - The ability to count two owners of one lot as two votes compared with one owner of a same size lot.[15]
- **Arbitrary and discriminatory practices**
  - The current right of HOAs to act selectively against homeowners.[16]
  - The current law that permits a new deed restriction to apply only to part of a subdivision – even to a single lot or owner – without the consent of the affected owner[17]
  - The current presumption that any HOA action concerning a deed restriction is reasonable and the not quite symmetrical burden upon a homeowner to show that the action is arbitrary, capricious, or discriminatory.[18]
- **Legal fees**
  - The current right of HOAs to recover for legal fees before trying to work out a solution.
  - The current right of HOAs to recover for legal fees before the debt reaches a certain minimum level.
  - The current right of HOAs to recover for legal fees without any measure against the basic debt or issue
  - The failure of new Chapter 209 to include any meaningful attorneys' fees protection.[19]
- **Lack of owner consent or notice**

- The current law allows creation of HOAs, mandatory dues and foreclosure rights against longtime residents who never agreed to the new restrictions or even who believe that their longtime bylaws and deed restrictions prohibit such unapproved actions.[20]
- The current law allows creation of a new HOA or deed restriction binding on a homeowner without the homeowner having ever heard of the proposal for a new HOA or deed restriction.[21]
- The lack of any real effect for the Chapter 209 requirement that an HOA provide notice and an informal hearing before taking action.[22]

- **HOA inherent powers**
  - The current law that provides to HOAs inherent powers if not expressly withheld.[23] Because of the effect that HOA powers have on individual rights, an HOA should not have a power unless expressly granted -- at least not a power that affects personal rights.
  - The retroactive effect of these new inherent powers as applied to existing HOAs and prior bylaws and deed restrictions.[24] The new laws change basic assumptions and strip away rights of homeowners who have lived in their homes for decades, putting formerly secure homeowners at risk of foreclosure.
- **Mediation and ADR**
  - The failure of Chapter 209 to create any meaningful right of mediation.[25]
  - The failure of any concept of mediation or ADR or prior negotiations to recognize that the HOA has all the leverage in negotiations -- the right of foreclosure, the presumptions of reasonableness, and the right to repayment of attorneys fees that will accumulate.
- **Redemption**
  - Chapter 209 creates a right of redemption, but it is a right that few can exercise at the cost required. Like the concept of mediation or ADR, The “right of redemption” fails to recognize that by failing to address limitations on attorneys fees, assessments and fines, the right of redemption is quite impotent.
- **HOA attorney files**
  - The extraordinary and unprecedented protection of an HOA attorney's files from "production in a legal proceeding."[26]
  - The extraordinary change in the law that made an HOA attorney's files his property rather than his client's property.[27]
- **Other problems**
  - The lack of sunset review within subdivisions for HOAs and deed restrictions
  - The ambiguity surrounding the meaning of Section 204.005(a)[28]

- The ambiguity about the long-followed maxims that deed restrictions are construed "to favor free and unrestricted use of land" and "in favor of the grantee and against the drafter."[29]
- The lack of consistent definitions of HOAs.

- **Laws applicable to less than all of Texas:** Most of the new Property Code Chapters on deed restrictions and HOAs are for specific counties, cities or subdivisions.[30] I believe that if the legislation applied to all of Texas, then the Legislature would more closely scrutinize the legislation and its erosion of individual rights.
  - While the current law remains -- applicable to subdivisions, cities, or counties of different sizes, the law creates conflict as the rules applicable to existing subdivisions, HOAs, and deed restrictions change over time as the population changes. A particularly vexing issue can arise if HOAs for different subdivisions merge to form one HOA to govern all the subdivisions. The residents can find -- without their knowledge or intent -- that they are suddenly subject to new rules quite contrary to the rules that applied before the merger.
- **Lack of "neighborliness":** The overall problem that I see in all of this is the lack of "neighborliness." A neighborhood is supposed to be about"neighbors helping neighbors." That focus is entirely missing in the conduct of many if not most HOAs. It is wholly absent from the structure of the current statutes.

NOTES

1. In fact, Chapter 209 provides to HOAs a right that not even the President of the United States enjoys. Chapter 209 provides simply and absolutely:

> An attorney's files and records relating to the association [an HOA], excluding invoices requested by an owner under Section 209.008(d), are not: ... (3) subject to production in a legal proceeding.

Section 209.005(b)(3). This is a right that President Nixon, President Clinton, and Vice-President Cheney would have loved to have.

2. Our forefathers refused to adopt the Constitution without a promise of a Bill of Rights. Creation of the quasi-governmental HOAs has stripped Texas homeowners' rights away without this protection.

3. Many news items in the last year concerned HOAs fining homeowners for flying the American flag.

4. Most of the problems detailed in the remainder of this article concern a lack of due process protection.

5. See "Voting" below.

6. I believe that HOAs should not have any power to foreclose. HOAs should not be in a better position than a doctor who saves a person's life or a credit card company or a lawyer or any other creditor.

7. Under *Inwood*, the term "assessment" was limited to "maintenance assessments for the purpose of repairing and improving the common areas and recreational facilities." This narrow definition was necessary because the right of foreclosure would arise only if the obligation to pay met -- among other elemental requirements -- the requirement that "it touches and concerns the land." *Inwood*, citing *Westland Oil Devel. Corp. v. Gulf Oil Corp.*, 637 S.W.2d 903, 910-11 (Tex.1982); Williams, Restrictions on the Use of Land; Covenants Running with the Land at Law, 27 Tex.L.Rev. 419, 423 (1949).

Although nothing in the Legislative history suggests an intent to expand the types of assessments that can be the subject of foreclosure, Chapter 204 contains a much broader definition of assessments than "maintenance assessments for the purpose of repairing and improving the common areas and recreational facilities." It defines assessments as:

> (3) "Regular assessment" means an assessment . . . that each owner . . . is required to pay . . . on a regular basis and that are to be used by

> the association for the benefit of the subdivision . . . .
> (4) "Special assessment" means an assessment . . . that each owner . . . is required to pay . . . after a vote . . . for the purpose of paying for the costs of capital improvements to the common areas . . .

§§ 204.001.

8. Some anecdotal evidence suggest that a few HOAs have accounts with hundreds of thousands of dollars.

9.I believe that HOAs should not have any power to assess fines.

10. Chapter 209 appears to prohibit HOA foreclosures where the foreclosure is "solely" related to fines, however, this prohibition is illusory. The prohibition applies only to a foreclosure where "the debt securing the lien consists solely of: (1) fines assessed by the association; or (2) attorney's fees incurred by the association solely associated with fines assessed by the association." An HOA need only sue to enforce a deed restriction (the source of a fine) and, in that case, the debt will include amounts outside the "solely for" requirement. 209.009. The website www.HOAdata.org lists more than 15,000 Houston-area foreclosure-related filings from 1985 to 2001 and refers to an additional 4,000 HOA injunction cases. I do not know any of these 19,000 (plus) cases that could be said to involve a lien that "consists solely of: (1) fines assessed by the association; or (2) attorney's fees incurred by the association solely associated with fines assessed by the association." To my knowledge, each case concerns either unpaid assessments or seeks an injunction to enforce deed restriction violations. (In the injunction cases, the HOA can claim a lien for attorneys fees related to enforcement of the deed restriction. This is different from attorneys fees related to recovery of a fine.) Each of these claims removes the case from the foreclosure prohibition.

11. HOAs disqualify owners from voting on grounds that were long ago ruled improper for disenfranchising voters in general elections.

12. The chapters are not consistent or even often explicit about whether the percentage of votes is based on the number of individual owners, number of lots, acreage, or other criteria. Under Chapter 204, the 75% may be derived by counting the total of all owneres in all sections. Thus, a deed restriction can be imposed on a section having its own separate deed restrictions even if no owner in that section consented to the new deed restriction. §§ 204.005(c). Further, Chapter 204 seems to count each individual owner separately. Thus, a single lot owned by three people counts for three votes, while the same lot, if owned by one person, counts for one vote.

13. The instances of injustice in votes are anecdotal, but quite heinous.

14. § 206.003(b). If passed, the extension is enforceable against all properties in the subdivision,

both residential and commercial. § 206.003(c).

15. § 206.004(d).

16. Many anecdotal stories exist of HOAs acting against individual owners for "problems" that are ignored for other owners.

17. In 1985, with enactment of Chapter 201, the Legislature prohibited any challenge to deed restrictions on the grounds that the restrictions are not applicable to all property in the subdivision. §201.011. Since 1995, with the enactment of Chapter 204, homeowners in Harris County are now at risk of new deed restrictions to which they did not consent. Combined with Chapter 201.011, this means a homeowner in Harris County could be subject to a deed restriction to which he/she does not consent and that applies *only to his/her property*.

18. §202.003.

19. Sec. 209.008(f) contains some limitations for attorneys fees, but only if the HOA conducts a nonjudicial foreclosure. I do not know today whether any HOA in Texas has conducted a nonjudicial foreclosure. The limitation has no teeth since it does not apply if the HOA conducts a judicial foreclosure. Further, even if the HOA conducts a nonjudicial foreclosure, 209.008(g) takes away the limitation by providing:

> Subsection (f) does not prevent a property owners' association from recovering or collecting attorney's fees in excess of the amounts prescribed by Subsection (f) by other means provided by law.

In other words, the HOA can still recover attorneys' fees in any manner it could before enactment of the statute. Since HOAs were permitted before enactment of Chapter 209 to recover their attorneys fees in a foreclosure action, this purported limitation on attorneys fees should have no real world effect.

20. Before enactment of Property Code Chapter 204 in 1995, a deed restriction could not arise without the consent of the home owner. In 1985, Property Code Chapter 201 changed this by requiring the homeowner to take steps to exclude the home from new, extended, added, or modified deed restrictions. In 1995, Property Code Chapter 204 radically changed the long-standing principle of required agreement by permitting creation of an HOA, imposition of mandatory assessments, and subsequent deed restrictions on nonconsenting homeowners, and it applies *ONLY TO HARRIS COUNTY*.

If a subdivision does not have an HOA and requires 60% or even 100% owner approval to change the deed restrictions, Chapter 204 overrides that intent and agreement. Chapter 204 allows 60% of the owners to create an HOA with mandatory membership and assessments (regular or special). (204.006) In other words, 60% of the owners can force 40% of the owners to suddenly

have a legal obligation to pay assessments. A decades-long homeowner can lose his or her home for failure to pay assessments that he or she never agreed to pay.

21. Under Chapter 204, 60% of the homeowners could create an HOA and adopt new deed restrictions without the knowledge of the other 40%. Section 204.008 permits several alternate methods of adoption of a petition. Only one of those methods requires notice to all homeowners -- §204.008(2)(a meeting of members). Adoption of a petition without notice to all homeowners could occur written ballots (204.008(1)) or door-to-door circulation. 204.008(3).

Section 201.008 requires notice of a petition to change deed restrictions only within 60 days *AFTER* the petition is filed in the county clerk's office. However, whether this requirement applies to an HOA is uncertain, and even if it does apply, the deed restrictions could be passed before all owners receive notice -- even before the petition is filed.

22. Chapter 209 appears to protect homeowners by requiring that the HOA provide notice and an informal hearing before taking action. However, this notice requirement DOES NOT offer any real world protection. The website www.HOAdata.org lists more than 15,000 Houston-area foreclosure-related filings from 1985 to 2001 and refers to an additional 4,000 HOA injunction cases. None of these cases would have been subject to the notice and informal hearing requirements (or at least, each case could have avoided the requirement) because the statute does not apply to a request for foreclosure or a request for a temporary restraining order or temporary injunction. 209.007(d). Thus, An HOA can avoid these "protections" by following the same course that HOAs followed before Chapter 209.

23. § 204.010. Owners therefore unwittingly grant powers to the HOA without knowing they have done so. Among the powers that Chapter gives to an HOA unless expressly excluded are:

1 Deciding whether to have and hire a managing agent (or others employees);
2 Contracting and incurring liabilities relating to the subdivision or the HOA;
3 Imposing interest, late charges, and returned check charges for assessments, collecting attorneys' fees and reasonable costs for violations of deed restrictions, bylaws, or other rules, charging and collecting costs, and adopting and amending rules for delinquent assessments and application of payments;
4 Deciding whether to purchase insurance and fidelity bonds, including D&O liability insurance; and
5 indemnify a director or officer named in a lawsuit because the person is or was a director.

24. One case is before the Texas Court of Appeals on this very point. The retroactive effect of these inherent powers changes the basic assumptions of longtime residents about the powers they have or have not surrendered to their HOA.

25. Chapter 209 appears to grant both the HOA and the homeowner an absolute right to demand mediation. However, this "protection" has little if any real world effect. The website www.HOAdata.org lists more than 15,000 Houston-area foreclosure-related filings from 1985 to

2001 and refers to an additional 4,000 HOA injunction cases. **None of these cases would have been subject to the mediation "right."**

The second sentence of Section 209.007(d) provides:

> If a suit is filed relating to a matter to which those sections [209.006 and 209.007] apply, a party to the suit may file a motion to compel mediation.

Thus, when this right of mediation applies, then either party, the HOA or the homeowner, can require mediation.

However, this mediation provision concerns only suits to which 209.007 and 209.006 apply. THOSE SECTIONS DO NOT APPLY TO AN HOA SUIT THAT:

1. seeks a TRO or temporary injunction (209.007d)
2. seeks foreclosure (209.006 and 209.007d)
3. concerns a temporary suspension of a right to use common areas if the suspension:
   - is the result of a violation that occurred in a common area and
   - involved a significant and immediate risk of harm to others in the subdivision (209.007d)
4. seeks to collect a regular or special assessment (209.006)
5. charges an owner for property damage (209.006)
6. concerns a fine for a violation of the restrictions, bylaws, or rules of the HOA

So, subject to the above carve outs, the Chapter 209 right to demand mediation applies to:

1 cases concerning suspension of an owner's right to use a common area (209.006) (See carve out 3 above.)

2 cases by an HOA against an owner. (only what is left after the carve outs)

I am not aware of any actual HOA case to which this right of mediation would apply.

26. Section 209.005(b)(3).

Considering the widely publicized debates concerning executive privilege involving President Nixon, President Clinton, and now Vice-President Cheney, Chapter 209 (Section 209.005(b)(3)) introduces a most remarkable and sweeping change in the law. State and federal law does recognize certain privileges from production in legal proceedings, but those privileges are usually carefully thought out and balanced. Tossing aside hundreds of court decisions balancing (1) the need for production of attorney's files and records in a legal proceeding with (2) the interest of free communications between a lawyer and client, Chapter 209 provides simply and absolutely:

> An attorney's files and records relating to the association [an HOA], excluding invoices requested by an owner under Section 209.008(d), are not: ... (3) subject to production in a legal proceeding.

Chapter 209 does not limit this prohibition to any type of suit. Because the section is new and untested, we cannot predict how the courts will interpret the section. (Perhaps, and hopefully, the

courts will read an implied limitation into the section so that it applies only to lawsuits between an association and an owner. Until we have such a decision, we can only address the language of the statute.)

Texas law is similar to the law of most other states and to federal law on the issue of what is subject to production in a legal proceeding. The courts and legislatures have spent decades balancing many important and competing values and principles. Issues such as relevance, materiality, and burden govern the initial inquiry, but if these considerations suggest that a court should compel production of documents, the court must also consider (if raised) issues of "privilege."

The law grants privilege to certain communications -- a privilege to withhold from production -- when the Legislature or courts determine that some principle or value outweighs the need for full disclosure in the courts to achieve justice. We want justice in our courts, but that is not always the most important value or principle.

Before Chapter 209, communications between a client and lawyer were privileged only according to the following conditions:

1. The communication must be intended to be confidential.
2. The communication must be made for the purpose of facilitating the rendition of professional legal services to the client.
3. The communication must be between the client or its representative and his lawyer or his lawyer's representative, or between his lawyer and the lawyer's representative; or by him or his representative or his lawyer or a representative of a lawyer to a lawyer, or a representative of a lawyer representing another party in a pending action and concerning a matter of common interest therein; or between representatives of the client or between the client and representative of the client; or among lawyers and their representative representing the same client.
4. The communication is not privileged if in furtherance of crime or fraud.
5. The communication is not privileged if relevant to an issue between parties who claim through the same deceased client.
6. The communication is not privileged if relevant to any issue of breach of duty by the lawyer to his client or by the client to his lawyer.
7. The communication is not privileged if relevant to an issue concerning an attested document to which the lawyer is an attesting witness.
8. The communication is not privileged if relevant to a matter of common interest between or among two or more clients if the communication was made by any of them to a lawyer retained or

> consulted in common when offered in an action between or among any of the clients.

Also under Texas law, an attorneys "work product" is exempt from discovery, except that some work product is discoverable upon a showing of substantial need. (192.5(b)(2)) (Generally, "work product" refers to attorney material prepared or mental impressions developed in anticipation of litigation or for trial and to communications and in anticipation of litigation (before trial) between an ultimate party to the litigation and the party's representatives. TRCP 192.5 (a).) These carefully crafted rules concerning attorney records and files in all other matters must now be contrasted with the blanket, absolute protection granted to the files and records of an HOA attorney.

27. Under the general Texas law regarding lawyer/client relations, a client owns the files relating to his/her cases and matters, and the attorney must deliver the files (or a copy) to the client (or its designee, such as substitute counsel) upon demand. New §209.005(b)(1) creates an apparent conflict with this general law by declaring that "An attorney's files and records relating to the association, excluding invoices requested by an owner under Section 209.008(d), are not: (1) records of the association."

28. Section 204.005(a) contains a very sweeping exception for actions by HOAs to extend, add, or modify deed restrictions that did not exist before 1995:

> A property owners' association is not required to comply with Sections 201.009—201.012.

This sentence is puzzling because Sections 201.009—201.012 do not appear to state requirements for compliance by an HOA or by anyone. Until a court addresses this sentence, we cannot know how it will be interpreted.

It is possible that this sentence is meaningless because Sections 201.009—201.012 do not state requirements for compliance by an HOA or by anyone.

It is also possible that a court will -- after a struggle -- find some meaning in the sentence. No court is likely to read the sentence as meaningless. The following results are possible. Again, I caution that until a court rules on these issues, we do not know what will happen, but the following are at least possible under the language of §204.005(a).

1. Deed restrictions extended, added, or modified by action of an HOA are binding on all members of the subdivision, even those who actively seek to be excluded or who did not receive notice of the proposed restrictions. (§ 201.009(b))
2. Deed restrictions extended, added, or modified by action of an HOA may bind property exclusively dedicated for use by the public or for use by utilities. (§ 201.009(b)(1))
3. Deed restrictions extended, added, or modified by action of an HOA may bind property owned by a minor or incompetent without meeting any required safeguards. (§

201.009(b)(5). Note, this could also happen under Chapter 201, but only if certain safeguards were met.)

4. Deed restrictions extended, added, or modified by action of an HOA may bind a prior lienholder without its consent. (§ 201.009(d)) However, any new deed restriction relating to assessments (an extension, addition, or modification) is subordinate to purchase money or home improvement liens, but the lienholder is not entitled to notice of such subordinate restrictions. (§204.007)
5. The regularity of procedures to extend, add, or modify deed restrictions by action of an HOA (Did they follow the statute or their own bylaws and rules?) may NOT be challenged in court by a homeowner. (I would be amazed if this is the case, but it follows quite clearly from application of §204.005(a) to §§204.009(a) and 204.010.)

29. §202.003 provides: "A restrictive covenant shall be liberally construed to give effect to its purpose and intent."

30. Chapter 206 was intended for one subdivision. Other Chapters have been drafted for just Houston and Harris County.