

**BEFORE THE
COMMISSION ON COMMON OWNERSHIP COMMUNITIES
FOR MONTGOMERY COUNTY, MARYLAND**

SANDRA TALLEY)	
)	
Complainant)	
)	
v.)	Case No. 2019-029
)	
NEW MARK COMMON HOMES ASSOCIATION, INC.)	
)	
Respondent)	

DECISION AND ORDER

The above-captioned case came before a hearing panel of the Commission on Common Ownership Communities for Montgomery County, Maryland on May 23 and May 28, 2019 pursuant to Mont. Cnty. Code Ch. 10B. Upon consideration of the testimony and documentary evidence presented at the hearing and argument by and on behalf of the parties, the Panel finds, concludes and orders as follows.

Background

The governing documents of Respondent New Mark Common Homes Association, Inc. (the "Association") provide a number of methods for increasing HOA fees ¹ against unit owners for the operation, upkeep, and improvement of the Association's facilities. One method allows the Association's Board of Directors ("Board") to increase annual HOA fees proportional to increases in the tax assessments of the units within the Association (the "tax method") and a second method allows the Board to increase HOA fees proportional to increases in the consumer price index ("CPI method"). Neither method requires a vote of the general membership.

In addition, by vote of two-thirds of the entire membership, annual HOA fees may be increased beyond the limits allowed by the tax method and the CPI method. The

¹ The Association's governing documents refer to annual and special "assessments." We will use the term "HOA fees" here to avoid confusion with the similar term, "tax assessments."

entire membership may, also by a two-thirds vote, impose a one-time special HOA fee for various purposes. Largely because of the difficulty in mustering a two-thirds vote of the membership, Respondent has historically increased HOA fees by Board action alone – mostly under the CPI method, but on a few occasions using the tax method as well.

For fiscal years 2017, 2018 and 2019, the Board increased HOA fees using the tax method. In particular, the HOA fee for 2019 was 50% greater than the HOA fee for 2018. Complainant Sandra Talley (“Ms. Talley”) challenges the Board’s authority to use the tax method to increase HOA fees after having used the CPI method for many years. She also argues that when using the tax method, the Board is limited to the percentage increase in real estate tax assessments for the preceding year only. Finally, she argues that since the increased HOA fees are being used for what she characterizes as capital improvements, a two-thirds vote of the entire membership was required.

Prior to the hearing, the Association filed a motion to dismiss Ms. Talley’s complaint, which Ms. Talley opposed. The Panel reserved decision on the motion until after the hearing. In light of the Panel’s ruling on the merits, the Panel will deny the motion as moot.

Findings of Fact

1. The Association is a homeowners association as defined in the Maryland Homeowners Association Act, Md. Code Ann., Real Prop. § 11B-101, *et seq.*, and it is a common ownership community as defined in Mont. Cnty. Code § 10B-2(b).
2. The Association consists of 394 residential units in the City of Rockville, Maryland. About half the units are townhouses and the remainder are detached houses.
3. Ms. Talley owns and resides in a unit within the Association. She and her unit are therefore subject to the Association’s governing documents.
4. Among the Association’s governing documents are its Declaration of Covenants and Restrictions (“Declaration”) and Bylaws. CE-1 at 67, 207.² The Declaration is recorded in the Montgomery County land records and copies of both the Declaration and Bylaws, among other documents, are on deposit with the Circuit Court for Montgomery County in Case No. 222X.

² “CE-1” refers to Commission Exhibit 1 – the entire administrative record in this case – which was admitted in evidence without objection. Ms. Talley’s exhibit is referred to as “Cmplt. Ex. ___” and the Association’s exhibits are referred to as “Rspt. Ex. ___.”

5. Article III of the Bylaws provides as follows:

Section 2. Assessments. The rights of the membership are subject in all respects to the payment of initial, annual and special assessments [i.e., HOA fees] levied by the Association, the obligation of which assessments is imposed upon each Class A member and becomes a lien upon the Living Unit against which such assessments are made as more fully provided in Article VI of the Declaration . . . ^[3]

6. Article V of the Bylaws provides as follows:

Section 3. Duty to Fix Assessments. As more fully set out in the Declaration of Covenants and Restrictions, it shall be the duty of the Board of Directors of this Corporation: (a) To fix the amount of the assessment against each Living Unit for each assessment period at least thirty (30) days prior to the beginning of such period . . .

7. Article VI, Section 5, of the Declaration provides as follows:

(a) From and after January 1, 1968, the maximum annual assessment for any Class A Membership *may be increased* by the Board of Directors of the Association, without a vote of the membership, by the percentage of increase, if any, of the Total Assessment for land and improvements for any Living Unit to which such membership is appurtenant. [Emphasis added.]

(b) From and after January 1, 1968, in any event, the maximum annual assessment and the maximum initial assessment for all Class A Memberships *shall be increased* by the Board of Directors of the Association, without a vote of the membership by the percentage increase, if any of the United States Department of Labor Cost of Living Index for the Washington, D. C. Metropolitan Area *during the preceding year*, provided, however, that the maximum assessments shall not be decreased by any decrease in the aforementioned index. *The increases provided for in sub-paragraphs (a) and (b) of this Article are intended to be cumulative.* [Emphasis added.]

(c) From and after January 1, 1968, the maximum annual assessment and the maximum initial assessment for all Class A Memberships may be increased above that established by the two preceding paragraphs by a vote

³ Class A members are unit owners other than the original developer.

of members, as hereinafter provided, for the next succeeding year and at the end of such year for each succeeding year. Any change made pursuant to this paragraph shall have the assent of two-thirds (2/3) of the then members of the Association. A meeting of the members shall be duly called for this purpose, written notice of which shall be sent to all members at least thirty (30) days in advance of such meeting, which notice shall set forth the purpose of such meeting.

8. Article VI, Section 6, of the Declaration, provides as follows:

In addition to the annual assessments authorized by this Article, the Association may levy in any assessment year a special assessment, applicable to that year only, for the purpose of defraying in whole or in part, the cost of any *construction or reconstruction, unexpected repair or replacement of a described capital improvement* located upon the Common Areas, including the necessary fixtures and personal property related thereto, provided that any such assessment shall have the assent of two-thirds (2/3) of the then members of the Association. A meeting of the members shall be duly called for this purpose, written notice of which shall be sent to all members at least thirty (30) days in advance of such meeting, which notice shall set forth the purpose of such meeting. [Emphasis added.]

9. Until 2017, the Board used the CPI method almost exclusively to increase HOA fees. The two exceptions are calendar years 1987 and 2011, when the Board used the tax method. Rspt. Ex. 2 at 6; Rspt. Ex. 3.

10. The use of the tax method for 1987 was supported by a legal opinion dated December 16, 1986. CE-1 at 166; Rspt. Ex. 2. That opinion addressed the question whether, when using the tax method, the increase in the tax assessment is measured from January 1, 1968, or instead is measured only from the immediately preceding year. The opinion writer concluded that “the Board may vote to increase the maximum annual assessment [HOA fee] under Section 5(a) [of Article VI of the Declaration] based upon a cumulative percentage of increase in Total Assessment for the land and improvements,” *i.e.* from January 1, 1968.

11. For calendar years 2017 and 2018, the Board again used the tax method to increase annual HOA fees. *See, e.g.*, minutes of April 6, 2017 Board meeting, CE-1 at 349.

12. In 2017, the Association commissioned a reserve study, included in the record at 91 of CE-1. The study’s authors concluded that reserves were only about 39% of what

was needed for full funding, and they recommended substantial increases in HOA fees over a multi-year period to achieve full funding.

13. In addition to underfunded reserves, the Association also suffered an operating deficit for 2016 as a result among other things of tree work, snow removal, defense of three lawsuits by a unit owner, and a recommended salary increase for the Association's employee-administrator. The Board concluded that "relying on the CPI alone is insufficient." Rspt. Ex. 3. The Board proposed a 16% increase in annual HOA fees for 2017, relying on the tax method described in Article VI, Section 5(a), of the Declaration.

14. By notice to unit owners dated April 17, 2018 (CE-1 at 222), the Association's president invited unit owners to a special town hall meeting scheduled for May 6. The purpose of the meeting was to "discuss[] how to address several major capital replacement projects facing" the Association. The notice identified the following projects:

Drainage and erosion corrections	\$ 920,000
Asphalt & concrete	500,000
876 NME retaining wall	100,000
100 block NME retaining wall	<u>250,000</u>
Grand total	\$1,770,000

15. In late 2017, the Association switched from being self-managed to hiring an outside property manager. The outside manager's charges were greater than the compensation previously being paid the Association's employee-administrator.

16. In 2018 the Association suffered a substantial increase in insurance costs as a result of its then current insurer's refusal to renew coverage following multiple lawsuits by a unit owner. CE-1 at 81.

17. The minutes of the Board's August 2, 2018 meeting reflect several failed votes for a substantial increase in dues, followed by a vote in favor of applying for a \$750,000 line of credit. CE-1 at 147.

18. On October 3, 2018, the Board held an informal budget work session. According to informal notes of the meeting, various budget issues facing the Association were discussed, but no formal action was taken. CE-1 at 81.

19. On October 4, 2018, the Board formally proposed a 2019 budget calling for a 50% increase in annual HOA fees. Notice of the proposed budget was thereafter sent to

unit owners. CE-1 at 16; CE-1 at 225. The notice cited Article VI, Section 5(a) – the tax method -- as authority for the Board’s action. The notice stated that the Board plans to approve the budget at its November meeting.

20. Ms. Talley expressed her opposition to the 50% increase by telephone call and several emails, specifically challenging the Board’s interpretation of Section 5(a).

21. At an open meeting held on November 1, 2018, the Board unanimously approved the proposed budget. CE-1 at 85. The minutes of that meeting cite Section 5(a) of the Declaration as authority for the HOA fee increase.

22. At the hearing before the Panel, an Association witness described how the 2019 HOA fee increase was calculated. According to his testimony, he researched the tax assessments for a sample of some 42 units within the Association as of 1968 as compared with the current tax assessments. That yielded an increase well over 1000%. Similarly, he researched the annual HOA fees of those same units from the time they were first sold by the developer to the present. He determined that the budgeted HOA fee increases for 2019 are well below the maximum permitted by the tax method. *See* Cmplt. Ex. 1.

23. Ms. Talley conceded at the hearing that her complaint does not challenge the Board’s computations of the 2019 HOA fee increases, assuming (without conceding) that the Board correctly used and interpreted Section 5(a). Accordingly, and relying on that same assumption, the Panel finds that the Board’s computations of the 2019 HOA fee increases are consistent with Section 5(a).

Conclusions of Law and Analysis

A homeowner association’s governing documents are subject to the same rules of interpretation as contracts generally. If the provisions of a governing document, when viewed within the four corners of the document, are clear and unambiguous, then a court, or in this case the Panel, must apply the provisions without resort to extrinsic evidence. *See Markey v. Wolf*, 92 Md. App. 137, 150-158 (1992) and cases cited therein.

The Panel concludes that the Declaration provisions at issue, though perhaps not a model of draftsmanship, are sufficiently clear to require application according to their plain meaning. Section 5(b) requires that “from and after January 1, 1968” annual HOA fees shall be increased in proportion to the CPI increase “during the preceding year.” Section 5(a), in contrast, permits proportional increases “from and after January 1, 1968”

based the increase in tax assessments, without being limited to “the preceding year.” It follows that the base for computing the percentage increase in tax assessments is January 1, 1968, not the tax assessment for the preceding year.⁴

Ms. Talley argues that, having used the CPI method more or less consistently for some 50 years, the Board should not now be permitted to change its methodology. But nothing in the Declaration prohibits the Board from doing so. Both methods are available to the Board when and as needed. In times of low inflation coupled with an aging and deteriorating infrastructure, the CPI method may well prove insufficient and resort to the tax method may be necessary. That seems to be what happened here.

As a variation of that argument, Ms. Talley suggests that the Board cannot use *both* the CPI method and the tax method simultaneously. But the Board has not done that. In the Panel’s view, the Board is free, in its discretion and in the exercise of its fiduciary duties, to use the methodology that permits the larger assessment increase. By choosing the tax method for 2019, the Board is not simultaneously using the CPI method.

It should also be pointed out that the CPI method under Section 5(b) is mandatory, in that it uses the term “shall.” Thus, if the Board were precluded from using the tax method under 5(a) for any year that it used the CPI method, the Board could never use the tax method.

Ms. Talley also argues that since the Board itself characterized the projects being funded by the increased HOA fees as “capital” improvements, those projects could only be funded by a special assessment under Declaration Article VI, Section 6. That section requires a two-thirds vote of the entire membership.

It could be argued that the projects are more akin to repairs and replacements. *See Lee v. University Towers Condo.*, CCOC No. 52-08 (Apr. 7, 2009) (concluding that replacement and upgrading of a leaking water supply system was properly categorized as “maintenance,” “repair,” or “replacement,” not as an “addition,” “alteration,” or “improvement”). But the Panel need not resolve that issue here. Even if the projects are capital improvements, nothing in the Declaration bars the Board from using annual HOA fees for that purpose.

⁴ The Declaration says that increases under 5(a) and 5(b) “are intended to be cumulative.” That statement is not helpful in resolving the issues presented because it applies to both the tax method and the CPI method. The Panel interprets the statement to mean that the base for computing future percentage increases in HOA fees includes accumulated fee increases.

A conclusion that Section 5(a) is ambiguous would not change the result, since, under the business judgment rule, a corporate body's interpretation of its own ambiguous governing document is entitled to deference.

In general, and subject to limited exceptions, the courts will not interfere with the internal affairs of a corporation. *Black v. Fox Hills North Community Ass'n, Inc.*, 90 Md. App. 75, 81 (1992). Further, "there is a presumption that directors of a corporation acted in good faith and in the best interest of the corporation." *Reiner v. Ehrlich*, 212 Md. App. 142, 153 (2013). Once a corporate body's decision ostensibly falls within the protection of this business judgment rule, a party attacking the decision must show that the decision was not made in good faith, or that it was the product of fraud or arbitrariness. The rule is fully applicable to community associations. *Black v. Fox Hills; Reiner v. Ehrlich*.

The Commission is bound by the business judgment rule. In general, a hearing panel of the Commission "must apply state and County laws and all relevant caselaw to the facts of the dispute" before it. Mont. Cnty. Code § 10B-13(e). More particularly, the Code excludes from the definition of "dispute" over which the Commission has jurisdiction "any disagreement that only involves . . . the exercise of a governing body's judgment or discretion in taking or deciding not to take any legally authorized action." Section 10B-8(5).

The business judgment rule arises, among other circumstances, when a corporate board is called on to decide a matter in the face of ambiguous governing documents. *Tackney v. United States Naval Academy Alumni Ass'n*, 408 Md. 700, 718 (2009) ("Because the Association's Bylaws are ambiguous as to . . . [the issue presented in that case], we cannot say that the Board acted in a manner sufficiently arbitrary to invoke intervention by a Maryland court"). Furthermore, a board's interpretation of its own documents will be upheld by the courts if the interpretation is reasonable. *NAACP v. Golding*, 342 Md. 663, 681 (1996) ("The disputed language in . . . [the NAACP's constitution] is ambiguous To resolve this ambiguity, the NAACP consulted legal counsel, and adopted an interpretation that was consistent with past practice. . . . The organization's interpretation was not arbitrary, and therefore is entitled to deference").

The Panel concludes that the Board's interpretation of its authority under Section 5(a), supported by a legal opinion and past practice, was reasonable and not sufficiently arbitrary to invoke the intervention of the Commission.

Order

For the foregoing reasons it is, this 17th day of June, 2019, ORDERED as follows:

1. The complaint and all claims therein are DISMISSED WITH PREJUDICE.
2. The Association's motion to dismiss is DENIED as moot.

Panel members Marietta Ethier and David Gardner concur in this Decision and Order.

/s/ Charles H. Fleischer
Charles H. Fleischer, Panel Chair

NOTICE TO PARTIES

The parties are hereby notified that, pursuant to Mont. Cnty. Code § 10B-13(j), failure to comply with this Decision and Order is a Class A violation. As set forth in Mont. Cnty. Code § 1-19, a Class A violation is punishable by a civil fine of up to \$500.00 per day until there is compliance with this Decision and Order.

In addition to imposition of a \$500.00 civil fine, the Commission may also refer the matter to the Office of the County Attorney in accordance with Mont. Cnty. Code § 10B-13(i) for appropriate legal action.

In the event of noncompliance with any order by the deadline set forth in this Decision and Order, the party in whose favor the order has been issued may request enforcement of the order by submitting a Complaint for Enforcement with the Department of Housing and Community Affairs, using the form available at:

www.montgomerycountymd.gov/ccoc

or

<https://www3.montgomerycountymd.gov/311/SolutionView.aspx?SolutionId=1-Y3KNW>

Any party aggrieved by the action of the Commission may file an appeal to the Circuit Court for Montgomery County, Maryland, within thirty (30) days from the date of

this Decision and Order pursuant to the Maryland Rules of Procedure governing administrative appeals.