

# FORGET THE PINK FLAMINGOS: THE MISHANDLING OF COMMON-INTEREST- COMMUNITY CONFLICTS

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## FORGET THE PINK FLAMINGOS: THE MISHANDLING OF COMMON-INTEREST- COMMUNITY CONFLICTS

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*Tens of millions of Americans can only enjoy their homes subject to the regulations of a common-interest community: condominium, homeowners association, or cooperative. These regulations impact not only homeowners' daily lives but also the worth of their most valuable asset. Yet, the judicial approach toward these regulations has garnered limited scholarly attention. This Article ferrets out the law's current state, finds it normatively lacking, and proposes a better approach.*

*Over the last three decades, courts' review of common-interest-community regulations has grown exceptionally deferential. Most courts no longer insist on review for reasonableness as treatises assume. Instead, courts imported the business judgment rule from corporate law. Under this standard, courts refrain from assessing a regulation's substance and merely ensure that the regulation was promulgated through proper procedures.*

*Unfortunately, this shift is grounded in a misunderstanding of the business judgment rule's doctrinal function in corporate law and in a concomitant failure to appreciate common-interest communities' unique internal dynamics. Corporate law only employs the business judgment rule when a corporate board is disinterested. But the common-interest community and its board are rife with potential conflicts of interest between different owner groups. In these circumstances, corporate law would never mechanically apply the rule because the expanded discretion it affords those controlling decision-making processes would allow them to promote their individual or group interests at others' expense.*

*Accordingly, this Article proposes to replace courts' current approach to common-interest communities' regulations with a two-tiered review system. Where no conflicts of interest exist, the business judgment rule is appropriate. But for cases characterized by structural conflicts of interest between different owner groups in the community, a higher standard, which entails meaningful review of regulations for reasonableness, is necessary. Through an investigation of the economic dynamics within common-interest communities, this Article catalogues the classes of regulations warranting concern and identifies the factors courts should consider when analyzing them under the reasonableness standard.*

### INTRODUCTION

Is the decision whether to repair a house's foundation as trivial as the decision whether to repaint the house in a different color? Is the calibration of savings levels for house-related emergencies as simple as pondering the costs and benefits of installing grills in the patio? Most would probably intuitively realize that some decisions respecting a property are of greater importance—

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i.e., they have further repercussions and are more liable to implicate conflicting interests—than others. Thus, such decisions merit increased consideration. Yet, in one exceptionally consequential context affecting the living conditions of more than a quarter of Americans,<sup>1</sup> property law reckons otherwise. When analyzing the decisions of common-interest communities, current law insists on applying to all decisions the same standard of judicial review.<sup>2</sup> Whether a common-interest community's decision deals with paint color or with structural foundations, with grills or with rainy day funds, courts believe it always merits identical, and deferential, analysis. That judicial attitude defies intuition. It also runs counter to core normative principles. As this Article argues, it mistakes intracommunity conflicts of interest—that inevitably materialize around, for example, decisions about costly structural renovations or about savings levels—for mere conflicts of tastes, like those associated with questions about preferred paint colors or about grills' desirability.

Common-interest communities (mostly, homeowners associations and condominiums<sup>3</sup>), whose numbers have exploded over the past fifty years,<sup>4</sup> mix private ownership with communal control.<sup>5</sup> Residents own their individual units, but they are also members of a homeowners association or condominium that manages common spaces.<sup>6</sup> Additionally, the association or condominium issues rules governing owners' use and transfer of their units.<sup>7</sup> The long-established property-law tool on which common-interest communities rely to exercise such powers is the covenant: a right over another's land.<sup>8</sup> Covenants creating the common-interest community authorize it to adopt decisions affecting individual owners' rights in the common spaces and in their own units.<sup>9</sup> When early common-interest communities first employed this power, courts ruled that those decisions are subject to some form of judicial review.<sup>10</sup>

Courts mostly refrained from considering how different types of decisions might necessitate differing levels of such review.<sup>11</sup> Instead, they formulated one

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1. *See infra* note 4.

2. *See infra* Subpart I.D.

3. Cooperatives are the third common-interest-community type. Outside of New York City, however, cooperatives have a very minor presence. Michael H. Schill et al., *The Condominium Versus Cooperative Puzzle: An Empirical Analysis of Housing in New York City*, 36 J. LEGAL STUD. 275, 280 (2007).

4. In 2020, 74.1 million Americans lived in common-interest communities. In 1970, the first year for which data was collected, only 2.1 million lived in such settings. *See* FOUND. FOR CMTY. ASS'N RSCH., 2020–2021 U.S. NATIONAL AND STATE STATISTICAL REVIEW, [https://foundation.caionline.org/wp-content/uploads/2021/07/2021StatsReview\\_Web.pdf](https://foundation.caionline.org/wp-content/uploads/2021/07/2021StatsReview_Web.pdf) (last visited Feb. 11, 2023).

5. RESTATEMENT (THIRD) OF PROP.: SERVIDITUDES § 6.2 (AM. L. INST. 2000).

6. JOSEPH WILLIAM SINGER, PROPERTY § 8.5.1, at 372 (5th ed. 2017).

7. *Id.*

8. *See infra* notes 119–123 and accompanying text.

9. SINGER, *supra* note 6, § 8.5.1, at 380.

10. *See infra* Subpart I.C.

11. California is an exception, but the type of disputes its courts subject to heightened scrutiny is of very limited import. In disputes affecting owners' security against criminal conduct in the common spaces,

standard of review patterned in response to the one type of decision that has dominated thinking about common-interest communities. As commonly perceived in the media and much of the legal literature, the typical common-interest-community decision involves an aesthetic rule, or some other intrusive lifestyle regulation, imposed by the community on the individual property owner.<sup>12</sup> News stories depict an owner spending more than a million dollars in litigation costs to keep his flowerpots after the homeowners association banned them;<sup>13</sup> a TV commercial ridicules an association president who saws off a resident's nonconforming mailbox;<sup>14</sup> one property casebook draws students' attention to the case of a homeowners association suing to force an owner to tidy up his bedroom;<sup>15</sup> and almost all property casebooks excerpt as their leading case a ruling regarding a condominium's pet regulation.<sup>16</sup>

For the parties involved, these disputes tend to inevitably elicit strong feelings.<sup>17</sup> For observers, they provide an exaggerated, and exceptionally amusing, illustration of dynamics they already link with America's fastest growing home-ownership form.<sup>18</sup> For legal commentators, they raise interesting philosophical questions, as such regulations constitute drastic impositions on individual freedom<sup>19</sup>—a value closely associated with ownership.<sup>20</sup> The salience of these disputes in discussions about common-interest-community decision-making is, therefore, hardly surprising.

When courts consider challenges to common-interest-community decisions of this salient type, traditional property concepts nudge them toward a permissive standard of review. Aesthetic and lifestyle disputes call for highly deferential judicial review mainly for two reasons: subjectivity and mutuality.

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the community is treated as a landlord. *Lamden v. La Jolla Shores Clubdominium Homeowners Ass'n*, 980 P.2d 940, 951–52 (Cal. 1999). In all other disputes, the standard of review is lessened. *See id.*

12. *E.g.*, UNIF. COMMON INT. OWNERSHIP ACT prefatory note to 2008 amendments (UNIF. L. COMM'N 2014) (indicating in a prefatory note that amendments are suggested given growing media and professional focus on boards' interferences with owners' daily lives); Paula A. Franzese, *Common Interest Communities: Standards of Review and Review of Standards*, 3 WASH. U. J.L. & POL'Y 663, 663–65 (2000) (mentioning such cases as generating the greatest public and legal concerns).

13. Jim Carlton, *The \$1 Million HOA Blowup: It Started with the Misplaced Flower Pots*, WALL ST. J. (Mar. 19, 2019, 10:43 AM), <https://www.wsj.com/articles/the-1-million-hoa-blowup-it-started-with-the-misplaced-flower-pots-11553006590>.

14. *See, e.g.*, Geico, *HOA Cynthia Advises New Neighbors*, ISPOT.TV (May 30, 2020), <https://www.ispot.tv/ad/nBpP/geico-involved-hoa>.

15. *See* Fountain Valley Chateau Blanc Homeowner's Ass'n v. Dep't of Veterans Affs., 79 Cal. Rptr. 2d 248, 250 (Ct. App. 1998), *discussed in* JOSEPH WILLIAM SINGER ET AL., PROPERTY LAW 615 (7th ed. 2017).

16. *See* Nahrstedt v. Lakeside Vill. Condo. Ass'n, 878 P.2d 1275 (Cal. 1994), *discussed in, e.g.*, JESSE DUKEMINIER ET AL., PROPERTY 876–86 (9th ed. 2018).

17. *Levandusky v. One Fifth Ave. Apartment Corp.*, 553 N.E.2d 1317, 1322 (N.Y. 1990) (“As this case exemplifies, board decisions concerning what residents may or may not do with their living space may be highly charged and emotional.”).

18. *See, e.g.*, OVER THE HEDGE (DreamWorks Animation 2006).

19. *E.g.*, Uriel Reichman, *Residential Private Governments: An Introductory Survey*, 43 U. CHI. L. REV. 253, 269–75 (1976) (detailing the ways in which private communities curtail traditional property rights).

20. Nadav Shoked, *The Duty to Maintain*, 64 DUKE L.J. 437, 448–53 (2014).

First, property law normally perceives aesthetic issues as subjective and thus unamenable to principled judicial decision-making.<sup>21</sup> This attitude manifests in property law's traditional refusal, for example, to recognize aesthetic nuisances or implied easements for light and air.<sup>22</sup> Although markets probably price aesthetic elements, when a common-interest community bans, for example, lawn ornaments, courts feel that they can call upon no clear, neutral criteria to determine whether the ban would indeed promulgate a more pleasing environment.<sup>23</sup>

Second, courts discount the need for protecting owners against common-interest communities' aesthetic or lifestyle regulations because these regulations involve an "average reciprocity of advantage," a concept drawn from regulatory takings law.<sup>24</sup> Overall and over time, a common-interest community's aesthetic or lifestyle regulation burdens and benefits all community owners to roughly the same extent.<sup>25</sup> The complaining owner is upset about a lifestyle or aesthetic regulation's effects on her, but she benefits from that regulation's same effects on other owners.<sup>26</sup> John is unhappy today that his common-interest community banned him from placing a beloved pink flamingo on his lawn; tomorrow, that same regulation saves him from his neighbor Jane's hideous garden gnomes.<sup>27</sup>

These two characteristics associated with aesthetic and lifestyle decisions—subjectivity and mutuality—have motivated courts to expand the latitude they afford common-interest-community decision-making.<sup>28</sup> The original standard of judicial review for community decisions, which casebooks and treatises still cite as reigning,<sup>29</sup> is reasonableness. However, most courts have shifted, often with limited acknowledgement, to a different standard, borrowed from corporate law: the business judgment rule.<sup>30</sup> This standard, unlike reasonableness, does not require courts to assess a contested decision's merits.<sup>31</sup>

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21. *Ness v. Albert*, 665 S.W.2d 1, 2 (Mo. Ct. App. 1983) ("Aesthetic considerations are fraught with subjectivity.").

22. *E.g.*, *Fontainebleau Hotel Corp. v. Forty-Five Twenty-Five, Inc.*, 114 So. 2d 357, 359 (Fla. Dist. Ct. App. 1959).

23. *E.g.*, *Beach Forest Subdivision Ass'n v. Omran*, No. 326976, 2016 WL 6495742, at \*2 (Mich. Ct. App. Nov. 1, 2016) (prohibiting "lawn ornaments, sculptures or statues").

24. *Pa. Coal Co. v. Mahon*, 260 U.S. 393, 415 (1922).

25. *See generally* *Levandusky v. One Fifth Ave. Apartment Corp.*, 553 N.E.2d 1317, 1320–21 (N.Y. 1990).

26. *Lee Anne Fennell, Contracting Communities*, 2004 U. ILL. L. REV. 829, 842–43 (explaining that reciprocal control generates the "premium ambience" all owners seek).

27. *See supra* note 23 and accompanying text.

28. *E.g.*, *Levandusky*, 553 N.E.2d at 1326–27 (Titone, J., concurring). In 2014, the language in the Uniform Common Interest Act endorsing the business judgment rule, adopted in 2008, was reinforced after noting the daily owner/board tensions characterizing common-interest communities. UNIF. COMMON INT. OWNERSHIP ACT § 3-103 cmt. 5 (UNIF. L. COMM'N 2014).

29. *See infra* note 182.

30. *See infra* notes 204–205 and accompanying text.

31. *Max Schanzenbach & Nadav Shoked, Reclaiming Fiduciary Law for the City*, 70 STAN. L. REV. 565, 614 (2018).

Rather, courts merely ensure that proper procedures were adhered to before the decision was finalized.<sup>32</sup>

Unfortunately, while this ultra-deferential standard might be appropriate for decisions about aesthetic and lifestyle matters, it is inappropriate for other, less salient kinds of community decisions, where subjectivity and mutuality hardly ever prevail. These other decisions, albeit drawing much less public attention, endanger dramatically more substantial property interests than aesthetic and lifestyle decisions.

Prohibitions on leasing an owner's unit,<sup>33</sup> limits on the number of units an owner can acquire,<sup>34</sup> embarking (or not embarking) on major building projects,<sup>35</sup> the management of the community's financial reserves,<sup>36</sup> and the sale or redevelopment of common spaces<sup>37</sup> normally do not "so generally strike[] the imagination, and engage[] the affections of mankind."<sup>38</sup> Disputes respecting such decisions are often tame in their facts—especially when compared to battles over flowerpots or pink flamingos. Nonetheless, this Article argues, common-interest-community disputes of this type are those that present the real challenge to property law. The downplaying of these disputes—in favor of juicier disputes over mailboxes, personal hygiene, and the like—has for decades distorted American property law.

For in this other, less salient type of dispute, the characteristics allegedly justifying the law's turn to the business judgment rule are absent. Most obviously, nonaesthetic or lifestyle disputes often touch on overtly economic matters. Financial challenges or engineering problems are not read through the exclusive prism of personal taste or sentiment. An outsider-judge can determine, just as effectively as an insider-resident, how necessary a costly structural renovation is. Perhaps less obviously, but more importantly, a common-interest community's nonaesthetic rule often affects different owners within the same community in disparate ways; even over time, mutuality might never materialize.<sup>39</sup> A community rule barring owners from leasing their units will always have a dramatic effect on an owner holding her unit as an investment while it might never burden an owner residing in her unit;<sup>40</sup> frequent recourse

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32. *Id.*

33. *See infra* Subpart III.A.1.

34. *Olander v. Woodcliff Condo. Unit Owner Ass'n*, No. 92AP-1518, 1993 WL 34575, at \*1 (Ohio Ct. App. Feb. 9, 1993).

35. *E.g.*, *Lake Tishomingo Prop. Owners Ass'n v. Cronin*, 679 S.W.2d 852, 857 (Mo. 1984) (approving a special assessment to fund lake dredging).

36. *Ebert v. Briar Knoll Condo. Ass'n*, No. C-210-04, 2007 WL 188241, at \*7 (N.J. Super. Ct. App. Div. Jan. 26, 2007).

37. *E.g.*, *Hughes v. New Life Dev. Corp.*, 387 S.W.3d 453, 472–74 (Tenn. 2012) (converting a wilderness preserve into a golf course).

38. 2 WILLIAM BLACKSTONE, COMMENTARIES \*2 ("There is nothing which so generally strikes the imagination, and engages the affections of mankind, as the right of property . . .").

39. *See infra* Subpart III.A.

40. *See infra* Subpart III.A.1.

to special assessments each owner must pay will always disproportionately impact lower income owners.<sup>41</sup>

The limited levels of subjectivity and mutuality in such disputes should force the law to rethink the standard of review applied to nonaesthetic disputes. Otherwise, both efficiency and fairness suffer. An outright refusal to objectively scrutinize management decisions that are amenable to such assessment undermines the common-interest-community regime's pretenses of providing an efficient system of land management.<sup>42</sup> Community decisions that are objectively irrational, even dangerous, for the wellbeing of all owners stand without challenge. Mutuality's absence threatens basic notions of fairness. Some owners are empowered to consistently promote their interests at the expense of their neighbors' interests.

Very much relatedly, due to their nonsubjective and nonmutual nature, these decisions would be regarded in corporate law—the origin of the business judgment rule—as poor candidates for the rule's application. In corporate law, the rule is used when a shareholder alleges that the corporation's board of directors acted incompetently.<sup>43</sup> It accords corporate decision makers broad leeway, acknowledging the reality whereby fair minds might differ on the best course of business action.<sup>44</sup> The rule thus assumes—as a condition for its application—fair minds. It is explicitly irrelevant for cases of alleged conflicts of interest.<sup>45</sup> For such cases of potentially conflicted decisions, corporate law has a different, elevated review standard focusing on the decision's actual substance.<sup>46</sup>

Accordingly, when applying the business judgment rule to all common-interest-community conflicts, courts conflated a problem of potential incompetence with a problem of potential corruption.<sup>47</sup> The business judgment rule is a tool for handling conflicts of opinion (respecting, say, the appropriateness of pink flamingos on lawns), not conflicts of interest (respecting, say, the income some, but not all, owners derive from renting units). It is thus inapposite to the most important of disputes afflicting common-interest communities.

The summer of 2021 provided an exceptionally tragic illustration. In the aftermath of the catastrophic collapse of a condominium building in Surfside, Florida, in which scores perished, newspaper reports and court filings exposed the dysfunction that had for years plagued decision-making processes within

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41. See *infra* Subpart III.A.3.

42. See generally Robert C. Ellickson, *Alternatives to Zoning: Covenants, Nuisance Rules, and Fines as Land Use Controls*, 40 U. CHI. L. REV. 681, 714–18 (1973).

43. Schanzenbach & Shoked, *supra* note 31, at 612.

44. *Id.*

45. *E.g.*, *Auerbach v. Bennett*, 408 N.Y.S.2d 83, 87 (App. Div. 1978).

46. 18B AM. JUR. 2D *Corporations* § 1458, Westlaw (database updated Feb. 2023).

47. See *infra* Subpart II.C.

that common-interest community.<sup>48</sup> The board and many owners were aware of the building's poor structural health.<sup>49</sup> But some balked at the high costs of repairs which would have required the payment of special fees ranging in amount from \$80,000 to \$200,000 per individual owner.<sup>50</sup> Having already been subject to an array of high special assessments in the preceding years, mostly for cosmetic improvements, less affluent owners were frustrated.<sup>51</sup> Battles within the community, often pitting members of different means against each other, delayed necessary decisions.<sup>52</sup>

The conflicts between different owner groups within the Surfside condominium put the law's failings this Article identifies into sharp relief. Before the collapse, the one lawsuit brought against the community, in 2015, only demanded compensation for particularized water damages a specific unit had already endured.<sup>53</sup> That suit settled,<sup>54</sup> and any broader lawsuit challenging the community's general inaction on structural issues would have faced daunting odds given Florida courts' adherence to the ultra-deferential business judgment rule.<sup>55</sup>

Such judicial abstention could perhaps be excusable if legislative remedies were forthcoming. However, legislators' track record on the issue—in Florida and elsewhere—is hardly reassuring. State laws mostly refrain from

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48. The filing lawyers were quick to explain that the goal of these lawsuits was to assure a fair distribution of the insurance moneys to which the association was eligible. Complaint at 1–3, *Drezner v. Champlain Towers S. Condo. Ass'n*, No. 2021-015089-CA-01 (filed Fla. Cir. Ct. June 24, 2021), 2021 WL 2660742, at \*1–3; Jon Jackson, *Surfside Resident Steve Rosenthal Files Lawsuit Against Property, 2nd Since Collapse*, NEWSWEEK (June 28, 2021, 3:52 PM), <https://www.newsweek.com/surfside-resident-steve-rosenthal-files-lawsuit-against-property-2nd-since-collapse-1604925>. The lawyers relied on diverse legal theories, including negligence, nuisance, and breach of contract. Jim Sams, *Judge Says \$48M in Coverage for Collapsed Condo Tower Won't Be Enough*, CLAIMS J. (July 2, 2021), <https://www.claimsjournal.com/news/southeast/2021/07/02/304641.htm>.

49. Patricia Mazzei et al., *Inside the Tumultuous Years Before the Florida Condo Collapse*, N.Y. TIMES, <https://www.nytimes.com/2021/07/03/us/miami-florida-surfside-collapse.html> (July 23, 2021).

50. *Id.*

51. *Id.*

52. *Id.* Recent unit prices varied widely, ranging from \$460,000 to over \$2 million. *See id.*; Mike Baker & Kimiko de Freytas-Tamura, *Infighting and Poor Planning Leave Condo Sites in Disrepair*, N.Y. TIMES, <https://www.nytimes.com/2021/07/01/us/condo-associations-surfside-collapse.html> (July 3, 2021). As some owners, many of whom were retirees, moved in decades ago before the area was transformed, wealth gaps were wider still. *See Mazzei et al., supra* note 49.

53. Complaint, *Fainstein v. Champlain Towers S. Condo. Ass'n*, No. 2015-022299-CA-01 (Fla. Cir. Ct. Sept. 28, 2015).

54. Justin Rohrlich & Zoe Richards, *'Something Off': Miami Collapse Complex Had Issues*, DAILY BEAST, <https://www.thedailybeast.com/ill-fated-champlain-towers-showed-signs-of-something-off> (Jun. 26, 2021, 1:22 PM).

55. *Farrington v. Casa Solana Condo. Ass'n*, 517 So. 2d 70, 71 (Fla. Dist. Ct. App. 1987). For a survey of all states, see *infra* notes 204–205 and accompanying text. *Cf.* Susan F. French, *Making Common Interest Communities Work: The Next Step*, 37 URB. LAW. 359, 365 (2005) (noting that “individual owners . . . have little recourse against board misconduct”).



meaningfully regulating common-interest-community boards.<sup>56</sup> Only a handful of states—Florida not among them<sup>57</sup>—mandate maintenance of adequate funding levels to address potential structural expenses.<sup>58</sup> While Florida had enacted a requirement for periodic inspections to ascertain building and amenity maintenance costs,<sup>59</sup> the requirement was made waivable<sup>60</sup> and then repealed less than two years after its adoption.<sup>61</sup> State legislators attribute the dearth of regulation to the effectiveness of interest group lobbying by common-interest-community law firms invested in keeping this form of housing artificially cheap.<sup>62</sup> They further cite the lack of political will to upset cost-conscious owners in common-interest communities by forcing them to pay fees that fairly reflect maintenance charges.<sup>63</sup> These political dynamics reinforce this Article’s central contention: some common-interest-community disputes involve conflicts of interest, rather than of taste, and courts must be ready to intervene to protect a losing group’s interests.

In accordance, this Article promotes a tiered system of judicial review for common-interest-community decisions. Decisions that do not disparately affect a defined interest group within the community—that is, decisions where mutuality prevails—should remain subject to permissive review. Aesthetic or lifestyle decisions need not be subjected to substantive review.<sup>64</sup> Conversely, decisions that distinctly implicate a defined group of owners’ interests should be scrutinized more closely.<sup>65</sup> The substance of these decisions, not just the process producing them, should be inspected for fairness.

This Article thus differs in its normative suggestion from preceding works dealing with the common-interest community. Those writings all aimed at promoting one or another review standard for common-interest-community

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56. State laws mostly consist of disclosure requirements. *E.g.*, D.C. CODE §§ 42-1903.14, 42-1904.11 (2001) (amended 2014); FLA. STAT. § 718.3027 (2022); 765 ILL. COMP. STAT. ANN. 605/22 (West 2017); N.M. STAT. ANN. § 47-7D-3 (West 2003).

57. Florida’s requirement is wholly waivable, FLA. STAT. § 718.112 (2022), as is the requirement in most other states that have such a requirement, *see, e.g.*, MINN. STAT. § 515B.3-1141(a)(5) (2022); MASS. GEN. LAWS ANN. Ch. 183A, § 10 (West 2014); VA. CODE ANN. § 55.1-1965 (2022); UTAH CODE ANN. § 57-8-7.5(2) (West 2016) (amended 2021); OHIO REV. CODE ANN. § 5311.081 (West 2016); WASH. REV. CODE ANN. § 64.34.380 (West 2019) (requiring a reserve study only if no “hardship”).

58. MICH. ADMIN. CODE R. 559.511 (1979) (mandating “10% of . . . annual budget”); DEL. CODE ANN. Tit. 25, § 81-315 (2021) (mandating 5%–15%); NEV. REV. STAT. ANN. § 116.31152 (2021) (discussing adequate reserves); HAW. REV. STAT. § 514B-148 (1993) (amended 2022) (mandating 50% of estimated replacement costs); OR. REV. STAT. § 94.595 (2021) (noting that the requirement is waivable but only with all owners’ annual approval). In 2020, California added a reserves study requirement, which does not mandate actual funding of reserves. CAL. CIV. CODE. § 5550 (West 2016).

59. FLA. STAT. § 718.113(6) (2009) (repealed 2010).

60. 2008 Fla. Laws 27, 29.

61. 2010 Fla. Laws 56.

62. Matthew Shaer, *The Towers and the Ticking Clock*, N.Y. TIMES MAG. (Jan. 28, 2022), <https://www.nytimes.com/interactive/2022/01/28/magazine/miami-condo-collapse.html>.

63. *Id.*

64. *See infra* Subpart III.

65. *See infra* Subpart III.

decisions.<sup>66</sup> This Article advocates for a dual review standard.<sup>67</sup> In explicating that suggested framework, this Article also repudiates previous commentators' fears that particularly problematic common-interest-community decisions cannot be pinpointed a priori.<sup>68</sup> Because, as this Article argues, the most normatively troubling conflicts of interest within the community are structural, some of the circumstances giving rise to them can be isolated. Instances mentioned earlier already alluded to several of these circumstances, such as conflicts between owners of different means or between owner–occupants and owner–investors.

To systemically categorize all such instances and establish a principled framework for their treatment, the Article proceeds as follows. Part I draws the legal landscape. After describing how property law came to accommodate common-interest communities following their introduction in the early twentieth century, it investigates the law's current state respecting common-interest communities' decision-making powers. It demonstrates that most states have shifted from the original property law standard of reasonableness, which many commentaries still portray as dominant, to a standard drawn from corporate law: the business judgment rule. Part II turns to the normative assessment. It investigates the original function of the business judgment rule in corporate law and establishes the extent to which its application in common-interest-community law fails to reflect that function. It shows that a rule corporate law applies to disinterested decisions alone is applied here across the board, even though conflicts of interest are even more pervasive in the common-interest community than in the corporation. Part III then sets out to identify the circumstances where structural conflicts of interest in common-

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66. For examples of authors supporting a lax review standard, see Clayton P. Gillette, *Courts, Covenants, and Communities*, 61 U. CHI. L. REV. 1375, 1431 (1994) (grounding the argument in community homogeneity); Stewart E. Sterk, *Minority Protection in Residential Private Governments*, 77 B.U. L. REV. 273, 341 (1997) (grounding it in buyers' expectations); Robert C. Ellickson, *Cities and Homeowners Associations*, 130 U. PA. L. REV. 1519, 1530 (1982) (grounding it in the need to follow the association's own original purposes); Richard A. Epstein, *Covenants and Constitutions*, 73 CORNELL L. REV. 906, 924–25 (1988) (grounding it in courts' limited competence as compared to parties' own contractual schemes). For examples of authors supporting tightened judicial review, see Gregory S. Alexander, *Dilemmas of Group Autonomy: Residential Associations and Community*, 75 CORNELL L. REV. 1, 7 (1989) (basing it on communitarian theory); Fennell, *supra* note 26, at 893–95 (arguing that strict enforcement of community regulations forecloses on possibilities of efficient individualized adjustments to them); Robert G. Natelson, *Consent, Coercion, and "Reasonableness" in Private Law: The Special Case of the Property Owners Association*, 51 OHIO ST. L.J. 41, 87–88 (1990) (arguing courts must review to verify regulations' efficiency); Michael C. Pollack, *Judicial Deference and Institutional Character: Homeowners Associations and the Puzzle of Private Governance*, 81 U. CIN. L. REV. 839, 880 (2013) (arguing the right analogy is an administrative agency); Franzese, *supra* note 12, at 669–71 (arguing adherence to a community's stated purposes should be ensured).

67. In a different doctrinal context, the *Restatement (Third) of Property: Servitudes* also envisions a two-tiered system of regulation. For votes on declaration amendments, it normally only requires majority approval. RESTATEMENT (THIRD) OF PROP.: SERVITUDES § 6.10 (AM. L. INST. 2000). However, unanimity is needed for amendments “depriv[ing] individual owners of significant property or civil rights.” *Id.* at cmt. g. The clause is dispositive—a declaration could override it—and fails to define the “significant” rights it would cover.

68. See Gillette, *supra* note 66, at 1431.

interest communities are most likely. It constructs a catalog of common-interest-community cases that should be subject to heightened scrutiny. To illustrate the approach's usefulness, that Part concludes by elaborating on the factors courts should ponder when applying the reasonableness standard.

From this analysis, a new conceptual view of the common-interest community will emerge. The common-interest community is not merely a product of contractual agreements or a producer of community—the two visions theorists normally put forward.<sup>69</sup> It is also a nexus of interests, including, sadly but inevitably, conflicting interests.

## I. THE LAW OF COMMON-INTEREST COMMUNITIES

More than a quarter of Americans now live in common-interest communities.<sup>70</sup> Yet the common-interest community is, in relative terms, a recent arrival. To allow for its original introduction, in the early twentieth century, traditional property law was modified. Then, later in the century, property law adjusted even further to facilitate the common-interest community's incredible spread. To set the stage for this Article's normative assessment of the law's treatment of the common-interest community, this Part presents the law's evolution. First, it provides a brief history of the common-interest community's rise. This review explains why common-interest communities' founders and promoters needed to rely on the property law tool known as the covenant. The discussion then explores the elements of traditional covenant law that could have made such reliance difficult and the legal reforms that removed those hurdles. One such reform, necessitated as common-interest communities grew more proactive, was the introduction of a mechanism for reviewing community decisions. Because the legal review of communities' decisions is the Article's topic, this move is explored in some detail. This Part concludes by surveying the law's current state, showing that courts replaced the property law review mechanism they had originally introduced for community decisions with a much weaker one drawn from corporate law.

### A. *The Common-Interest Community's Rise*

Today, the common-interest-community form of housing is most clearly associated with sprawling suburban middle-class, or even lower-middle-class, subdivisions.<sup>71</sup> But its earliest forerunners were very different. They are to be

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69. See e.g., Ellickson, *supra* note 66, at 1535–36 (discussing the contractual vision); Alexander, *supra* note 66, at 27 (discussing the communitarian vision).

70. See *supra* note 4.

71. Compare this Article's title, Aaron Gott, Note, *Ticky Tacky Little Governments?: A More Faithful Approach to Community Associations Under the State Action Doctrine*, 40 FLA. ST. U. L. REV. 201 (2012), with these

found in Boston's Louisburg Square and New York City's Gramercy Park, constructed in 1826 and 1831, respectively.<sup>72</sup> At the center of both these posh projects, developers reserved a private park for the use of surrounding residences' owners.<sup>73</sup> Gramercy Park's developer placed title to the park with trustees.<sup>74</sup> Louisburg Square's developer failed to provide arrangements for the park's maintenance.<sup>75</sup> To remedy the omission, the twenty-eight lot owners signed an agreement in 1844 binding themselves and subsequent purchasers to maintain the park. For that purpose, the agreement also established the Committee of the Proprietors of Louisburg Square.<sup>76</sup> The committee is considered the first American homeowners association.<sup>77</sup>

This earliest incarnation was not only aesthetically and socially remote from the current idea of a common-interest community but also legally distinct. The Louisburg Square committee's powers were limited: it solely maintained the owners' common property, which amounted to one small park.<sup>78</sup> The committee had no powers over owners' lives or properties. Louisburg Square—or Gramercy Park—thus required no legal innovation. Traditional property-law devices easily accommodated these projects. Property law's boundaries would only be pushed later in the nineteenth century, as more potent homeowners associations began emerging.

The powerful homeowners associations we know today were the product of the reaction of two very distinct groups—developers and utopians—to the industrial transformations of the late-nineteenth century. Among developers, the era's dramatic population growth and technological improvements bred a realization that housing was now, for the first time in history, a mass manufacturing business.<sup>79</sup> Yet, unlike other mass manufacturers, residential builders had to retain control over uses of their products, even ones already sold, until all products in the given production line were dispensed with. Once a widget is sold, the widget manufacturer normally cares little about how it is used, even if their factory still has thousands more such widgets to sell. A developer of multiple neighboring houses confronts a different marketing

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classic lyrics, MALVINA REYNOLDS, *Little Boxes*, on MALVINA REYNOLDS SINGS THE TRUTH (Columbia Recs. 1967) ("Little boxes made of ticky tacky . . . And they all look just the same.").

72. See ROBERT G. NATELSON, *LAW OF PROPERTY OWNERS ASSOCIATIONS* 16–17 (1989); EVAN MCKENZIE, *PRIVATOPIA* 34 (1994); see also EDWIN G. BURROWS & MIKE WALLACE, *GOTHAM: A HISTORY OF NEW YORK CITY TO 1898*, at 577 (1999).

73. See NATELSON, *supra* note 72, at 17.

74. The developer laid out the park before surrounding lots were built or sold. BURROWS & WALLACE, *supra* note 72. He then deeded the square collectively to owners of the sixty surrounding plots he had platted out. *Id.*

75. See MCKENZIE, *supra* note 72.

76. *Id.*

77. *Id.*

78. See *id.*

79. See MARC A. WEISS, *THE RISE OF THE COMMUNITY BUILDERS* 45 (1987).

reality. The developer must make sure that the entire area is developed in ways that maintain the value of all homes they built—until they sell the last.

Today, public regulation through zoning helps achieve that goal, but in the late nineteenth-century, zoning still lay decades in the future.<sup>80</sup> One visionary developer, Edward Bouton, conceived a solution: in his 1891 project of Roland Park in Baltimore, Maryland, he incorporated into the deeds for each sold parcel restrictions he could enforce on a buyer's uses of the lot.<sup>81</sup> Later that decade, Bouton gave up control of the project.<sup>82</sup> He placed the deed restrictions' administration, as well as the project's maintenance fund, with a new entity residents managed.<sup>83</sup>

The next famous project in this vein—Country Club District in Kansas City, Missouri, which was initiated in 1905<sup>84</sup>—perfected the model. The developer, J.C. Nichols, established the homeowners association before he sold any land.<sup>85</sup> He then inserted an automatic membership requirement into all lots' deeds.<sup>86</sup> The homeowners association had now truly arrived.

At around the same time, a group very different in its motivations from these developers began relying, for its own distinct reasons, on the same mechanism, thereby solidifying the homeowners association's stature as the new age's most promising housing model. Like developers, late-nineteenth-century social reformers were struck by the changes unprecedented population growth and industrial transformation wrought in housing patterns.<sup>87</sup> Reformers were dismayed at urban living conditions, which they found physically—and socially—unhealthy.<sup>88</sup> Thus, they sought to reinvent housing—not for the rich, on whom developers focused, but for the working classes. The model they embraced as a replacement for the era's existing cities was most prominently expounded upon by an English writer, Ebenezer Howard, in an immensely influential book, *Garden Cities of Tomorrow*.<sup>89</sup>

The book was first published in 1902,<sup>90</sup> early in what became dubbed the Progressive Era.<sup>91</sup> This was the period when the social sciences evolved into

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80. On zoning's rise, see Nadav Shoked, *The Reinvention of Ownership: The Embrace of Residential Zoning and the Modern Populist Reading of Property*, 28 *YALE J. ON REGUL.* 91, 94–98 (2011).

81. DONALD STABILE, *COMMUNITY ASSOCIATIONS* 49–50 (2000).

82. *Id.* at 50.

83. *Id.*

84. *Id.* at 51.

85. *Id.* at 52.

86. *Id.*

87. ROBERT H. WIEBE, *THE SEARCH FOR ORDER: 1877-1920*, at 166–67 (1967).

88. *Id.* at 168–69.

89. See EBENEZER HOWARD, *GARDEN CITIES OF TO-MORROW* (F.J. Osborn ed., M.I.T. Press 1965).

90. See *id.* at 9.

91. See generally RICHARD HOFSTADTER, *THE AGE OF REFORM* 3–22 (1955) (discussing the Progressive Era).

research fields and faith in expertise was at its zenith.<sup>92</sup> As befitting such an intellectual climate, Howard believed that only rational planning could improve life in general and urban life in particular.<sup>93</sup> Leaning on such planning, he dreamt of self-sufficient small towns.<sup>94</sup> Howard's proposed Garden City was meticulously designed around a central park, with industries situated at the edges and an agricultural belt beyond those.<sup>95</sup> The inventiveness of this spatial organization, contrasting as it did with the congested cities of Howard's day, was matched by the originality of the social organization governing Garden City. Legally, Garden City was to be based on public ownership.<sup>96</sup> Residents would be the municipality's tenants.<sup>97</sup> Howard envisioned this powerful municipal government as a democratic technocracy molded according to tenets of efficient business management.<sup>98</sup>

Howard's many American acolytes wholeheartedly embraced this model where they discerned "the splendid possibilities of a new civilization based on service to the community."<sup>99</sup> Lewis Mumford, a prominent American intellectual, excitedly endorsed Howard's municipal management scheme, noting:

No longer were the most essential agents of city development to be left to the individual investor, whether speculator or owner, dealing with individual building lots, individual houses, individual business sites; for no individual exercise of either foresight or public spirit could produce the equivalent of a co-ordinated and meaningful whole.<sup>100</sup>

Such enthusiasm for the scheme notwithstanding, American reformers had good reason to doubt its realizability under the specific legal model Howard envisioned. Decades earlier, a previous Garden City, unrelated to Howard's, had followed a similar legal model on Long Island, New York but failed miserably.<sup>101</sup> Retail magnate A.T. Stewart had hoped to control that community he developed in 1871 by renting, rather than selling, homes.<sup>102</sup> For America, this was a bold experiment. As historian Kenneth Jackson explained:

The Garden City leasing scheme recalled European systems of social control which had never been incorporated into American traditions. It was similar to

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92. See, e.g., DANIEL T. RODGERS, *ATLANTIC CROSSINGS: SOCIAL POLITICS IN A PROGRESSIVE ERA* 98–101 (1998) (discussing economists).

93. See HOWARD, *supra* note 89, at 136–37.

94. See *id.* at 51–57.

95. See *id.* at 50–55.

96. Lewis Mumford, *Introduction* to HOWARD, *supra* note 89, at 35.

97. HOWARD, *supra* note 89, at 123.

98. For more on Howard and his influence on the common-interest-community movement, see MCKENZIE, *supra* note 72, at 1–7.

99. LEWIS MUMFORD, *THE CITY IN HISTORY* 515 (1961).

100. *Id.* at 521.

101. KENNETH T. JACKSON, *CRABGRASS FRONTIER* 81–84 (1985).

102. *Id.* at 83.

the procedure in small industrial towns—such as Lowell—where mill hands rented small quarters from the all-powerful company. Stewart, however, was attempting to control the lives of affluent businessmen, not the powerless workers of a mill village.<sup>103</sup>

The experiment fell flat. Two decades after it had been built, only half the houses were rented.<sup>104</sup> Not until land was sold for private ownership did Garden City begin attracting residents.<sup>105</sup> Thus, as Jackson summarizes its historical role, “[I]he most enduring lesson of A.T. Stewart’s planned suburb was negative; it demonstrated that affluent families would not support a rental market for expensive detached homes.”<sup>106</sup>

With Howard’s rental model already shown to be impractical in the New World, the reformers seeking to build his Garden City in America had to find an alternative legal mechanism still supplying the same control over residents necessary for a rationally planned and managed community.<sup>107</sup> The solution they landed upon was the same that developers had employed in Roland Park and Country Club District. In 1928, the Regional Planning Association of America, whose board members included architects, social workers, and Progressive Era luminaries such as Eleanor Roosevelt, built the town of Radburn, New Jersey.<sup>108</sup> Radburn is famous for its inventive physical layout,<sup>109</sup> but its organizational structure was also innovative. Radburn relied on deed restrictions for its governance.<sup>110</sup> It further infused the earlier developer model with progressive reformers’ values of expertise-driven government. For example, Radburn was to have a “manager”: an expert the homeowners association hired.<sup>111</sup>

The project was exceptionally ill-timed, and it was felled by the Great Depression.<sup>112</sup> Still, Radburn set the stage for the many communities that popped up when the market recovered and then boomed following World War II.<sup>113</sup> Radburn signaled that the common-interest-community model was appealing not only for the economic reasons motivating developers but also for the social and lifestyle concerns reformers—and residents—valued.

Developer- or reformer-guided, upscale or middle-class, the common-interest community would be the favored housing mode for the remainder of

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103. *Id.*

104. *Id.* at 84.

105. *Id.*

106. *Id.*

107. See JON A. PETERSON, *THE BIRTH OF CITY PLANNING IN THE UNITED STATES, 1840–1917*, at 235 (2003) (discussing Howard’s influence on American planners).

108. STABILE, *supra* note 81, at 53–54.

109. *Id.* at 54.

110. MCKENZIE, *supra* note 72, at 48.

111. For more on Radburn, see STABILE, *supra* note 81, at 53–55.

112. MCKENZIE, *supra* note 72, at 9.

113. *Id.* at 51.

the century and beyond. And this housing pattern, defined by control over individual residents, was legally constructed not through leaseholds—the landholding form historically associated with controls over residents’ freedom—but through restricted ownership.

*B. Property Law Adjusts to the Common-Interest Community’s Introduction*

The common-interest community, as ushered in by developers and reformers in Roland Park, Country Club District, and Radburn, was based on “deed restrictions.”<sup>114</sup> Although instituting a new housing form, these deed restrictions were enforceable through a rather ancient legal tool: the covenant. But to fully accommodate the goals that modern developers and reformers sought to pursue, traditional covenant law required major adjustments. By the 1930s, these adjustments were largely achieved, and the modern law of covenants, facilitating the common-interest community’s expansion, was mostly in place.

To enable control over the use of lots after their sale, developers and reformers needed a legal device more powerful than a contract. A contract is a personal promise: it places an obligation on the buyer making the promise but not on any subsequent owner who might purchase the property from that original buyer.<sup>115</sup> A common-interest community requires something more; it requires a promise that obliges *whoever* holds the land at any given time.<sup>116</sup> It needs, that is, a property, rather than a contract, obligation. Property law originally recognized the power to create such obligations back in the Middle Ages.<sup>117</sup> English courts read a 1368 case as establishing “covenants”<sup>118</sup>: obligations whose burdens and benefits “run[] with the land.”<sup>119</sup> These are, in a sense, promises assumed by and toward lands, not by and toward specific owners.

Later, during the Enlightenment, courts limited the power to create covenants. Because covenants attach to the land and constrain a current property owner’s powers, courts in this age of liberalism found them abhorrent.<sup>120</sup> Liberalism was committed to ownership’s liberating power and to

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114. STABILE, *supra* note 81, at 50–53.

115. See SINGER, *supra* note 6, § 6.1, at 226.

116. *Id.* § 6.1, at 226–27.

117. See Pakenham’s Case, YB 42 Edw. 3, fol. 3, Hilary, pl. 14 (1368) (Eng.), reprinted in 2 JOHN CHIPMAN GRAY, SELECT CASES AND OTHER AUTHORITIES ON THE LAW OF PROPERTY 357–59 (2d ed. 1905).

118. *Id.*

119. SINGER, *supra* note 6, § 6.1, at 226.

120. These ideological commitments and the resultant suspicious attitude toward covenants still resonate. For example, the Wisconsin Supreme Court stated: “This court consistently holds that public policy favors the free and unrestricted use of property. Accordingly, restrictions contained in deeds . . . must be strictly construed to favor unencumbered and free use of property.” *Crowley v. Knapp*, 288 N.W.2d 815, 822



market transactions.<sup>121</sup> In this light, covenants were viewed as feudal not only in origin but also in effect and logic.<sup>122</sup> Through a series of decisions spanning centuries, English courts, therefore, saddled those attempting to enforce a covenant against an owner with requirements that included proof of notice, writing, intent, privity, and that the covenant “touches and concerns” the land.<sup>123</sup>

The last two traditional requirements for an enforceable covenant—privity and touch and concern—presented major hurdles for those relying on covenants to establish common-interest communities. The doctrinal problems came to a head in the famed 1938 New York case of *Neponsit Property Owners’ Ass’n v. Emigrant Industrial Savings Bank*.<sup>124</sup> In *Neponsit*, a bank refused to pay association dues to the homeowners association of which the property it had foreclosed formed part.<sup>125</sup> The obligation to pay the dues was included in the property’s original deed, but the bank argued that the two parties to the original transaction—the buyers whose property was later foreclosed and the association—lacked privity and that the obligation did not touch and concern the land.<sup>126</sup> Thus, the bank contended that the covenant was unenforceable.

Privity is a highly complicated, technical, and contested doctrine, but at a minimum, it demands a property relationship between the owner of the land the covenant burdens and the owner of the land it benefits.<sup>127</sup> In *Neponsit*, the party formally benefitting from the covenant to pay association dues was the homeowners association.<sup>128</sup> Because the association owned no land, it could not be in a property relationship—and thus, it could not have privity—with the burdened land’s owner.<sup>129</sup>

Touch and concern, another rather opaque requirement for a covenant’s enforcement, demands that both the covenant’s burden and benefit affect the relevant lands themselves rather than their owners as individuals.<sup>130</sup> While an obligation to refrain from doing something on the land—for example, building a second structure—clearly meets that requirement, an obligation to pay money might not.<sup>131</sup> An obligation to pay is affirmative (i.e., it requires that the land’s

(Wis. 1980); see also *Wheeler v. Southport Seven Planned Unit Dev.*, 2012 ND 201, ¶ 13, 821 N.W.2d 746, 753 (“[Restrictive covenants are] not favored.”).

121. C. B. MACPHERSON, *THE POLITICAL THEORY OF POSSESSIVE INDIVIDUALISM* 3 (1962).

122. Thomas C. Grey, *The Disintegration of Property*, in 22 *NOMOS: PROPERTY* 69, 74 (J. Roland Pennock & John W. Chapman eds., 1980).

123. *Spencer’s Case* (1583) 77 Eng. Rep. 72, 74; 5 Co. Rep. 16 a; *Webb v. Russell* (1789) 100 Eng. Rep. 639; 3 T. R. 393; *Keppell v. Baile* (1834) 39 Eng. Rep 1042; 2 My. & K. 517.

124. *Neponsit Prop. Owners’ Ass’n v. Emigrant Indus. Sav. Bank*, 15 N.E.2d 793 (N.Y. 1938).

125. *Id.* at 794.

126. *Id.* at 797–98.

127. SINGER, *supra* note 6, § 6.2, at 245–46.

128. *Neponsit*, 15 N.E.2d at 797.

129. *Id.*

130. SINGER, *supra* note 6, § 6.3, at 254–55.

131. *Id.* at 256.

possessor do something), and courts traditionally hesitated to characterize such obligations as touching and concerning land.<sup>132</sup> Courts believed that these obligations placed the burden not on the land but on the individual whom the given obligation forced to act.<sup>133</sup> These obligations also, courts held, benefited an owner as a person—receiving money or services—not as a landholder.<sup>134</sup>

Although the bank's double-barreled challenge to the association's dues requirement was thus well-grounded in traditional property law, the New York Court of Appeals rejected it.<sup>135</sup> The court found a solution for the covenant law obstacles, thereby providing the common-interest community with its Magna Carta. The court reasoned that the law should look past the homeowners association's technical architecture and treat it based on its real essence.<sup>136</sup> True, the homeowners association was the entity formally enforcing the covenant and the association itself owned no land.<sup>137</sup> But functionally, the association was merely the homeowners' agent, employing the funds it collected to improve the common spaces serving them.<sup>138</sup> The owners themselves owned land—and hence had privity with each other—and the common spaces benefitted from the dues—hence the duty to pay the dues touched and concerned that land.<sup>139</sup>

Concluding that the common-interest community's dues requirement, and any other such requirements the community might have, were enforceable, the *Neponsit* decision opened the legal door for the common-interest community's spread. Other state courts followed the lead of the New York Court of Appeals, and homeowners associations' establishment via covenants rapidly became an uncontested practice.<sup>140</sup> The common-interest community's legal foundations were further solidified in the 1960s, when all states—prompted by Puerto Rico's 1958 initiative—legislated condominium laws.<sup>141</sup> These introduced a form of common-interest community whose major doctrinal innovation was vertical division of ownership—allowing one building to contain multiple units each owned by a distinct owner. The regime the statutes set for the condominium closely mirrored that of the homeowners association, and today, little distinguishes the two.<sup>142</sup> Thus, condominium acts reflected legislatures'

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132. *Miller v. Clary*, 103 N.E. 1114, 1116 (N.Y. 1913).

133. *Id.* at 1117.

134. *Id.*

135. *Neponsit Prop. Owners' Ass'n v. Emigrant Indus. Sav. Bank*, 15 N.E.2d 793, 797 (N.Y. 1938).

136. *Id.* at 798.

137. *Id.*

138. *Id.*

139. *Id.*

140. 7 NORMAN WILLIAMS, JR. & JOHN M. TAYLOR, *AMERICAN LAND PLANNING LAW* § 163:9 (rev. ed. 2003) (characterizing *Neponsit* as the “leading American case on covenants”).

141. Nadav Shoked, *The Community in the Planned Community*, 29 CORNELL J.L. & PUB. POL'Y 675, 676 n.4 (2020).

142. NATELSON, *supra* note 72, at 58–60 (positing that “the integration between the law of condominium and the law of other *covenanted subdivisions* is well on the way to being complete,” and thus, it is

embrace of the judicial innovations in traditional covenant law and awarded the common-interest community a statutory imprimatur.<sup>143</sup>

### C. Courts' Initial Encounters with Common-Interest-Community Decisions

Court decisions and legislative reforms from the twentieth-century's middle decades rendered the legal ability to construct a common-interest community uncontested. But once communities were erected throughout the country, their daily operations soon presented a new legal problem. After it is established, a common-interest community, like any other collective entity, is not passive: the community and its board adopt decisions on an ongoing basis. Similarly, the original rules detailed in the declaration establishing a common-interest community are not static—they must be enforced, interpreted, and at times changed. *Neponsit* held that the original declaration establishing and granting powers to the community and its board represented a legally binding covenant.<sup>144</sup> Do the decisions the community and board later make also therefore enjoy—automatically—the status of legally enforceable covenants?

Courts that confronted common-interest-community decisions answered in the negative. They subjected community and board decisions to further judicial scrutiny.<sup>145</sup> In 1975 a Florida appellate court became the first to face a challenge to a common-interest-community decision. Assessing its legality, the court proclaimed: “[W]e believe the test is reasonableness.”<sup>146</sup> Two years later, a Texas appellate court similarly invoked reasonableness as the standard that a common-interest community’s decision must meet.<sup>147</sup> Another year passed, and, citing the Florida decision, a Missouri court also stated, “[W]e believe the standard to be applied is reasonableness.”<sup>148</sup>

Thus, the first courts to face challenges to common-interest-community decisions, in the late 1970s, settled on a reasonableness test.<sup>149</sup> Yet they

improper “to speak or write of ‘condominium law’ and ‘homeowners association law’ as if they were discrete topics”).

143. *Sea Watch Stores LLC v. Council of Unit Owners of Sea Watch Condo.*, 691 A.2d 750, 753 (Md. Ct. Spec. App. 1997) (“One must always remember that the condominium statutes did not create new real property.”).

144. *See supra* notes 136–139 and accompanying text.

145. *Levandusky v. One Fifth Ave. Apartment Corp.*, 553 N.E.2d 1317, 1321 (N.Y. 1990) (“Even when the governing board acts within the scope of its authority, some check on its potential powers to regulate residents’ conduct, life-style and property rights is necessary to protect individual residents from abusive exercise . . .”).

146. *Hidden Harbour Ests., Inc. v. Norman*, 309 So. 2d 180, 182 (Fla. Dist. Ct. App. 1975).

147. *Holleman v. Mission Trace Homeowners Ass’n*, 556 S.W.2d 632, 635 (Tex. Civ. App. 1977).

148. *Ryan v. Baptiste*, 565 S.W.2d 196, 198 (Mo. Ct. App. 1978).

149. The test was first mentioned in a 1969 Colorado case. *Rhue v. Cheyenne Homes, Inc.*, 449 P.2d 361, 362–63 (Colo. 1969). That decision, however, addressed specific factual settings: a covenant empowering an architectural review committee to approve any new house construction, or in that case, the moving of an existing house into the community. *Id.* at 362.

provided meager and muddled doctrinal grounding for this requirement.<sup>150</sup> As the quotations above indicate, courts basically established the test by proclamation. The resulting uncertainty surrounding the requirement's doctrinal source might be partially responsible for its erosion over time—a process that the next Subpart will survey.

Because this Article's argument is largely a critical reaction to that process, it is important to note that whether the first courts to call on the test acknowledged as much or not, a reasonableness test is a necessary outgrowth of traditional covenant rules associated with important normative values.<sup>151</sup> The reasonableness test should be seen as necessitated by covenant law's notice requirement, a requirement that expresses property law's key goal of protecting individuals' reasonable expectations.<sup>152</sup>

As noted, for a covenant to be enforceable, traditional property law requires the elements of writing, intent, notice, privity, and touch and concern.<sup>153</sup> *Neponsit* removed the challenge the more complex elements, privity and touch and concern, presented to establishing a common-interest community.<sup>154</sup> But when the obligations the common-interest community imposes on owners are adopted after the community's creation, they arguably fail the much more straightforward covenant law element of notice.<sup>155</sup>

An owner buying a unit in a common-interest community is on notice of all restrictions included in the declaration establishing the community.<sup>156</sup> Even if she did not read the declaration, she is under constructive notice of its contents as the declaration is—and given current laws, must be—recorded.<sup>157</sup> Hence, the foreclosing bank in *Neponsit* could not have argued that it was unaware of the duty to pay dues, even if that obligation did not appear in the specific contract it had signed with the mortgagors. But what if the association had decided to introduce new dues after the bank had issued the loan?

On the one hand, the owner (here, the bank) did not know of the decision to impose the dues when it bought its interest. The decision had not yet been made. On the other hand, the owner (here, the bank) did know at the time of

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150. Note, *Judicial Review of Condominium Rule Making*, 94 HARV. L. REV. 647, 658 (1981).

151. See also *Worthinglen Condo. Owners' Ass'n v. Brown*, 566 N.E.2d 1275, 1280 (Ohio Ct. App. 1989) (Whiteside, J., concurring) (criticizing the majority opinion for relying on other bodies of law when "it is solely real estate law issues that confront us; an analogy would be to deed restrictions").

152. Nestor M. Davidson, *Property's Morale*, 110 MICH. L. REV. 437, 439 (2011) ("One of the most enduring arguments deployed in favor of strong property rights is the imperative to protect the 'settled expectations' of property holders.>").

153. See RESTATEMENT (FIRST) OF PROP. §§ 530-538 (AM. L. INST. 1944).

154. See *Neponsit Prop. Owners' Ass'n v. Emigrant Indus. Sav. Bank*, 15 N.E.2d 793, 797-98 (N.Y. 1938).

155. See *Tulk v. Moxhay* (1848) 41 Eng. Rep. 1143; 2 Ph. 774 (first establishing the notice requirement).

156. *Hidden Harbour Ests., Inc. v. Basso*, 393 So. 2d 637, 639 (Fla. Dist. Ct. App. 1981) (explaining that such restrictions count as covenants because of "the fact that each individual unit owner purchases his unit knowing of and accepting the restrictions to be imposed").

157. SINGER, *supra* note 6, at 241.

purchase that the association had authority to adopt future decisions. These decision-making powers were established in the original declaration.<sup>158</sup>

Thus, while some courts have refused to enforce such community decisions,<sup>159</sup> others do enforce them.<sup>160</sup> The disagreement boils down to one question: what a unit buyer, who knowingly joined a common-interest community, can be said to have expected. The options courts supplied in these cases appear binary: either the unit buyer can expect no new decisions, or the unit buyer can expect any new decision. But a middle option is possible. A buyer expects decisions made after the buyer had bought their unit—but only reasonable ones.<sup>161</sup>

This option probably reflects the average buyer's actual expectations.<sup>162</sup> Contract law interpretation principles also recommend it.<sup>163</sup> Contract law's implied covenant of good faith and fair dealing views parties as expecting counterparties to exercise rights reasonably.<sup>164</sup> This legal theory reigns in several contract and property contexts.<sup>165</sup> It could easily apply to the interpretation of the common-interest-community declaration as well.<sup>166</sup> Given the ongoing

158. *Woodside Vill. Condo. Ass'n v. Jahren*, 806 So. 2d 452, 461 (Fla. 2002); *see also* *Cape May Harbor Vill. & Yacht Club Ass'n v. Sbraga*, 22 A.3d 158, 165 (N.J. Super. Ct. App. Div. 2011) (“[A]lthough the original Declaration did not prohibit (and indeed contemplated) leasing of homes, it also contained provisions authorizing amendments of its provisions. Therefore, any purchaser was on notice that the provisions in the Declaration were not immutable.”).

159. *Breene v. Plaza Tower Ass'n*, 310 N.W.2d 730, 734 (N.D. 1981).

160. *Worthington Condo. Unit Owners' Ass'n v. Brown*, 566 N.E.2d 1275, 1279 (Ohio Ct. App. 1989) (“[I]f a declaration has provided notice . . . to a potential purchaser that the condominium association may amend the declaration, then the fact that the purchaser has not foreseen a *particular* amendment is not dispositive.”); *Levandusky v. One Fifth Ave. Apartment Corp.*, 553 N.E.2d 1317, 1320 (N.Y. 1990) (“[A]greement to submit to the decisionmaking authority of a cooperative board is voluntary . . .”).

161. *Natelson*, *supra* note 66, at 68 (“The courts review . . . [common-interest-communities] decisions on a reasonableness standard not because that standard defines the scope of consent, but because . . . the standard serves as a plausible *substitute* for consent.”).

162. *Sterk*, *supra* note 66, at 286–87 (“Few homeowners would believe that when purchasing their homes . . . they ceded to the association the power to act unreasonably.”).

163. An early court relied on this rationale to review a common-interest-community regulation, but it was an easement interpretation case, not a covenants case. *See Drabinsky v. Sea Gate Ass'n*, 146 N.E. 614, 615–16 (N.Y. 1925).

164. As the United States Court of Appeals for the First Circuit noted:

The principle is well established: “That in every contract there is an implied covenant that neither party shall do anything which will have the effect of destroying or injuring the right of the other party to receive the fruits of the contract, which means that in every contract there exists an implied covenant of good faith and fair dealing.”

*Uproar Co. v. Nat'l Broad. Co.*, 81 F.2d 373, 376–77 (1st Cir. 1936) (quoting *Kirke La Shelle Co. v. Armstrong Co.*, 188 N.E. 163, 167 (N.Y. 1933)).

165. For example, specific performance will not be ordered if enforcement would be unreasonable, RESTATEMENT (SECOND) OF CONTRACTS § 364(1)(b) (AM. L. INST. 1981); similarly, a grantor's approval clauses are read to include a reasonableness requirement, *Donoghue v. Prynwood Corp.*, 255 N.E.2d 326, 329 (Mass. 1970).

166. Interpretation was not necessary in the original Florida and Missouri cases discussed, *see supra* notes 146, 148, as the litigated declarations specifically referred to the board's power to adopt “reasonable rules and regulations.” *Hidden Harbour Ests., Inc. v. Norman*, 309 So. 2d 180, 181 (Fla. Dist. Ct. App. 1975)

nature of the relationship between owners in a common-interest community, an assumption that parties expect counterparties to enforce their rights reasonably is particularly appropriate.<sup>167</sup>

Thus, to meet covenant law's notice requirement—and thereby be fair toward owners who buy land based on expectations respecting what can be done with that land—a common-interest-community regulation adopted post-purchase must meet a two-step test. The regulation must fall within the community board's powers as enumerated in the declaration and it must be a reasonable exercise of those powers.<sup>168</sup> While early courts in Florida, Missouri, Texas, and elsewhere did reach this result,<sup>169</sup> they never provided the doctrinal—and normative—explanation. Therefore, the reasonableness test that was actually a natural outgrowth of traditional covenant law requirements took the unfortunate shape of casual dictum.

#### D. Courts' Current Approach to Common-Interest-Community Decisions

1970s courts' failure to explicitly ground the reasonableness requirement in property law contributed to the test's erosion in the ensuing decades.<sup>170</sup> Even when they still insisted on reasonableness, courts showed great latitude toward common-interest-community decisions. In none of the early cases introducing the requirement was reasonableness used to actually strike down the contested community regulation. Indeed, the Florida court of appeals first announcing the standard specifically employed it to reverse the lower court's refusal to enforce a community's rule.<sup>171</sup> The early decisions proclaiming the reasonableness requirement, while sparse in allusions to any property law source,<sup>172</sup> were rich with assertions highlighting the importance of unchaining common-interest-community boards.<sup>173</sup> These assertions were often lifted from

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(emphasis added); *Ryan v. Baptiste*, 565 S.W.2d 196, 197 (Mo. App. 1978) (emphasis added). The courts did not explicitly rely on that fact though. See *Hidden Harbour*, 309 So. 2d at 181-82; *Ryan*, 565 S.W.2d at 198.

167. On relational contracts, see Charles J. Goetz & Robert E. Scott, *Principles of Relational Contracts*, 67 VA. L. REV. 1089, 1127 (1981).

168. See James J. Scavo, *Dispute Resolution in a Community Association*, 17 URB. L. ANN. 295, 317 (1979).

169. See *Hidden Harbour*, 309 So. 2d. at 182; *Ryan*, 565 S.W.2d at 198; *Holleman v. Mission Trace Homeowners Ass'n*, 556 S.W.2d 632, 636 (Tex. Civ. App. 1977).

170. For example, the Wisconsin court adopting the rule explained that it was part of the equity analysis that precedes an injunction. *Le Febvre v. Osterndorf*, 275 N.W.2d 154, 159 (Wis. Ct. App. 1979). This reasoning could not explain why the analysis should be followed in cases where the requested remedy was damages. As the state supreme court later clarified, "Such equitable principles require the enforcement of a contract's terms be reasonable, not that the terms themselves be reasonable." *Solowicz v. Forward Geneva Nat'l*, 2010 WI 20, ¶ 45, 780 N.W.2d 111, 127.

171. See *Hidden Harbour*, 309 So. 2d at 180.

172. Consider an Ohio court's reasoning that amounted to one rather abstract claim: "We do not, though, endorse the view that a person who voluntarily enters the ranks of condominium ownership surrenders all individual property rights. Individual property receives some protection in the condominium arrangement, although less than that accorded non-condominium property." *Worthinglen Condo. Unit Owners' Ass'n v. Brown*, 566 N.E.2d 1275, 1277 (Ohio Ct. App. 1989).

173. Note, *supra* note 150, at 659-63 (noting this tendency).

decisions dealing with business associations.<sup>174</sup> Indeed, some courts explained their initial decision to subject common-interest-community decisions to review as owing to the community board's similarity to the corporate board.<sup>175</sup>

The references to business associations offered more than mere inspiration. The common-interest community's legal status is often that of a corporation.<sup>176</sup> Even if covered by specific statutes, condominiums and homeowners associations are incorporated under state laws.<sup>177</sup> Their key design feature is that of the business corporation: an owner-elected board of directors managing the entity's affairs.<sup>178</sup>

The emphasis on the common-interest community's corporate nature as demanding a weak form of review would soon lead courts to further liberalize the standard of review they employed. Reasonableness's grounding in property law's notice requirement having been largely ignored, courts came to question the standard's doctrinal rationale. One court, wholly committed to the analogy between the common-interest community and the corporation, explicitly wondered why the reasonableness standard that "originat[ed] in the quite different world of governmental agency decisionmaking . . . found favor with courts reviewing board decisions."<sup>179</sup> Following such criticisms, courts in the nation's most populous states announced the abandonment of the reasonableness test within two decades of its introduction.<sup>180</sup> In its stead, those courts and the others that soon followed them embraced a laxer standard that is more readily associated with corporate law.<sup>181</sup>

Most treatises and casebooks today still identify reasonableness as the leading review standard for common-interest-community board decisions.<sup>182</sup>

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174. *Holleman*, 556 S.W.2d at 635 (introducing the permissive reasonableness standard (citing *Hoyer v. San Antonio Real Est.*, 297 S.W.2d 214 (Tex. Civ. App. 1956))).

175. *Papalexiou v. Tower W. Condo.*, 401 A.2d 280, 285 (N.J. Super. Ct. Ch. Div. 1979) ("The actions of the board of directors of a corporation must meet the test of reasonableness. This standard also applies to the actions of the governing body of a condominium."); *Schwarzmann v. Ass'n of Apartment Owners*, 655 P.2d 1177, 1181 (Wash. Ct. App. 1982) ("Like their corporate counterparts, condominium directors have a fiduciary responsibility to exercise ordinary care in performing their duties and are required to act reasonably and in good faith."); *Levandusky v. One Fifth Ave. Apartment Corp.*, 553 N.E.2d 1317, 1321 (N.Y. 1990) ("Application of a similar doctrine is appropriate because a cooperative corporation is—in fact and function—a corporation, acting through the management of its board of directors, and subject to the Business Corporation Law.>").

176. See Eric T. Freyfogle, *A Comprehensive Theory of Condominium Tort Liability*, 39 FLA. L. REV. 877, 887 (1987).

177. See *id.* at 878.

178. See *id.* at 886.

179. *Levandusky*, 553 N.E.2d at 1322.

180. *Id.* at 1324.

181. Perhaps most extreme was a 2010 Wisconsin decision, where the court rejected claims that the community declaration should be subject to the reasonableness requirement it normally applies to covenants. *Solowicz v. Forward Geneva Nat'l*, 2010 WI 20, ¶ 2, 780 N.W.2d 111, 115. The court insisted that the declaration "is not simply a covenant." *Id.* ¶ 43, 780 N.W.2d at 126.

182. See, e.g., RESTATEMENT (THIRD) OF PROP.: SERVITUDES § 6.7(1) (AM. L. INST. 2000) ("Except as limited by statute or the governing documents, a common-interest community has an implied power to adopt

However, a survey of current decisions indicates that reasonableness is no longer the majority test.<sup>183</sup> Rather, most courts have shifted to another test: the business judgment rule, imported from corporate law.<sup>184</sup>

Under the business judgment rule, courts presume that corporate board decisions were made in good faith and accordingly do not substantively review them.<sup>185</sup> Most courts applying the rule still engage in procedural review to verify that the corporate board's decision-making process was rational.<sup>186</sup> Thus, while the review of a corporate board's decisions is circumspect, a court "may still review *how* those decisions are made."<sup>187</sup>

Courts began transplanting corporate law's business judgment rule into the property law of common-interest communities almost imperceptibly—framing it as mere implementation of the then existing reasonableness standard. The rule was first mentioned in a common-interest-community case by the Colorado Court of Appeals which employed it to legitimize a board decision that a lower court had struck down.<sup>188</sup> That appeal ruling, though, could hardly be said to have truly transported into property law the corporate law rule, which, as noted, focuses on procedural review. The Colorado appeals court was reversing a lower court's holding that was specifically based on faulty procedures the defendant common-interest community's board had employed.<sup>189</sup> Five years later, in 1979, a New Jersey court came closer to applying the rule as known in corporate law.<sup>190</sup> It explained that under the business judgment rule, "Courts will not second-guess the actions of directors unless it appears that they are the result of fraud, dishonesty or incompetence."<sup>191</sup> While the court did not mention the importance of good decision-making processes, it only upheld the contested common-interest-

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reasonable rules."); 1 GARY A. POLIAKOFF, *THE LAW OF CONDOMINIUM OPERATIONS* § 1:25 (Sept. 2022 update) ("The standard of reasonableness serves as a limitation on the unfettered power of associations."); DUKEMINIER, *supra* note 16, at 952; SHELDON KURTZ ET AL., *CASES AND MATERIALS ON AMERICAN PROPERTY LAW* 1123 (6th ed. 2012). While some treatises acknowledge the more deferential business judgment rule, they describe it as applying to exercises of the board's authority to make rules, while rules themselves are still reviewed for reasonableness. *See* POLIAKOFF, *supra*, §§ 4:32–4:33 ("For . . . unrecorded restrictions, the standard for validity is 'reasonableness.' . . . In reviewing the reasonableness of the board's exercise of its rule-making authority, 'absent claims of fraud, self-dealing unconscionability or other misconduct,' courts have applied the business judgment rule which limits the court's inquiry to whether the action was authorized, taken in good faith and in furtherance of the legitimate interests of the corporation.").

183. *See infra* notes 204–205 and accompanying text.

184. *See* RESTATEMENT (THIRD) OF AGENCY § 8.08 (AM. L. INST. 2022).

185. *See, e.g.*, *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946, 954 (Del. 1985).

186. *See, e.g.*, MODEL BUS. CORP. ACT § 8.30 off. cmt. (1969) (AM. BAR ASS'N, amended 2016).

187. Schanzenbach & Shoked, *supra* note 31, at 615.

188. *Rywalt v. Writer Corp.*, 526 P.2d 316, 317 (Colo. App. 1974).

189. *Id.* at 317–18.

190. *Papalexiou v. Tower W. Condo.*, 401 A.2d 280 (N.J. Super. Ct. Ch. Div. 1979).

191. *Id.* at 286.



community board decision after highlighting the exceedingly informed processes preceding it.<sup>192</sup>

Still, the New Jersey court did not acknowledge the major differences between the business judgment rule and the reasonableness standard that other courts, whose decisions it favorably cited, had adopted. Quite the opposite:

The actions of the board of directors of a corporation must meet the test of reasonableness. This standard also applies to the actions of the governing body of a condominium.

....

The refusal to enforce arbitrary and capricious rules promulgated by governing boards of condominiums is simply an application of the “business judgment” rule.<sup>193</sup>

It was not until ten years later, in 1990 when the New York court adopted the business judgment rule for the analysis of common-interest-community decisions,<sup>194</sup> that the business judgment rule and the previously dominant reasonableness test were clearly distinguished. Indeed, the New York court explicitly rejected the reasonableness test which the lower court had applied in the appealed decision.<sup>195</sup>

It further noted:

The difference between the reasonableness test and the [business judgment] rule we adopt is . . . [that] although in practice a certain amount of deference appears to be accorded to board decisions, reasonableness review permits—indeed, in theory requires—the court itself to evaluate the merits or wisdom of the board’s decision.

The more limited judicial review embodied in the business judgment rule is preferable.<sup>196</sup>

A decade later, California, which, at the time, was home to about a fifth of the nation’s condominium units,<sup>197</sup> followed New York’s lead and formally jettisoned reasonableness.<sup>198</sup> Forced to choose between the trial court that had adopted the business judgment rule and the court of appeals that had insisted on reasonableness, the Supreme Court of California sided with the trial court.<sup>199</sup>

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192. *See id.* at 286–87.

193. *Id.* at 285 (citation omitted).

194. *Levandusky v. One Fifth Ave. Apartment Corp.*, 553 N.E.2d 1317 (N.Y. 1990).

195. *Id.* at 1322.

196. *Id.* (citation omitted).

197. U.S. DEP’T OF COM., BUREAU OF THE CENSUS, STATISTICAL BRIEF (1994), <https://www2.census.gov/library/publications/1994/demographics/sb94-11.pdf>.

198. *Lamden v. La Jolla Shores Clubdominium Homeowners Ass’n*, 980 P.2d 940, 942 (Cal. 1999).

199. *Id.*

It dismissed arguments—founded on its own precedents<sup>200</sup>—that common-interest-community board decisions adopted after units sold could not be enforceable covenants because owners lacked notice.<sup>201</sup> Sidestepping property-law concerns respecting expectations, it grounded its decision in arguments typical of the corporate context.<sup>202</sup>

The New York and California court decisions were, perhaps inevitably, influential.<sup>203</sup> Other states' courts have since tended to adopt the same approach: replacing reasonableness with the business judgment rule. As of the writing, twenty-seven states appear to follow it<sup>204</sup> while only twelve states and the District of Columbia still clearly retain reasonableness.<sup>205</sup> Of course, the demarcation line may be somewhat porous.<sup>206</sup> Courts might announce adherence to one standard while in fact applying the other.<sup>207</sup> They might focus

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200. *See* *Nahrstedt v. Lakeside Vill. Condo. Ass'n*, 878 P.2d 1275 (Cal. 1994) (discussing the enforceability of covenants included in the declaration, the court there explained that those are different from covenants the board adopted later because an owner had full notice of the included covenants when buying. So it stood to reason that in contrast, a later board decision should not enjoy such leeway); *see also Lamden*, 980 P.2d at 949.

201. *Lamden*, 980 P.2d at 942.

202. *Id.* at 953–54.

203. A year before New York's decision, an Ohio court, considering as a matter of first impression the validity of board regulations, noted, without even mentioning the rule as an alternative, that other states had generally adopted a reasonableness requirement. *Worthington v. Brown*, 566 N.E.2d 1275, 1277 (Ohio Ct. App. 1989).

204. States adopting the rule expressly, or applying a deferential standard closely resembling it, are as follows: *Colo. Homes, Ltd. v. Loerch-Wilson*, 43 P.3d 718, 724–25 (Colo. App. 2001); *Williams v. 5300 Columbia Pike Corp.*, 901 F. Supp. 208 (E.D. Va. 1995) (applying Delaware law); *Abdullah v. Winslow*, 823 S.E.2d 872, 875–76 (Ga. Ct. App. 2019); *Lee v. Puamana Cmty. Ass'n*, 128 P.3d 874, 888 (Haw. 2006); *Leppaluoto v. Warm Springs Hollow Homeowners Ass'n*, 752 P.2d 605, 608 (Idaho 1988); *Henderson Square Condo. Ass'n v. LAB Townhomes*, 2015 IL 118139, ¶ 77, 46 N.E.3d 706, 727; *Oberbillig v. W. Grand Towers Condo. Ass'n*, 807 N.W.2d 143, 154–56 (Iowa 2011); *Williams v. Randall*, No. 115,586, 2017 WL 1369953, at \*7 (Kan. Ct. App. Apr. 14, 2017); *America v. Sunspray Condo. Ass'n*, 2013 ME 19, ¶¶ 14–16, 61 A.3d 1249, 1255–56; *Robbins v. Penn Ctr. House Inc.*, 138 A.3d 734, 743–44 (Pa. Commw. Ct. 2016) (applying Maryland law); *MJ Dev. Co. v. Inn at Bay Harbor Ass'n*, No. 330496, 2017 WL 726591, at \*2 (Mich. Ct. App. Feb. 23, 2017); *Smith v. Ridgeview Homeowner's Ass'n*, No. A10–1122, 2011 WL 1743787, at \*1 (Minn. Ct. App. May 9, 2011); *Schaefer v. Eastman Cmty. Ass'n*, 836 A.2d 752, 755 (N.H. 2003); *Alloco v. Ocean Beach & Bay Club*, 192 A.3d 24, 30 (N.J. Super. Ct. App. Div. 2018); *Levandusky v. One Fifth Ave. Apartment Corp.*, 553 N.E.2d 1317, 1322–23 (N.Y. 1990); *Happ v. Creek Pointe Homeowner's Ass'n*, 717 S.E.2d 401, 406–07 (N.C. Ct. App. 2011); *Agassiz W. Condo. Ass'n v. Solum*, 527 N.W.2d 244, 248 (N.D. 1995); *Burgoyne v. Pinecrest Cmty. Ass'n*, 924 A.2d 675, 682–83 (Pa. Super. Ct. 2007); *Dockside Ass'n v. Detyens*, 362 S.E.2d 874, 874 (S.C. 1987); *Ass'n of Regency Park Condos. v. Thomasson*, 878 S.W.2d 560, 565–66 (Tenn. Ct. App. 1994); *Fort Pierce Indus. v. Shakespeare*, 2016 UT 28, ¶¶ 26–29, 379 P.3d 1218, 1229–30; *Schwarzmann v. Ass'n of Apartment Owners*, 655 P.2d 1177, 1180 (Wash. Ct. App. 1982); *Mueller v. Zimmer*, 2005 WY 156, ¶ 21, 124 P.3d 340, 352–53.

205. The states are Alaska, Kentucky, Louisiana, Massachusetts, Mississippi, Missouri, Nebraska, New Mexico, Ohio, Rhode Island, Virginia, and Wisconsin.

206. *See, e.g., Levandusky*, 553 N.E.2d at 1323 (arguing that the difference between the test the court suggested and that the dissent proposed was “a matter of label”).

207. For example, in an Arkansas case, the court adopted a “reasonableness” standard but tested reasonableness by applying the factors the business judgment rule uses: “(1) whether the decision or rule is arbitrary, (2) whether the decision or rule is applied in an even-handed or discriminatory manner; and (3) whether the decision or rule was made in good faith for the common welfare of the owners and occupants of the condominium.” *Hutchens v. Bella Vista Vill. Prop. Owners' Ass'n*, 110 S.W.3d 325, 330 (Ark. Ct. App.

more on a desired result than on a doctrinal test (and, for example, only mention the business judgment rule in cases where they side with a community board).<sup>208</sup> Formal categories always have their limits.<sup>209</sup> Still, formal categories and rhetorical shifts are not meaningless. Courts' tightening embrace of the business judgment rule indicates eagerness to profess increased deference to common-interest-community decisions.

From our vantage point in 2023, the trend in the law's treatment of common-interest communities thus materializes as clear. As this new mode of property-ownership rose in prominence, property law strained to accommodate it. Early on, covenants doctrine was reinterpreted so that it could serve as basis for creating common-interest communities. Later, courts also assented to the enforcement of common-interest-community rules adopted after the community's creation, subject to a requirement that those rules be reasonable. More recently, focusing on corporate law notions and ignoring the requirement's (mostly unstated) property-law logic, courts have drifted away from reasonableness and toward the more permissive business judgment rule. This turn to corporate law must be normatively assessed—a task the next Part will undertake.

## II. THE FAILINGS OF THE LAW OF COMMON-INTEREST COMMUNITIES

Courts have rendered the law much more hospitable to common-interest-community powers by shifting the core of their analysis away from property law's covenants concerns and toward corporate law concerns. Some observers have argued that courts should not have instigated this move without first meaningfully comparing the two underlying entities' natures.<sup>210</sup> These critics claim that a principled comparison shows that in its most pertinent attributes, the common-interest community differs from the corporation and thus the business judgment rule is inappropriate for it.<sup>211</sup> These insights are mostly persuasive. But this Article seeks to highlight another way in which American courts' turn to corporate law when designing attitudes toward the common-interest community was uninformed. Whether or not courts mistook the nature

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2003). See also *Riverside Park Condos. v. Lucas*, 2005 ND 26, ¶¶ 14, 17, 691 N.W.2d 862, 871–72 (explaining that “[a]ctions of a condominium’s board of directors are reviewed under the business-judgment rule” but then applying “the reasonableness test of the business judgment rule”).

208. Compare *Hidden Harbour Ests., Inc. v. Norman*, 309 So. 2d 180, 182 (Fla. Dist. Ct. App. 1975) (“[W]e believe the test is reasonableness. If a rule is reasonable the association can adopt it; if not, it cannot.”), with *Farrington v. Casa Solana Condo. Ass’n*, 517 So. 2d 70, 71–72 (Fla. Dist. Ct. App. 1987) (citing *Hidden Harbour Estates* for the proposition that the business judgment rule applies to maintenance decisions).

209. See generally Felix S. Cohen, *Transcendental Nonsense and the Functional Approach*, 35 COLUM. L. REV. 809 (1935).

210. See, e.g., Pollack, *supra* note 66, at 852–53; Sterk, *supra* note 66, at 306–19.

211. See, e.g., Pollack, *supra* note 66, at 852–53; Sterk, *supra* note 66, at 306–19.

of the corporation when equating the common-interest community to it, they mistook the nature of the corporate law doctrine they imported into common-interest-community law. That is, courts transporting the business judgment rule into property law disregarded the rule's function in corporate law.

Common-interest-community law has ignored a basic corporate law tenet: the business judgment rule is a standard of review for a specific type of board decisions.<sup>212</sup> Board decisions of other types are subject to a more demanding standard. As many common-interest-community decisions resemble corporate disputes that fall into the latter category, the rule should be applied much more selectively than it currently is in common-interest-community law.

This Part first clarifies the business judgment rule's corporate-law function. The corporate-law rule applies to cases in which solely the director's competence is challenged, not when the director's impartiality is questioned. Corporate law defines impartiality broadly to include structural conflicts of interest. This Part then shows that in applying the business judgment rule in common-interest-community law, courts have failed to internalize this broad definition of impartiality. They only refrain from resorting to the rule in cases of flagrant community board corruption. Unfortunately, as this Part concludes by explaining, even when not involving obvious corruption, many of the decisions adopted in the common-interest-community setting correspond to the broad definition of interested decisions that corporate law removes from the realm of the business judgment rule.

#### *A. Corporate Law's Business Judgment Rule Only Applies to Disinterested Decisions*

The business judgment rule is "corporate law's central doctrine."<sup>213</sup> Therefore, to understand its original—and limited—province, we must appreciate the basic tension corporate law presents. The core problem corporate law contends with arises from the separation of ownership from management that is innate—and vital—for the corporate form.<sup>214</sup> The shareholders are the corporation's primary owners, yet they do not manage the corporation.<sup>215</sup> They leave that task to the board of directors who serve as their agents.<sup>216</sup> Because directors manage assets they do not own themselves, they might not pursue the best course of action for those assets.<sup>217</sup> The "agency

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212. Pollack, *supra* note 66, at 847–48.

213. Stephen M. Bainbridge, *The Business Judgment Rule as Abstention Doctrine*, 57 VAND. L. REV. 81, 81 (2004).

214. See ADOLF A. BERLE, JR. & GARDINER C. MEANS, *THE MODERN CORPORATION AND PRIVATE PROPERTY* 4–5 (1933).

215. *Id.*

216. Bainbridge, *supra* note 213, at 103 n.114.

217. Schanzenbach & Shoked, *supra* note 31, at 568.

problem” inherent to divorcing control from ownership consists of at least two distinct risks: a risk of unsound management (the agent will be careless with assets not their own) and a risk of corruption (the agent will use assets that are not their own to benefit themselves).<sup>218</sup> To solve the agency problem, the law subjects agents, such as corporate directors, to fiduciary duties: a duty of care treating the risk of unsound management and a duty of loyalty tending to the risk of corruption.<sup>219</sup> The duty of care requires that the agent exercise the degree of care that an ordinarily prudent person would follow.<sup>220</sup> The duty of loyalty prohibits faithlessness and self-dealing.<sup>221</sup>

The business judgment rule shields a director from liability for an alleged breach of her fiduciary duty if, in making the challenged decision, she was exercising her business judgment.<sup>222</sup> However, a director can only invoke the rule as a defense when accused of breaching the duty of care.<sup>223</sup> The rule is wholly irrelevant for duty of loyalty cases.<sup>224</sup> As the United States Court of Appeals for the Seventh Circuit unequivocally announced: “If a director breaches the fiduciary duty of loyalty . . . the business judgment rule affords no protection.”<sup>225</sup> An uncontested precondition for resort to the rule is proof that the director had no personal interest in the challenged decision,<sup>226</sup> a conflict of interests,<sup>227</sup> or otherwise acted in bad faith.<sup>228</sup> These requirements are only logical given the nature—and, indeed, name—of the business judgment rule. Any director pursuing their own interests cannot be said to have made a judgment call respecting the corporation’s business interests.<sup>229</sup> Therefore, in these cases, courts’ scrutiny of the director’s decision is greater than under the business judgment rule: the metric is reasonableness (sometimes also called “fairness” or “entire fairness”),<sup>230</sup> demanding the decision be “fair and serve[] the best interests of the corporation and its shareholders.”<sup>231</sup>

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218. *Id.*, at 567–68; Darian M. Ibrahim, *Public or Private Venture Capital?*, 94 WASH. L. REV. 1137, 1146 (2019) (“Agency costs inside corporations come in two main forms: opportunism and mismanagement.”).

219. *Mills Acquisition Co. v. Macmillan, Inc.*, 559 A.2d 1261, 1280 (Del. 1989).

220. *Id.*

221. *Guth v. Loft, Inc.*, 5 A.2d 503, 510 (Del. 1939) (“Corporate officers and directors are not permitted to use their position of trust and confidence to further their private interests.”).

222. 18B AM. JUR. 2D *Corporations*, *supra* note 46, § 1450.

223. *Id.*

224. 3 WILLIAM MEADE FLETCHER, FLETCHER CYCLOPEDIA OF THE LAW OF CORPORATIONS, DUTY OF LOYALTY § 837.60 (rev. vol. 2018).

225. *Westmoreland Cnty. Emp. Ret. Sys. v. Parkinson*, 727 F.3d 719, 725 (7th Cir. 2013).

226. *Auerbach v. Bennett*, 393 N.E.2d 994, 1001 (N.Y. 1979).

227. *Warren v. Campbell Farming Corp.*, 2011 MT 324, ¶ 30, 363 Mont. 190, 204, 271 P.3d 36, 46.

228. *Lodis v. Corbis Holdings, Inc.*, 292 P.3d 779, 795 (Wash. Ct. App. 2013).

229. *Aronson v. Lewis*, 473 A.2d 805, 816 (Del. 1984) (“The requirement of director independence inheres in the conception and rationale of the business judgment rule. The presumption of propriety that flows from an exercise of business judgment is based in part on this unyielding precept.”).

230. 18B AM. JUR. 2D *Corporations*, *supra* note 46, § 1458.

231. *Shoen v. Shoen*, 804 P.2d 787, 794 (Ariz. Ct. App. 1990); *see also* *Cookies Food Prods., Inc. v. Lakes Warehouse Distrib., Inc.*, 430 N.W.2d 447, 453 (Iowa 1988).

Courts have stressed that the director's independence must be established before they will find the disinterestedness required to apply the more forgiving business judgment rule.<sup>232</sup> "The requirement of director independence inheres in the conception and rationale of the business judgment rule. The presumption of propriety that flows from an exercise of business judgment is based in part on this unyielding precept."<sup>233</sup> Independence means that the director's decision be "based on the corporate merits of the subject before the board rather than extraneous considerations or influences."<sup>234</sup>

Such extraneous considerations or influences are present if the director stands in a "dual relation": to the corporation and to another interest.<sup>235</sup> Courts define this concept of another interest broadly<sup>236</sup> to mean any benefit that will not "devolve[] upon the corporation or all stockholders generally."<sup>237</sup> Certain circumstances suffice to immediately and inherently raise an inference of conflict of interests.<sup>238</sup> "[T]he realities of the decision-making context can subtly undermine the decisions of even independent and disinterested directors" and thus foreclose on the possibility of recourse to the business judgment rule.<sup>239</sup>

Because the law's focus is thus squarely placed on the director's structural independence, corporate law's definition of a duty of loyalty breach extends well beyond instances that meet lay notions of corruption or bad faith.<sup>240</sup> The legal test is not subjective: even if the director never believed that they were promoting an interest not all stockholders share, they could be found in violation.<sup>241</sup> The director's heart might be pure, but if circumstances are such that the director's decision could serve interests of that director which not all shareholders hold, the business judgment rule cannot remove the cloud of suspicion.<sup>242</sup> Relatedly, the duty of loyalty forbids *interested* decisions, a prohibition encompassing much more than flagrant self-dealing.<sup>243</sup> A person can easily be interested in a decision—that is, derive some benefit from it—even if that decision does not directly put money in that person's pocket. The

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232. *Aronson*, 473 A.2d at 814–15.

233. *Id.* at 816.

234. *Id.*

235. *Auerbach v. Bennett*, 393 N.E.2d 994, 1006 (N.Y. 1979).

236. *Omnibank of Mantee v. United S. Bank*, 607 So. 2d 76, 90 (Miss. 1992).

237. *Aronson*, 473 A.2d at 812.

238. *Lee v. Interinsurance Exch. of the Auto. Club of S. Cal.*, 57 Cal. Rptr. 2d 798, 811 (Ct. App. 1996).

239. *Reis v. Hazelett Strip-Casting Corp.*, 28 A.3d 442, 457 (Del. Ch. 2011).

240. *FLETCHER*, *supra* note 224 ("The duty of loyalty is a broad encompassing duty, that in appropriate circumstances is capable of impressing a special obligation upon a director or officer in any of their relationships with the corporation.").

241. *Id.*

242. *Omnibank of Mantee v. United S. Bank*, 607 So. 2d 76, 90 (Miss. 1992).

243. *Stone ex rel. AmSouth Bancorporation v. Ritter*, 911 A.2d 362, 370 (Del. 2006) ("[T]he fiduciary duty of loyalty is not limited to cases involving a financial or other cognizable fiduciary conflict of interest.").

duty of loyalty removes from the business judgment rule's realm any decisions "affected by an *inherent* conflict of interest."<sup>244</sup>

In sum, under corporate law, the test that must be satisfied before resorting to the business judgment rule is objective and comprehensive.<sup>245</sup> Blatant self-dealing situations are not the only cases subject to a more demanding reasonableness test. Instances when a director has a dual relation that entails a partial, rather than full, overlap between that director's interests and those of all corporation members are similarly subject to heightened review.<sup>246</sup> As shall be seen next, courts importing the business judgment rule into common-interest-community law have failed to note the full breadth of this definition of conflicts of interest prevalent in corporate law.

*B. The Limited Conditions Where Common-Interest-Community Decisions Have Been Deemed Interested*

Courts transplanting the business judgment rule into common-interest-community law have acknowledged that it does not apply to interested board decisions.<sup>247</sup> They have thus mostly refrained from applying the business judgment rule in the most obvious cases to which it would not have applied in corporate law.

Courts often note that a common-interest-community decision will not be upheld if made in bad faith.<sup>248</sup> They have struck down decisions where a common-interest-community board member clearly engaged in self-dealing: the board member committed the community to a transaction with an entity they own,<sup>249</sup> conveyed a financial benefit upon themselves,<sup>250</sup> or pursued a personal vendetta against another member.<sup>251</sup>

Lawmakers have focused this strict attitude on one specific category of common-interest-community decisions with obvious risks of self-dealing: those involving developer-controlled boards. As Subpart I.A explained, the common-interest-community model's appeal to developers is the control it affords them over already-sold units.<sup>252</sup> This power is vital for the developer who seeks to preserve the value of remaining units that the developer is still trying to sell. As discussed, the developer's control over already-sold units is exercised through

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244. 18B AM. JUR. 2D *Corporations*, *supra* note 46, § 1494 (emphasis added).

245. FLETCHER, *supra* note 224.

246. Guth v. Loft, Inc., 5 A.2d 503, 510 (Del. 1939).

247. See, e.g., Kai v. Bd. of Dirs. of Spring Hill Bldg. 1 Condo. Ass'n, 2020 IL App (2d) 190642, ¶ 171 N.E.3d 42.

248. *Id.* at 53.

249. POLLAKOFF, *supra* note 182, § 2.7.

250. Willens v. 2720 Wis. Ave. Coop. Ass'n, 844 A.2d 1126, 1136–38 (D.C. 2004) (refusing to apply the rule to a challenged transaction whereby a co-op board forgave debts of some but not all members).

251. Boisson v. 4 E. Hous. Corp., 514 N.Y.S.2d 374, 375 (App. Div. 1987).

252. See *supra* text accompanying notes 79–86.

restrictions inserted into the common-interest-community declaration before units sell.<sup>253</sup> But the developer can further supplement these restrictions later with new rules—through the developer’s control of the common-interest-community board. Until all units are sold, the developer enjoys disproportionate power on the board.<sup>254</sup> Some of this power is natural: as the developer owns multiple unsold units, the developer holds more voting rights in board elections than other individual units’ buyers.<sup>255</sup> Even more dramatic in its effect, however, is the common practice whereby the developer retains control—often full control—of the board until all units (or at least a large number thereof) are sold.<sup>256</sup>

Because the developer’s central goal in exercising this control is to preserve or enhance market values of units the developer aims to sell, the developer’s interests often align with those of other owners. Everyone wants to see their property values increase. But the potential for the developer to pursue their own distinct interests is inescapably present: certain board decisions could make it easier for the developer to sell the last units they own, or otherwise enrich themselves, while decreasing the value of already-sold units.<sup>257</sup> For example, a developer could have the board change its bylaws to remove restrictions from unsold units that would still apply to already-sold units;<sup>258</sup> the developer could have the board allow the conversion into rentals of units the developer cannot sell;<sup>259</sup> or the developer could have the board sign an unfavorable lease with a firm the developer owns.<sup>260</sup>

As these practices embody obvious self-dealing, courts and legislatures have gradually curtailed them, setting specific rules to police decisions adopted while the board is developer-controlled. Courts applied the reasonableness standard to limit developer-controlled boards’ powers to rescind or amend regulations included in the original declaration.<sup>261</sup> State legislatures adopted laws mandating a timely transfer of board control to buyers.<sup>262</sup> Congress enacted a statute permitting boards to cancel service contracts an earlier board entered whilst under the developer’s thumb.<sup>263</sup> These regulatory moves conceived of the developer controlling a community board as an outside force whose external interest generates a potentially corruptive influence which must be

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253. See *supra* text accompanying notes 79–83.

254. MCKENZIE, *supra* note 72, at 128.

255. See *id.* at 128.

256. *Id.*

257. *Belvedere Condo. Unit Owners’ Ass’n v. R.E. Roark Cos.*, 617 N.E.2d 1075, 1080 (Ohio 1993).

258. *E.g.*, *Appel v. Presley Cos.*, 806 P.2d 1054, 1055 (N.M. 1991).

259. *E.g.*, *Scarfione v. P.C.-Plantation, LLLP*, 59 So. 3d 371, 371–72 (Fla. Dist. Ct. App. 2011).

260. *E.g.*, *Penthouse N. Ass’n v. Lombardi*, 461 So. 2d 1350, 1351 (Fla. 1984).

261. *E.g.*, *Appel*, 806 P.2d at 1056.

262. *E.g.*, 765 ILL. COMP. STAT. ANN. 605/18.2 (West 1999) (requiring turnover after 75% of units are sold or three years after a declaration is recorded, whichever is earlier).

263. 15 U.S.C. § 3607. See generally 15 U.S.C. § 3601.



curbed.<sup>264</sup> The permissive approach toward boards embodied in the business judgment rule has largely not been applied to this type of blatantly corrupt decision-making process.

But courts reviewing common-interest-community decisions have shown little willingness to extend this more demanding attitude outside such obvious cases of corruption.<sup>265</sup> Their understanding of the corporate law function of the business judgment rule reviewed in the preceding Subpart has thus only been partial. Corporate law naturally views blatantly corrupt decisions, like those this Subpart discussed, as interested. But those are not the only decisions corporate law regards as such. As described in Subpart II.A, corporate law is also concerned with decisions adopted by directors who are not independent—who, even if not clearly self-dealing, are situated in a structural conflict of interest.<sup>266</sup> Unfortunately, as shall be seen now, a great number of common-interest-community decisions fall into this category.

### C. *The Questionable Independence of the Common-Interest-Community Board*

Corporate law's business judgment rule, and the normative support for its laissez faire approach toward a given corporate board decision, assumes that in making that decision the board was not only not corrupt but also independent. When making many, indeed most, business decisions, a corporation's board can be characterized as such; but, as Subpart II.A showed, corporate law refuses to automatically accept that characterization in every case.<sup>267</sup> In turning to common-interest communities, however, the law fails to realize just how often assumptions respecting the community board's independence are detached from reality. As this Subpart explains, many common-interest-community decisions, even when not afflicted by obvious corruption, are particularly susceptible to inherent conflicts of interest—the chief impediment to the rule's application in corporate law.<sup>268</sup>

The similarity between the common-interest-community board and the corporate board induced courts, as Subpart I.D highlighted, to turn to corporate law's business judgment rule when treating the otherwise property law problem of common-interest-community decision-making.<sup>269</sup> But while

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264. RESTATEMENT (THIRD) OF PROP.: SERVITUDES § 6.20 cmt. a (AM. L. INST. 2000) (“Conflicts of interest are inherent in the developer’s role while it retains control of the association.”).

265. *E.g.*, *Frankel v. Bd. of Managers*, 112 N.Y.S.3d 65, 68 (App. Div. 2019) (insisting that the plaintiff provide evidence of actual “fraud, self-dealing, unconscionability, or other misconduct”).

266. *See supra* text accompanying notes 213–246.

267. 18B AM. JUR. 2D *Corporations*, *supra* note 46, § 1484 (“The business judgment doctrine, which forbids inquiry by the courts into the soundness of decisions made by the officers and directors of a corporation in the operation of its affairs, should not be interpreted to stifle legitimate inquiry by stockholders of management decisions which present ostensible situations of conflict of interest.”).

268. *Id.* § 1494.

269. *See supra* text accompanying notes 170–209.

some similarities unquestionably exist, the common-interest-community board does not truly replicate the corporate board model. The corporate form's keystone is a board of experts whom shareholders—the corporation's actual owners—elect.<sup>270</sup> The common-interest community's architecture purports to follow this template: unit owners elect board members to manage their property.<sup>271</sup> But, while very similar, the common-interest-community board is not the corporate board's spitting image—and what might appear a slight variation carries major normative ramifications.

Unlike the corporate board, the common-interest-community board is constituted not of experts, or of any other external actors, but of individual owners.<sup>272</sup> Some courts have realized that this characteristic removes a traditional justification corporate law notes for the resort to the business judgement rule: courts' need to defer to business experts' judgment.<sup>273</sup> Common-interest-community board members wield no special expertise unavailable to judges.<sup>274</sup> Still, as Subpart I.D showed, courts proceed to apply the rule to common-interest-community boards.<sup>275</sup> They reason that even if not experts, community board members, as member-owners, enjoy special insight into community needs. Thus, their judgments are preferable to those of external observers.<sup>276</sup>

Yet, the common-interest-community board's membership scheme drains the common-interest-community board, as compared to the corporate board, not only of expertise (as courts acknowledge) but also of independence (as they do not). The corporate board model assumes, and largely institutes, a management group of third parties that represent, but are not, the owners. The theory of corporate governance envisions a sharp divide between principals—shareholders—and agents—directors.<sup>277</sup> The common-interest community has no such division. Common-interest-community board members are both agents and principals. This is no mere technical difference. In stark contrast to

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270. *Smith v. Van Gorkom*, 488 A.2d 858, 895 (Del. 1985) (McNeilly, J., dissenting) (discussing directors' "business acumen, interest and expertise"), *overruled in part by* *Gantler v. Stephens*, 965 A.2d 695, 714 n.54 (Del. 2009) (holding that shareholder ratification could not cleanse interested decisions, only decisions the board had lacked authority to make).

271. See *supra* note 178 and accompanying text.

272. See CAL. CIV. CODE § 5105 (West 2022); CAL. CIV. CODE § 4160 (West 2014) (A "[m]ember" [of an association] means an owner of a separate interest.).

273. *Dodge v. Ford Motor Co.*, 170 N.W. 668, 684 (Mich. 1919) ("There is committed to the discretion of directors . . . the infinite details of business . . . The judges are not business experts.").

274. *Levandusky v. One Fifth Ave. Apartment Corp.*, 553 N.E.2d 1317, 1322 (N.Y. 1990) ("[D]ecisions of a cooperative board do not generally involve expertise beyond the usual ken of the judiciary[.]").

275. See *supra* text accompanying notes 170–209.

276. *Levandusky*, 553 N.E.2d at 1322 ("[A]t the least board members will possess experience of the peculiar needs of their building and its residents not shared by the court."); *Lamden v. La Jolla Shores Clubdominium Homeowners Ass'n*, 980 P.2d 940, 953–54 (Cal. 1999).

277. Michael C. Jensen & William H. Meckling, *Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure*, 3 J. FIN. ECON. 305, 309 (1976).

the corporate architecture, in the common-interest community, the agent is by definition not independent from some of the principals—as the agent is one of them. The solutions corporate theory recommends for the pure agency problem<sup>278</sup>—where one party, the “principal,” relies on actions taken by another, the “agent”<sup>279</sup>—cannot be perfectly applicable.

Unlike in the corporate context, all board members in the common-interest community always have a dual relation. They are agents but also principals: they are both managers and individual owners. As is axiomatic in corporate law, a dual relationship can generate a conflict of interests.<sup>280</sup> The dual relationship of the community board member engenders a structural conflict due to the possibility that the interests each relationship generates for the owner–board member will conflict. In her capacity as board member, the owner–board member’s relationship is with the community as a whole and the interests she must consider are only those benefiting all owners. In her capacity as an owner, the owner–board member’s relationship is with that owner–board member’s individual unit and the interests she considers are those benefitting her as the individual owner of her specific unit. If a board decision potentially increases the value of the board member’s own unit while decreasing the values of others, the agent–owner cannot be disinterested.

This would not be a problem if the law could safely assume that the two interests the owner–board member serves—the interests of all owners and their interests as specific individual owners—always overlap.<sup>281</sup> Yet, in similar contexts the law never makes a similar assumption. It recognizes the reality that the interests of an individual can diverge from those of any collective of which the individual forms a part.<sup>282</sup> Therefore, the bodies of law that deal with collectives—corporate law but also public law—dictate that when one group of members holds authority to manage the collective and exercises power over all members’ interests, courts must meaningfully review those decisions for fairness.<sup>283</sup>

One highly relevant example is corporate law’s treatment of majority shareholders. The business judgment rule does not apply to some decisions of majority shareholders.<sup>284</sup> The law acknowledges the fact that shareholders’

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278. *Id.*

279. *Id.* at 308.

280. *Omnibank of Mantee v. United S. Bank*, 607 So. 2d 76, 90 (Miss. 1992).

281. *See Fennell, supra* note 26, at 858 (“People within those communities may be heterogeneous with regard to the benefits they would derive from violating each of those many rules.”).

282. THE FEDERALIST NO. 10 (James Madison) (explaining that society will always, inevitably, have conflicting “factions”).

283. *E.g., United States v. Carolene Prods. Co.*, 304 U.S. 144, 152 n.4 (1938) (explaining that government decisions are subject to exacting judicial review—strict scrutiny—when endangering the interests of a “discrete and insular minorit[y]”).

284. *See* 18B AM. JUR. 2D *Corporations, supra* note 46, § 647.

interests can diverge<sup>285</sup> and that if one shareholder group controls the board, it can use its power to serve its own distinct interests.<sup>286</sup> In particular, a shareholder who holds the most shares often has interests that conflict with other shareholders' interests.<sup>287</sup> When exercising their power over the corporation's decision making, the majority shareholder can hardly be expected to be fully impartial. Majority shareholders and their board representatives, therefore, are subject to special fiduciary obligations toward other shareholders.<sup>288</sup> Some of their decisions, such as those that "oppress" minority shareholders' interests,<sup>289</sup> cannot be saved through appeal to the business judgment rule.<sup>290</sup>

In some situations, certain states go even further in scrutinizing the majority shareholder's decisions.<sup>291</sup> They establish special rules for closely-held corporations—corporations whose stock is not traded but is owned by a handful of shareholders often sharing some personal ties.<sup>292</sup> The risks of controlling-shareholder opportunism in these tight settings are particularly heightened as the majority shareholder is often also a director and manager.<sup>293</sup> Accordingly, some courts subject the decisions of controlling directors in closely-held corporations to particularly demanding review.<sup>294</sup> Minority shareholders can seek a remedy if a corporate decision benefitting the majority does not extend to them the same benefits.<sup>295</sup>

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285. Robert P. Bartlett, III, *Venture Capital, Agency Costs, and the False Dichotomy of the Corporation*, 54 UCLA L. REV. 37, 61 (2006) ("[A]n interinvestor conflict can exist among a company's investors and thereby give rise to a horizontal agency problem.").

286. See, e.g., 18B AM. JUR. 2D *Corporations*, *supra* note 46, § 1484 ("Directors . . . cannot serve themselves and the corporation at the same time.").

287. *Id.* § 649.

288. Although shareholders of a corporation ordinarily owe no fiduciary duties to the corporation or other shareholders, "[w]hen a shareholder exercises control over a corporation by directing its actions, a shareholder assumes the same fiduciary duties as those owed by a director to the corporation." *Id.* § 620.

289. See *id.* § 641.

290. See *id.* § 647.

291. See Michael A. Rosenhouse, *Majority's Fiduciary Obligation to Minority Shareholder of Close Corporation—Breach and Remedy*, 39 A.L.R. 6th 1, 1 (2008).

292. Edward B. Rock & Michael L. Wachter, *Waiting for the Omelet to Set: Match-Specific Assets and Minority Oppression in Close Corporations*, 24 J. CORP. L. 913, 916 (1999) ("Several traits typically characterize the closely held firm: there are few shareholders; no public market for the shares; and a substantial overlap between suppliers of capital and suppliers of labor."). The Internal Revenue Service defines a closely held corporation as having more than half of the value of its outstanding stock owned by five or fewer individuals. INTERNAL REVENUE SERV., U.S. DEP'T OF THE TREASURY, PUBLICATION 542 CORPORATIONS, at 3 (rev. Jan. 2022).

293. Rock & Wachter, *supra* note 292, at 916 ("Due to the overlap between managers and shareholders and the absence of public markets, the shareholder/managers of the close corporation are in continuous contact with each other. The lack of a public market causes the parties to be locked into their investments to a much greater extent than in either the partnership or the publicly traded corporation. Because the majority shareholders elect the directors and control the management of the corporation, minority shareholders are particularly vulnerable if there is a falling-out with the majority.").

294. E.g., *Donahue v. Rodd Electrotype Co. of New England*, 328 N.E.2d 505, 517 (Mass. 1975). The Delaware court rejected this approach and does not treat closely-held corporations differently in this regard. *Nixon v. Blackwell*, 626 A.2d 1366, 1379–81 (Del. 1993).

295. *Spangler v. Spangler*, 451 F. Supp. 3d 813, 826 (N.D. Ohio 2020).

The problem present in the unique case of the majority shareholder, which corporate law seeks to solve with these elevated fiduciary duties, is the problem inherent to all common-interest communities. Some owners make board decisions, and when their interests diverge from other owners' interests—as they sometimes inevitably do—those owners are prone to abuse the interests of the other owners. Corporate law's standard approach of deferring to decisions made by a disinterested board is ill-suited for such a context where a director, by design, lacks independence.<sup>296</sup>

Common-interest-community law must incorporate this insight. The interests of one unit owner or group of owners may not always overlap with the interests of all owners, generating a conflict of interests for all owner–board members.<sup>297</sup> Because of the lack of separation between some owners and the board, the concerns respecting the board's independence that corporate law stresses are not only apposite but magnified.<sup>298</sup> Corporate law demands from a board member “an undivided and unselfish loyalty to the corporation[,]” insisting “that there shall be no conflict between duty and self-interest.”<sup>299</sup> In contrast, a common-interest-community board member's duty will sometimes—when all owners' interests are not identical—conflict with the board member's self-interest as an owner. A decision the board member makes as a board member (say, to fund a temporary beautification project) could carry more benefits to a class of owners of which that board member forms part (say, owners who are currently marketing their units) than to others. Such an owner might not be acting in a flagrantly corrupt manner—unlike the developer exempting unsold units from restrictions—but that owner–board member is still not disinterested. The board member has a “positional conflict,”<sup>300</sup> making a deferential judicial attitude toward their decisions questionable under traditional corporate law principles.

Courts transplanted the business judgment rule into common-interest-community law with little attention to key doctrinal components that sustain the rule's normative logic.<sup>301</sup> Corporate law's limits on the rule's application

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296. Elizabeth Pollman, *Startup Governance*, 168 U. PA. L. REV. 155, 219 (2019) (discussing startups).

297. Two courts did take note of the fact “that the directors of a residential cooperative (or condominium) association will typically be unit owners who ‘will rarely be wholly disinterested’ in any decision the board may make.” *Willens v. 2720 Wis. Ave. Coop. Ass'n*, 844 A.2d 1126, 1136–38 (D.C. 2004); see also *In re Croton River Club, Inc.*, 52 F.3d 41, 44 (2d Cir. 1995). However, the courts refused to view it as preempting the rule. One even hypothesized that “it may be a justification for applying the rule with a degree of tolerance for some director interestedness where cooperative and condominium boards of directors are involved.” *Willens*, 844 A.2d at 1138. The other observed that “the typical conflicts of interest that inhere in such boards will not be sufficient to deprive decisions of the business judgment rule's protection.” *Croton River Club*, 52 F.3d at 44.

298. See Note, *supra* note 150, at 665.

299. *Guth v. Loft, Inc.*, 5 A.2d 503, 510 (Del. 1939).

300. *Reis v. Hazelett Strip-Casting Corp.*, 28 A.3d 442, 457 (Del. Ch. 2011).

301. Common-interest-community law has also largely been ignoring the fact that in corporate law, the rule serves primarily as a director's defense in personal liability suits. PRINCIPLES OF CORP. GOVERNANCE: ANALYSIS AND RECOMMENDATIONS § 4.01 (AM. L. INST. 1994). Of the original cases

were read narrowly and it was applied to virtually all common-interest-community decisions other than those involving blatant self-dealing. Yet in its original corporate law formulation, the rule was never intended to apply to cases where decision makers might consistently ignore other members' interests. As this Part showed, that eventuality might sometimes—perhaps oftentimes—materialize in the common-interest-community setting given the entity's unique organizational structure. Thus, for some common-interest-community decisions, the permissive approach the business judgment rule embodies is inadequate.

### III. THE LAW OF COMMON-INTEREST COMMUNITIES REIMAGINED

The preceding Part pointed out the error courts committed when they mechanically imported corporate law's business judgment rule into common-interest-community law. It concluded that given the rule's origins and logic, some common-interest-community decisions demand a different review standard. This closing Part translates those findings into an operational approach. First, it identifies the common-interest-community cases where decisions are structurally conflicted and hence require heightened review—reasonableness rather than the business judgment rule. Second, it shows how reasonableness analysis differs from business-judgment-rule analysis and can effectively be applied to those decisions.

#### A. *The Structural Conflicts of Interest Within Common-Interest Communities*

The common-interest community brings together multiple owners who individually own their units and collectively control their environment by (1) sharing public amenities and (2) exercising communal power over all owners' private property uses.<sup>302</sup> These elements are premised on mutuality.<sup>303</sup> All residents submit themselves to the communal way of life so that they all benefit from it together.<sup>304</sup> All owners are subject to restrictions and all benefit from

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importing the rule into common-interest-community law, only one involved personal liability claims against board members. *Schwarzmann v. Ass'n of Apartment Owners*, 665 P.2d 1177, 1180–81 (Wash. Ct. App. 1982). Few cases today involve such claims for damages. Pollack, *supra* note 66, at 876.

302. See POLIAKOFF, *supra* note 182, § 1.2, 1.15.

303. *Hidden Harbour Ests., Inc. v. Norman*, 309 So. 2d 180, 181–82 (Fla. Dist. Ct. App. 1975) (“[I]nherent in the condominium concept is the principle that . . . each unit owner must give up a certain degree of freedom of choice which he might otherwise enjoy in separate, privately owned property. Condominium unit owners comprise a little democratic sub society of necessity . . .”); *Nahrstedt v. Lakeside Vill. Condo. Ass'n*, 878 P.2d 1275, 1282 (Cal. 1994) (“[S]ubordination of individual property rights to the collective judgment of the owners association together with restrictions on the use of real property comprise the chief attributes of owning property in a common interest development.”).

304. *Burgess v. Pelkey*, 738 A.2d 783, 788–89 (D.C. 1999) (“[U]niformity[] [is] a principal purpose of cooperative and condominium living arrangements . . .”).

the enforcement of those same restrictions on their neighbors.<sup>305</sup> Each gives away part of their individual freedom; in exchange, they gain some control over their co-members.<sup>306</sup>

Mutuality renders residents interchangeable as far as common-interest-community policies go. It thus alleviates risks that an owner–board member may be structurally conflicted: by definition, a board decision affects the owner–board member’s interests as an individual owner just as it affects those of other owners. In fact, mutuality should eliminate any claim of unfairness a discontented owner could raise against a community decision.<sup>307</sup> That owner’s peers are just as affected by any contested decision. Even if today the unhappy owner views herself as particularly burdened, tomorrow the policy will burden the owner’s neighbor and benefit the owner.<sup>308</sup> Things even up.

Mutuality is so central to common-interest-community law because it is necessary to ensure the fairness in board decision-making that is a prerequisite for application of the business judgment rule under traditional corporate law tenets. Importantly, mutuality should also be seen as instituting the notice owners must have before a covenant is applied to them, as the traditional principles of property law reviewed in Part I require. A commonality of interests is at the heart of buyers’ expectations when they acquire units in a common-interest community. Buyers are on notice that a future community decision might be adopted that curtails their freedom—and the freedom of all their neighbors. In this way, even though the future community decision was unknown when an owner bought in, the owner can be held to have agreed to it.

If mutuality, which implies that overall all owners’ interests coincide, dispels conflict-of-interest risks in common-interest-community decision-making,<sup>309</sup> mutuality’s absence will characterize the cases where structural conflicts of interests demand stricter judicial review.<sup>310</sup> With no mutuality, those adopting the decision might acquire some personal advantage not equally enjoyed by all owners.<sup>311</sup> That decision is thus a poor fit for relaxed scrutiny under both

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305. See generally *Worthinglen Condo. Unit Owners’ Ass’n v. Brown*, 566 N.E.2d 1275, 1279 (Ohio Ct. App. 1989) (“[U]niformity in condominium living [is] . . . one of the purposes of condominium rules and regulations.”).

306. *E.g., id.* at 1276 (noting “the need in condominium living for a stable environment with the concomitant relinquishing of some measure of individuality”); *Villas W. II of Willowridge Homeowners Ass’n v. McGlothlin*, 885 N.E.2d 1274, 1279 (Ind. 2008) (“Property owners who purchase their properties subject to such restrictions give up a certain degree of individual freedom in exchange for the protections from living in a community of reciprocal undertakings.”).

307. See *Nabrstedt*, 878 P.2d at 1282.

308. See *Natelson*, *supra* note 66, at 80 (arguing that if the special harm to the complaining owner is limited she might still be a net gainer once all the decision’s effects are considered).

309. See *Levandusky v. One Fifth Ave. Apartment Corp.*, 553 N.E.2d 1317, 1321 (N.Y. 1990).

310. *Cf. Cede & Co. v. Technicolor, Inc.*, 634 A.2d 345, 361 (Del. 1993) (explaining that the duty of loyalty is breached whenever a director prioritizes an interest not shared by stockholders generally).

311. *Cf. FLETCHER*, *supra* note 224, § 884 (explaining that this violates loyalty obligations).

corporate law notions (focusing on agency problems) and property law ones (focusing on notice problems). This Part thus catalogues case types where a decision always affects different owner groups within the community differently. In these cases, members of one group would have an interest inherently conflicting with that of members of other groups; thus, no owner can make, in these cases, a wholly disinterested decision.

Three preliminary caveats. First, while the Part provides the first systemic and principled treatment of the overall problem, it is not written on a clean slate. Existing controversies and rulings serve as sources. Second, overlap exists between some of the categories identified. That overlap is of no concern because in all cases depicted, the legal result should be identical: heightened judicial review. Third, this list is not exhaustive. Other structural conflicts within common-interest communities might exist and the hope is that others—commentators and lawmakers—identify them in the future.

### 1. *Owner–Occupants versus Owner–Investors*

As noted throughout, courts tend to too easily equate the common-interest community with the corporation.<sup>312</sup> One flaw in the analogy owes to the disparate motivations leading owners to hold interests in each body. The difference is intuitive—all realize that a home is not a stock—yet it generates an underappreciated structural conflict of interest within the common-interest community that does not arise in the corporation.

An interest held in a corporation—a share—is a single thing: an investment.<sup>313</sup> Individuals buy and hold a share for one reason: to make money.<sup>314</sup> This goal unites shareholders.<sup>315</sup> They all desire that the corporation’s market value increase because then the value of their shares—which they hold solely due to their market value—climbs.<sup>316</sup> Thus, a corporate decision affects all shareowners’ interests identically.<sup>317</sup> Different owners might disagree on the best route to increase the corporation’s value, but if none are self-dealing (for example, seeking to increase the value of another corporation they own through

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312. See *supra* text accompanying note 210.

313. See Ellickson, *supra* note 66, at 1534 n.61 (“[B]usiness shareholders tend to have a single common purpose: maximizing the value of their shares.”).

314. See *Dodge v. Ford Motor Co.*, 170 N.W. 668, 684 (Mich. 1919).

315. Ellickson, *supra* note 66, at 1534 n.61.

316. Daniel J.H. Greenwood, *Fictional Shareholders: For Whom Are Corporate Managers Trustees, Revisited*, 69 S. CAL. L. REV. 1021, 1058 (1996) (describing the notion of a shareholder as “a person with . . . no will other than the desire to maximize the value of that shareholding”).

317. See HENRY HANSMANN, *THE OWNERSHIP OF ENTERPRISE* 40–44 (1996) (observing the “nearly complete absence of large firms in which ownership is shared among two or more different types of patrons, such as customers and suppliers or investors and workers” and theorizing the high cost of collective decision making that would result from having different types of owners); see also Pollman, *supra* note 296, at 217 (noting that corporate law’s assumption of a homogenous shareholder does not accord with the reality of startups, and thus they demand a distinct judicial attitude).



decreasing this one's value),<sup>318</sup> they will all be affected equally.<sup>319</sup> The result is that, in most cases, debates about the right course of action for the corporation boil down to differences of opinion, not conflicts of interest.<sup>320</sup>

Now consider the common-interest community. An interest held in a common-interest community—a residence—can represent two, not necessarily overlapping, things: an investment and a home. An owner can hold real property to generate revenue by renting it to others. An owner can also hold the property to use it themselves as a residence. For the former, the property is not a home while for the latter it is. In a common-interest community therefore, there are two distinct classes of owners, each with a different method for deriving value from their asset.

With respect to many common-interest-community decisions, these two groups' interests align. Because the market prices a common-interest-community unit in accordance with its usefulness as a home (if more appealing, tenants will pay higher rents), an investor, while not residing in the unit, is still sensitive to its use value. Correspondingly, even for the owner occupying their unit, that unit is also an investment (indeed, for most Americans, their home is their major asset).<sup>321</sup> The unit can be, and is, bought and sold.<sup>322</sup> Thus, the owner-occupant is also sensitive to the unit's market value. Consequently, most common-interest-community decisions affect both owner types—investors and occupants—similarly.<sup>323</sup>

But this is not true respecting all decisions. Some, but not all, unit owners care about values outside market value: they care about the unit's value as a home.<sup>324</sup> Decisions that interfere with the unit's value as a home without clearly affecting its pricing solely harm these owners. Conversely, decisions that advance the unit's value as a home in ignorance of potential negative impacts on investment values only harm investors. The different goals the two owner groups have for their units create, with respect to such decisions, an irreconcilable conflict of interests.

318. See, e.g., *Sinclair Oil Corp. v. Levien*, 280 A.2d 717, 720–21 (Del. 1971).

319. See Henry T.C. Hu, *Risk, Time, and Fiduciary Principles in Corporate Investment*, 38 UCLA L. REV. 277, 289–90 (1990).

320. See Stephen M. Bainbridge, *In Defense of the Shareholder Wealth Maximization Norm: A Reply to Professor Green*, 50 WASH. & LEE L. REV. 1423, 1445 (1993) (explaining that the abstraction of a homogenous shareholder enables directors to make coherent decisions and prevents them from using potential discrepancies in shareholder interests to justify acts pursuing personal gain).

321. WILLIAM A. FISCHER, *THE HOMEVOTER HYPOTHESIS* 4 (2001).

322. Fennell, *supra* note 26, at 871.

323. E.g., *Le Febvre v. Osterndorf*, 275 N.W.2d 154, 159 (Wis. Ct. App. 1979) (noting that since a regulation should increase market values, it benefits both residents and investors).

324. Ellickson, *supra* note 66, at 1534–35 n.61 (“[B]ecause of the uniqueness of real estate and the emotional ties that bind one to one’s residence, an association member may have a reservation price well above market price. The member will thus consider the effect of an amendment not only on the market value of his unit, but also on his subjective valuation of the unit . . . [this fact] make[s] it more likely that an association’s amendments (compared to a business corporation’s amendments) will seriously disgruntle a minority.”).

The clearest decisions which affect only one of the two groups are those that block the use on which that group relies to realize the primary value it assigns to the unit. The effect of such decisions is not only disparate but also dramatic and perhaps irreversible. If the unit can no longer serve the value for which its owner acquired it, the owner must either find a way to benefit from its other value—by changing their living patterns—or, more realistically, sell. Another owner who did not acquire the unit for the endangered value feels nothing.

The decision terminating the value relevant for owner–investors alone is a decision restricting leasing.<sup>325</sup> An owner–investor, but not an owner–occupant, realizes the unit’s value by leasing it to tenants. Thus, while a community’s leasing restriction formally burdens all owners (none can now rent out their units), the effect is much more marked for owner–investors. Owner–occupants probably never planned to rent out their units, so they experience no burden. At most, a potential future course of action (to relocate and keep the unit as an investment) is blocked. The position of the owner–investor is radically different. For the owner–investor, the whole, and only, reason for originally acquiring the unit is gone. The owner–investor now must either sell the unit (which no other investor will buy) or keep it empty (unless the owner–investor uproots herself and moves in). The effects on the two classes thus diverge dramatically. One group, but not the other, almost always bears leasing restrictions’ brunt. Hence, this is a case of an inherent conflict of interests.

The same is true in the inverse scenario: when the decision eviscerates the current value that owner–occupants, but not owner–investors, derive from their units. An owner–occupant realizes the value for which they hold their unit through habitation. A decision terminating the occupant’s value would thus be a decision forcing all owners to move out. Such is a decision to sell the community in its entirety, both common spaces and individually owned units, to a developer (who normally then converts all units into rentals).<sup>326</sup> Once a community makes a bulk-sale decision, all owners (even those who opposed the decision) must sell. The owner–occupants, however, feel this obligation’s effect much more acutely than the owner–investors. The investor must liquidate an investment; the occupant must leave their home. An investment is fungible—it can fully be replaced with money or other assets;<sup>327</sup> a home is not—it is the quintessential personhood property, an asset held not solely, or even primarily, for its monetary value.<sup>328</sup> Thus, although the decision to force a sale affects all owners similarly in monetary terms, only the owner–occupants feel the decision’s devastating effects on personhood values.

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325. On leasing restrictions, see SINGER, *supra* note 6, at 647.

326. *E.g.*, 765 ILL. COMP. STAT. ANN. 605/15 (West 2018) (regulating such sales).

327. Margaret Jane Radin, *Property and Personhood*, 34 STAN. L. REV. 957, 959–61 (1982).

328. *Id.* at 991–92.

The two extreme decisions—leasing restrictions or forced sales—annihilate the motivation one group of owners has for holding their units while sparing the other group such harsh repercussions. Mutuality here is a chimera. When these decisions are contemplated, neither group, nor its board representatives, can be viewed as disinterested: either, if controlling a majority of the votes, will act to serve its own distinct interest. These decisions must be subject to substantive review.

## 2. *Owners with Different Time Horizons*

Important heterogeneity exists in the common-interest community not only between owner-occupants and owner-investors but also among the owner-occupants. Such owners do not all plan on occupying their units for the same amount of time. They thus differ in their time horizons, and this difference generates inherent conflicts of interest.

Some occupants view the unit as a home where they plan to stay long-term, i.e., for decades or even a lifetime. For others, it is a short-term home: a starter home as they save funds, or a home fitting their current and transient needs, say before expanding their family or retiring.<sup>329</sup> Investors in a corporation might of course also vary in their time horizons. They might desire or need to liquidate their investments at different times.<sup>330</sup> However, shares are liquid and fungible, so an investor can always at least try to switch to a share that better reflects her time horizon.<sup>331</sup> Homes are not nearly as liquid or fungible, hence the diversity in time horizons among owners is much likelier to generate serious conflicts of interest in the common-interest community.

Because of their different time horizons, the two owner-occupant subgroups' interests diverge. People with disparate time horizons strike very different balances between short-term benefits and long-term costs.<sup>332</sup> An owner who knows they will not stay at their current unit for long will have a clear preference for short-term benefits and a desire to delay costs. This would allow the owner to exploit current benefits while avoiding their costs. Conversely, decisions that are costly now but beneficial in the future will serve long-term owners.

The quintessential common-interest-community decision pitting long-term benefits against short-term benefits pertains to the community's reserves fund. The common-interest community funds itself through monthly dues that

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329. See generally Stephanie M. Stern, *Residential Protectionism and the Legal Mythology of Home*, 107 MICH. L. REV. 1093, 1125 (2009) (discussing homeownership mobility across Americans' life cycles).

330. Stephen M. Bainbridge, *The Board of Directors as Nexus of Contracts*, 88 IOWA L. REV. 1, 21 (2002).

331. FRANK H. EASTERBROOK & DANIEL R. FISCHER, *THE ECONOMIC STRUCTURE OF CORPORATE LAW* 29 (1991).

332. See generally Leo E. Strine, Jr., *Who Bleeds When the Wolves Bite? A Flesh-and-Blood Perspective on Hedge Fund Activism and Our Strange Corporate Governance System*, 126 YALE L.J. 1870, 1884 (2017).

owners pay.<sup>333</sup> These dues are used for day-to-day expenses and to sustain reserves. Aside from routine needs the community addresses every year, there are major maintenance and improvement projects it engages in more rarely.<sup>334</sup> Additionally, emergencies such as flooding, roof damage, etc., are ever-present risks.<sup>335</sup> The reserves fund is the savings account into which the community dips when such occasions arise.

Savings are always more important for those with long-term plans. A short-term focus entails a strong preference for spending money now over saving it for a perhaps irrelevant future. Short-term occupants would rather spend community funds on projects prompting immediate benefits (like common spaces' beautification).<sup>336</sup> They thereby shift the costs of major projects or potential disasters to the future—when they might be gone. Long-term occupants would, conversely, prefer to sustain reserves at high levels.<sup>337</sup>

The same dynamics materialize when boards consider infrastructure projects. As in decisions over reserves, here too residents must decide whether to dedicate current funds for the promotion of mostly future benefits. Infrastructure projects, such as roof or plumbing-risers replacement, building sealing, and the like, must be paid for immediately to avert potential future harms. Owners with a short time horizon are less concerned about future harms and may thus agree to assume future risks rather than pay now to forestall them. Long-term owners have the opposite incentive: they might even be too eager to engage projects now so as to share costs with short-term owners.

Market pricing undoubtedly mitigates some of these conflicts. A unit in a community with poor reserves and deferred infrastructure projects should be priced lower than one in a community with better reserves and infrastructure. Because all owners, particularly short-term ones, care about their unit's market value, none can wholly ignore future costs that future owners (who are current owners' potential buyers) will bear.<sup>338</sup>

However, markets are never perfect, and the market for houses is far less efficient than the corresponding market for corporate shares.<sup>339</sup> Shares are traded constantly on an open market that sophisticated actors dominate.<sup>340</sup> For houses, no central clearinghouse exists and most buyers are not expert, or even

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333. POLLAKOFF, *supra* note 182, § 5:3.

334. *Id.* § 5:9.

335. *See id.*

336. They might similarly seek to have dues reduced. *See* EVAN MCKENZIE, BEYOND PRIVATOPIA: RETHINKING RESIDENTIAL PRIVATE GOVERNMENT 112 (2011) (arguing residents refuse to sacrifice resources to maintain amenities for future owners).

337. Evidence suggests that overall communities have about half the reserve funds they need. *Id.* at 113.

338. *See supra* notes 321–322.

339. Abraham Bell & Gideon Parchomovsky, *The Integration Game*, 100 COLUM. L. REV. 1965, 2022 (2000) (“[T]he stock market suffers from fewer imperfections than the housing market.”).

340. *See id.* at 2022–23.

repeat, players. Hence, the housing market does not provide buyers with all pertinent information about an asset's condition and future potential.<sup>341</sup> Furthermore, buyers might fail to fully internalize even the information that is disclosed.<sup>342</sup> Therefore, perfect information respecting a common-interest community's infrastructure deficiencies might be hard to come by, and buyers are liable to discount future risks.<sup>343</sup> Because short-term owners know that the market is highly unlikely to fully penalize them for shifting some community costs to buyers, their incentive to do so stands.<sup>344</sup> Conflicts between short- and long-term owners thus persist.

In cases involving tradeoffs between the present and the future, mutuality often disappears. Whichever of the two groups—short- or long-term owners—controls the board is liable to adopt decisions serving its interests that are not shared with the other group. Decisions respecting reserves and infrastructure projects put long- and short-term owners at an inherent conflict of interests and are thus a poor fit for the business judgment rule.

### 3. *Owners with Different Means*

Another difference between owners that can undermine mutuality in the common-interest community is wealth. Individuals' interests respecting economic decisions inevitably differ in accordance with their financial situations. The equality of subjecting rich and poor to the same financial liability is merely formal.<sup>345</sup> Given differences in ability to pay and the declining marginal utility of money,<sup>346</sup> those with limited means experience a liability much more acutely than others. Mutuality is a mirage when a financial obligation is an afterthought for some whilst devastating for others.

The one common-interest-community decision that directly forces upon owners a financial obligation is the decision to raise a special assessment (that is, a payment outside of regular dues) to fund a communal project.<sup>347</sup> Affluent

341. See generally Daniel R. Fischel, *Use of Modern Finance Theory in Securities Fraud Cases Involving Actively Traded Securities*, 38 BUS. LAW. 1, 5–8 (1982) (discussing the theory that an efficient market rapidly impounds all available information into the price of any security).

342. See Russell Korobkin, *Bounded Rationality, Standard Form Contracts, and Unconscionability*, 70 U. CHI. L. REV. 1203, 1227–29 (2003) (citing a study suggesting accuracy in house-choice decision-making drops as the number of house attributes rises).

343. Another problem is that the house is a bundled product whose price incorporates many structural and environmental attributes. Consequently, a house's price fails to provide signals respecting the market for any one attribute or problem. Fennell, *supra* note 26, at 873.

344. Korobkin, *supra* note 342, at 1234 (“[N]on-salient attributes [of products] are subject to inefficiencies driven by the strategic behavior of sellers attempting to increase their profits at the expense of unknowing buyers.”).

345. See ANATOLE FRANCE, *THE RED LILY* 91 (Winifred Stephens trans., 1925) (“[T]he majestic equality of the laws, which forbid rich and poor alike to sleep under the bridges . . .”).

346. Joseph Bankman & Thomas Griffith, *Social Welfare and the Rate Structure: A New Look at Progressive Taxation*, 75 CALIF. L. REV. 1905, 1947 (1987).

347. POLLAKOFF, *supra* note 182, § 5:11.

owners who have discretionary income suffer little from special assessments. They may welcome them. Through the assessments, they procure nicer amenities for a cost insignificant given their wealth, further lowered since the burden is shared with others. Owners of limited means, conversely, might find a particularly high special assessment or a pattern of special assessments unbearable. To fund better amenities shared with richer neighbors, they might have to forsake other personal and more vital expenses. They might even be unable to afford the expense and be forced to sell their units. Indeed, assessments can be used to intentionally push out lower income residents, making living in a community unsustainable financially for them or adding amenities that exude class-based “exclusionary vibes” (golf courses are often cited as example).<sup>348</sup> These decisions may embody an unfolding class warfare within the community. Thus, inherent conflicts of interest often pervade such decisions about special assessments.<sup>349</sup>

That is only the case, however, if the common-interest community actually houses owners of diverging wealth levels. Unlike the variations among owners reviewed in the previous two Subparts, wealth disparities are not inevitable within a common-interest community. Indeed, common-interest communities are associated with socioeconomic homogeneity.<sup>350</sup> Owners pay to join a common-interest community (they must buy a unit); hence, a given common-interest community is unlikely to be as diverse as more organic communities like the state or city.<sup>351</sup>

Still, in some common-interest communities, variations in wealth, even wide ones, are not improbable. Because the economic homogeneity between members is generated through the price they pay to join, homogeneity might dissipate when prices paid vary. Per-unit prices paid can diverge because units differ meaningfully in size or value. Another, perhaps even more prevalent, possibility is that older owners bought units decades ago before market appreciation; even if, like newer owners, they are now property rich, they might be cash poor.

Granted, the correlation is imperfect. A rich individual might occupy a small or less expensive unit or one purchased decades ago for a measly sum. A home’s value, let alone its historical price, does not necessarily reflect an individual’s wealth. Wealth is a function of the totality of the person’s assets,

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348. Lior Jacob Strahilevitz, *Information Asymmetries and the Rights to Exclude*, 104 MICH. L. REV. 1835, 1851, 1858 (2006).

349. There might be other rarer instances implicating inherent conflicts between owners along wealth lines. One example is *Williams v. 5300 Columbia Pike Corp.*, 891 F. Supp. 1169, 1172–73 (E.D. Va. 1995), where a co-op decided to convert into a condominium. Under the plan, current co-op members had to pay to buy their units and thereby retire the co-op’s debt. *Id.* at 1172. Not all owners had access to capital, and thus some were unable to preserve their units. *Id.* at 1173. The court decided—mistakenly, given the analysis suggested here—to refrain from thoroughly reviewing the decision. *Id.* at 1182–83.

350. Gillette, *supra* note 66, at 1412–13.

351. Sterk, *supra* note 66, at 297.

income, and more.<sup>352</sup> Yet such detailed data about each owner is not and cannot be available to neighbors and courts. Information about units' value and time of purchase is. This information thus serves as a means for approximating owners' relative wealth. It is a useful—albeit imperfect—proxy for identifying communities characterized by wide wealth differentiation.

In those communities where great variation in unit values or purchase times can be found, a wealth gap might divide owners. This divide generates inevitable conflicts of interest respecting special assessment decisions: the group controlling the board can issue decisions ignoring the interests of the other. Hence, in such communities, those decisions cannot be subjected to the business judgment rule.

#### 4. *Owners of Different Unit Types*

So far, this Part has identified instances where mutuality among unit owners is absent because owners differ in some important attribute. As this final Subpart will show, the variation subverting owner mutuality could also be rooted in the units', rather than their owners', character. Perhaps this is the inherent conflict of interests easiest to grasp.<sup>353</sup> If only type *A* units are affected by certain community decisions, owners of type *B* units never experience those decisions' effects. Hence, if type *B* unit owners adopt decisions detrimental to type *A* units—or if type *A* unit owners adopt decisions beneficial to type *A* units—they are not disinterested.<sup>354</sup>

The pertinent differences between units—the distinction between type *A* and *B* units—can be a function either of physical characteristics or of location.<sup>355</sup> Distinct physical characteristics can take the form of amenities attached to certain units.<sup>356</sup> Perhaps only some units have parking spots or patios. Units can further differ physically if a community consists of both

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352. See generally *Wealth*, MERRIAM-WEBSTER.COM, <https://www.merriam-webster.com/dictionary/wealth>.

353. Indeed, it is the one case where some courts have been open to meaningful review. See, e.g., *Johnson v. Hobson*, 505 A.2d 1313, 1318 (D.C. 1986) (“[C]ourts have analyzed the substance of condominium regulations to determine whether they have an unfair or disproportionate impact on only certain unit owners.”).

354. A similar conflict can arise within a corporation between holders of different classes of stock. *Starring v. Am. Hair & Felt Co.*, 191 A. 887, 890 (Del. Ch. 1937). Directors are subject to special duties in such cases. *Equity-Linked Invs., L.P. v. Adams*, 705 A.2d 1040, 1042 (Del. Ch. 1997).

355. These cases of inherent conflict hinge on the fact that the pertinent regulation applying to some units and not to others; hence, it is the physical difference between units that is key. Potential differences in owners' abilities or preferences are irrelevant. See, e.g., *Garrison Apartments, Inc. v. Sabourin*, 449 N.Y.S.2d 629, 633–34 (Civ. Ct. 1982) (holding that a condominium regulation establishing a security patrol and providing for service on the patrol in lieu of an assessment was not discriminatory to owners physically unable to serve).

356. E.g., *Vernon Manor Coop. Apartments, Section I, Inc. v. Salatino*, 178 N.Y.S.2d 895, 899 (Cnty. Ct. 1958) (noting that only some units were allowed washers).

multiunit and freestanding buildings<sup>357</sup> or of both residential and commercial buildings.<sup>358</sup> A unit's location can also endow it with peculiar attributes. In a multiunit building, top-floor units are more affected by the roof,<sup>359</sup> and the higher within the building a unit is, the more it depends on the elevator.<sup>360</sup> In a sprawling common-interest community, only some units border appealing common spaces, such as golf courses or lakes,<sup>361</sup> or less appealing spaces, such as major roads.<sup>362</sup>

Community decisions regarding a specific unit's physical characteristics or distinct location within the community can then affect the use and enjoyment of some but not other units.<sup>363</sup> Another way in which community decisions can have a disparate impact on different units is by shifting voting rights or per-unit fees between them. A community can amend its declaration to decrease or expand the weight, in community decision-making, of the votes of owners of a specific type of unit.<sup>364</sup> It can also reallocate expenses to some units' owners.<sup>365</sup> Such cases are blatant examples of abuse of minority interests.<sup>366</sup>

The premise of mutuality whereby all property owners are impacted similarly by common-interest-community decisions can disappear whenever properties are not identical. Certain decisions can then only affect some properties. Decision makers considering such decisions, whether they own the affected or the unaffected properties, are hardly disinterested. These decisions are inappropriate for business-judgment-rule analysis.

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357. *E.g.*, *Thiess v. Island House Ass'n*, 311 So. 2d 142, 142–43 (Fla. Dist. Ct. App. 1975) (noting that a condominium with thirty-eight villas and thirty-five apartment units passed amendments increasing the dues of the latter and ceasing maintenance of washers they used).

358. *E.g.*, *Ridgely Condo. Ass'n v. Smyrnioudis*, 660 A.2d 942, 951 (Md. Ct. Spec. App. 1995) (striking down a board decision in a condominium of residential and commercial units prohibiting commercial units from utilizing the condominium's lobby).

359. *E.g.*, *Stein v. Garfield Regency Condo.*, 886 N.Y.S.2d 54, 56 (App. Div. 2009) (discussing top-floor owners claiming special rights to roof deck); *Cohen v. CASSM Realty Corp.*, 39 N.Y.S.3d 597, 602 (Sup. Ct. 2016) (discussing top-floor owners enduring special harm due to roof disrepair).

360. *E.g.*, *Peck Plaza Condo. v. Div. of Fla. Land Sales & Condos.*, 371 So. 2d 152, 152 (Fla. Dist. Ct. App. 1979) (disputing a rule whereby only a floor using it will pay elevator electricity).

361. *E.g.*, *Weatherby Lake Improvement Co. v. Sherman*, 611 S.W.2d 326, 332 (Mo. Ct. App. 1980).

362. *E.g.*, *Boyles v. Hausmann*, 517 N.W.2d 610, 613–14 (Neb. 1994) (discussing an association prohibiting construction within 120 feet of the road, thereby affecting only one owner).

363. Other differences in unit types are also imaginable. In *In re Croton River Club, Inc.*, 52 F.3d 41, 43–44 (2d Cir. 1995), the same community encompassed residential units and marina slip-owners. The former controlled the board and imposed financial liabilities on the latter. *Id.*

364. *See, e.g.*, *Twin Lakes Vill. Prop. Ass'n v. Crowley*, 857 P.2d 611, 615 (Idaho 1993) (discussing a bylaw amendment changing the basis for allocating votes from square footage to one lot—one vote).

365. *E.g.*, *Francis v. Aspen Mountain Condo. Ass'n*, 2017 COA 19, ¶ 3, 401 P.3d 125, 127 (discussing a bylaw amendment shifting from assessments based on square footage to a uniform fee).

366. These are equivalent to interferences with the political process to disempower a minority, which generate heightened constitutional review. *United States v. Carolene Prods. Co.*, 304 U.S. 144, 153 n.4 (1938).



B. *Handling the Structural Conflicts of Interest Within Common-Interest Communities*

Part II concluded that courts should employ a two-tiered review system for common-interest-community decisions. Subpart III.A just identified the decisions that merit heightened review. When the community adopts other decisions, mutuality among owners can mostly be assumed, and thus, courts are justified in refraining from inspecting decisions' substance. In the absence of structural conflicts of interest, the independence, or disinterestedness, of decision-making members can be assumed. As in corporate law whence the business judgment rule hails, those are the decisions that do not require demanding judicial review and should thus be evaluated under the deferential business judgment rule.

A permissive approach focusing on the procedures generating these decisions rather than their substance is not only possible—it is advisable. With mutuality present, the fairness concerns that would justify substantive review are moot. Moreover, in these cases where structural conflicts of interest are unlikely, courts often lack a clear objective standard that they can resort to for assessing a decision's merits. When the interest of a certain owner group is threatened, that well-defined interest, as spelled out in the preceding Part, provides a benchmark against which the decision's fairness can be assessed.<sup>367</sup> In decisions implicating no conflict of interests, that benchmark is inevitably missing.

Assessments of such decisions' merits are thus prone to be somewhat more subjective.<sup>368</sup> The quintessential decisions characterized by mutuality— aesthetic regulations—illustrate this point.<sup>369</sup> Objective answers cannot easily be found to questions such as what is the relative worth of gnomes as compared to pink flamingos,<sup>370</sup> whether a specific light fixture complements others,<sup>371</sup> how many Christmas lights are too many,<sup>372</sup> or whether palm trees “upset the natural setting and beauty of the neighborhood.”<sup>373</sup> Hence, these decisions can be equated with corporate board decisions that corporate law subjects to the

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367. See *infra* notes 387–390 and accompanying text.

368. A California decision appears to rely on this rationale. *Lamden v. La Jolla Shores Clubdominium Homeowners Ass'n*, 980 P.2d 940, 942 (Cal. 1999). Here, the Supreme Court of California ruled that for economic and maintenance issues, the rule would apply, but for decisions raising physical bodily injury, the review standard could be higher. *Id.* at 951–52.

369. See *supra* notes 24–27 and accompanying text.

370. See *supra* text accompanying note 27.

371. See *Hawk's Landing Homeowners Ass'n v. Cox*, No. 2009AP701, 2010 WL 2519317, at \*1 (Wis. Ct. App. June 24, 2010).

372. *Morris v. W. Hayden Ests. First Addition Homeowners Ass'n*, 382 F. Supp. 3d 1093, 1107–13 (D. Idaho 2019) (discussing 200,000(!) lights).

373. *Esfahani v. Steelwood Prop. Owners' Ass'n*, 271 So. 3d 839, 846 (Ala. Civ. App. 2018).

business judgment rule.<sup>374</sup> Although these aesthetic decisions rarely involve traditional business judgment calls, let alone draw on business acumen,<sup>375</sup> their more subjective nature—implicating issues of taste—renders them less amenable to external judicial review.<sup>376</sup>

Non-aesthetic decisions that still do not implicate one of the conflicts of interests the preceding Subpart identified are often even more reminiscent of routine business decisions. Examples include a common-interest community's choice of service provider or of strategy for addressing a maintenance problem.<sup>377</sup> An entity's own board is better situated to make subjective calls about these business-strategy issues.<sup>378</sup> Courts can thus limit themselves to procedural review to ensure that before making the decision the community or its board held deliberations, considered alternatives, provided notice to owners, etc.<sup>379</sup>

The normative picture shifts dramatically, however, when decisions implicate inherent conflicts of interest. These cases, which the preceding Subpart catalogued, necessitate meaningful judicial review. As Subpart I.C explained, the higher review standard that common-interest-community law adhered to prior to the business judgment rule's rise was reasonableness.<sup>380</sup> Corporate law, the business judgment rule's birthplace, applies reasonableness analysis to interested decisions.<sup>381</sup> That standard should thus be employed in cases of common-interest-community decisions involving conflicts between owner–occupants and owner–investors, between owners with disparate time horizons, between owners of different means, and between owners of distinct unit types.

What would the reasonableness analysis this Article suggests look like? Unpacking the test is important because some might argue that distinctions between different review tiers—say, business judgment rule and reasonableness—are mere formalities. Courts, so the argument goes, are prone to conflate different standards, announcing adherence to one rather than the other while in essence resorting to the same analysis.<sup>382</sup> As seen when early

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374. See *Levandusky v. One Fifth Ave. Apartment Corp.*, 553 N.E.2d 1317, 1325–28 (N.Y. 1990) (Titone, J., concurring) (explaining that a board's decision to pursue a particular repair program in preference to what a shareholder suggested was, in essence, a business judgment, i.e., a choice between competing and equally valid economic options, albeit one not motivated by the desire to generate a profit).

375. See Note, *supra* note 150, at 665.

376. See *Levandusky*, 553 N.E.2d at 1322.

377. See, e.g., *Lamden v. La Jolla Shores Clubdominium Homeowners Ass'n*, 980 P.2d 940, 941 (Cal. 1999) (discussing a decision whether to treat a termite infestation locally or to fumigate).

378. *Id.* at 954.

379. A 2012 amendment to California's law reflects this approach. CAL. CIV. CODE § 4765 (West 2014). It requires that in approving architectural changes to units, boards adhere to basic due process requirements, such as notice, reasoning, and appeal rights. *Id.*

380. See *supra* notes 146–149 and accompanying text.

381. See *supra* notes 230–231 and accompanying text.

382. See Alexander, *supra* note 66, at 13.

common-interest-community rulings were reviewed, judicial behavior sometimes lends credence to these suspicions.<sup>383</sup>

This need not be the case, however.<sup>384</sup> Corporate law's lengthy experience with the distinction between review standards for duty of care and duty of loyalty cases illustrates that a meaningful difference between scrutiny levels is achievable. The standard used for duty of care breaches—the business judgment rule—implies a purely procedural review, only verifying that the board employed proper decision-making processes.<sup>385</sup> In contrast, for duty of loyalty breaches, a court inspects the decision's substance to ensure that it is in the corporation's best interests.<sup>386</sup>

A court confronted with a common-interest-community decision inherently tainted by a conflict of interests ought to do the same.<sup>387</sup> It must certify that the decision is not merely an attempt to promote, at the expense of other owners' interests, the interests of those owners controlling decision-making processes. Concrete factors can aid in making the determination. Specifically, courts should inquire (1) whether some members of the losing interest group supported the decision;<sup>388</sup> (2) whether the decision somehow addressed, if only partially, the losing side's interests;<sup>389</sup> and (3) whether some rationale exists for the decision aside from a majority's ability to promote its interests.<sup>390</sup>

In each of the four types of inherently conflicted decisions identified in Subpart III.A, these three factors suggested here translate into distinct indicia pointing at a specific decision's reasonableness (or unreasonableness).

383. See *supra* notes 206–209 and accompanying text.

384. In current law, reasonableness makes it possible for different judges, especially in lower courts where evidentiary issues dominate, to reach different conclusions respecting the same decision. Thus, for example, in *Hawk's Landing Homeowners Ass'n v. Cox*, No. 2009AP701, 2010 WL 2519317, at \*1 (Wis. Ct. App. June 24, 2010), the majority deemed the refusal to approve a specific light reasonable given the community's design while the dissent disagreed. *Id.* at \*14 (Dykman, P.J., dissenting).

385. See Schanzenbach & Shoked, *supra* note 31, at 614.

386. See *supra* notes 230–231 and accompanying text.

387. Lower courts employing reasonableness before being overruled understood it as entailing such substantive analysis. Thus, a court was not swayed by the fear that allowing one owner to drill a well would lead to other owners doing the same. *Hidden Harbour Ests., Inc. v. Basso*, 393 So. 2d 637, 640 (Fla. Dist. Ct. App. 1981). And another court made its own judgment that a renovation would endanger the building. *Levandusky v. One Fifth Ave. Apartment Corp.*, 553 N.E.2d 1317, 1322–23 (N.Y. 1990).

388. See, e.g., *Willens v. 2720 Wis. Ave. Coop. Ass'n*, 844 A.2d 1126, 1136–38 (D.C. 2004) (noting that no owners detrimentally affected by a decision voted for it).

389. Such compensation can also render the decision Pareto efficient, thus improving all parties' well-being. Natelson, *supra* note 66, at 81.

390. In corporate law, a majority shareholder's decision for the corporation is struck down when “there [i]s no reason for [the decision] . . . except to enable the [majority] stock to profit at the expense of the [minority] stock.” *Zahn v. Transamerica Corp.*, 162 F.2d 36, 46 (3d Cir. 1947); see also *River Terrace Condo. Ass'n v. Lewis*, 514 N.E.2d 732, 737 n.8 (Ohio Ct. App. 1986) (“[T]he test of reasonableness . . . requires, among other things, that there be some rational relationship of the decision or rule to the safety and enjoyment of the condominium . . . [and that] the decision or rule was made in good faith for the common welfare of the owners and occupants of the condominium.”); Note, *supra* note 150, at 666 (suggesting that a court verify that those voting for a decision did not act solely on spite).

The first type of structural conflicts the preceding Subpart highlighted involves owner–occupants and owner–investors, where the former can sabotage the interests of the latter through leasing restrictions and the latter can harm the former’s interests with bulk-sale decisions. Common-interest-community restrictions on leasing have often been contested.<sup>391</sup> Most courts approve them, usually through the business judgment rule.<sup>392</sup> Some courts note the built-in unfairness toward owner–investors,<sup>393</sup> but none appear to analyze these common-interest-community decisions under a conflict-of-interests framework as suggested here.<sup>394</sup> These decisions should be scrutinized for reasonableness, considering the three factors mentioned.

Owner–investors are highly unlikely to support a leasing restriction, so the first factor, pertaining to the degree of buy-in from the affected interest group, will almost always weigh against reasonableness.<sup>395</sup> The other two factors can still render the leasing restriction reasonable, however. If the decision acknowledges owner–investors’ loss and somehow addresses it, it is more reasonable. Partial restrictions should thus be more acceptable. Such are restrictions grandfathering currently leased units, allowing leasing for certain—if limited—time periods,<sup>396</sup> or merely subjecting leasing to fees.<sup>397</sup> The third factor should ask whether the leasing restriction expresses considerations other than a desire to harm investors’ interests (or mere anti-tenant bias).<sup>398</sup> Courts can insist on proof that widespread leasing was harming, in objective terms, the common-interest community. Were banks refusing to extend mortgages

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391. Jordan I. Shifrin, *No-Leasing Restrictions on Condominium Owners: The Legal Landscape*, 94 ILL. BAR J. 80, 80–81 (2006).

392. “Courts commonly enforce no-lease restrictive covenants.” *Villas W. II of Willowridge Homeowners Ass’n v. McGlothlin*, 885 N.E.2d 1274, 1279 (Ind. 2008).

393. *E.g.*, *Cape May Harbor Vill. & Yacht Club Ass’n v. Sbraga*, 22 A.3d 158, 166 (N.J. Sup. Ct. App. Div. 2011) (“We agree with appellant that the restriction here is a significant one, in that it does affect a fundamental property right and not some less significant aspect of the manner in which properties are used.”).

394. *See Kelley v. Broadmoor Coop. Apartments*, 676 A.2d 453, 461 (D.C. 1996) (refusing to entertain plaintiff’s argument that a leasing regulation should be held invalid just because “one class of owners (owners/occupants) has imposed a regulation ‘which discriminates financially’ against another class (owners/renters)”).

395. The *Restatement* thus requires unanimous consent for amendments restricting such uses. *RESTATEMENT (THIRD) OF PROP.: SERVITUDES* § 6.10(3) (AM. L. INST. 2000). It permits a declaration to disclaim this requirement, however. *Id.*

396. For example, restricting leasing periods or the number of units that can be leased at any given time.

397. *E.g.*, *Kelley*, 676 A.2d at 455 (approving a regulation imposing a surcharge of 5% for each rented apartment).

398. Caselaw provides examples for such unsatisfactory justifications: a bland statement whereby the regulation’s goal is “to promote owner occupancy, maintain the value of each owner’s investment in his or her home, and ensure a consistently high quality of life for . . . residents[.]” *id.*; claims that “tenants presented problems peculiar to a condominium area, including a limited and indirect control by the board over the tenants’ conduct[.] . . . that the board had difficulty giving notices to nonresident owners[.] and that the tenants were ignorant of the provisions of the declaration and bylaws . . . [.]” *Le Febvre v. Osterndorf*, 275 N.W.2d 154, 157 (Wis. Ct. App. 1979); and concerns “about the negative effects of . . . renters’ perceived lack of attention to the property[.]” Shifrin, *supra* note 391, at 80.

secured by units in the community due to a high percentage of leased units?<sup>399</sup> Were unit values dropping?<sup>400</sup> If the answer is yes, the restriction can more easily be perceived as addressing a real communal need and thus as reasonable.

This proposed three-factor analysis can also help determine the reasonableness of decisions representing the opposite dynamic between occupants and investors: forced sales. First, courts can assess the level of buy-in from the group with determinately affected interests—owner—occupants. A large owner majority voting for the forced-sale decision may indicate that the decision reflected more than the brute power of the less affected group—investors. If a big majority voted in favor, the likelihood rises that some owner—occupants were among those who voted in support. Some state statutes that specifically police forced sales in common-interest communities reflect this insight.<sup>401</sup> Second, courts should see whether the losing group was at least partially compensated for its special losses. Owner—occupants use units as homes, and thus, units offer them values, subjective and otherwise (for example, avoiding moving costs), beyond market value. One way of accounting for these interests lost in a forced sale is to insist that the consideration owners receive for their units' forced sale reflect this extra value. A premium paid to owner—occupants, especially if above market value, renders the forced-sale decision fairer toward that group.<sup>402</sup> Finally, the third factor presses courts to verify that the bulk-sale decision is not born of owner—investors' opportunistic behavior. For this purpose, courts must discern the forced sale's motivation. The economic rationale for converting a common-interest community into a rental complex is normally rooted in the financial predicament of owners in buildings constructed decades ago.<sup>403</sup> Sometimes these require not only constant and expensive maintenance but also major renovations. Owners of individual units that, due to the building's deterioration, are now of limited value, sometimes cannot afford these costs. In contrast, developers have deep pockets. They also economize on construction costs through reliance on their expertise and on economies of scale achieved through simultaneous renovation

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399. *E.g., Kelley*, 676 A.2d at 460 (noting that a board member explained “the difficulty of securing a . . . Fannie Mae[] mortgage if twenty to thirty percent of the apartments were rental units. . . . To her affidavit was attached a copy of a Fannie Mae document containing some of its regulations”); *Burgess v. Pelkey*, 738 A.2d 783, 790 (D.C. 1999) (“[L]enders will not extend financing if less than 70% to 80% of the units are owner-occupied.”).

400. *Natelson*, *supra* note 66, at 73 n.150 (citing a study concluding that “[a] high number of leased units . . . can impair significantly the market position of the subdivision”). Other justifiable rationales are imaginable. For example, a co-op board argued that the building might lose eligibility for certain tax benefits and local fee exemptions if less than 50% of units are “used as a primary residence.” *Kelley*, 676 A.2d at 460.

401. *E.g.*, 765 ILL. COMP. STAT. ANN. 605/15(a) (West 2018) (requiring 75% of owners to approve a bulk-sale).

402. *Id.* (entitling opponents to the higher of unit's market value or remaining mortgage debt plus relocation costs).

403. *Carisa Crawford Chappell, Chicago's Condos Are Turning into Rentals*, CHI. TRIB. (Nov. 4, 2019, 11:12 AM), <https://www.chicagotribune.com/real-estate/ct-re-condo-deconversion-1110-20191104-qluzf5donvende6k56orv3eb-wu-story.html>.

of the entire building.<sup>404</sup> A bulk-sale deal can thus be efficient and appealing to both sides. Courts should check whether that is true in the case at hand. They should seek proof of consistent declines in unit values and continuing inability to keep up with escalating maintenance costs.<sup>405</sup>

As the three factors' application to leasing restrictions and forced sales illustrates, the reasonableness standard this Article envisions provides guidance for meaningful review of the most loaded common-interest-community decisions. Its treatment of these extreme cases also shows that the two-tiered approach (business judgment rule versus reasonableness) suggested does not imply that certain decisions will always be struck down. The tests are not mere code names for predetermined denial or permission.<sup>406</sup> As these examples highlight, even in the clearest of conflicts of interest, where scrutiny should be at its peak, decisions can still pass muster. The conflicted decisions surveyed in Subpart III.A are not decisions that should be disallowed; they are decisions whose effects and rationale should be vetted.

The suggested three-factor reasonableness test's utility is further illustrated through its application to the other categories of conflicted decisions Subpart III.A detected. For decisions which pit owners with different time horizons against each other—those pertaining to reserves and infrastructure—the first factor observes how many short-term owners supported a decision refurbishing reserves and infrastructure or how many long-term owners supported the opposite decisions. Though perfectly determining a given owner's time horizon is difficult, time horizon tends to correspond to a person's age and familial status.<sup>407</sup> Thus, some diversity along these variables among those voting for the decision should help render it reasonable. The second reasonableness factor requires ascertaining whether the losing party's interests were acknowledged. Here, decision patterns can be informative. If the community consistently refrains from refurbishing reserves and investing in infrastructure, or conversely, consistently bolsters reserves at spending's expense, one group's interests are never appreciated. Accordingly, a decision that extends an undeviating pattern in one direction or the other might appear less reasonable. The third factor—a community-wide rationale for the decision—demands a comparison of the community's decisions to common market practices. Will the disputed decision bring reserve levels roughly into line with the area's market standard? If so, the decision (whether to increase or decrease reserves) is likelier to be reasonable. With respect to decisions to assume—or refrain

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404. Developers also pay a premium for an existing building because the construction of a new building is often more expensive.

405. See MCKENZIE, *supra* note 336, at 118–19 (discussing the risks many communities that can no longer sustain themselves and might have to de-convert present).

406. But see Gerald Gunther, Foreword, *In Search of Evolving Doctrine on a Changing Court: A Model for a Newer Equal Protection*, 86 HARV. L. REV. 1, 8 (1972) (remarking that constitutional law's strict scrutiny is "strict" in theory and fatal in fact").

407. See *supra* note 329 and accompanying text.

from assuming—long-term infrastructure projects, expert opinions can ascertain rationality. Engineers and architects can attest to such projects' necessity—or lack thereof.

In communities where owners' wealth fluctuates, Subpart III.A found that decisions about special assessments require heightened review.<sup>408</sup> The first reasonableness factor, as always, centers on determining if any members of the disadvantaged group—poorer owners when the assessment is imposed, richer owners when it is rejected—voted for the challenged decision. The second factor can be established through inspecting the frequency and manner of the community's resort to special assessments. A community's routine turn to special assessments could indicate that less affluent residents' interests are consistently ignored. An indicator pointing in the opposite direction would be a community's offer of financing options to owners to alleviate their plight, or if it otherwise exhibits flexibility in treating those struggling to pay.<sup>409</sup> The third factor—the decision's rationality—hinges on the nature of the project an assessment seeks to fund.<sup>410</sup> Expert testimony respecting that project's advisability should be sought. Perhaps stronger evidence is needed to establish the reasonableness of decisions to embark on aesthetic, as opposed to structural, projects (and conversely, a decision to refrain from proceeding with a project demands stronger evidence when the project is structural).

For the final category of inherently conflicted decisions Subpart III.A identified, those affecting only some units, the first reasonableness factor would count the number of owners of detrimentally affected (or not benefited) units voting for the decision.<sup>411</sup> Indeed, in particularly extreme instances of discrete impacts, such as when one group of units stands to lose voting rights or to face increased liability for common expenses, the affirmative consent of those affected might be a prerequisite for reasonableness.<sup>412</sup> For the second reasonableness factor—the board's level of concern for the losing group's interests—a relevant factor can be found in the community's decision-making record. If some properties are repeatedly singled out for favorable or

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408. See *supra* Subpart III.A.3.

409. E.g., *Williams v. 5300 Columbia Pike Corp.*, 891 F. Supp. 1169, 1172–73 (E.D. Va. 1995) (offering, as part of a conversion plan, bank credit for owners with no access to credit).

410. See, e.g., *Papalexioiu v. Tower W. Condo.*, 401 A.2d 280, 286 (N.J. Super. Ct. Ch. Div. 1979) (“The facts . . . refute any suggestion that the board’s motives in levying the special assessment were other than a good faith effort to remedy what it considered a crisis that threatened to jeopardize the interests of all the unit owners . . .”).

411. The *Restatement* holds, “Amendments that do not apply uniformly to similar lots or units . . . are not effective without the approval of members whose interests would be adversely affected.” *RESTATEMENT (THIRD) OF PROP.: SERVITUDES* § 6.10 (AM. L. INST. 2000). However, it allows the declaration to override this requirement. *Id.*

412. *UNIF. CONDO. ACT* § 2–117 (UNIF. L. COMM’N 1980) (requiring unanimous vote for decisions altering units’ voting rights or common expense liability); see also *Twin Lakes Vill. Prop. Ass’n v. Crowley*, 857 P.2d 611, 614–15 (Idaho 1993) (holding that such an amendment deprives the affected owners of “[a]n [e]xisting [r]ight” and thus cannot be forced upon them).

unfavorable treatment, a decision targeting them yet again might be less reasonable. Conversely, a history of mixed decisions—at times singling out certain unit types, and at other times other unit types—should help establish reasonableness. The third factor, assessing the decision's rationale, demonstrates reasonableness when the decision affecting only some properties embodies more than desires to benefit, or harm, those affected properties.<sup>413</sup> If the enhanced benefits the decision bestows on specific properties are just more direct than those the community in its entirety derives, or if the decision merely attunes special benefits to special costs (for example, imposing a higher assessment on lakefront units to fund a lake improvement project),<sup>414</sup> this factor tilts toward reasonableness.

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The challenge courts face when assessing structurally conflicted common-interest-community decisions is real. While, as Part II strived to show, corporate law's established principles indicate that courts are currently shirking their most basic responsibilities by mechanically falling back on the business judgment rule in every common-interest-community dispute, the contention is not that reassuming these judicial duties would be easy. This Part showed that identifying cases of inherent conflict of interests that demand real scrutiny and analyzing those cases under a substantive reasonableness standard are achievable endeavors. Yet, the argument is not that the correct outcome of each such case is preordained or even that each case will necessarily involve the same inquiries. Neither is it that no other cases, different from those already identified, of conflicted decisions can be imagined, or that structural solutions cannot be fashioned to alleviate some of the currently inescapable conflicts. Reasonableness is a flexible standard; conflicted decision-making is an open category. The analysis's goal was to prove that meaningful guidelines can be developed to draw the contours for these concepts' application. While conclusive answers to forestall each problem associated with community decision-making before it even arises cannot be provided, this Part sketched a principled approach to tackling problems once they materialize.

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413. *In re Croton River Club, Inc.*, 52 F.3d 41, 44–45 (2d Cir. 1995), represents a case where no rationale other than harming the smaller interest group could be discerned. A special financial liability imposed on certain property owners, marina slip-owners, served to fund expenses that did not benefit them. *Id.* In a particularly egregious manner, those owners were asked to fund a pool which they had no rights to use and pay a manager who had no duties relating to the marina. *Id.*

414. *Weatherby Lake Improvement Co. v. Sherman*, 611 S.W.2d 326, 332 (Mo. Ct. App. 1980).



## CONCLUSION

A great, and constantly growing, number of Americans now live in common-interest communities. Yet perplexingly, both courts and commentators have expended limited energy observing and rationally analyzing the legal regime instituted within these communities.<sup>415</sup> The communal decisions that are the hallmark of the way so many Americans now live have elicited far too little principled examination. Perhaps, the reason for the oversight is that collective decision-making does not fall within property law's wheelhouse. Traditionally, property law was understood as centered on individual rights and powers: mostly the owner's right to manage her property by excluding others.<sup>416</sup> Property law's launching metaphor is that "the house of every . . . [man] is . . . his . . . castle."<sup>417</sup> Arrangements that center on an inescapable need to collaborate with others and to consequently adhere to others' partial control never formed the core of property law's work.<sup>418</sup>

Because property law was ill-equipped to address the questions of collective decision-making that the common-interest community presents, turning to a body of law whose domain is the treatment of such questions—corporate law—was natural. Corporate law's chief charge is to order the relationship between disparate co-owners and regulate the management body governing their interests. Drawing on corporate law's long experience with the attendant problems should have been highly beneficial. However, because courts in property cases mechanically transplanted corporate law's most salient doctrine—the business judgment rule—with little attention to its original context and nuances, property law's turn to corporate law proved counterproductive. The business judgment rule, a doctrine that is useful in the settings for which it was devised, was applied willy-nilly throughout. It was used in settings corporate law deems, explicitly and for good normative reasons, incompatible with it.

A true appreciation of the corporate law doctrine's actual workings on the one hand, and for the common-interest community's economic settings on the other, can, as this Article showed, generate a better—a more normatively principled—judicial approach. That approach incorporates a two-tiered system of judicial review for common-interest-community decisions. It demands

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415. *Lamden v. La Jolla Shores Clubdominium Homeowners Ass'n*, 980 P.3d 940, 947 (Cal. 1999) ("Our existing jurisprudence specifically addressing the governance of common[-]interest developments is not voluminous."); *Worthington Condo. Unit Owners' Ass'n v. Brown*, 566 N.E.2d 1275, 1276 (Ohio Ct. App. 1989) ("This case [regarding the validity of condominium rules] launches the court into largely uncharted waters of Ohio law.").

416. See David A. Dana & Nadav Shoked, *Property's Edges*, 60 B.C. L. REV. 753, 763 (2019).

417. *Semayne's Case* (1604) 77 Eng. Rep. 194, 195; 5 Co. Rep. 91 a, 93 b (footnote omitted).

418. See Gregory S. Alexander, *Governance Property*, 160 U. PA. L. REV. 1853, 1858 (2012) (arguing that exclusion property—property's traditional core—continues to decline while governance property, which is multiple-ownership and thus focused on internal dynamics, rises).

meaningful review for certain decisions where built-in tensions between owners render the interests of some vulnerable to abuse. Thankfully, those cases can be identified and effectively addressed. Once they are addressed, fair treatment of all owners in the common-interest community will become imaginable. Property law will thereby effectively adjust to provide solutions not only for problems plaguing castles but also for those associated with the way we live now.<sup>419</sup>

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419. *See also* Nahrstedt v. Lakeside Vill. Condo. Ass'n, 11 Cal. Rptr. 2d 299, 314 (Ct. App. 1992) (Hinz, J., dissenting), *rev'd*, 878 P.2d 1275 (Cal. 1994) ("What is true of the law is even more true of metaphor. An Englishman's home may be a castle. Increasingly, however, a Californian's home is a condominium, and I must question the majority opinion's attempt to recast the respondent's incidents of ownership by calling a condominium a 'castle.' I have never seen a condominium that even remotely resembled a castle.").