SENATE JUDICIARY COMMITTEE
Senator Thomas Umberg, Chair
2023-2024 Regular Session

AB 572 (Haney)
Version: May 26, 2023
Hearing Date: July 6, 2023
Fiscal: No
Urgency: No
AM

SUBJECT

Common interest developments: imposition of assessments

DIGEST

This bill caps annual increases in regular assessments on deed-restricted affordable housing units in homeowners associations (HOAs) at 5 percent greater than the preceding regular assessment, for HOAs that record their original declaration on or after January 1, 2024.

EXECUTIVE SUMMARY

Common interest development (CID) communities are, with rare exceptions, managed by a homeowners association (HOA) which essentially acts as a mini-government. Each property owner within the CID is a member of the HOA and the membership elects the HOA's board of directors, which is responsible for making key decisions about the CID community on behalf of everyone, including the annual assessments, which are like taxes that members must pay in order to cover communal expenses. If members do not pay their assessments in full or on time the board has the power to fine the members and, if necessary, the power to foreclose upon the offending member's property. According to the proponents, this bill is intended to address an issue that has been repeatedly brought to them as a major problem – high HOA fees for below market rate (BMR) homeowners and how this can leads to a foreclose on their homes as the increases in HOA fees can significantly outpace the income increases for many BMR homeowners.

The bill is sponsored by the Nonprofit Housing Association of Northern California and the San Francisco Housing Development Corporation. The bill is supported by various local organizations supporting housing policies. The bill is opposed by organizations representing HOAs, HOA homeowners, retired Californians, and building developers and one individual. The bill passed the Senate Housing Committee on a vote of 7 to 2.

PROPOSED CHANGES TO THE LAW

Existing law:

1) Establishes, within the Davis-Stirling Common Interest Development Act, rules and regulations governing the operation of a residential common interest development (CID) and the respective rights and duties of an HOA and its members. (Civ. Code § 4000 et seq.)

2) Requires an HOA to levy regular and special assessments sufficient to perform its obligations under the governing documents and the Davis-Stirling Act, and prohibits an HOA from imposing or collecting an assessment or a fee that exceeds the amount necessary to defray the costs for which it is levied. (Civ. Code §5600)

3) Requires the owner of a separate interest to provide a prospective purchaser a written statement from an authorized HOA representative with the amount of the HOA's current regular and special assessments and fees, any assessments levied upon the owner's interest in the CID that are unpaid on the date of the statement, and any monetary fines or penalties levied upon the owner's interest and unpaid on the date of the statement. The statement must also include any change in the HOA's regular and special assessments and fees that have been approved by the board but have not become due and payable yet. The statement must be provided to the prospective purchaser as soon as practicable before the transfer of title or execution of a sales contract. (Civ. Code §4525(a)(4))

4) Prohibits an HOA board from imposing annual increases in regular assessments for any fiscal year unless the board has complied with the annual budget requirements with respect to that fiscal year, or has obtained the approval of a majority of a quorum of members at a member meeting or election. (Civ. Code § 5605(a); § 5300(a)-(b)).)

5) Authorizes an HOA board, notwithstanding more restrictive limitations in governing documents, to impose a regular assessment up to 20 percent greater than the regular assessment for the HOA's preceding fiscal year. (Civ. Code § 5605(b).)

6) Prohibits a board from imposing regular assessments over 20 percent higher than the preceding year's regular assessment, or imposing special assessments which in the aggregate exceed 5 percent of the budgeted gross expenses of the HOA for that fiscal year, without the approval of a majority of a quorum of the members at a member meeting or election. (Civ. Code § 5605(b).)

7) Defines "quorum" for purposes of 5) and 6), above, to mean more than 50 percent of the members. (Civ. Code § 5605(c).)

8) Requires, under regulations adopted by the Department of Real Estate (DRE), that governing instruments for CIDs provide for a variety of items, including:
    a) procedures for calculating and collecting regular assessments from owners to defray expenses attributable to the ownership, operation, or furnishing of common interests or to the enjoyment of mutual and reciprocal rights of use; and
    b) procedures for establishing and collecting special assessments for capital improvements or for other purposes. (10 Cal. Code Reg. § 2792.8(a)(4)-(5).)

9) Requires, under DRE regulations, that regular assessments are ordinarily to be levied against each owner according to the ratio of the number of subdivision interests owned by the owner assessed to the total number of interests subject to assessments. In the case of a subdivision offering in which it is reasonable to anticipate that any owner will derive as much as 10 percent more than any other owner in the value of common services supplied by the HOA, the assessment against each owner may be determined according to a formula or schedule under which the assessments against the various subdivision interests bear a relationship which is equitably proportionate to the value of the common services furnished to the respective interests. (*Id*. § 2792.16)

10) Provides that regular and special assessments are delinquent 15 days after they become due, unless the declaration provides a longer time period. If an assessment is delinquent, the HOA may recover all of the following:
    a) reasonable costs incurred in collecting the delinquent assessment, including reasonable attorney's fees;
    b) a late charge not exceeding 10 percent of the delinquent assessment or $10, whichever is greater, unless the declaration specifies a late charge in a smaller amount; and
    c) interest on all sums imposed at an annual interest rate not to exceed 12 percent, commencing 30 days after the assessment becomes due, unless the declaration specifies the recovery of interest at a lesser rate. (Civ. Code § 5650(b).)

11) Requires an HOA to notify the owner of record in writing by certified mail at least 30 days prior to recording a lien upon the separate interest of the owner of record to collect a past-due debt under 10), above. The notice must include the following information:
    a) a general description of the collection and lien enforcement procedures of the HOA and the method and calculation of the amount, and other specified notices;
    b) an itemized statement of the charges owed by the owner, including the amount of any delinquent assessments, the fees and reasonable costs of collection, reasonable attorney's fees, any late charges, and interest, if any;

c) the right to request a meeting with the board to discuss a payment plan for the debt; and
d) other statements and rights of the owner. (Civ. Code § 5660.)

12) Prior to initiating a foreclosure on an owner's separate interest, the HOA must offer the owner and, if so requested by the owner, participate in dispute resolution pursuant to the HOA's meet and confer program or other alternative dispute resolution as required by law. The board must approve a decision to initiate a foreclosure of a lien for delinquent assessments by a majority vote of the directors in an executive session. (Civ. Code § 5705.)

13) Prohibits an HOA that seeks to collect delinquent regular or special assessments of an amount less than $1,800 from collecting that debt through judicial or nonjudicial foreclosure, but allows the HOA to attempt to collect or secure that debt by a civil action in small claims court, by recording a lien on the owner's separate interest upon which the HOA can foreclose after the debt reaches or exceeds $1,800 or the debt is more than 12 months delinquent, or any other manner provided by law. (Civ. Code § 5720.)

14) Provides that the covenants and restrictions in the declaration are enforceable equitable servitudes, unless unreasonable, and must inure to the benefit of and bind all owners of separate interests in the development. Unless the declaration states otherwise, these servitudes may be enforced by any owner of a separate interest or by the HOA. (Civ. Code § 5975.)

This bill:

1) Prohibits HOA boards that record their original declaration on or after January 1, 2024, notwithstanding more restrictive limitations in governing documents, from imposing a regular assessment against an owner of a deed-restricted affordable housing unit that is more than 5 percent greater than the preceding regular assessment.

2) Authorizes HOA boards that record their original declaration on or after January 1, 2024 to impose an assessment against an owner of a deed-restricted affordable housing unit that is lower than the assessment imposed against other owners according to the proportional ownership of total subdivision interests subject to assessments.

3) Exempts from these provisions a development where 100 percent of the units, exclusive of a manager's unit or units, are occupied by, or available at affordable housing cost to, lower income and moderate-income households, as defined.

COMMENTS

1. Stated need for the bill

The author writes:

> The Below Market Rate (BMR) Homeownership programs are one of the best tools we have to provide homeownership opportunities to low-income Californians – but the rapidly increasing HOA fees are defeating the purpose of these programs. BMR homeowners are foreclosing on their homes faster than ever because their HOA fees are becoming more expensive than their mortgage. A foreclosure impacts people's credit scores for years to come. So instead of helping low-income people build generational wealth through homeownership, the HOA fee increases are pushing them into more debt. AB 572 addresses this issue by capping annual HOA fee increases at 5% for BMR homeowners to make sure that low-income Californians are not forced into foreclosing on their homes.

2. Background on HOAs

CIDs are self-governing groups of dwellings that share common spaces and amenities. They come in a wide variety of physical layouts: condominium complexes, apartment buildings, and neighborhoods of detached, single-family residences, for example. Units within common housing developments currently account for approximately a quarter of the state's overall housing stock, meaning that the laws governing such developments have a large impact on the population. In California, CIDs are governed by the Davis-Stirling Act. (Civ. Code §§ 4000-6150.)

The Davis-Stirling Act sets forth a system for CID self-governance. The owners of the separate properties within the community are the members of the HOA. HOA members vote for the board of directors of the association that oversees operation of the community. An HOA board has a number of duties and powers. The board manages the community, frequently by hiring an individual or entity to do so on its behalf. The board determines the annual assessments – much like taxes – that members must pay in order to cover communal expenses. The board enforces the community rules and can propose as well as make changes to those rules. If members do not pay their assessments in full or on time, or if members violate the community rules, the board has the power to fine the members and, if necessary, the power to foreclose upon the offending member's property. This combination of responsibilities and authority has led multiple courts to observe that HOAs function in many ways almost "as a second municipal government, regulating many aspects of [the homeowners'] daily lives." (*Villa Milano Homeowners Ass'n v. Il Davorge* (2000) 84 Cal.App.4th 819, 836. Internal citations omitted.)

The Senate Housing Committee analysis notes:

> There are a variety of different types of CIDs, including condominium complexes, planned unit developments, and resident-owned mobilehome parks. In recent years CIDs have represented a growing share of California's housing stock. Data from 2019 indicates that there are an estimated 54,065 CIDs in the state that are made up of 5 million housing units, or about 35% of the state's total housing stock.[1]

HOAs must collect assessments from members to fund a variety of budgeted costs, such as maintenance and repair, amenities, shared services, taxes, insurance the HOA is required to purchase, and other general operating expenses. Under existing law there are three types of assessments HOAs levy on members in order to fund their obligations: regular assessments, special assessments, and emergency assessments.

A board must adopt a budget for the year in order to increase a regular assessment, and existing law caps regular assessments at up to 20 percent over the regular assessment for the preceding fiscal year. Boards are prohibited from imposing regular assessments over 20 percent higher than the preceding year's assessment, or imposing special assessments that, in the aggregate, exceed 5 percent of the budgeted gross expenses of the HOA for that fiscal year, unless they get approval of a majority of a quorum of the members of the HOA to impose assessments larger than the caps.

Emergency assessments can only be levied to cover extraordinary expenses required by a court order, necessary to repair or maintain CID property where there is a threat to personal safety, or necessary to repair or maintain CID property that could not have been reasonably foreseen by the board in the annual budget preparation. (Civ. Code § 5610.) In the latter circumstance, the board must pass a resolution containing findings as to why the extraordinary expense is necessary and why it was not anticipated during the budgeting process, and must distribute the resolution to members along with the notice of increased assessment.

Assessments can be equally assessed among owners or, in some instances, differently depending on what DRE regulations refer to as "unequal access to common services provided by the HOA." (10 Cal. Code Reg. § 2792.16.) These types of assessments are called variable assessments. According to DRE's "Operating Cost Manual for Homeowners Associations" section on variable assessments:

> Equal proration involves the simple process of dividing the total costs of a budget item by the number of units in the subdivision. Variable prorations entail the use of a factor or factors that differ from one unit to the next, e.g., square footage of floor space. Equal assessments should be used wherever reasonably equitable, since variable proration can be a complicated and controversial process.

[1] Sen. Comm. on Housing analysis of AB 572 (2023-24 Reg. Sess.) as amended May 26, 2023 at p. 4.

> Variable prorations should be employed only when services are provided to units in unequal proportions. DRE regulations allow the use of variable assessments against units only if one unit will derive as much as 10 percent more than another unit in the value of common goods and services supplied by the association. Examples of services provided in unequal proportions directly to units are insurance, domestic water and gas, if applicable, and exterior and roof maintenance. […] In most instances, however, variable proration is not considered preferable to equal proration if differential in the level of services supplied by the association to the units is less than 20 percent. Variable assessments should be used when the differential exceeds 20 percent.[2]

3. This bill seeks to address the issue of high HOA fees for below market rate (BMR) homeowners by placing a 5 percent cap on HOA assessments for BMR homeowners

The proponents of the bill note that many cities across the state have created inclusionary housing programs that require private developers to provide a percentage of affordable homes sold at below market rate value due to the importance of homeownership as a means to create intergenerational wealth for low-income and BIPOC families. These BMR homeownership programs are aimed at first-time homebuyers who are low and moderate income, and are usually condos in mixed-income buildings, many with monthly Homeowners Association (HOA) fees. Low-income, first-time buyers must meet various qualifications and then they are entered into a lottery system to purchase a home. The proponents of the bill argue that while BMR ownership programs are specifically designed to make the initial cost of homeownership more affordable, the increases in HOA fees can significantly outpace the income increases for many BMR homeowners. Since current law sets the maximum HOA fee increase at 20percent for all homeowners regardless of income level, after only a few years of large increases, the HOA fees of a BMR homeowners can increase beyond the original mortgage of a house, pushing them toward the risk of foreclosure.

Home foreclosure can have devastating impacts on a person's credit score. Borrowers with a good credit score can lose 100 points or more on their score if a lender forecloses on their home.[3] After a foreclosure it can take up to seven years to rebuild your credit score. Additionally, credit scores are used for housing applications, auto loans, insurance coverage, and more. The Federal Housing Administration Home Loan program requires a three-year waiting period after a foreclosure before someone can apply for a loan, while Fannie Mae/Freddie Mac can require as much as seven years. A low-income homeowner whose home is foreclosed on may not only lose the opportunity to own a home, but it can send them down a path of decades of debt and other financial hardship.

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[2] Operating Cost Manual, Cal. Dept. or Real Estate at p. 3, available at https://www.dre.ca.gov/files/pdf/re8.pdf.

[3] *How Does a Foreclosure Affect Your Credit Score?* Consumer Education Services Inc., available at https://www.cesisolutions.org/resources/credit-and-debt-resource-center/consequences-of-foreclosure.

The proponents of the bill also argue that the potential for large increases of HOA fees also discourages low-income buyers from purchasing BMR units, leading to vacancies and upending the potential positive impact of the BMR homeownership program. This only worsens California's housing crisis.

In response to this issue, the bill seeks to prohibit HOA boards that record their original declaration on or after January 1, 2024, notwithstanding more restrictive limitations in their governing documents, from imposing a regular assessment against an owner of a BMR unit that is more than 5 percent greater than the preceding regular assessment. The bill provides an exception to these provisions for a development where 100 percent of the units, exclusive of a manager's unit or units, are occupied by, or available at, affordable housing cost to lower income and moderate-income households. The bill's provisions only apply to regular assessments and does not impact special assessments or emergency assessments. The author amended this bill in the Assembly to makes it provisions only apply prospectively. This change led to several groups that were in opposition, such as the California Association of Realtors and the California Bankers Association, to change their position to neutral.

4. Remaining opposition concerns

a. The bill shifts burden on HOA assessments to market rate homeowners

The California Alliance for Retired Americans, the Center for California Homeowner Association Law, and the Community Associations Institute's California Legislative Action Committee write in opposition to the bill all raising the same concern—that the bill shifts the costs of HOA assessments onto market rate homeowners. They state that while sympathetic to the issue the bill is trying to address, the solution is not to place more cost burdens on market rate homeowners. They note that there is no evidence to show that market rate homeowners can afford to subsidize the cost of homeownership for BMR homeowners, and state that all residents in HOAs are currently struggling to afford the increase in HOA fees. They point out that many residents of HOAs are seniors on fixed and reduced incomes who have very little ability to absorb additional costs into their limited budgets. They fear that this bill will lead to more foreclosures for market rate homeowners as HOAs will try and shift the costs they will no longer be able to allocate evenly among all owners onto the market rate owners, exacerbating the already concerning issue of exorbitant HOA fees and housing crisis the sponsors of the bill are trying to address. The opposition additionally argues that the bill will create tension within a community when neighbors realize that they are paying more than some of their neighbors. They posit that this bill will invite litigation from HOA members. They also raise issues that purchasers of a unit will be unaware that they will be required to pay a higher proportion of HOA fees than other owners.

b. Concerns from the California Building Industry Association

The California Building Industry Association (CBIA)is opposed unless amend stating in their opposition letter that the cap on an HOA assessment fee in this bill is not adjusted for the cost of living as the 5 percent rent cap is in AB 1482 (Chiu, Ch. 579, Stats. 2019). CBIA writes "we are opposed to AB 572 because the 5% cap does not keep pace with inflation or increases due to changes in law" and that "the limit proposed in AB 572 does not allow for the cost to comply with new laws as they are enacted."

They also want the effective date pushed back a year to January 1, 2025, claiming it takes a year to get approval of the governing documents by the Department of Real Estate (DRE) and fear the current effective date of January 1, 2024 will "mess up or delay" projects that have already been submitted to DRE. Lastly, they seek an amendment to "limit the number of units in a development whereby a cap would apply to 15% to ensure that the cost shift to the market rate homeowners is not unduly burdensome" as under the bill currently you "could have a situation in which 90% of units in a development are deed-restricted and have a cap, while the other 10% of market rate units would have to subsidize all of those units, raising their costs significantly."

5. Proposed Amendments

The Committee may wish to amend the cap on the fee assessment in this bill to provide for more flexibility and account for the percentage change in the cost of living. Looking at the provisions of AB 1482 as a guide, the Committee may wish to provide that the assessment cap be amended to be the greater of either: 5 percent or the percentage change in cost of living, whichever is greater, than the prior assessment. However, in no instance would the assessment be higher than 10 percent of the prior assessment for BMR homeowners. "Percentage change in the cost of living" would have the same definition as it does in AB 1482, existing subdivision (g) of Section 1947.12 of the Civil Code.

Additionally, the Committee may wish to amend the bill to provide that the cap on assessments for BMR homeowners does not apply to a development where 30 percent or more of the units, exclusive of a manager's unit or units, are occupied by, or available at affordable housing cost to, lower income and moderate-income households.

The specific amendments are as follows:[4]

Section 5606 of the Civil Code is amended to read:

(a) Annual increases in regular assessments for any fiscal year shall not be imposed unless the board has complied with paragraphs (1), (2), (4), (5), (6), (7), and (8) of subdivision (b) of Section 5300 with respect to that fiscal year, or has obtained the approval of a majority of a quorum of members, pursuant to Section 4070, at a member meeting or election.

(b) Notwithstanding more restrictive limitations placed on the board by the governing documents, the board may not impose a regular assessment that is more than 20 percent greater than the regular assessment for the association's preceding fiscal year or impose special assessments which in the aggregate exceed 5 percent of the budgeted gross expenses of the association for that fiscal year without the approval of a majority of a quorum of members, pursuant to Section 4070, at a member meeting or election.

(c) (1) *(A)* For an association that records its original declaration on or after January 1, 2024, notwithstanding more restrictive limitations placed on the board by the governing documents, except as provided in paragraph (3), the board shall not impose a regular assessment against an owner of a deed-restricted affordable housing unit that is more than 5 percent greater than the preceding regular ~~assessment.~~ a*ssessment or that is greater than the percentage change in cost of living, whichever is larger.*

(B) When calculating the imposition of a regular assessment against an owner of a deed-restricted affordable housing unit under this subdivision, the board shall not impose a regular assessment that exceeds 10 percent greater than the preceding regular assessment.

(C) For purposes of this paragraph, "percentage change in the cost of living" means the percentage change from April 1 of the prior year to April 1 of the current year in the regional Consumer Price Index for the region where the residential real property is located, as published by the United States Bureau of Labor Statistics. If a regional index is not available, the California Consumer Price Index for All Urban Consumers for all items, as determined by the Department of Industrial Relations, shall apply.

(2) For an association that records its original declaration on or after January 1, 2024, notwithstanding any other law, except as provided in paragraph (3), the board may impose an assessment against an owner of a deed-restricted affordable housing unit that is lower than the assessment imposed against other owners according to the proportional ownership of total subdivision interests subject to assessments.

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[4] The amendments may also include technical, nonsubstantive changes recommended by the Office of Legislative Counsel.

(3) This subdivision does not apply to a development where ~~100~~ *30* percent *or more* of the ~~units~~ *units,* exclusive of a manager's unit or ~~units~~ *units,* are occupied by, or available at affordable housing cost to, lower income and moderate-income households, as defined by Sections 50079.5 and 50052.5, respectively, of the Health and Safety Code.

(d) For the purposes of this section, "quorum" means more than 50 percent of the members.

6. Statements in Support

The San Francisco Housing Development Corporation and the Non-Profit Housing Association of Northern California, the sponsors of the bill, write in support stating:

> Recently, increases in HOA dues have significantly outpaced the income increases for many BMR homeowners, putting them at risk of foreclosure or HOA fee default. This development is highly troubling for a program that is meant to be a promise of stability and financial security to low- and moderate-income homeowners.
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> From large urban areas like San Francisco, to smaller suburban centers like San Ramon, and beyond the Bay Area, affordable housing developers and advocates are reporting similar problems wherever these deed-restricted BMR programs exist. This is also not a new issue – BMR programs have struggled with this issue for decades but the recent spikes in HOA fees have highlighted this long standing issue.
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> In addition to the problem of foreclosures, BMR units with higher HOA dues are harder to sell, which can lead to lengthy vacancies, undermining the goals of this program during a statewide housing crisis. In one especially egregious example, the monthly dues in a San Francisco BMR unit started from $1,500 per month. Fewer buyers applied to the BMR units because HOA dues were a concern, especially when they can increase by a large percentage each year.
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> This is a small yet important change intended to slow down the fee increases that are forcing many families out of their homes.

7. Statements in Opposition

The Center for California Homeowner Association Law writes in opposition stating:

> AB 572 is well-intentioned legislation seeking to solve the problem the very real problem of escalating regular assessments. As noted above: regular assessments can increase by 20% a year, when we can safely say that few working people get salary increases of 20% a year. But shifting the cost burden onto another class of owners doesn't solve it.

> Yes, affordable homeownership units built by public and private developers should be preserved. Public monies and resources – land, for example – are poured into building homes that are to become the key to establishing economic security.
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> However, AB 572 will not solve the assessment affordability problem but instead will trigger litigation and dissension in the association community. (footnotes omitted)

The California Alliance for Retired Americans writes in opposition stating:

> Our reading of AB572 is that it would force seniors who buy homes at market rates to subsidize the assessments of owners who buy homes at reduced prices or with some form of public assistance. Owners who would be required to take on these new costs would include seniors who now live on fixed and reduced incomes. Their main source of income is Social Security – not pensions or investments in the stock market.
>
> Of special concern to us are senior women who were never in the job market or who had part-time or sporadic employment and whose chief financial asset is now their home. Such women have no pensions to speak of and their chief income is miniature Social Security checks. Senior women in particular have a hard time stretching income to cover housing costs, increasing health care costs, and the costs of transportation and utilities.
>
> AB572 would require seniors to take on another cost: not just increased regular assessments but the burden of subsidizing the assessments of their neighbors who own Below-Market-Rate homes.

SUPPORT

Nonprofit Housing Association of Northern California (sponsor)
San Francisco Housing Development Corporation (sponsor)
Devine & Gong, Inc.
East Bay YIMBY
Generation Housing
Grow the Richmond
Homeownership San Francisco
Housing Leadership Council of San Mateo County
How to ADU
Mission Economic Development Agency (MEDA)
Mountain View YIMBY
Napa-Solano for Everyone
Northern Neighbors
Peninsula for Everyone
People for Housing Orange County

Progress Noe Valley
San Francisco YIMBY
San Luis Obispo YIMBY
Santa Cruz YIMBY
Santa Rosa YIMBY
South Bay YIMBY
Southside Forward
Ventura County YIMBY
YIMBY Action

OPPOSITION

California Alliance for Retired Americans
California Building Industry Alliance
Center for California Homeowner Association Law
Community Associations Institute's California Legislative Action Committee
1 individual

RELATED LEGISLATION

Pending Legislation: AB 1458 (Ta, 2023) would authorize a reduced quorum requirement for homeowner association board elections if the first attempt at holding the election failed to establish a quorum and certain procedural requirements are met, as specified. AB 1458 is currently pending in this Committee.

Prior Legislation: None known.

PRIOR VOTES

Senate Housing Committee (Ayes 7, Noes 2)
Assembly Floor (Ayes 55, Noes 18)
Assembly Housing and Community Development Committee (Ayes 5, Noes 1)

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