May 8, 2013

VIA EMAIL – Maggie.Carlton@asm.state.nv.us; William.Horne@asm.state.nv.us; Paul.Aizley@asm.state.nv.us; David.Bobzien@asm.state.nv.us; Andy.Eisen@asm.state.nv.us; Lucy.Flores@asm.state.nv.us; Joe.Hogan@asm.state.nv.us; Marilyn.Kirkpatric@asm.state.nv.us; Mike.Sprinkle@asm.state.nv.us; Paul.Anderson@asm.state.nv.us; Tom.Grady@asm.state.nv.us; John.Hambrick@asm.state.nv.us; Crescent.Hardy@asm.state.nv.us; Pat.Hickey@asm.state.nv.us; Randy.Kirner@asm.state.nv.us; AsmWM@asm.state.nv.us

To: Maggie Carlton - Chair, William C. Horne – Vice Chair, and Members of the Assembly Committee on Ways and Means

Re: ASSEMBLY BILL 370

Dear Members of the Assembly Committee on Ways and Means:

The Common-Interest Committee of the State Bar's Real Property Section ("CIC Committee") respectfully submits this opposition to the First Reprint of Assembly Bill 370 ("AB 370") on behalf of the CIC Committee. Because of time constraints, we speak only for members of the CIC Committee and not the Section or the State Bar. The membership list of the CIC Committee is attached hereto as **Exhibit "1"**.

AB 370
General Comments:

AB 370 would allow for the creation of an unspecified program, i.e. the Referee Program introduced in AB 34. In the original bill, the Referee Program would have replaced and circumvented the current and highly successful mandatory mediation/arbitration program adopted by the Nevada Legislature in 1995. The First Reprint makes the Referee Program an option, and mandates Mediation if not selected, but leaves Arbitration as only an option if the Referee Program or Mediation do not produce the desired results, and allows the parties to go directly to District Court. While this is an improvement over the original bill, the Referee Program raises serious due process concerns, and Mediation is not applicable to many disputes; in the existing ADR framework of NRS 38.300 et seq., the parties may select either Mediation or Arbitration (binding or non-binding), whichever is more suited to the circumstances.

AB 370 is an attempt to grant to the Division the power to implement the Referee Program, which was widely opposed when presented to the entire Assembly Committee on Judiciary in AB 34. In fact, the Referee Program has drawn a lot of criticism from numerous organizations, including this CIC Committee, which recommended that the Referee Program introduced in AB 34 be deleted in its entirety. AB 370 is the forerunner to adoption of that Referee Program. Additionally, the Referee Program was recently the subject of litigation in *Rancho Bel Air Property Owners' Association, Unit 2, Inc. vs. State of Nevada, Department of*

Business and Industry, Real Estate Division, Office of the Ombudsman for Common-Interest Communities and Condominium Hotels, et. al., Eighth Judicial District Court Case No. A-13-679889-C, filed April 12, 2013.

In the *Rancho Bel Air* case, the Plaintiff filed a Complaint and Motion for Preliminary Injunction, to prohibit the Real Estate Division and Ombudsman from proceeding with a matter in the Pilot Referee Program (the Pilot Referee Program has been held up as a model of success for both AB 34 and AB 370 proposed versions of the Referee Program). Shortly after the Complaint and Motion were filed, the Division and Ombudsman agreed to withdraw the matter from the Pilot Referee Program, and the case was dismissed.

The pilot Referee Program, and the program contemplated by AB 370 (and AB 34), might contain some of the same due process issues involved in the *Rancho Bel Air* case. We simply do not know. There are currently no official procedural rules in place to guide the parties or the Referee in the Pilot Referee Program Hearings that the CIC Committee is aware of. Despite prior requests for written procedural information of both the Department and Division, no official information has been produced. All that is known procedurally about the Referee Program, as proposed in AB 370, is that it is selected by the parties, there is a Complaint and Answer and a Hearing (which can be waived), a Decision will be rendered, and the Referee may not award attorney's fees. Contrast this with the numerous procedural due process rules currently in statute for an Arbitration under NRS chapter 38:

- NRS 38.231: the conduct of Hearings; power to hold conferences; determination of admissibility, relevance and materiality of evidence; summary disposition of claims or issues; time and date for Hearing and notice requirements; postponement and adjournment rules; replacement Arbitrators,
- NRS 38.232: representation by counsel,
- NRS 38.233: subpoenas for attendance of witnesses, production of records and other evidence, and administration of oaths; depositions for witnesses who may be unable to attend the Hearing; discovery rules and enforcement for noncomplying parties; protective orders to prevent disclosure of privileged information,
- NRS 38.236: Award requirements including authentication, notice, extension of time,
- NRS 38.237: change or modification of Award motions and procedure,
- NRS 38.238: Remedies of Award,
- NRS 38.242: Modification or correction of the Award in Court due to mathematical miscalculation, Award on a claim not submitted, or imperfect in form,

Although the First Reprint of AB 370 allows Confirmation of a Referee Decision under NRS 38.239, the enabling language for Arbitrations found in NRS 38.330(4) [*"the arbitration of a claim pursuant to this section must be conducted in accordance with the provisions of NRS 38.231, 38.232, 38.233, 38.236 to 38.239, inclusive, 38.242 and 38.243"*] does not exist for the Referee Program in AB 370, and thus all of the due process concerns above remain unaddressed.

In fact, at this point in time, all that is known about the potential procedural rules for the Referee Program itself, if AB 370 is enacted, is the conduct of the current Pilot Referee Program, which has been the subject of litigation for due process violations. The Nevada Legislature is being asked to codify a program which has serious due process issues, without knowledge of how the program would be conducted after the bill is adopted.

Since the only guide for the Legislature as to what procedure might be adopted if AB 370 is enacted is the current pilot Referee Program, the current due process issues need to be examined:

- The Pilot Referee Program Hearing Notices state that the program is *"**not** mandatory,"* while setting a date for the Hearing approximately two weeks from the Hearing Notice, setting a date for submission of documents of four (4) calendar days before the Hearing, stating that the Decision of the Referee will be non-binding, and that *"A non-binding decision is a determination that is intended to be persuasive, but that neither party is required by law to comply with,"* that the Hearing *"will be recorded."*
    - When the parties appear, they are sworn under oath (this is not disclosed in the Hearing Notice) and the proceedings are recorded. There is no procedure to object to the recording of the proceedings, which are supposedly *"non-binding,"* but are *"intended to be persuasive."* There has been no response as to who the proceedings are intended to persuade.
    - If a party does not appear, the Hearing proceeds regardless, and a Decision is rendered which is *"intended to be persuasive"* to an undisclosed recipient(s).
    - The Parties are given no procedures for the conduct of the Hearing – they enter the proceedings without any knowledge of how they will be conducted, other than the fact they will be recorded.
- Despite the fact that the Division and Ombudsman have no current authority under the statutes to administer a program to render *adjudicative* Decisions, they have done so regardless.
- Despite the fact that an Assistant Attorney General rendered a legal opinion on May 5, 2008, which made clear that adjudication of governing document disputes must go through the mediation/arbitration process in NRS 38.300 et seq., and not through the Division and Ombudsman Intervention Affidavit process under NRS 116.760, the Ombudsman and Division have, nonetheless, adjudicated governing document disputes through the Pilot Referee Program and the Intervention Affidavit process.
- Because the Intervention Affidavit process is investigative in nature, and NRS 116.757 requires the Division keep the written affidavit confidential, including from the Respondent, the Respondents in the Pilot Referee Program have been denied one of the most basic due process rights in that program; the right to know the charges. In other words, Respondents in the Pilot Referee Program are expected to Answer an Intervention Affidavit Complaint they do not get to see.

The above is just a handful of the due process issues addressed in the *Rancho Bel Air* Complaint and Motion, which should be reviewed for more detail on this subject. **However, suffice it to say for purposes of this submission that the Division, which would be tasked with producing the rules to provide due process in the AB 370 Referee Program, is the same Division which has failed miserably in providing any due process in the Pilot Referee Program, and has been the subject of litigation as a result. The Legislature is being asked to take it on faith they will not run the AB 370 Referee Program the same way they have run the Pilot Referee Program.**

NRS 38.300 et seq., enacted by the Nevada Legislature in 1995, was designed to provide a fast, effective and economical means of resolving contested claims relating to issues arising out of sometimes complex declarations of covenants, conditions and restrictions and other governing documents, as well as coordinating them with the statutory impacts of Chapter 116. The arbitration and mediation panels were expected by parties to have substantive knowledge, experience and understanding of community association law and the issues facing homeowners and community associations, as well as skill in management of the arbitration process.

Chapter 38.300 et seq., included options for choice by the parties of either binding or non-binding arbitration, or mediation. If the arbitration was non-binding, Chapter 38.300 et seq. offered the option of filing a complaint for trial de novo in the District Court if a party to the arbitration believed that an arbitrator's decision was incorrect. If no trial de novo was requested, either party could apply to the District Court for entry of judgment on the award.

Courts were pleased with this ADR process because it reduced their caseloads involving homeowner association disputes. Although there would always be a winner and loser (as is the case in all litigation), most parties were nevertheless pleased with the process because it was less expensive but provided necessary procedural and substantive safeguards, including enforcement of valuable contractual rights set forth in the Governing Documents, statutes and case law.

While no dispute resolution system is perfect, this program has been remarkably successful over its near 20 year history in achieving its targeted goals of having community association disputes resolved faster, more economically, and with trustworthy and respected results have been satisfied for more than twelve years. While no ADR process is perfect, revisions to a program that has been demonstrated to be effective over a long period of time should identify and target specific problems so that the best aspects of the process can be preserved and the difficulties addressed and fixed.

The CIC Committee is unaware of the specific issues which this Bill is designed to address. However, a review of the proposed legislation would suggest that the primary areas of concern are as follows:

1. The cost of arbitration proceedings:
   a. Assessment of attorney's fees in arbitration awards
   b. Assessment of arbitrator's fees

2. Control of the selection and appointment of decision makers

Each of these concerns are worthy of consideration and, to the extent that the current system can be improved, legislative attention to such improvement is certainly legitimate. Creating an entirely new system may have a number of unknown and unintended consequences, including, but not limited to, the following:

Arbitration Costs

Costs of ADR proceedings, in contrast to its alternative (litigation in court) should always be a concern. The inquiry, however, is whether the proposed legislation will actually cut costs, or increase them, and if the parties' constitutionally protected rights to due process will be preserved. We have not had the time to obtain statistics regarding the number of arbitral awards issued through Chapter 38.300 et seq., that have been subjected to trial de novo, and of those cases, in how many cases have court decisions conformed with the arbitral awards. Based on general conversations with counsel in both Reno and Las Vegas, however, over the past several years, it appears that most of these disputes end with the arbitration or mediation under NRS 38.300 and court process is thereby reduced.

Arbitration awards pursuant to that statute have typically been governed by the rights, obligations and remedies conferred by declarations of covenants, conditions and restrictions, which are uniformly held by the Nevada courts as well as courts of every other jurisdiction to be contracts between and among homeowners and binding on all owners. The Declaration is recorded; prospective owners have the opportunity to review these documents prior to buying. Negating or modifying these documents after the fact affects all owners in the community not just those who may run into problems.

Some of the costs which AB 370 appears to address are as follows:

1. Attorneys' Fees

   a. The proposed legislation would prevent a referee from awarding attorneys' fees and costs. Most CC&R's authorize an award of attorneys' fees to prevailing parties, whether the association or an aggrieved homeowner. Nevada statutes (NRS 17.010 and other statutes) authorize an award of attorneys' fees to prevailing parties in court proceedings and non-HOA arbitrations (NRS 38). Contractual rights to an award of attorneys' fees are generally enforced by Nevada statutes and case law. Since CC&R's are uniformly considered a contract, according to Nevada law, if attorneys'

fees are deemed appropriate, an arbitrator or judge may award them in a reasonable amount. The proposed legislation may contravene Nevada statutes, case law, and the right of parties to enforce contracts by overriding the parties' contractual rights.

b. The Nevada legislature has consistently recognized that the threat of having to pay an opposing party's attorneys' fees and costs has always been deemed a disincentive to filing frivolous lawsuits and to require parties to seriously consider the implications of refusing legitimate offers to settle claims.[1] AB 370 eliminates the risk that attorneys' fees may be awarded, even in appropriate cases, whether the claims are legitimate or frivolous. The unintended effect of this may be to eliminate the normal constraints upon filing claims, whether by associations (who may have sufficient funds to support such filings) or by individual homeowners who wish to file claims in an effort to harass an opponent. The legislation cannot stop parties from retaining counsel, only from recouping costs from opponents. Thus, homeowners and associations may still incur substantial attorneys' fees and costs in prosecuting or defending legitimate positions, without the ability to have those costs assessed against a wrongdoer.

c. Nothing in AB 370 will prevent a court on trial de novo from awarding fees and costs, as it may be authorized to do in enforcing the CC&R's and Nevada statutes. If this is the only way that a prevailing party can obtain an award of attorneys' fees and costs, it is anticipated that virtually every Referee's decision will be subjected to filing a trial de novo. Instead of working with the courts to streamline the dispute resolution process, as was the goal of NRS Chapter 38, this legislation will have the opposite effect.

2. Arbitration Costs

a. Under Chapter 38.300 et seq., the cost of arbitration is borne by the disputants; there is no similar provision for funding this new program. There is also no indication that the number of disputes arising out of Governing Documents and Chapter 116 will be reduced. Before embarking on a program to be funded through the Account for Common-Interest Communities, there should be significant inquiry into the anticipated cost. Moreover, while it is a commendable goal to provide adjudicative processes at little or no cost to litigants, once again parties (both homeowners and associations) may be more likely to file claims because the disincentive of cost will be eliminated.

[1] NRS 17.115, 18.010, NRCP 68, NRS attorneys' fees awards under mechanic's lien and construction defect statutes, for example, illustrate the extensive use of this policy.

b. An absolute necessity in protecting the rights of the parties in any dispute resolution proceeding is the neutrality of the arbitrator or mediator. AB 370 has the potential of influencing that neutrality. Chapter 116 gives the Ombudsman's office and Division the right to investigate, prosecute and impose penalties on those who violate rules applicable to community associations. AB 370 would give the Division the right to select and pay Referees who would be rendering decisions on claims brought pursuant to the proposed legislation. An appearance of impropriety and potential lack of neutrality is inherent in this process due to the potential that the referees selected by the Division who are rendering these awards may be improperly influenced to conform to policies of the Ombudsman's office and Division. This raises due process concerns.

c. A further potential risk of the appearance of impropriety is the fact that under NRS 116.625 as it currently exists, unit owners may come to the Ombudsman for assistance in "understanding their rights and responsibilities as set forth in this chapter 116B of NRS and the governing documents of their associations" and members of executive boards may seek the assistance of the Ombudsman "to carry out their duties; . . ." Confidentiality of settlement discussions is recognized in the Nevada Rules of Civil Procedure. Any confidentiality expected by the parties in their discussions with the Ombudsman, including potentially attorney work product information, has the potential under AB 370 of being disclosed to the Referee appointed by the Division, for which the Ombudsman works, and potentially thereafter to investigators and prosecutors under Chapter 116. Once again, neutrality of mediators and arbitrators which is critical to the respect required of these ADR processes is jeopardized by this proposed legislation.

d. By preventing parties from availing themselves of the selection of appropriate forums and methods of resolution of NRS 38.300 et seq., at the inception of the dispute, this proposed legislation takes discretion away from the parties, and may increase costs. Additionally, this unintended consequence may result in a threat to procedural and substantive due process of the parties to the dispute, as prosecutorial and adjudicative functions are consolidated in the same agency.

e. The proposed legislation, essentially repeals NRS 38.300 et seq., a statutory ADR process which has been effective as noted above, for almost 20 years, and substitutes an unknown (or known process violative of due process).

Based on the foregoing, discarding the current, extremely successful, alternate dispute program should not be taken so carelessly and recklessly. The current ADR program has exceeded the expectations of those that were involved in its adoption by creating a balanced process that allows for quicker and less expensive proceedings, while retaining accountability for those initiating the claim and asserting wrongdoing on the part of an association, its directors

or officers or its community manager. The current ADR program had the desired effect of keeping cases out of the judicial system, thereby, substantially reducing the legal fees and costs incurred by associations and owners. The Division has not offered any data or evidence to support a flaw in the program. What is being offered in its place is an unspecified pilot program with very little history and the appointment of Referees that are approved by the Division that lack experience with association operations and the laws and codes that govern conduct therein.

Summary:

If AB 370 is adopted, it would have the following effects:

- Deny due process to associations.
- Bypass the current mandatory ADR process and cause more association disputes to be filed in district courts.
- Eliminate highly qualified arbitrators with extensive experience in association matters from the ADR process and replace them with Referees, approved by the Division, that lack knowledge and experience in association law.
- Purportedly reduce costs but if a new program is adopted, i.e. the Referee program, the same costs would still be required.
- Add costs to association, and thus to homeowners, and removes accountability of individual homeowners. When associations are required to incur additional expenses, those expenses are passed back to the owners. Division Administrator Gail Anderson, when asked to explain why Referees should not be able to award fees and costs to the prevailing party, stated that the owner is the "little guy" and the association has the "deep pocket." An association does not have any "pockets" of its own. An association's "pockets" are its owners. So, if an association is required to bear fees and costs which have traditionally been awarded as part of a successful arbitration, then the association will have to reach into the pockets of its owners. This is just another example of legislation that does not make owners who initiate legal proceedings accountable, but rather passes another expense back to other owners. This will result in increased assessments to all owners.
- Centralizes too much power in the Administrator.

The CIC Committee opposes AB 370. This Bill are clearly an attempt to piece-meal legislation which was highly objectionable and unacceptable when presented in AB 34. It is unconscionable to think that the Division would recommend substituting a new, unknown program which whose pilot program predecessor had a track record of due process violations, while simultaneously limiting the parties other ADR choices, and, in essence, disbanding and undermining the existing mediation and arbitration program that has been so successful.

Exhibit "1"
Members of the Common Interest Community Committee
of the State Bar Real Property Section

Michael Buckley, Co-Chair
Karen Dennison, Co-Chair

Other Members:

Adam H. Clarkson
Avece M. Higbee
Brian S. Pick
Bruce I. Flammey
David G. Johnson
Donald G. Martin
Douglas R. Malan
Eleissa C. Lavelle
Elizabeth Fielder
Gayle A. Kern
Joan C. Wright
John E. Leach
Mandy S. Shavinsky
Mark T. Shipley
Matthew E. Watson
Renee R. Reuther
Sandra D. Turner
William P. Wright