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Community Association Rental Restrictions
Current Issues and Evolving Law

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Rentals in community associations have been the topic of debate for years. Recent decisions of the Washington Courts have given some clarity to our laws, but have created more difficulty for associations and managers alike. As general counsel to Washington community associations, we hope to answer questions about the current state of the law relating to rental restrictions and provide some clarity for associations about their options going forward.

History of Rental Restrictions

Traditionally, associations favored owner-occupancy over rentals. The prevailing theories were that owners were more invested in community associations, would take better care of their units and limited common elements, and that long-term residence would help create a better sense of community. Lenders offered favorable rates to primarily owner-occupied communities, and these communities had more options for refinancing and resales. Rental restrictions limiting the amount of Units that could be rented in a condominium were prevalent, as were minimum owner-occupancy provisions that typically required owners to live in their units for a year or two before leasing.

When the bottom dropped out of the mortgage industry in 2008, the perception of rentals changed. Communities often could not afford to exclude investors from the pool of potential purchasers. Rentals, in many cases, were an alternative to short sales and foreclosures. Tenants were a better option than banks and vacant foreclosure properties.

In response, the FHA changed its guidelines for lending on Units in condominium associations, moving away from spot approvals and instituting project approval. Project approval meant that rental restrictions were allowed, but they became more difficult to enforce and still achieve FHA approval for lending. Minimum owner-occupancy periods and tenant screening are now considered a restraint on alienation, and will prevent FHA approval. Associations often struggle with the decision as to whether the benefits of FHA condominium project approval are worth eliminating provisions that previously made a great deal of sense for associations in administering rentals.

Recently, Washington courts have also issued several rulings that affect associations' ability to adopt and enforce rental restrictions.

Washington Law on Rental Restrictions

Since the adoption of the Washington Condominium Act, a debate existed in our industry about how properly to adopt a rental restriction, and what a proper restriction could contain. For nearly 15 years, the only real guidance we had were the Court of Appeals' and Washington Supreme Court's decisions in *Shorewood West Condominium Association v. Sadri*. This case, involving the Horizontal Property

Regimes Act that preceded the Washington Condominium Act, considered the minimum requirements for a valid rental restriction.

The Court of Appeals in *Shorewood West* adopted a reasonableness standard for evaluating condominium declarations, and held that: (1) leasing restrictions must be reasonable; (2) amendments may apply retroactively to existing owners; and (3) "grandfathering" existing rentals is reasonable. Although the Court of Appeals' decision was reversed by the Supreme Court, this portion of the opinion appears to remain good law as to the Horizontal Property Regimes Act.

In reviewing the Court of Appeals' decision in *Shorewood West*, the Washington Supreme Court decided that specific use restrictions must be stated in the condominium declaration, and that a restriction only found in the bylaws is unenforceable. The Washington Supreme Court also read the definition of "use" in the Horizontal Property Regimes Act broadly, to include leasing restrictions.

This was the only real guidance that the industry had for quite some time. An ongoing debate existed regarding whether leasing was a "use" under the Washington Condominium Act, because RCW 64.34.264(4) requires a ninety percent (90%) vote of the total voting power of the association for an amendment that changes "the uses to which any unit is restricted."

Beginning in 2014, Washington courts issued several opinions affecting community associations and rental restrictions, and none have been very good news for associations. In *Wilkinson v. Chiwawa Communities Association*, the Washington Supreme Court invalidated an amendment in a planned unit development restricting short-term rentals. The Court held that an association exceeded its authority in adopting an amendment that was inconsistent with the "general plan of development" reflected in the governing documents, despite the express provisions in the governing documents allowing for amendment of use restrictions. Because this case dealt with a planned unit development consisting of single-family homes, its holding may be limited in scope.

Later in 2014, the Court of Appeals, Division 1 decided *Filmore LLP v. Unit Owners Association of Centre Pointe Condominium*. The Court specifically considered whether the 90% vote for a change in use was applicable to an amendment adopting a rental restriction, or whether "use" under the Washington Condominium Act was limited to describing simply residential versus non-residential use, since the term is undefined in the Act and that is the only sense in which the term is used in the Act. The Court of Appeals held that a declaration amendment imposing a lease restriction is in fact a change in use requiring a 90% vote. The Court declined to consider what other types of "uses" under its broad definition may also require a 90% vote. The Court also relied significantly on *Shorewood West* and *Chiwawa*, despite the fact that neither was a Condominium Act case.

Recently, the Washington Supreme Court issued an opinion reviewing the Court of Appeals' decision in *Filmore*. The opinion affirmed the Court of Appeals' decision, but only apparently on the very narrow ground that in that case, the association's Declaration specifically defined leasing as a use. It may be that where a declaration defines "use" differently, or not at all, a 90% super majority would not be required. However, there is no significant risk to the continued viability of rental restriction amendments passed with less than a 90% majority vote.

These two decisions leave us in the dark as to whether removing or relaxing a rental restriction would also be considered a change in use requiring a 90% vote. The Supreme Court's decision does leave the possibility that an association's declaration might be changed or already specifically define "use" to exclude leasing, and thus may not be subject to the 90% vote requirement for implementing rental

restrictions. At the very least, any amendment adopting a rental restriction should specifically address the "use" issue.

Prior to these decisions, given the uncertainty as to the required approval threshold for implementing rental restrictions, many associations were advised to attempt to achieve a 90% approval, but if they could only muster a 67% supermajority approval required of regular amendments, to record the amendment and then hope it survived without challenge for one year. Under RCW 64.34.264, "[n]o action to challenge the validity of an amendment adopted by the association pursuant to this section may be brought more than one year after the amendment is recorded." In theory, once the one-year mark passed, the issue of the vote would become moot.

Unfortunately, this approach was shot down in *Club Envy of Spokane, LLC v. The Ridpath Tower Condo. Ass'n*, where the Court of Appeals held that where an amendment was not adopted pursuant to the vote requirements set out in RCW 64.34.264(2), the one-year statute of limitation to challenge the amendment does not apply. We can assume that, given the holding in *Filmore*, a rental restriction approved by less than 90% of owners would also not be adopted in conformance with RCW 64.34.264, and that therefore the one-year statute of limitations would not bar a challenge to such an amendment. In short, rental restrictions adopted without a 90% vote are now less likely to become unchallengeable with the passage of time.

Where Do We Go From Here?

Associations need to weigh several factors in deciding whether they would benefit from a rental restriction and/or FHA approval. Every association is different, and while some may be moving toward more restrictive provisions, others are moving away from having any rental cap at all. Boards must use their sound business judgment to determine what is best for their community.

For now, we have some guidance as to amendments and rental restrictions:

- Rental restrictions should be in the Declaration;
- Rental restrictions must be reasonable;
- Grandfathering existing rentals is reasonable;
- Where a Declaration includes a definition of "use" or includes leasing as "use," and probably even where the declaration is silent on the definition of "use," a 90% approval is required to adopt a rental restriction;
- The one-year challenge period in the Condominium Act will not protect an amendment from challenge if it was void at inception because of the manner in which it was adopted.

We can't be sure about amendments that loosen or remove rental restrictions, but it seems likely that the lower threshold for regular amendments would be acceptable under the courts' logic. In any amendment dealing with a rental restriction, it would be a good idea to define "use."

We would be happy to meet with you to discuss these issues in more detail, and to assist you in determining the best way forward based on your specific situation.

About our firm:

Flanagan Strauss, PLLC is a full-service law firm dedicated to serving community associations, homeowners, managers, building owners, and others involved in community associations and construction activities. Our partnership brings together over three decades of experience and

outstanding success working with community associations. We are singularly focused on problem-solving for our clients, offering creative solutions to complex issues. Our experience includes trials, appeals, arbitration, negotiation and mediation that have resulted in a collective recovery of well over a hundred million dollars for our clients. We have also provided general counsel services to hundreds of communities throughout Washington State, helping boards of directors and their managers address issues from the simplest to the extremely complicated.