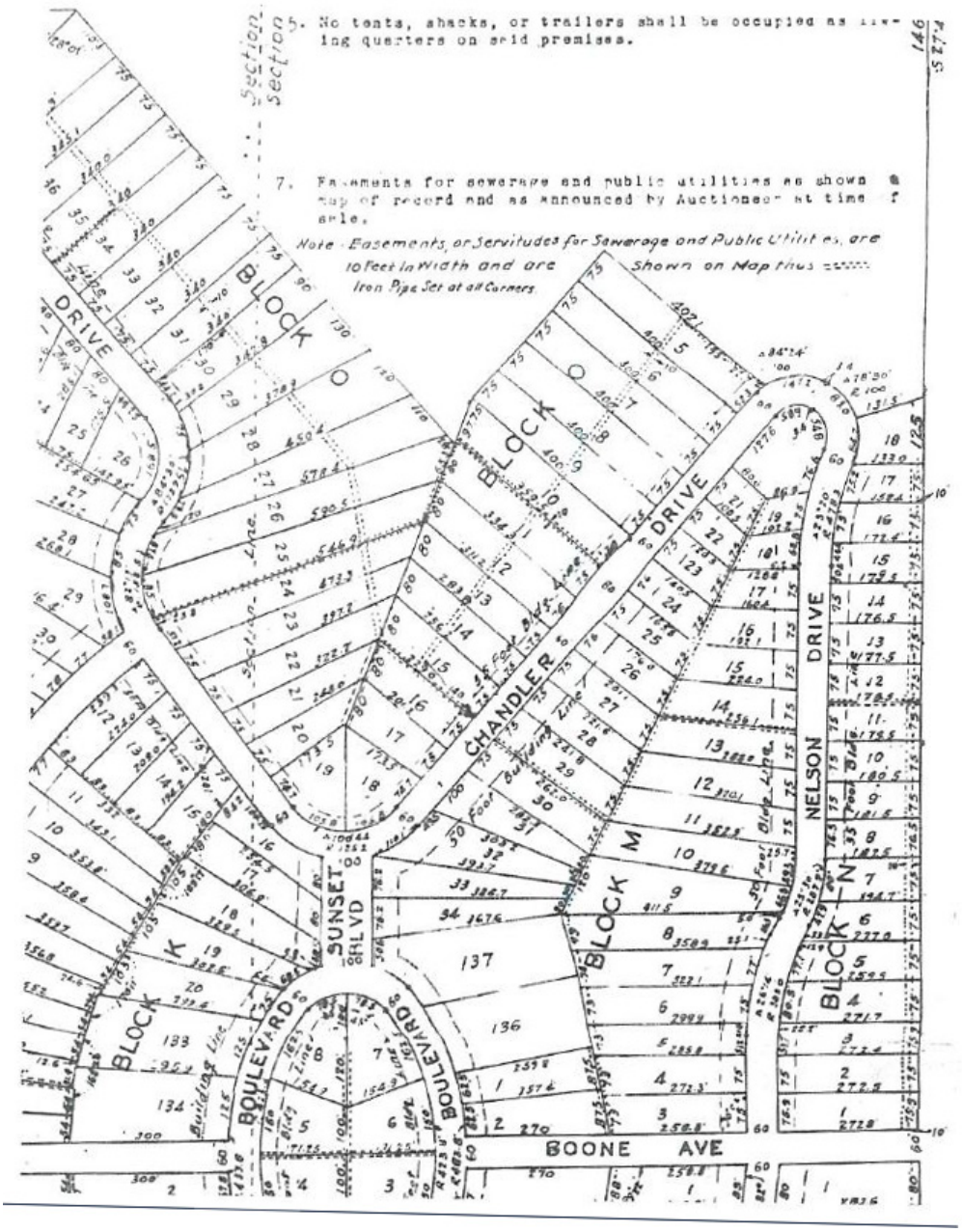
The Planned Community Act:

Providing Comprehensive Rules and Consumer Protection for Real Estate Developments

By Randy Roussel



A basic principle of property law is that an owner cannot place an encumbrance on its ownership interest for the benefit of the owner itself. For that reason, a mortgage in favor of an owner encumbering the owner's property is not valid. The same principle applies to servitudes. If the same person owns both the dominant and servient estate, the servitude does not come into existence until ownership of the servient estate is severed from ownership of the dominant estate.

Prior to the enactment of Louisiana Civil Code articles 775 *et. seq.* ("Building Restrictions"), courts examined whether Building Restrictions violated the principle of encumbering an estate in favor of its owner. Since Building Restrictions are charges on real estate, and at the time of adoption, all lots are owned by the same person, some practitioners considered Building Restrictions to be a servitude encumbering each lot in violation of this fundamental rule. In many cases, the Building Restrictions were not formal juridical acts, but rather notes on the final plat. The final plat of University Acres in Baton Rouge provides an excellent example.

The Louisiana Supreme Court recognized the validity of Building Restrictions in *Queensborough Land Co. v. Cazeaux*, 136 La. 724, 67 So. 641 (1915). The *Queensborough* case involved a restriction prohibiting the sale of property to members of a certain race. The Supreme Court reasoned that the restriction was an alienation of certain rights of ownership and, if created for a limited term, was valid. Courts then, on a case-by-case basis, developed rules applying to Building Restrictions. If perpetual Building Restrictions violated public policy against free use of real estate, what term was acceptable? When were restrictions considered abandoned? If Building Restrictions were a partial alienation of ownership rights, did they ever prescribe? The general rule is that ownership is only lost through adverse possession. Were restrictions limited to restraints on ownership?

The adoption of the Civil Code articles in 1977 established that Building Restrictions are *sui generis* real rights, subject only to the requirement that Building Restrictions be part of a uniform plan of development and uniformly enforced. The Civil Code established that Building Restrictions are reciprocal servitudes and, in many aspects, subject to certain exceptions. Unlike predial servitudes under the Civil Code, Building Restrictions may impose affirmative duties. Further, while the general rules of servitudes require a dominant estate, there is no such requirement for Building Restrictions.

The Building Restrictions common in 1977 applied to the use of real estate (i.e., for residential purposes only; no farm animals) and basic architectural standards (i.e., no home to be constructed of less than $10,000 in value). Building Restrictions have evolved since 1977 to create a complex governance and use scheme. Architectural restrictions are now more detailed, describing architectural styles (i.e., southern vernacular; Acadian; New Orleans). Architectural control committees are established to approve plans prior to construction. Common areas, such as parks, are no longer dedicated to the public but dedicated to the lot owner's association. The association is granted the right to impose assessments to fund the lot owner's association committees, enforce restrictions, and maintain common areas. Current real estate projects now frequently contain multiple uses, including blocks with varying densities. Community documents no longer are limited to Building Restrictions but combine the *sui generis* regime of real rights with the legal regime of corporate law governance. The rights and obligations of property owners are created by real estate rules but are enforced under corporate governance rules. Despite the changes in real estate developments, the Civil Code articles on Building Restrictions have remained somewhat static.

The interface of the rules of strict construction of Building Restrictions and the majority rule of corporate governance was tested in *Brier Lake v. Jones*, 97-2413 (La. 04/14/98); 710 So. 2d 1054. The issue before the Court was whether a property owner was required to comply with a more burdensome restriction adopted after acquisition of the lot. The Louisiana Supreme Court concluded that under Civil Code article 780 in effect at the time, the consent of all property owners was necessary to impose more burdensome restrictions.

Homeowner associations were not pleased with the Court's decision and in response, the Louisiana Legislature adopted the Homeowners Association Act. The impact of the Homeowners Association Act was to overrule the *Brier Lake* decision. The Homeowners Association Act applied only to communities that were solely residential in nature and formed by granting an association the right to impose periodic assessments.

The Louisiana Homeowners Association Act did not address issues arising in "mixed use" communities – those that contain varying housing and use types, such as traditional single-family homes, townhomes, condominiums, and retail all subject to the same community documents. The Homeowners Association Act also did not address whether the developer was obligated to construct community amenities if contained in sale promotional materials. Furthermore, the Homeowners Association Act lacked detail on voting requirements for HOA members. In 2014, the Louisiana Legislature passed a resolution directing the Law Institute to study the issue and to consider if revisions were necessary to the Homeowners Association Act. As a result of this resolution, the Planned Community Act was adopted in 2024. It applies to planned communities established after January 1, 2025. The Planned Community Act also applies in the event existing planned communities fail to address an issue governed by the Homeowners Association Act.

The Planned Community Act will impact practitioners in several ways. The first major change involves the mandatory requirements for community documents. These are outlined in Louisiana Revised Statutes § 9:1141.5. The Planned Community Act provides that except in certain limited circumstances, the community documents govern a planned community. However, should the community documents fail to address an issue, the Planned Community Act governs. Prior to the Planned Community Act, neither the Civil Code nor the Homeowners Association Act contained suppletive

rules. This is no longer the case. If not addressed in the community documents, the default rules of the Planned Community Act will govern issues such as voting, assessments, and action necessary to alter lot sizes. As a result of this change, drafters of community documents must be knowledgeable of all of the provisions of the Planned Community Act in order to avoid the application of rules inconsistent with the intent of the developer.

Another major change adopted in the Planned Community Act involves consumer protection provisions. For example, the drafter of community documents will need to prepare a public offering statement if the number of anticipated lots in all phases of the development exceeds 75 lots. Furthermore, the community documents, as discussed in more detail below, impose limitations on the rights of the declarant (developer). Prior property law did not contain such limitations. Unlike the Homeowners Association Act or the Civil Code articles on Building Restrictions, mandatory disclosures are now required to be contained in the community documents. Additionally, the failure to provide a public offering statement now grants a purchaser certain rights, including the right to withdraw from a purchase agreement.

The Planned Community Act requires the declarant (developer) to disclose rights retained which permit the declarant to modify the existing Building Restrictions and to add future filings. These rights are contained in the definition of "Special Declarant Rights." Declarant control of the community under the Planned Community Act is limited to seven years, unless the declarant submits additional filings to add to the community. Declarant control terminates 120 days after 75% of the lots have been sold, regardless of the time period in the community documents. This time period does not apply if the right to add additional filings to the community has not expired.

In forming associations, it is common practice to create two classes of stock in the corporation. Typically, the Class A shares of stock are "voting shares" and owned solely by the declarant. The Class B shares of stock are "non-voting shares" and owned by the lot owners not related to the declarant. Assessments are imposed only against lot owners that are also owners of the Class B shares. This structure was challenged in *Santa Maria Homeowners Ass'n v. Classic Props. Mgmt. Corp.*, 2022-0086 (La. App. 1 Cir. 11/16/22); 2022 La. App. Unpub. LEXIS 200. The Santa Maria community documents established two classes of voting stock in the association. The declarant retained 100% of the Class A stock, and the individual lot owners were issued Class B stock. The community documents did not contain a mandatory redemption period for the Class A stock. The declarant, as owner of the Class A stock, conveyed his stock to a management company that was able to retain control over the association, although neither the original developer nor the management company owned any lots. This allowed the management company to receive management fees and to govern the association without approval of the lot owners. The Planned Community Act provides otherwise, limiting the declarant's right to maintain control over the association and prohibiting the declarant from issuing two classes of stock to circumvent this rule. Drafters should be aware that different classes of stock may be allocated to all owners of a certain housing or use type, but not as a method to retain declarant control. This will require changes to the drafting of community documents.

As discussed previously, the Planned Community Act requires the declarant to provide a public offering statement if the current filing and future contemplated filings contain more than 75 lots. The public offering statement for planned communities is similar to the disclosure requirements for condominiums under existing law. The key disclosure elements include a statement of limitations on title (such as outstanding mineral surface rights use over common elements), as well as a disclosure of amenities in sales promotional materials that "MUST BE BUILT" or "MAY BE BUILT." Prior law did not require any labeling of promotional materials. Attorneys representing developers/declarants should review promotional materials or at least advise their clients of the need to identify their obligation in promotional materials.

The *Brier Lake* decision highlights the most contentious issue in planned communities. Many lot owners assert that restrictions are limited to those contained in community documents at the time of their lot acquisition. Other lot owners assert that the community documents should be flexible to consider changing market conditions or lot owner expectations. Many community documents did not contemplate short-term rentals, where a traditional single-family home functions more like a hotel. There are other instances that involve design elements not considered or addressed in the original community documents. The *Brier Lake* decision involved a limitation on the height of a fence adopted after a lot owner acquired his lot. The Homeowners Association Act recognized the problem of requiring a lot owner to comply with newly adopted rules. The Homeowners Association Act protects existing lot owners from more burdensome provisions by allowing lot owners to "opt out" of new, more burdensome restrictions. However, this concession to a lot owner under the Homeowners Association Act was only temporary. Upon the sale of the lot, the "opt out" right terminated and the new owner was required to comply with the more burdensome restrictions.

The Planned Community Act substantially changes this rule. A more burdensome restriction requires a "supermajority" vote, defined as 80% of the lot owners. Further, an existing lot is not required to comply with the more burdensome restriction but is considered a nonconforming use. The nonconforming use is allowed to continue, even upon sale, until the nonconforming use ceases, or in the case of building guidelines, on substantial improvement or reconstruction to the structure on the lot. Brief interruptions in the nonconforming use are allowed under the Act. The rule follows nonconforming use provisions typically found in zoning ordinances. It should be highlighted that the vote necessary to achieve a supermajority vote includes all lot owners, not just lot owners at a meeting of the association at which a quorum is present. The minimum vote of 80% of the lot owners is

mandatory and cannot be waived. Community documents can require 100% of the vote, but not 50%. Drafters should ensure that the community documents are consistent with this mandatory requirement.

The Planned Community Act provides for electronic voting, notices, and meetings. Electronic meetings conducted during the COVID-19 period allowed more participation in a convenient format. The Planned Community Act has adopted this new social norm. Notices, voting, and other matters can be handled electronically, provided the platform used by the association allows lot owners to participate. Electronic notices (or traditional mail notices) are at the option of the lot owner. The corporate articles and bylaws should be drafted, or revised, to stay consistent with the Planned Community Act and the community documents.

Another major change involves the ownership of common areas, as well as the right to encumber those areas. The designation of a common area on a plat now conveys full ownership to the association. Under prior law, there was an issue whether the designation of common areas on the plat constituted an implied dedication of a servitude over the common areas, or whether the declarant retained ownership free of the servitude. Many declarants separately convey common areas at the time declarant control terminates. In the absence of an actual conveyance, a declarant could assert fee ownership in a common area, especially for common areas given a separate lot designation. Now, the declarant must expressly reserve rights if something other than full ownership in the association common areas is contemplated. Attorneys should be careful that the final plat, often subject to municipal regulations containing mandatory statements, is consistent with the declarant's intent. The right to encumber common areas (as well as encumber assessments) requires a two-thirds vote of the association. Careful attention should be given to security rights created by the declarant over common areas. The Planned Community Act also restricts the ability of lenders to exercise voting rights over the association. Provisions in loan documents can restrict the association from reducing assessments but cannot give a lender the right to require that assessments be increased.

The ability of the declarant to create new lots or to combine lots is a "development right," provided this right is reserved in the declaration. This gives the declarant flexibility in the community design. If there is no market demand for large lots, the developer is able to create small lots. If the community park is too large, it can be subdivided into lots. Of course, the community documents can restrict such action. If the right to alter lot sizes or to convert common areas to a lot is not reserved by the declarant, it is necessary to obtain a minimum of a supermajority vote in order to take such action. The community documents must also address the method of reallocating voting rights and assessment obligations. If the right is reserved, the method of reallocating the voting rights and assessment obligation must be contained in the declaration. This addresses issues raised in *English Turn Prop. Owner's Ass'n v. Short*, 2016-0460 (La. App. 4 Cir. 11/30/16); 204 So. 3d 672 and *Lakewood Estates Homeowner's Ass'n v. Markle*, 2002-1864 (La. App. 4 Cir. 04/30/03); 847 So. 2d 633. The community documents in each case did not adequately address the issue. Drafters should be careful to address not only the rights reserved to the declarant, but also the ability of the association to grant modifications to the final plat.

The Planned Community Act provides for mandatory budget disclosures. Since many communities have annual budget procedures, this change should not have a major impact on planned communities. The Planned Community Act mandates these procedures for the annual budget. The Planned Community Act further requires that the association provide certain detailed financial information to lot owners upon request. One potential change involves the imposition of assessments on unsold lots owned by the declarant. The Planned Community Act now requires that a declarant disclose whether unsold lots are exempt from assessments. Further, the Planned Community Act requires the declarant to fund operating expenses of the association until assessments are imposed. This provision addresses the issue raised in *Faubourg Saint Charles, LLC v. Faubourg Saint Charles Homeowners Ass'n*, 2018-0806 (La. App. 4 Cir. 02/20/19); 265 So. 3d 1153.

The Planned Community Act adopts existing law with respect to expressed and implied warranties with one important modification. In many cases, the declarant owns or controls the contractor that developed the community. The Planned Community Act provides for a direct cause of action by lot owners to enforce warranties when the declarant and contractor are related parties.

The right to enforce liens is covered by Part III of Title 9 of the Louisiana Revised Statutes on Building Restrictions. Revisions to Part III adopted in connection with the Planned Community Act now uniformly apply to planned communities, condominiums, and traditional communities. Planned communities are now allowed to accelerate future dues under certain circumstances. This right previously was available only to condominium associations.

The summary in this article of the Planned Community Act covers major issues and should not be considered a comprehensive analysis of the entire Planned Community Act. Attorneys practicing in this area are encouraged to undertake a comprehensive review of its many provisions.

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