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“[W]e fail to see why a developer should be placed in a better position than other parties [who seek] to obtain an enforceable waiver of the right to a jury.”

Developer Cannot Enter Into Arbitration Agreement With Himself

THIS ISSUE

The Fourth Appellate District Court of Appeal recently held that an arbitration agreement that was recorded as part of the initial CC&Rs in a condominium development was unenforceable. The agreement, recorded before any of the units were sold, was not a true agreement, and was not binding, despite having been recorded with the CC&Rs.¹

SUMMARY

A homeowners association filed a construction defect action against the developer of a condominium project for damage to common areas, property owned by the association, and property owned by individual members. The Court concluded that an arbitration provision in a declaration of covenants, conditions and restrictions (CC&Rs) recorded by the developer of the condominium project, that could not be changed by the association without the written consent of the developer, did not constitute an “agreement” sufficient to compel arbitration or waive the constitutional right to jury trial for construction defect claims brought by the homeowners association.

BACKGROUND

Pinnacle Development constructed and sold condominiums in a common interest development project in downtown San Diego known as the Pinnacle Museum Tower Condominium Project. Pinnacle recorded CC&Rs forming the Pinnacle Museum Tower Association to manage and repair the Project’s common areas. Under the CC&Rs each condominium owner must be a member of the Association, and pay an assessment to the Association for its maintenance and repair of the common areas.

¹ *Pinnacle Museum Tower Assoc. v. Pinnacle Market Development* (2010)

The second page of the CC&Rs states, in capital letters, that article 18 contains a mandatory procedure for the resolution of construction defect disputes that includes the waiver of the right to a jury. Article 18 contains an arbitration provision reciting in capital letters that Pinnacle, the condominium owners and the Association agree to resolve any construction dispute through binding arbitration. Specifically, the arbitration provision states that by accepting a deed for any portion of the Association property, the Association and each owner agree to give up their right to a jury trial and have any construction dispute between an Owner or the Association and Pinnacle decided by arbitration.

The arbitration provision provides that no amendment may be made to the arbitration provision without Pinnacle's written consent.

In selling the condominiums Pinnacle used a standard purchase and sale agreement that recited on the first page that the buyer agrees to comply with the CC&Rs by accepting a grant deed to the condominium. Page 8 of the document contained a section pertaining to dispute notification, resolution procedures, and waivers. The section, which required the initials of the buyer and seller, stated:

"Buyer and Seller agree that any certain disputes shall be resolved according to the provisions set forth in Article XVIII of the [CC&Rs] and waive their respective rights to pursue any dispute in any manner other than as provided in [the CC&Rs]. [¶] Buyer and Seller acknowledge that by agreeing to resolve all disputes as provided in [the CC&Rs], they are giving up their respective rights to have such disputes tried before a jury. [¶] WE HAVE READ AND UNDERSTOOD THE FOREGOING AND AGREE TO COMPLY WITH ARTICLE XVIII OF THE [CC&Rs] WITH RESPECT TO THE DISPUTE REFERENCED THEREIN." (Capitalization and bold type in original.)

APPELLATE COURT ANALYSIS

The Court held that the Association did not "agree" to anything. Paraphrasing the Court, the Association was created by the developer, and in that process, the developer essentially agreed with himself that anyone later would be bound by the arbitration provisions.

The right to arbitration depends upon contract; a petition to compel arbitration is simply a suit in equity seeking specific performance of that contract. Essential components of a contract include parties capable of contracting and the consent of the parties to the contract. The consent of the parties to a contract must be communicated by each to the other. Acceptance of an arbitration agreement may be express or implied-in-fact.

Here, there was no express acceptance by the Association, or any conduct by the Association from which agreement could be implied. Although the arbitration provision states that by accepting a deed for any portion of the association property, the Association agreed to give up its right to a jury trial and have any construction dispute decided by arbitration, the Association had no choice but to accept the property that Pinnacle deeded to it. Thus, there was no "agreement" to arbitrate. It was merely a unilateral statement that matters would be arbitrated.

Pinnacle argued that it is required by law to draft and record CC&Rs before any units are sold. It contended that if a developer is not allowed to place an arbitration provision in the CC&Rs, it could never do so. But the Court said that there is no reason a developer cannot place a provision in the CC&Rs requiring a homeowners association and its members to decide via the amendment process to ratify a binding arbitration provision.

Alternatively, the CC&R's could provide that the failure of the homeowners association to amend the CC&R's to eliminate a binding arbitration provision amounts to an acceptance of the provision. But perhaps most fundamentally, the Court reasoned, "we fail to see why a developer should be placed in a better position than other parties that are required under general contract principles to obtain the knowing and voluntary agreement of another party to obtain an enforceable waiver of the right to a jury."

The Court also held – consistent with other California cases – that the Legislature has created a very specific statutory process for parties to use when they wish to mutually waive the right to a jury trial. Putting such a waiver in a contract is not consistent with that statutory process.

CONCLUSION

Customarily, CC&Rs are enforceable unless they violate some public policy; the Fourth Appellate District Court's decision may create an exception to that general rule.

It is apparent that the Court simply found the process by which Pinnacle obtained the "consent" for arbitration to be underhanded. There is a lengthy discussion in the decision regarding the surprise, oppression and unfairness of some arbitration agreements buried in prolix forms – contracts of adhesion where there is no bargaining power by the party against whom the provisions are sought to be enforced. That unfairness could be cured, they said, by having the Association adopt the arbitration provisions at a later time. But absent that adoption, there was simply no "meeting of the minds" of the parties to the alleged agreement.

NEXT ISSUE

Review of a new case discussing title company negligence in preparation of a preliminary report of title.

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