performed within the Le Parc project for the benefit of the owners, and its arbitration award does not include any such component. Rather, ZM claims that it was prevented from providing goods and services which would have benefitted the owners, and that it lost the benefit of the bargain it made with the Association. In addition, ZM claims that it was tortiously disparaged by the Association. It does not claim that the owners of the separate interests within the Le Parc project did the disparagement; or knew about the disparagement; or ratified the disparagement; or benefitted from it.

There is simply no nexus of any kind between the underlying basis for ZM's claims and the persons who are being asked to pay damages based upon those claims. Their position that a court can order the owners of the separate interests to pay for someone else's torts, and for goods and services which they did not receive, merely due to the existence of CC §1366(b), is unsupported, is illogical, is inequitable and is unjustified.

6. IMPLIED SURETYSHIP

The interpretation of Civil Code §1366(b) urged by the Claimant would mean, in effect, that the mandatory members of a community association, from which they cannot resign, are nonetheless the involuntary guarantors all of the association's liabilities. Such an interpretation and the expansion of surety obligations to unsuspecting owners of separate interests in California CIDs would be unprecedented. Except in the most extraordinary of circumstances, California law requires that a guarantor actually and affirmatively agree to become a surety; the law does not recognize any sort of "implied surety" under circumstances similar to those presented in the pending matter.

Historical distinctions between 'guaranty' and 'suretyship' have been abolished in California. [CC §2787] By statute, "A special promise to answer for the debt, default, or miscarriage of another" must be in writing and must be signed by the party or parties to be bound. [CC §1624(b)]

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See also McClenahan v Keyes (1922) 188 Cal. 574, where the Court stated:

> "If the services of the plaintiff were performed upon the credit of the daughter or if she was in any degree liable for the indebtedness, then the mother would be a mere guarantor and the contract of guaranty not being in writing would be void under the statute of fraud." McClenahan, infra, at page 582.

Claimant does not assert that the owners of the separate interests within the Le Parc project ever executed surety agreements in its favor, nor does it assert that they ever "promised", directly or indirectly, verbally or otherwise, to answer for the contractual breach or tortious conduct of the Association.

Likewise, Claimant does not assert that the members of the corporation ever executed surety agreements in its favor.

Rather, Claimant points to the bare language of CC §1366(b) and urges the Court to order the imposition of its proposed Special Plan Assessment, thereby making the owners of separate interests within the Le Parc project the *de facto* guarantors of the Association's 'default's and miscarriages', despite the logic, legal principles and body of law which argues against such an effect. Such an interpretation of CC §1366(b), and the effect of that interpretation, has no support in any of its history.

7. FLAWED ASSUMPTIONS UNDERLYING PLAN

Claimant's Plan assumes that the Association's power to assess its Owners in the future is a present 'asset' which can be reached in the current Bankruptcy proceeding. Although not articulated in either its original or its First Amended Disclosure Statement, this assumption is obliquely suggested in its Reply dated October 8, 1998, on page 6, lines 26 though 28, where it states that "The Association has a unique "asset"; namely, the ability to levy assessments and create liens on its members' units to secure payment of those assessments." Without any authority or legal support, the Plan attempts to 'create' an asset subject to the present proceedings by merely defining it as such. In reality, the 'asset' sought to be reached doesn't exist except as a concept.

The Plan, based upon the assumption, then creates the ultimate bootstrap argument, which goes something like this:

The Association has no present assets which would allow it to raise the funds necessary to propose a plan which might allow it to satisfy our judgment [if and when the judgment might become final]; however it might be forced to create an asset in the future if this Court can be convinced to interpret a statute in a way which is most favorable to us, which then might become collectable over a period of years, and which might be sufficient to satisfy our claims."

The problem is, the future ability to assess is not a **current** asset of the Association which is subject to the jurisdiction of the court.

What the Claimant is attempting to bring within the purview of the Court is merely something which might exist; it is a bare inchoate interest in real property which does not exist in the present and might never exist at all. "Inchoate" refers to something which is "Imperfect; partial; unfinished; begun, but not completed; as a contract not executed by all the parties." Black's Law Dictionary, 4th Revised Edition, (1968), page 904. An "Inchoate interest" is an interest in real estate which is not a present interest, but which may ripen into a vested estate, if not barred, extinguished, or divested." Black's, infra, page 609.

8. EQUITABLE AND REALITY CONSIDERATIONS

The present action involves a dispute between two corporate entities. These corporate entities became engaged with each other based upon a negotiated, arms length business transaction. The members of the Le Parc corporation were not asked to and did not vote to approve or ratify the contract with Claimant. The owners of the land subject to the Le Parc CC&Rs were not asked to and did not participate in the contract which was allegedly breached by the Association. As such, it would be inequitable for this Court to enter the order requested by Claimant.

As shown in the questionnaire results attached to the Declaration of James P. Lingl, filed herewith, the average value of the residences within the Le Parc project is approximately $106,167. As shown by those same questionnaire results, the average 'equity' of an owner of a residence in Le Parc is approximately $18,541.

The Creditor's Plan, if it were to be put into effect, would require a Special Plan Assessment

of $25,313.55 against each condominium unit, plus accruing interest. [Page 8, line 3 of Proposed First Amended Plan of Reorganization, dated October 26, 1998 - hereinafter First Amended Plan] This sum would represent something more than 25% of the average resale value of the Le Parc units and nearly 137% of the equity which the unit owners have in their homes. The amount of the initial Special Plan Assessment would be subject to increase based upon any collection costs incurred by the Plan Administrator to enforce and collect the assessments [Page 12, lines 7-10, First Amended Plan]; in dealing with any possible Avoidance Actions [Page 13, lines 5-14, First Amended Plan]; and could be further increased even after confirmation if collections under the Plan do not meet expectations and the Court authorizes the modifications [Page 14, lines 20-23, First Amended Plan]. In other words, the $25,313.55 plus interest cited as the amount of the initial Special Plan Assessment is only a beginning. As owners walked away from their units and commenced their own Bankruptcy proceedings to avoid payment of the assessment, the size of the assessment against each of the remaining units would necessarily increase to redistribute the portion of the payments uncollected from those owners. Subsequently foreclosing lending institutions would not be liable for any portion of the Special Plan Assessment, since CC 1367 mandates that such assessments "shall be a debt of the owner of the separate interest at the time the assessment ... [is] levied." Those lenders would avoid any lien created to secure the assessment both by virtue of their superiority of security interest and by virtue of CC 1466 which states in applicable part that: "No one, merely by reason of having acquired an estate subject to a covenant running with the land, is liable for a breach of the covenant before he acquired the estate...." As applied to community association assessments, see Mountain Home Properties v Pine Mountain Lake Association (1982) 135 CA3d959 wherein the Court opined:

> "The obvious purpose of section 1466 is one of fairness to a party who acquires property. Since such a party has no connection with the property until he comes into possession, the Legislature has provided that the party should not be liable for the debts of its predecessors in interest.... To impose over $40,000 in unpaid assessments on respondent is manifestly unfair in that no benefits have accrued to respondent prior to its purchase." Mountain Home Properties, infra, at page 971.

Incidentally, and as shown on the Questionnaire data mentioned above, it appears that as many as 57 owners acquired their separate interests in the Le Parc project subsequent to the

earthquake which led to Claimant's involvement with the Association, and as many as 42 owners acquired their interests subsequent to the actions which gave rise to Claimant's claim against the Association. If it is "manifestly unfair" to hold an owner liable for assessment monies which presumably were used to 'maintain, replace and repair' his real property prior to his acquisition of title as stated by the Mountain Home court, "in that no benefits have accrued" to the owner prior to obtaining title, then it seems even more remote, and even more 'manifestly unfair' to make owners liable for a contractual breach and trade disparagement by a third party which occurred prior to their acquisition of title to Le Parc units, as would be done in the instant case if the Plan were to be approved.

Were the Claimant attempting to collect $60,000 from the Le Parc association, or even $600,000, it might be possible for the Board of Directors to propose a plan of its own which would allow the obligation to be liquidated within a 5 year period. The Board has the power to increase assessments up to 20% per year without owner approval, and it impose a 5% special assessment per year without owner approval. Any increase beyond those limits requires owner approval pursuant to both the project's CC&Rs and statute.

The reality is, however, that the owners have virtually unanimously disapproved any form of special assessment which could generate the funds sought by ZM to satisfy its claims. The further reality is that the vast majority of owners of separate interests within the Le Parc project do not have the financial ability to pay the Special Plan Assessment sought by Claimant, and have made it unquestionably clear that they would walk away from their units and/or file for bankruptcy protection if such an assessment were to be made.

Assuming, arguendo, that the 'emergency situation' provision of CC § 1366(b) would permit this Court to "order" imposition of the Special Plan Assessment, where is the equity in forcing more than a hundred of the owners to lose their homes, or forcing several hundreds of people to become displaced, in order to try to satisfy the claim of a single corporate business.

9. RIGHTS AND REMEDIES OF THE OWNER/MEMBERS

Without seeming to appear insensitive to the merits of ZM's claims and losses, it needs to be

emphasized there are interests involved in this matter which extend beyond the narrow interests of one corporate entity fighting with another. Those other interests include the rights of the people who are being looked to for satisfaction of ZM's claim, i.e. the owner/members involved with the Le Parc project, and, on a much larger scale, the interests of all of the other owner/members in the 30,000 common interest developments within the State of California. Those persons, as owners, have statutory and historical rights by which they could properly attempt to 'fire' their community association by the simple expedient of an amendment to the CC&Rs of the project, thereby depriving their association from any right or power to assess them at all. Similarly, those persons, as members, have the statutory right to liquidate the assets of the corporation to which they belong and to wind up its affairs. For the Claimant's Plan to be feasible, the Court would need to prevent the owners from attempting to amend their CC&Rs and prohibit the members from attempting to liquidate and wind up the affairs of the corporation. No authority has been found which would support such a sweeping exercise of judicial power.

10. DISSOLUTION OF THE LE PARC ASSOCIATION

The California Corporations Code contains extensive statutory provisions dealing with involuntary dissolution of a nonprofit mutual benefit corporation [commencing with §8510], voluntary dissolution of a nonprofit mutual benefit corporation [commencing with §8610], and operation of a nonprofit mutual benefit corporation during the process of dissolution [commencing with §8710]. Even while making it difficult for a community association type of nonprofit mutual benefit corporation to dissolve itself, Corp. C. §8724 explicitly recognizes the right of members of a community association to dissolve their corporation.

11. AMENDMENT OF THE LE PARC CC&Rs

The CC&Rs of the Le Parc project specifically authorize their amendment. Article 15, §15.2 states in applicable part that:

> "[T]his Declaration or any Supplement may be amended in any respect or revoked by the vote or written consent of the holders of not less than seventy-five percent (75%) of the voting rights..." of the members .... Any amendment or revocation subsequent to the close

of the first sale shall be evidenced by an instrument certified by the Secretary or other duly authorized officer of the Association and shall make appropriate reference to this Declaration and its amendments and shall be acknowledged and recorded in the office of the County Recorder of the County."

Section 15.5 states that:

"Any amendments or revocation made in accordance with the terms of this Declaration shall be presumed valid by anyone relying on them in good faith."

The Civil Code, at §§1355 and 1366, contains additional provisions relating to amendment of CC&Rs. Civil Code §1355 provides in part that "(a) The declaration may be amended pursuant to the governing documents or this title." Civil Code §1356 permits an amendment to become effective upon the approval of as few as a simple majority of all of the owners.

11. CONSTITUTIONAL ISSUES

Both the United States Constitution and the Constitution of the State of California contain prohibitions against 'impairment of contracts', commonly known as the Contract Clause. The Federal Contract Clause provides that "[N]o state shall pass any ... law impairing the obligation of contracts ...." [Section 10, Article I, U.S. Constitution]. The parallel California prohibition is contained in Section 9 of Article I of the California Constitution.

In Energy Reserves v County of Los Angeles, 74 L.Ed.2d 569, the United States Supreme Court set forth a three part test for determining whether a state law unconstitutionally impairs the obligation of contracts. That three part test involves, first, a determination of whether the state law operates as a substantial impairment of a contractual relationship. If there is a substantial impairment, there must be a determination of whether the state can show a significant and legitimate public interest underlying the law, i.e., the need to remedy a broad and general social or economic problem. If such a legitimate public purpose is identified, then the third part of the analysis deals with whether the adjustment of rights and duties of the parties is based upon reasonable conditions and is of a character appropriate to the public purpose justifying the questioned legislation.

Should the 'emergency assessment' provision of California Civil Code section 1366(b) be given the effect requested by Claimant, it cannot pass the Constitutional tests demanded by the

Energy Reserve decision.

The concept and 'bargain' contained in the typical CC&Rs of a California community association, and in the CC&Rs of the Le Parc condominium project, allow an association to collect money from the owners of separate interests for the purpose of maintenance, repair and reconstruction of the real property and improvements which make up the development. The Le Parc CC&Rs do not provide for an assessment to be levied to pay for the tortious conduct of the Association or its Board, and certainly not for the tortious conduct of an independent contractor hired by the Board. Therefore, a statute which permitted the imposition of such an assessment, outside of the 'bargain' agreed to by the owners of the separate interests, would constitute a substantial impairment of the limits on assessment contained in the CC&Rs.

The imposition of the assessment requested by Claimant is for its own, narrow, personal, financial good. There is nothing to suggest that California community associations are or have been engaged in widespread fraudulent conduct designed to deprive legitimate contractors of their right to be paid for services provided. There is nothing to suggest that such associations are or have been engaged in widespread tortious conduct toward contractors or any other person or entity. In short, there does not appear to be any 'broad and general social or economic problem' involving community associations which would warrant application of CC 1366(b) to permit unlimited assessments against owners for purposes which they had not agreed to pay, and which are unrelated to the owners' interest in their real property.

Even if it could be argued that there was some legitimate public purpose in adopting a law which would allow the imposition of unlimited assessments against owners of separate interests for the wrongful activities of a community association, still it cannot be said that the change in assessment rights and duties is based upon any set of reasonable conditions which would allow the owners to prepare for or even contemplate such a possibility, or that the unlimited imposition of assessments for purposes unrelated to the repair, maintenance or replacement of improvements in a CID is an appropriate purpose justifying the law's enactment. In short, and if given the interpretation suggested by Claimant, Civil Code section 1366(b) has removed any meaningful limits on assessments as contained in the CC&Rs of the 30,000 community associations which exist

in the State, and which affect some 6 million citizens who reside in the State's common interest developments.

III. CONCLUSIONS

Claimant in this matter has obtained an arbitration award against the Debtor corporation which is not yet final. Any Plan which would mandate payment of the award by the owners of the separate interests within the Le Parc project before the judgment becomes final is premature.

The suggested application of Civil Code §1366(b) in the present circumstances has no basis or support in law, precedent or legislative history. The interpretation of Civil Code §1366(b) urged by Claimant is inconsistent with normal rules of statutory construction, and contrary to the intent of California law as evidenced by the statutory immunity which the Legislature has granted to owners of separate interests in CIDs for both tort claims and lien claims.

The Plan which has been proposed by Claimant is based upon an erroneous assumption that the future ability to assess is a present asset of the Debtor which is subject to Bankruptcy Court distribution.

The Plan, and the Special Plan Assessment, are simply not equitable because of the magnitude of the Assessment versus both the value of the units and the equity held by the owners of those units.

The Special Plan Assessment is not feasible because such a large number of owners would find a way to avoid payment, either by walking away from their homes or by filing personal bankruptcies, that the Plan could never satisfy the claim of the Claimant.

The statutory interpretation urged by the Claimant is so far reaching, and so dramatic, that were it to be applied in the instant case, the statute could not pass Constitutional scrutiny.

To have any chance of success, the Plan would require this Court to not only order the Special Plan Assessment, but also enter orders prohibiting owners not party to the proceedings to refrain from exercising their real property right to amend the CC&Rs, and ordering members who are not party to the proceedings to refrain from exercising their statutory right to seek dissolution of the corporation.

For any part of the Plan to be workable, or feasible, the admonitions underlying Occam's Razor would need to be ignored at every twist and turn, with unsupported assumptions, fictitious definitions, and tortured interpretations leading to irrational applications, on innocent third parties. Instead, the most direct and simple analysis of this matter leads inevitably to the conclusion that the Creditor's claims will not be able to be satisfied by the Le Parc Simi Valley Homeowners' Association, that the Plan is not feasible, and that the entire Bankruptcy proceedings should be dismissed.

DATED: November 10, 1998

Respectfully submitted.

KNOPFLER & ROBERTSON
A Professional Law Corporation

By: _____
JAMES P. LINGL, Attorney for Debtor, LE PARC SIMI VALLEY HOMEOWNERS ASSOCIATION