MICHIGAN
REAL PROPERTY REVIEW

Published by the Real Property Law Section State Bar of Michigan

Summer 2015 Vol. 42, No. 2

Contents

Major Revisions to the Michigan Nonprofit Corporation Act:

Why Michigan Condominium Associations Should Take Note

by Joe Wloszek and Brandan Hallaq***

I. Association Nonprofit Corporations: An Overview

According to the most recent statistics, there are approximately 337,000 community associations in the United States.[1] The phrase "community association" includes condominiums, housing cooperatives, homeowners associations, and summer resorts. These community associations—primarily composed of condominium and homeowners associations—represent close to 30 million housing units and almost 70 million residents.[2] By percentage of total population, this equals nearly 21 percent of the United States population residing in such community associations.[3] More specifically, Michigan alone has an estimated 8,200 community associations, which are occupied by approximately 1.4 million out of a total 9.9 million residents.[4] While the recent changes to the Nonprofit Corporation Act impact all types of community associations, this article focuses on condominiums and the impact of the recent changes on condominium associations and their boards of directors.

In Michigan, two primary statutes govern the affairs of a condominium association: the Condominium Act[5] and the Nonprofit Corporation Act.[6] In addition, Michigan condominium associations are governed by their Articles of Incorporation, a Master Deed, corporate Bylaws (in addition to condominium Bylaws in certain cases), and any applicable Rules and Regulations meant to implement or manage existing structural provisions of the Master Deed and Bylaws.[7] The principal duties of a condominium association include collecting assessments from members, and enacting and enforcing rules

1 National and State Statistical Review for 2014 (Community Associations Institute, 2014), *available at* http://www.caionline.org/about/press/Documents/2014%20Stat%20Review.pdf.

2 *Id.*

3 *Id. See also* State & County QuickFacts (United States Census Bureau, 2014*), available at http://quickfacts.census.gov/qfd/states/26000.html*.

4 *Id.*

5 MCL 559.101 et seq.

6 MCL 450.2101 et seq.; *see also* the several types of summer resort associations authorized under MCL 455.1 through 455.313.

7 *Meadow Bridge Condo Ass'n v Bosca*, 187 Mich App 280, 281-83; 466 NW2d 303, 304-05 (1990).

* *Joe Wloszek is an attorney with the law firm of Cummings, McClorey, Davis & Acho, P.L.C. where he focuses his practice on dispute avoidance, condominium law, commercial litigation, commercial real estate, large contractual disputes and title litigation. Mr. Wloszek received his J.D. degree from the University of Detroit Mercy School of Law and his B.A. degree in Economics from Hillsdale College. Mr. Wloszek is a Certified Real Estate Continuing Education Instructor for the State of Michigan. During law school, he interned for Justice Markman of the Michigan Supreme Court, served as a member on the Moot Court Board of Advocates and participated in the prestigious Inns of Court.*

** *Brandan Hallaq is a law clerk with the law firm of Cummings, McClorey, Davis & Acho, P.L.C. Mr. Hallaq will graduate with his J.D. degree from Wayne State University Law School in May, 2016. He obtained his B.A. degree in Political Science from Wayne State University. During law school, Mr. Hallaq interned for Judge Walter Shapero of the United States Bankruptcy Court for the Eastern District of Michigan.*

to govern the association for the collective benefit of the co-owners.[8] The assessments collected from members go toward, among other things, managing the association, improving and constructing common areas, paying utility expenses, and providing amenities such as fitness centers, pools, and tennis courts. The assessments are typically exempt from federal income taxation.[9] An estimated $70 billion in assessments are collected annually by community associations across the United States.[10]

Given that condominium associations are routinely incorporated under the Nonprofit Corporation Act, as amended, the association, its board of directors, and the co-owners should have a general knowledge of and familiarity with some of the more important sections of the Act.[11] Effective January 15, 2015, Governor Rick Snyder signed into law Michigan Senate Bill 623,[12] which made significant changes to the Nonprofit Corporation Act. This article addresses the recent amendments to the Nonprofit Corporation Act that impact Michigan condominium associations.[13]

II. Revisions to the Nonprofit Corporation Act

The recent amendments to the Nonprofit Corporation Act were sparked, in part, by several years of changes to the Business Corporation Act.[14] Over the last few years, the Michigan legislature spent significant time and resources reviewing and revising various provisions of the Business Corporation Act. Examples include Senate Bills 1317,[15] 1318,[16] 1319,[17] and 1320,[18] enacted as Public Acts 566, 567, 568, and 569 of 2012. Essentially, the Business Corporation Act, originally enacted into law in 1973 and revised in some detail in 1984, has undergone extensive revisions over the last few years and the Michigan legislature decided to make corresponding amendments to the Nonprofit Corporation Act. It appears that a number of changes were also made to address concerns in particular of the hospital and medical communities given that so many of those enterprises operate on a nonprofit basis.[19] With help from prominent members of the State Bar of Michigan's Business Law Section, especially retired attorney Jane Forbes, the 2015 amendments to the Nonprofit Corporation Act were drafted and enacted into law. Six significant updates that all Michigan condominium associations should review are discussed below.

A. Participation by Electronic Means: Required Unless Prohibited

By far, the biggest change for condominium associations involves participation by co-owners in membership meetings by electronic means, i.e. telephone or conference call, Skype, Go-To-Meeting, FaceTime, etc. Under the 2008 Amendments to the Nonprofit Corporation Act, participation in membership meetings was allowed by electronic means only if the Articles of Incorporation or Bylaws specifically permitted such participation.[20] Under the newly revised statute, unless the Articles of Incorporation or Bylaws specifically prohibit participation in membership meetings by electronic means the default position is that a co-owner may participate in membership meetings by telephone, conference call, Skype, Go-To-Meeting, FaceTime, or other

8 MCL 559.169.

9 26 USC 528(d)(3)(A).

10 National and State Statistical Review for 2014, *supra* note 1.

11 Other formats and applicable statutes also can be utilized to organize associations (e.g. the Summer Resort and Park Associations Act, MCL 455.1 et seq.). *See generally* Gregory J. Gamalski, *A Menagerie of Real Estate Interests: Housing Cooperatives, Chapter 455 Summer Resort Associations, and Less Frequently Seen Home Owner Entities*, 40 Mich. Real Prop. Rev. 24 (Spring 2013).

12 2014 PA 557, *available at http://www.legislature.mi.gov/documents/2013-2014/publicact/pdf/2014-PA-0557.pdf*.

13 While the recent changes to the Nonprofit Corporation Act also affect other community associations including homeowners associations, this article focuses primarily on condominium associations.

14 MCL 450.1101 et seq.

15 2012 PA 566, 2012 SB 1317, *available at* http://www.legislature.mi.gov/documents/2011-2012/publicact/pdf/2012-PA-0566.pdf.

16 2012 PA 567, 2012 SB 1318, *available at* http://www.legislature.mi.gov/documents/2011-2012/publicact/pdf/2012-PA-0567.pdf.

17 2012 PA 568, 2012 SB 1319, *available at* http://www.legislature.mi.gov/documents/2011-2012/publicact/pdf/2012-PA-0568.pdf.

18 2012 PA 569, 2012 SB 1320, available at *http://www.legislature.mi.gov/documents/2011-2012/publicact/pdf/2012-PA-0569.pdf*.

19 MCL 450.2261.

20 2008 PA 9, 2008 SB 123, *available at* http://www.legislature.mi.gov/documents/2007-2008/publicact/pdf/2008-PA-0009.pdf.

means of remote communication.[21]

One potential issue that may present itself as a result of these changes is the possibility of difficulty or inconsistencies in establishing a quorum with electronic participation in meetings. Associations can avoid this problem by including a provision into their Bylaws providing that co-owners must identify themselves by name and unit number. The Bylaws should also specify that if a co-owner is participating by electronic means, the member will count towards establishing a quorum.

Given the new changes, an association that wishes to prohibit electronic participation in membership meetings will need to amend its Articles of Incorporation or Bylaws.[22] If an association wishes to exclude remote participation, it must act expeditiously to avoid any issues before the next meeting takes place. There are certainly some associations that prefer in-person participation, but that decision is left to the discretion of the association.

On the other hand, if an association does not wish to restrict participation by electronic means, the board of directors will still need to:

(1) review and revise its notice procedures for member meetings to allow co-owners to participate through electronic means;

(2) determine how votes from electronic means will be taken; and

(3) determine how votes from electronic means will be verified.

This leads to the second most important change with the new law: voting.

B. Voting By Electronic Means or at a Polling Place Now Available

Under the new amendments, associations have the flexibility to conduct voting for annual and special meetings by electronic transmission or at a polling place (if such voting is permitted in the Articles of Incorporation or Bylaws).[23] Thus, with the recent changes, an action may be approved by:

(1) an in-person meeting;

(2) signing a written consent;

(3) electronic means such as e-mail or an online survey;

(4) an in-person polling place with printed ballots; or

(5) a written ballot provided to co-owners and returned not less than twenty days and no more than ninety days after the date the ballot is provided.

While these voting procedures provide associations with greater flexibility in voting, they also provide the added benefit of allowing snowbirds who travel south for the winter the ability to participate in community decisions. As such, every association should be aware of these changes in the law and should consider adopting such procedures. Simply, enacting these voting procedures may encourage participation among association members as a result of the increased level of convenience. Conversely, associations must also consider the potential drawbacks of permitting alternative voting mechanisms, including the expense and difficulty associated with validating the votes. Some of the larger issues that could result from these amendments include hacking, voter fraud, and duplicate voting. These problems are less likely to arise if only in-person voting is permitted. Requiring the voter to place his or her unit number or street address on the record would serve to ensure that no duplicate votes are being cast. The benefits of convenience these electronic voting means provide must be weighed against the potential costs to ensure that the votes cast are authentic.

Thus, while greater flexibility is typically a good thing, the decision rests with the association. Determining whether such voting mechanisms are desirable depends on the size of the association, the overall access by the members to computers or other means of remote participation, and the needs of the individual community. For example, if the association is comprised of predominately elderly and retired individuals, electronic voting may not be a desirable option. Conversely, for associations with hundreds of co-owners, electronic voting may be a practical solution. In summary, associations should determine whether e-mail, on-line webpages, or printed ballots are permissible voting mechanisms and, if so, whether the Articles of Incorporation or Bylaws need to be amended to accommodate such options pursuant to the new MCL 450.2208 and MCL 450.2209.

C. Additional Limitations on Director, Officer, and Volunteer Liability Now Available

In 1986, the Nonprofit Corporation Act was amended to allow nonprofit corporations, including condominium

21 MCL 450.2405.

22 MCL 450.2405(1).

23 MCL 450.2408 & 450.2409.

associations, the ability to limit the personal liability of a director, officer, or volunteer of the corporation, its shareholders, or its members for money damages for a breach of the person's fiduciary duty.[24] In order for the director, officer, or volunteer to obtain the benefits of the provision, the association had to determine that a specific fiduciary duty was involved.[25] However, the recent amendments allow an association to eliminate director, officer, or volunteer liability for money damages for *any* action taken or *any* failure to take action (not just limited to the person's fiduciary duty),[26] subject to five specific exceptions to this limitation of liability.[27] Specifically, the new amendments do not permit the elimination of a director, officer or volunteer's liability for the following:

(1) the amount of a financial benefit received by a director, officer, or volunteer to which he or she is not entitled;

(2) intentional infliction of harm on the corporation, its shareholders, or members;

(3) a violation of section 551 (concerning unlawfully declaring dividends, making distributions to shareholders, or making a loan to a director, officer, or employee that is contrary to the statute);

(4) an intentional criminal act; and

(5) liability imposed under section 497(a) (concerning liability for payment of expenses in derivative proceedings such as a court order requiring the corporation to pay the plaintiff's reasonable expenses, including reasonable attorney fees, incurred in the proceeding if it finds that the proceeding has resulted in a substantial benefit to the corporation).[28]

Given that directors and officers of condominium associations are typically unpaid volunteers, providing greater protections for good faith actions may be a worthwhile incentive mechanism to attract competent individuals to serve on the board of directors. On the other hand, in 2014, only approximately 54 percent of community association members polled stated that they believe community association board members serve the best interest of the community.[29] Thus, some associations may not wish to provide greater protections for the board of directors. This decision will typically depend on the level of trust the co-owners have in the competency of the board. The association may determine in its business judgment that such additional protections are inappropriate. Regardless, the recent amendments allow for new protections for directors, officers and volunteers that every association should review and consider.

D. Inspection of Records: New Restrictions Now Available

Under the previous MCL 450.2487, a co-owner could inspect certain records of the association for any proper purposes at a reasonable time and place including the following:

(1) the balance sheet at the end of the preceding fiscal year;

(2) the statement of income for that fiscal year; and

(3) if prepared by the corporation, its statement of source and application of funds for that fiscal year.[30]

In addition, a co-owner, upon at least ten days' written demand, could examine for any proper purpose, in person or by agent or attorney, during usual business hours, the minutes of stockholders' or members' meetings and record of shareholders or members.[31]

The new MCL 450.2487 states:

> If requested in writing by a shareholder or member, a corporation shall mail to the shareholder or member its balance sheet as at the end of the preceding fiscal year; its statement of income for that fiscal year; and, if prepared by the corporation, its statement of source and application of funds for that fiscal year.[32]

The statute further states: "Notwithstanding any other provisions of this act, the articles of incorporation, the bylaws, or a resolution of the board of directors may provide that the shareholders or members and attorneys or agents for shareholders or members do not have the right to inspect…."[33]

24 MCL 450.2209 (1986), *amended by* MCL 450.2209 (2015).

25 *Id.*

26 MCL 450.2209(1)(c).

27 MCL 450.2209(1)(c)(i-v).

28 *Id.*

29 Verdict: Americans Grade Their Associations, Board Members and Community Managers (Public Opinion Strategies, 2014), *available at* *www.cairf.org/research/Americans_Grade_2014.pdf.* Reprinted with permission of Community Associations Institute. Learn more by visiting *www.caionline.org*, writing *cai-info@caionline.org* or calling (888) 224-4321.

30 MCL 450.2487 (1982), *amended by* MCL 450.2487 (2015).

31 *Id.*

32 *Id.*

33 *Id.*

The new amendments clarify the procedures by which a co-owner may request the inspection of certain records and what information the co-owner is not permitted to inspect. The new statute allows for a co-owner, either in person, by attorney, or through another agent, to inspect the books and records of the association after providing a written demand.[34] The written demand must describe a proper purpose for the inspection and specify the records that the co-owner desires to inspect.[35] If the request is made by an attorney or agent of the co-owner, the written demand must include a power of attorney or other writing that authorizes the attorney or agent to perform the inspection.[36] In the event that the association does not allow the inspection within *five business days* after a demand is received, a co-owner may file an action in circuit court to compel an inspection of the books and records of the association.[37] If a court orders an inspection, the court must also order the association to pay the co-owner's costs, including reasonable attorney's fees, unless the association can demonstrate that it had a good faith basis for the denial.[38] Accordingly, it is extremely important for an association and/or its managing agent to provide a timely response to a request for inspection of records; otherwise, the association is exposing itself to potential liability for attorney fees, which may accumulate quickly.

The Articles of Incorporation or corporate Bylaws may be amended to disallow an inspection of the association's books and records if the association makes a good faith determination under certain specified circumstances.[39] The recent amendments provide that if the Articles of Incorporation or Bylaws so state, then no right to inspection exists: (1) when doing so would impair the privacy or free association rights of shareholders or members or the lawful purposes of the corporation, or (2) when opening lists of donors would not be in the best interests of the corporation.[40] Similarly, a board resolution could be passed preventing an inspection on the above grounds as well.[41]

As a result, associations and managing agents should be aware of the new rules relating to requests to inspect the books and records of the association. Merely putting the request on the association's "to do" list could be an expensive mistake based upon the new deadline in which an inspection must be permitted. Thus, associations and managing agents should take immediate action when receiving a request to inspect records and permit the inspection in a timely manner or disallow the inspection if the board of directors determines that the above criteria has been satisfied.

E. Mergers and Dissolutions: New Options for Twenty Co-owners or More

A condominium association does not often concern itself with mergers or the dissolution of the association. However, the procedures for implementing a merger or the dissolution of an association have changed with the new amendments. Previously, a plan of merger or dissolution could be approved if a majority of the co-owners entitled to vote approved such a measure at an in-person meeting or by proxy. Now, the amendments allow approval of a plan of merger[42] and dissolution[43] of the association by a majority of affirmative votes from co-owners present at the meeting, but only if a minimum of twenty co-owners entitled to vote are present. Both new statutes permit a greater number of votes if provided for in the Articles of Incorporation or Bylaws. Every association should consider whether the size of their association should require a greater number of co-owners present to effectuate either a merger or the dissolution of the association.

This provision of the Nonprofit Corporation Act has been criticized by members of the community association community for creating unintended consequences. For example, what would happen if a condominium association incurred excessive debt and the co-owners incorrectly believed that dissolving the association and forming a new association may remove that debt? Could twenty co-owners vote to dissolve the association? The result of such an action would be chaos and would create a significant likelihood of extensive litigation. Additionally, what would happen if an association only has sixteen co-owners? What if the association has two hundred co-owners? Community associations would be wise to address these concerns in their Articles of Incorporation and/or Bylaws. Otherwise, the statute may need to be amended to address these concerns for community associations.

34 MCL 450.2487.

35 *Id.*

36 *Id.*

37 *Id.*

38 *Id.*

39 *Id.*

40 *Id.*

41 *Id.*

42 MCL 450.2703a.

43 MCL 450.2804.

F. Nonexecutive Committees

Previously, the board of directors of a condominium association could designate "executive committees" consisting of one or more of the directors of the association. The new amendments state that unless otherwise prohibited in the Articles of Incorporation or Bylaws, the board of directors—or an individual designated in the Bylaws or by the board—can appoint one or more "nonexecutive committees."[44] Importantly, in nonexecutive committees, some or all of the committee members could be directors, officers, members, or shareholders of the association and some or all of the committee members could be individuals who are not directors, officers, members, or shareholders. In essence, a non-co-owner could then be a member of such a committee. For example, a large association may wish to appoint a nonexecutive committee including a non-co-owner when the association plans to construct additional units or common elements. The non-co-owner member of the nonexecutive committee might be an individual with special knowledge, such as an engineer who is asked to consult the association with respect to the construction.

By definition, a "nonexecutive committee" would not be an "executive committee" and would not be permitted to execute the Board's power or authority in the management of the association's business and affairs. A nonexecutive committee could, however, perform under the board of directors' direction any functions described in the Bylaws or determined by the board of directors. The appointment of a nonexecutive committee may be particularly helpful when the board of directors lacks the time or expertise to perform certain functions on its own. A nonexecutive committee may have one or more subcommittees as well. If a nonexecutive committee is approved, the approval must state:

(1) the purpose of the committee appointed;

(2) the terms and qualifications of committee members; and

(3) the ways in which committee members are selected and removed.[45]

This amendment will also impact the role of architectural control committees. These committees are established for the purposes of ensuring that any construction or aesthetic changes made to a condominium are in compliance with the association's governing documents. The changes could be large, such as building a balcony or patio, or small, such as simply replacing windows or placing a large statue in front of a unit. Regardless of the work done, the co-owner must typically go through the association's architectural control committee for approval of the proposed work. The new amendments would allow outsiders (individuals who are not co-owners of the condominium) to serve on such architectural control committees if they are designated as "nonexecutive committees."

Whether condominium associations are interested in permitting nonexecutive committees should be a case-by-case determination given the size, interest, and needs of the association. While the appointment of a nonexecutive committee might not be something associations feel compelled to do immediately, knowledge of the ability to do so should be helpful in the future if and when certain issues do arise that would be more efficiently addressed through the use of a nonexecutive committee.

III. Conclusion

Given the numerous changes to the Nonprofit Corporation Act, community associations in Michigan would be wise to review and/or amend their Articles of Incorporation and Bylaws. The new amendments provide greater flexibility to community associations regarding participation at meetings through electronic means, voting by electronic and other means, adopting broader limitations on director, officer, and volunteer liability, and the ability to appoint nonexecutive committees. In addition to the foregoing, every association must be specifically informed of the new requirements regarding inspection of records since the failure to comply with the inspection of records requirements can be costly.

We suggest that condominium associations do the following:

(1) review their Articles of Incorporation and Bylaws for compliance with the Nonprofit Corporation Act;

(2) discuss the recent statutory revisions with counsel;

(3) adopt a clear procedure for electronic voting; and

(4) adopt procedures for access to books and records.

44 MCL 450.2527.

45 *Id.*