Are Short-Term Rental Restrictions Valid?

August 31, 2018 jonathan dessaules

Short-term rental restrictions are currently a hot topic. Notwithstanding changes in tax laws providing significant benefits of short-term rentals of second homes, more and more HOAs and condominium associations are attempting to amend their CC&Rs to add short-term rental restrictions. We believe most of these amendments are invalid under Arizona law.

Before we address why short-term rental restrictions are likely invalid and unenforceable, it is first necessary to define the terms we will be using. A "short-term rental restriction" is, generally, any restriction on the length of time that a property can be leased and often refers to restrictions of less than six months though it also can refer to restrictions of less than one-year. For purposes of this article, restrictions of rentals on a daily, weekly, monthly, or biannual basis fall under the "short-term rental restriction" umbrella. "CC&Rs," short-hand for "Declaration of Covenants, Conditions and Restrictions," refers to the recorded document or documents that govern the Association. CC&Rs are **not** Bylaws or Articles of Incorporation or Organization.

The following is a common CC&R provision:

> **Leasing Restrictions**. Occupancy of an entire Dwelling Unit on a Lot, but not less than the entire Dwelling Unit, may be granted to a tenant from time to time by the Owner, subject to the provisions of the Master Declaration and the Association Rules. Written leases are required for any Dwelling Unit on a Lot. All leases must restrict occupancy to a Single Family. Before the commencement of each lease term, the Owner of the Lot shall provide the Board with written notice to the Board of the names of the lessee and their family members and the terms of the lease. In addition, if the Board of Directors creates and/or adopts a "rental registration form," the Owner shall submit such form to the Master Association for every rental. Any agreement for the lease of a Dwelling Unit must be expressly subject to the Governing Documents of the Master Association. The lease must contain a provision that any violation of the Governing Documents of the Master Association shall be a default under the lease and is grounds for eviction.

There is nothing in this "Leasing Restriction" prohibiting or restricting rentals to a set term. So the question is whether and under what conditions an Association can amend this Leasing Restriction to

prohibit short-term rentals. The CC&Rs also contain a generic amendment provision allowing for amendments based on a Majority of the Members (*i.e.*, 51%).

Notwithstanding such a generic amendment provision, the *Dreamland Villa* case states that a Majority of the Members generally does not have the right to amend CC&Rs to add new restrictions that "unreasonably alter the nature of the covenants." *Dreamland Villa Cmty. Club, Inc. v. Raimey*, 224 Ariz. 42, 51, 226 P.3d 411, 420 (App. 2010). In order to determine whether the new proposed restrictions "unreasonably alter the nature of the covenants," courts look at whether the proposed amendment is foreseeable based on the language of the existing CC&Rs. If the existing CC&Rs do not place a purchaser on notice that they might be subject to new restrictions of the nature of the one being proposed, then a majority vote of members is insufficient to pass the amendment and unanimous approval of all members is required.

We recognize that the requirement of unanimous consent might seem unfair to some. There are some who argue that the mere fact that CC&Rs can be amended should be sufficient to put an owner on notice that she or he might be subject to new restrictions. But this superficial analysis ignores that real estate is often the single biggest asset most people will buy and they are entitled to buy in reliance on the existing CC&Rs. An owner who buys property specifically to use as short-term rentals and relies on the absence of such a prohibition in the existing CC&Rs does not reasonably anticipate that the singular purpose for their purchase might be outlawed by 51% of their neighbors.

Accordingly, substantial and unforeseeable limitations on an owners' rights generally require unanimity (100%). Amendments to recorded declarations cannot create new obligations or restrictions where the recorded declaration’s provisions did not alert the homeowners to the possibility that they would be subject to the new restrictions. If a recorded declaration does not contain or at least provide for later adoption of a specific restriction or requirement, it is invalid.

The Arizona Legislature has made this unanimity requirement part of the Condominium Act. A.R.S. § 33-1227 states that "an amendment shall not create or increase special declarant rights, increase the number of units or change the boundaries of any unit, the allocated interests of a unit or the uses to which any unit is restricted, in the absence of unanimous consent of the unit owners." Because short-term rental restrictions change "the uses to which any unit is restricted," the Condominium Act expressly would require "unanimous consent of the unit owners." Although the Planned Condominium

Act does not contain a similar provision requiring unanimity, the *Dreamland Villa* case and other legal authorities recognize that the requirement of "unanimous consent" also applies in planned communities.

There are two final considerations. First, though the determination of whether a rental restriction is "substantial and unforeseeable" would appear to be one that can be made as a matter of law just be looking at the original CC&Rs, several courts have ruled that it is up to a jury to decide whether the new restrictions are "substantial and unforeseeable." Second, the Condominium Act requires that any challenge to the validity of an amendment "shall not be brought more than one year after the amendment is recorded." This means that, out of an abundance of caution, any lawsuit challenging the adoption of a rental restriction should be brought within one year of its adoption.

For more information or to discuss a short-term rental restriction in your association, contact Jonathan Dessaules at jdessaules@dessauleslaw.com or 602-274-2360.