

Legal Opinion: Limits of Board Authority & Indebtedness
January 11, 2019

REFER TO:

GVR Bylaws, Article VI: Powers, Duties and Responsibilities of the Board of Directors

Section 2: Limits of Authority and Indebtedness

The Board of Directors is not authorized to enter into any contract that requires an annual payment that exceeds ten percent (10%) of the annual budget. Any contract requiring an annual payment that exceeds ten percent (10%) of the annual budget shall only be valid if approved, in advance, by the affirmative vote of regular members representing a majority of the total votes cast, provided that the total number of votes cast equals at least twenty percent (20%) of the total votes in The Corporation.

From: Wendy Ehrlich, Esq. [<mailto:wehrlich@comcast.net>]
Sent: Friday, January 11, 2019 5:18 PM
To: 'Carol Crothers' <ccrothers@gvrec.org>
Subject: RE: Limits of Authority

You may share the opinion with the Board, but the Board will have to decide whether to share it with the members. Generally, large construction contracts are paid in installments (1/3 upon signing, 1/3 halfway to completion, 1/3 at the completion, or something similar). If a contract does not require payments of more than 10% of the annual budget over a 12 month period, then there would be no requirement to obtain member approval.

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From: Wendy Ehrlich, Esq. <wehrlich@comcast.net>
Sent: Friday, January 11, 2019 1:34:52 PM
To: Carol Crothers
Subject: RE: Limits of Authority

My responses to the following questions:

Do headings such as Section 2 - Authority and Indebtedness have any legal importance when interpreting this language? That is: Is the heading simply for document structure and organizational ease of reading or does it have significant interpretative meaning?

Most contracts - which include corporate bylaws - contain a provision that captions or headings are solely for the purpose of convenience and are not controlling. GVR's Bylaws do not contain such a provision. In Arizona, the only case law that offers some assistance applies to ordinances, and held that if the language of a provision is not clear, it would then be appropriate to look to the heading as an aid, although only a limited aid, in clarifying an ambiguity. *Garrison v. Luke*, 52 Ariz. 50, 78 P.2d 1120 (1938). That said, the language of this provision does not appear to be ambiguous: it applies to any "contract" in which GVR is required to pay an annual sum of money and thus, would be broad enough to include a bank loan or vendor agreement.

Section 2 says "a contract." Does that mean this language only applies to a legally binding contract? Does Section 2 apply to each individual contract not a group or series of contracts signed with the same bank, lender, supplier or vendor? That is: Every contract is evaluated using Section 2 criteria?

In my opinion, the limitation applies to a single contract, and any such contract would be presumed to be binding if approved by the Board. If it applied to a group of contracts with a single entity, then the provision should read "any contract or group of contracts with a single entity that requires an annual payment....."

What does the word "annual" mean as used in Section 2? Is the word "annual" and the words "year" or "twelve-months" the same as used in Section 2? To apply the Section 2 10% limitation, must a contract have a term of at least a year or twelve (12) months? Does the Section 2 10% limitation apply to a contract with a value greater than 10% of the annual budget as Ms. Ehrlich defines it but a term less than a year or twelve (12) months?

According to Black's legal dictionary, "annual" means "occurring or recurring once in each year; continuing for the period of a year; accruing within the space of a year; relating to or covering the events or affairs of a year." It does not necessarily mean a calendar year. For example, if GVR were to enter a contract in June of a particular year, but that contract required an annual payment (from June 1 through May 31 of the following year) that exceeded the 10% limitation, it would require approval of the members. It could be a contract that is for a term less than a year as well, because the provision applies to "any contract" - not just contracts that are of certain duration. The time that the calculation is made, however, i.e., whether the annual contract payment exceeds the annual budget, is when the contract is entered into. In other words, if GVR were contemplating a contract that over twelve months would require a payment of more than 10% of the annual budget at the time the contract is entered into, then member approval would be required.

Would Ms. Ehrlich expect the Section 2 words "annual payment" and the Section 2 title words "Indebtedness" lead a court to apply Section 2 to borrowing of money only, i.e., a loan agreement with a lender? Do the words "annual payment" imply a series of payments like a loan payments?

As discuss above, I do not see the caption as limiting the type of contract to which the provision applies. It is my opinion that the term "annual payment" is broad enough to include a series of payments made monthly in any twelve-month period, or a payment made once in a twelve-month period.

Would Ms. Ehrlich agree that Section 2 only applies if all three (3) conditions are met: (1) a contract, (2) one or more annual payment and (3) greater than 10% of the annual budget?

Yes.

Wendy Ehrlich, Esq.

From: Wendy Ehrlich, Esq. <wehrlich@comcast.net>
Sent: Monday, January 7, 2019 11:14 AM
To: Carol Crothers
Subject: RE: Limits of Authority

When you say that “our annual budget” is approximately \$11M, I assume you are referring to the annual *operating* budget. Article VI, Section 2, however, refers to the “annual budget,” and not the “operating budget” and this difference is significant. In contrast, Article III, Section 3 (Standard of Service) limits the Board’s authority to increase or decrease services exceeding 5% of the existing “Operating Budget” without a vote of the membership. The question, therefore, is whether the term “annual budget” used in Article VI is different than the term “Operating Budget” used in Article III. In other words, is the term “annual budget” in Article VI broader?

There are only two types of budgets referred to in the Bylaws: Operating Budgets and Capital Budgets. Although there is no definition provided for either capitalized term, “Operating Budget” has historically been interpreted to mean the budget for operating expenses and “Capital Budget” has been interpreted to mean the funds used for capital replacements and improvements (reserves). Article VI, Section 1(B)(3) uses the term “annual operating and capital budgets” and thus, it would follow that the term “annual budget” used in Article VI - which does not distinguish a particular budget - includes *both* the operating and capital budgets. If this were not the intent, then Article VI would have used the term “Operating Budget” as used in Article III, Section 3.

When courts interpret contract terms, they try to give meaning to each and every term used. While there is no way to know with certainty how a court would interpret “annual budget” in Article VI, it is likely that it would distinguish that term from other terms used in the Bylaws. Thus, it is a fair interpretation that Article VI limits the Board’s authority to enter into a contract that requires an annual payment which exceeds ten percent of both the annual operating and capital budgets *combined*. The question then is whether a contract payment that exceeds \$1.1M in one year, exceeds ten percent of GVR’s annual budget for both operating and capital expenses. If so, it would require the approval of members.

Wendy Ehrlich, Esq.