



New Jersey Appellate Court Holds Business Judgment Rule Protects Decisions of Common-Interest Community Board in Adopting and Enforcing Building Height Restrictions

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In a decision approved for publication, New Jersey's Appellate Division recently held that the business judgment rule protected the actions of a common-interest community's board of trustees in rejecting certain residents' requests to elevate their homes higher than the board's regulations allowed after Superstorm Sandy. See *Alloco v. Ocean Beach & Bay Club*, 2018 WL 3999039 (N.J. Super. Ct. App. Div. Aug. 22, 2018). The decision is significant in limiting challenges to a board's action to grounds of fraud, self-dealing or unconscionability.

The Ocean Beach and Bay Club (the "Club") is a Jersey Shore common-interest community established to manage almost 1,000 lots owned by its members, as well as some common areas. Among other things, the Club's certificate of incorporation provided that "no[] more than one residence nor more than [a] one-story one-family dwelling shall be allowed on any lot," and established a board of trustees (the "Board") to enforce and amend the regulations as necessary. After Superstorm Sandy, the Board amended the regulations to allow some members to elevate their homes. Plaintiffs, all of whom were members of the Club and lost their homes in the storm, attempted to elevate their homes even higher than the regulations allowed in order to use the new space under the homes for parking, but the Board rejected their request to do so. Plaintiffs then brought this action alleging, inter alia, that the Board violated the business judgment rule in its adoption and enforcement of the regulations and that the "Club acted incompetently in devising regulations limiting the height of structures." The parties both moved for

summary judgment, and the trial court granted the Board's motion and dismissed the complaint.

On appeal, the Appellate Division affirmed the trial court's decision. Under the business judgment rule, "when business judgments are made in good faith based on reasonable business knowledge, the decision makers are immune from liability from actions brought by others who have an interest in the business entity. The business judgment rule generally asks (1) whether the actions were authorized by statute or by charter, and if so, (2) whether the action is fraudulent, self-dealing or unconscionable." The first prong was met because the Club's by-laws authorize the Board to make "any and all rules and regulations and enforce compliance therewith[.]" With regard to the second prong, the Court found that Plaintiffs' claims that the Board engaged in self-dealing were unsubstantiated and unrelated to the height restrictions Plaintiffs challenged, and "[a]llegations of self-dealing in unrelated matters are insufficient." Additionally, the Court rejected Plaintiffs' claim that "incompetence" violates the business judgment rule. In doing so, the Court disapproved of the statement in Papalexioiu v. Tower W. Condo., 167 N.J. Super. 516, 527 (Ch. Div. 1979) that "[c]ourts will not second-guess the actions of directors unless it appears that they are the result of fraud, dishonesty or incompetence," finding that the chancery court in Papalexioiu mistakenly cited an inapposite section of another case for this "incompetence" language and that "[w]e must continue to follow the Supreme Court's lead and require a showing of fraud, self-dealing or unconscionable conduct." Finally, the Court found that any procedural errors made by the Board—such as its alleged failure to print and send its members notice of changes in rules and regulations within 30 days—were inconsequential and did not show that the Board's actions were fraudulent, self-dealing or unconscionable.

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