

DRAFTING COMMUNITY RULES

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Bob Burton is a shareholder in Winstead's Real Estate Development & Investments Practice Group. Bob's practice focuses on real estate, with an emphasis on the planning, development, risk management, administration and marketing of single-family, townhome, condominium, commercial, and mixed-use projects, as well as timeshares and resorts. Bob also works with developers and builders to ensure compliance with secondary mortgage market (FHA, VA, FNMA, etc.) and Interstate Land Sales registration requirements. Bob also represents condominium, residential, commercial, and mixed-use property owner associations.

Representative Experience

- Representation of national, regional, and local developers, builders, and investors in the development, governance, management, administration, marketing, and sale of single-family, townhome, condominium, commercial, and mixed-use projects
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- Representation of national, regional, and local developers and builders before municipalities and governmental agencies related to the development and administration of residential and mixed-use projects
- Representation of national, regional, and local developers and builders in the acquisition of real property for development
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Education

Tulane University Law School

- J.D., 1992
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- *Tulane Law Review* (Member, 1990-1991; Editor, 1991-1992)

University of North Texas

- M.S., Accounting, 1987
- B.S., Accounting, 1987

Professional Recognition & Community Involvement

- Fellow, *American College of Real Estate Lawyers*; Member, *Common Interest Ownership Committee*
- Martindale-Hubbell AV Rated (Top Rating)
- Best Lawyers™(Real Estate)
- Full Member, *Urban Land Institute*, Residential Neighborhood Council Member
- Attorney Committee (Voting Member) and Developer's Committee, *Texas Association of Builders*
- Texas Association of Builders: 2015 Presidential Distinguished Service Award (award conferred in recognition of advocacy regarding Texas condominium tort reform enacted by the Texas Legislature during the 84th Texas Legislative Session).
- Co-Chair (2013-2014, 2014-2015) and Member *Mixed-Use Development Council*, *Urban Land Institute*, Austin Chapter
- Founding Member, *Committee on Common Ownership*, Real Estate Probate and Trust Law Section of the Texas State Bar
- Member, *Federal Affairs Task Force*, Community Associations Institute. The Federal Affairs Task Force is a national task force organized to respond and comment upon Federal legislation affecting community associations and home ownership.
- Community Associations Institute, 2010 Award of Excellence for Government & Public Affairs - Federal Affairs Task Force (award conferred based on advocacy regarding federal mortgage lending requirements for residential product).

Admitted to Practice

- Texas
- Arizona

Presentations and Papers

- *Leasehold Condominiums*, 40th Annual Advanced Real Estate Law Course (July 2018)
- *Density Developments*, Community Association Institute (April 2018)
- *Risky Business: Avoiding Coverage Gaps and Overlaps When Insuring Mixed-Use Projects*, sponsored by the American Bar Association RPTe and the American College of Real Estate Attorneys (February 2018)
- *The Trouble with "Townhomes"*, Community Association Institute (January 2018)
- *85th Texas Legislature Update: Developers, Builders and POAs*, State Bar of Texas Webcast (November, 2017).
- *Insurance Issues for Mixed-Use Projects*, American College of Real Estate Attorneys (October 2017).
- *Life Cycle of a Master Planned Community*, First Service Residential Workshop (March 2017)
- *Condominium Tort Reform in Texas*, Texas Lawyer (2016).
- *84th Texas Legislative Update: Condos and Owners Associations HOA*, State Bar of Texas Webcast (July 2015).
- *HOA Pre-Foreclosure Due Diligence, Handling Your First (or Next) HOA Assessment Lien Foreclosure for Condos and Subdivisions*, Texas Bar CLE (October 2014).
- *Master Planned Communities: A Survey of Governance Models*, American College of Real Estate Attorneys (October 2014).
- *Commercial Restrictions: Advanced Real Estate Drafting Course* (March 2014).

- *Using the Condominium Form of Ownership to Segregate (Plat) Land*, Advanced Real Estate Strategies, State Bar of Texas (December 2013).
- *Drafting Condominium Documents to Comply with FHA, FannieMae and VA Requirements*, Advanced Real Estate Drafting Course (March 2013).
- *Uncommon Condominiums*, Texas Land Title Association Webcast (November 2012).
- *Condominium Alternatives, Mixed and Non-Traditional Uses*, 34th Annual Advanced Real Estate Law Course (July 2012).
- *HOA Reform Laws, Select Issues: Developers and Declarants*, State Bar of Texas Webcast (April, 2012).
- *The 82nd Texas Legislature and Community Association Reform—Developer Issues*, State Bar of Texas Webcast (April, 2012).
- *Planned Community Governance Models: Serial, Expandable, Nested and Busted*, 21st Annual Advanced Real Estate Drafting Course (March, 2010).
- *MOMUPs, Lollypops, and Snowmen*, Princeton University Higher Education Real Estate Lawyers (HEREL8) (October 2009).
- *Transitioning Property Owner Association Control*, 20th Annual Advanced Real Estate Drafting Course (March 2009).
- *Texas Condos 101*, State Bar of Texas Real Estate Section (December 2007).

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DRAFTING COMMUNITY RULES

I. SCOPE

This paper provides a broad overview of matters to consider when drafting rules for a Texas property owners' association (a "POA"). The scope of this paper is limited to residential condominium projects subject to Chapter 81 or 82¹ of the Texas Property Code, and non-condominium residential projects subject to Chapter 209² of the Texas Property Code.

II. PRELIMINARY OBSERVATIONS

Drafting rules and regulations for POAs is unique in that, unlike most projects where documents are prepared for a single client in relation to a transaction to occur in the near-term, POA rules will continue to be used for many years and will be relied on and interpreted by future owners, directors, and managers. For the to-be-developed project, rules also have an effect on the perception of the project and can affect marketability. This is especially the case for the condominium project, where the condominium information statement provided to prospective purchasers in almost all circumstances will include the rules and regulations governing the community.³

Rules also need to conform to the character of the community. Rules for a dense townhome project will differ from the rules necessary to govern a traditional detached home subdivision. Rules also differ dependent on project components and amenities, geography and location, product price point, community programming, and anticipated management structure (on-site management versus a portfolio managed project⁴).

The challenge when drafting rules is resolving the tension between the need to be *comprehensive, comprehensible, and flexible*. Flexibility is critical. The drafter will need include an appropriate mechanism to modify the rules as the community matures and conventions change. In many cases, the rules are drafted well before the rules will be applied. In the case of a large mixed-use project or a high-rise condominium, the lender presale requirements for the project usually require that a certain percentage of contracts be in place prior to commencement of construction, and the period between drafting the rules and application of a specific rule (when the project is complete and occupied), may span several years. For the condominium project, and to enable delivery of a valid condominium information statement, these rules are necessarily drafted without a full understanding of the character of the community since the character of the community is formed by residents and owners over time.

Drafting rules is similar to drafting legislation but with a twist. Drafting legislation has been described as having twin aspects – “the conceptual aspect, in which the drafter ascertains and perfects the concepts to be employed in his draft, and the literary aspect, in which the drafter selects the best means of expressing those concepts.”⁵ The twist? The timeline between the behavior and legislation to address the behavior is usually long. The issue arises, and legislation is later adopted to address the issue. The process is reversed for rules, at least for the initial rules adopted for the project. The drafter must anticipate the issue and behavior based on prior experience, custom, and project specifics. The rules try to anticipate a future problem, legislation tries to solve an existing problem. Rules are predictive, and predictions can be wrong. Admittedly, some rules are commonly used and accepted, but each community necessarily has its own character and conventions, and an attempt should be made to confirm the rules to the community. That is not to say that each community will have wholly different rules. It is likely that some rules will be exactly the same between two communities. However, there will be unique features present in each community. Also, the drafter should keep in mind that the community will mature, new issues will arise, and original rules will fall out of favor or need to be adjusted. Conditions affecting the community will change over time, and the drafter must anticipate change.

¹ Chapter 81 of the Texas Property Code applies to condominiums created prior to January 1, 1994. Chapter 82 of the Texas Property Code applies to condominiums created on or after January 1, 1994.

² Chapter 209 applies to residential subdivisions that are subject to restrictions or provisions in a declaration that authorize the property owners' association to collect regular or special assessments on all or a majority of the property in the subdivision and that require mandatory membership. TEX. PROP. CODE 209.003.

³ Section 82.152 of the Texas Property Code requires that the developer of the project prepare a condominium information statement prior to offering condominium units for sale to the public. Unless the condominium information statement is delivered to the purchaser prior to the purchaser's execution of a contract to acquire the unit, the purchaser has 6 days after receipt of the statement to rescind the purchaser contract. See TEX. PROP. CODE 82.156(a). Section 82.153 of the Texas Property Code includes a list of information or documents which must be included in the condominium information statement. Rules are required to be included as part of the statement. TEX. PROP. CODE 82.153(a)(5).

⁴ In community association management parlance, a portfolio managed property has no on-site manager and is managed off-site usually from the local management company office.

⁵ Reed Dickerson, *How to Write A Law*, 31 Notre Dame Lawyer 14 (1955).

III. THE EFFORT TO UNDERSTAND THE COMMUNITY

Whether drafting rules for a new community or preparing and/or amending rules for an existing POA, the drafter needs to fully understand the community. When amending and/or preparing rules for an existing community, the drafter needs to understand what initiated the need for change. Understanding the specific character and needs of the community is the first step in the rule-making process.

For the new community, an understanding of the project includes a review of the conceptual or actual development plans, review of existing encumbrances affecting the project, the planned amenities for the project, local municipal requirements,⁶ whether the project will be self-developed and built or lots sold to builders, project price-point of homes or units,⁷ and whether the project will utilize on-site community management.⁸ For a condominium project, it is crucial for the drafter to review the construction plans in conjunction with the developer and the architect. Features that may not be readily apparent from the plans may need to be addressed.⁹ The best rules are rules that, once drafted, are carefully reviewed by the developer, community manager, and, if possible, the sales staff or listing broker.¹⁰ For new condominium communities, and due to the longer timeline between drafting and application, there is a much greater likelihood that as the project is constructed, the rules may change from the rules initially provided to prospective purchasers.¹¹ Changes may be required due to new or modified project features, issues revealed but not addressed in the initial rules, prospective purchaser feedback during the sales process, or special contract provisions negotiated between the developer and a prospective purchaser.

For an existing community with rules in place, the rule revision or new rule adoption process will have political issues that often overshadow the drafting process. With the exception of changes or additions mandated by statute,¹² modifying or adding new rules to an existing community can be controversial. The process has a much higher degree of difficulty compared to drafting rules for a new community. Revising or adding new rules for an existing community can take many months from initial drafting to formal adoption. Depending on the rule-making authority in the existing documents, the modification process may require a vote of the members, and in some cases, due to the requisite percentage of members required to approve any changes, may be impossible to achieve. In most circumstances, the desire for new or modified rules will be prompted by poorly drafted existing rules or changed circumstances. Before initiating the drafting process, the drafter should meet with the board and manager to investigate the specific problems with the existing rules or the circumstance that has prompted the request for a new rule. If any change to existing rules or additional rules must be approved by the membership and approval is not practical, it may be possible to address the

⁶ Municipalities in Texas have become more sensitive to the importance of the community association for the proper operation of a residential or mixed-use community. The municipality may require, in conjunction with permitting, that the developer require the association to enforce specific rules and requirements pertaining to the community and mandate that those requirements be incorporated into the association rules. For example, the City of Austin requires that the association adopt certain maintenance requirements for landscaping and trees and enforce integrated pest management practices against its members.

⁷ The price point of homes or condominium units can provide some indication of the type of rules that will be needed for the community. For example, a starter home community may be amenity poor compared to its move-up counterpart. Custom home communities may include specific features that must be incorporated into a residence or lot which require specific maintenance requirements that are incorporated as part of the rules.

⁸ Some rules, for example on-street parking prohibitions, may be difficult to administer and enforce without on-site association management. For projects without on-site management, detailed procedures may be needed for reporting rule violations.

⁹ In one recent project, a close review of the plans in conjunction with the architect revealed that the exterior window washing apparatus for certain levels of the building were accessible only by accessing the actual unit. Rules were needed to address access and to protect the apparatus, which was located on the roof of the balcony appurtenant to the unit.

¹⁰ The listing broker and their agents are often the only means to receive direct feedback from future owners, which can be helpful when designing or evaluating previously drafted rules. The movie industry pre-screens a film prior to general release, based on audience feedback, changes are sometimes made based on this feedback. For the new community, it is not possible to “screen” the rules for community owners, but the developer, management company, and listing broker can serve as the test audience.

¹¹ As noted in Part II of this article, a condominium information statement is delivered to each prospective purchaser and the statement is often delivered many months, or a few years, prior to completion of the project. The condominium information statement includes the proposed rules for the project. To the extent the rules change between the date they are delivered to the prospective purchaser and the closing of the unit, Section 82.153(c) of the Texas Property Code requires that the developer amend the condominium information statement to reflect a material and substantial change in its contents. If the change adversely affects a purchaser, the developer is required to deliver the amendment prior to the unit closing. Chapter 82 includes no express right of contract rescission for amendments to the condominium information statement.

¹² For example, in 2015 the Texas Legislature removed a provision from Section 202.010 which allowed a developer to prohibit solar facilities during the development control period. Solar rules adopted prior to 2015 often included the developer exemption and many communities modified their rules to revoke the exemption.

problem with policies or procedures adopted by the Board.¹³ If the drafter is commissioned with drafting rule revisions or new rules, the process for an existing community is often the reverse of the process for a new community. Rather than drafting the rules and providing to the developer or other stakeholders for review, it is often more efficient and effective to provide sample rules to the board or committee charged with the rule revision process and ask that the board or committee meet and provide the drafter with general instructions or a draft of the proposed rules. Asking the board or revision committee to initiate the process can create a sense of ownership and political buy-in which may ease the adoption process. Again, as in the case with drafting rules for the new community, the drafter must become familiar with the project, which will include reviewing all existing governance documents (recorded covenants, polices, procedures), plat maps, and illustrative plans if available. Interviews with management personal, board members, and a visit to the project is also important. There will be different considerations for the existing community, namely the existing community has a distinct personality formed through the personalities and perceptions of its members, leadership, and management personnel. The drafter should seek to determine what makes the community unique.

IV. DESIGNING THE GOVERNANCE STRUCTURE TO PRESERVE RULE FLEXIBILITY; AMENDING OR MODIFYING THE RULES

The initial or existing design of the governance system for a community will dictate, to a certain extent, how rules are drafted, and the process associated with rule changes.

For the non-condominium association, the structure of governance varies depending on who prepared the documents and the project. There is no one common approach in Texas to the structure of community governance other than all communities with a mandatory association will have a recorded restrictive covenant, often referred to as the “declaration”. Sometimes the founding declaration includes end-user rules or requirements, sometimes the declaration authorizes the creation of rules which are then established by a separate recorded document. The declaration may allow the board of directors to adopt or amend rules or require that members approve any amendments or new rules.¹⁴ Rules governing design, i.e., architectural requirements which apply to new construction or modifications, are sometimes included in the declaration or included in a separate document. Most frequently, the non-condominium governance system will include a mix of approaches. Top-level end-user rules, that is rules which are unlikely to change over time, are often included in the declaration. Examples include the rule against commercial use for a residential project, a rule requiring the owner to maintain their property and landscaping in good condition, or a rule prohibiting the modification of a home without prior written consent. Sometimes the declaration will include detailed and specific rules regarding pets, fireworks, leasing, etc. To the extent possible, when drafting the governance suite for a new project, consideration should be given to the distinction between stable and unstable rules. Stable rules are rules, such as the single-family use rule, that are appropriate for inclusion in the declaration. Stable rules are unlikely to change over time and are indicative of the character of the community, i.e., residential versus commercial. Unstable rules are generally detailed prohibitions against certain behavior or specific improvements that could change either as the community or culture changes, or that may be more prone to legislative direction. For example, specific rules governing the operation of drones would be considered unstable given the likelihood for regulation or changed perceptions. When drafting the governance suite for a new community, providing the right to adopt rules in the declaration, but placing unstable rules in a separate document may provide greater flexibility as the community changes over time and may also reduce the risk of rule obsolescence. Another way to conceive this approach is to view each component of the governance suite as addressing a specific task or constituency. The declaration serves the role as setting the parameters for association or developer power and establishes specific community critical obligations, such as the obligation to pay assessments and the obligation to obtain approval for dwelling modifications. Rules, established in a separate document, with the primary constituency being lot owners and the enforcing authority, include specific and detailed rules related to use and behavior. Design guidelines, the constituency being lot owners and the architectural review authority, address architectural and aesthetic conditions or requirements important to the community. The benefit to separating each component is preserving flexibility as the community matures and circumstances (technology or cultural) change.

¹³ Section 202.004 of the Texas Property Code allows the Board certain latitude in interpreting restrictive covenants provided the interpretation is not arbitrary, capricious, or discriminatory. This can be helpful provided the interpretation does not conflict with the rule. The words arbitrary and capricious have been defined as being fairly synonymous and generally describes something that is not founded in the nature of things, and depending on the will alone. *Webb v. Dameron*, 219 S.W.2d 581, 584 (Tex. Civ. App.—Amarillo 1949, writ ref'd n.r.e.) (citations omitted). The jury charge used in cases where there are allegations of arbitrary and capricious action is instructive here: “A decision is arbitrary if it is based on random choice or personal whim or without constraint. A decision is capricious if it is given to sudden and unaccountable changes of mood or behavior.”

¹⁴ For communities still subject to developer control, the declaration may also require that the developer consent to any modifications to the initial rules.

Separating each component also allows the drafter to set the change parameters in each document based on the specific project and needs of the community.¹⁵

When confronted with adding rules or amending existing rules for a mature non-condominium community, it may be possible to implement a process, in conjunction with the rule-making effort, that preserves future flexibility. Obviously, if the drafter is required to modify a rule in a declaration and the declaration requires that any change be approved by a requisite percentage of the membership, the declaration will need to be amended. However, to the extent new rules are required, and to the extent the new rule does not conflict with a rule embodied in the declaration, consideration should be given to adopting the rule by separate instrument rather than in an amendment to the declaration. It also may be possible to achieve even greater flexibility where the declaration includes the targeted rule by amending the declaration to remove the deficient rule and replacing with a replacement rule established by separate instrument.

For the non-condominium community, it is common (but by no means universal) for the developer to reserve the right to unilaterally amend the restrictive covenant. Section 209.0041 of the Texas Property Code, which includes a requirement that notwithstanding any provision in a “declaration”¹⁶ to the contrary, no greater than 67% of the total member votes may be required to amend the covenant, does not apply during the development period.¹⁷ However, there are some constraints on amendment by the developer even if the developer reserved the right to unilaterally amend the declaration or “dedicatory instruments”. The term dedicatory instrument is defined broadly and includes every “instrument covering the establishment, maintenance, and operation of a residential subdivision” and specifically includes rules and regulations and all amendments thereto.”¹⁸ Section 209.013 of the Texas Property Code prohibits any amendment to a dedicatory instrument, e.g., rules, between the period of time the developer loses majority voting control of the association and the date a new board is elected.¹⁹

Interestingly, most condominium governance systems do segregate each component of the governance suite by purpose. This is likely a byproduct of the comprehensive approach to condominium creation outlined in Chapter 82 of the Texas Property Code. Generally, the condominium governance suite consists of the condominium declaration, organizational documents for the condominium association (certificate of formation and bylaws), house rules, and associated policies and procedures, e.g., move-in/move-out policies, pet registration requirements, etc. Section 82.055 of the Texas Property Code includes a list of the required contents of the condominium declaration. Section 82.055(9) requires that the declaration include “any restrictions on use, occupancy, or alienation of the units.”²⁰ However, the custom and practice in Texas is similar to the approach recommended above for the non-condominium structure. That is, stable rules, e.g., a single family use rule, are usually included in the condominium declaration while unstable rules are relegated to a separate document adopted through the rule-making authority in the declaration.²¹ Section 82.102(a)(6) and (a)(7) of the Texas Property Code expressly provide that the condominium association, acting through the Board may: “regulate the use, maintenance, repair, replacement, modification, and appearance of the condominium.”; and “adopt and amend rules regulating the use, occupancy, leasing or sale, maintenance, repair, modification, and appearance of units and common elements, to the extent the regulated actions affect common

¹⁵ For example, the declaration may provide that it may only be amended by a requisite percentage of members, the rule document by a majority of the board, and the design criteria by a majority of the architectural review authority (often also with approval of a majority of the board).

¹⁶ A “declaration” for the purpose of Chapter 209 of the Texas Property Code is “an instrument filed in the real property records of a county that includes restrictive covenants governing a residential subdivision.” TEX. PROP. CODE 209.003(3).

¹⁷ A “development period” is the period established in the covenant “during which a declarant reserves: (A) a right to facilitate the development, construction, and marketing of the subdivision; or (B) a right to direct the size, shape, and composition of the subdivision.” TEX. PROP. CODE 209.002(4-a).

¹⁸ TEX. PROP. CODE 209.002(4).

¹⁹ The effect of this rule can be minimized by including an appropriate voting allocation provision in the dedicatory instrument.

²⁰ Chapter 82 of the Texas Property Code is based on the Uniform Condominium Act adopted by the Uniform Law Commission in 1980. Section 2.105 of the Uniform Act is the counterpart to Section 82.055 of the Texas Property Code. Interestingly, Section 2-105 of the Uniform Act does not require that the declaration include restrictions on the use and occupancy of units, but instead provides, in Section 2-105(b), that the declaration may include restrictions on the use of units. Be that as it may, the custom in Texas is to establish most of the restrictions (or rules) pertaining to the units in a separate document and not in the condominium declaration.

²¹ Section 82.102 of the Texas Property Code recites the powers of an association and expressly provides that those powers are exercised through the association’s board of directors.

elements or other units.”²² The drafter should note that when asked to evaluate the authority to adopt new rules, or modify existing rules, that Section 82.102(a)(6) and (a)(7) apply to a condominium created under Chapter 81 of the Texas Property Code, that is prior to the effective date of Chapter 82.²³ The drafter should also review and consider the effect of Section 82.067(e) which provides that an amendment to the declaration requires 100% consent of all votes allocated to members if the amendment will change the use restrictions applicable to a unit. Though there is no direct statutory support, or any Texas case law interpreting Section 82.067(e), experienced condominium practitioners have interpreted this provision as a prohibition from changing, for example, a residential use to a commercial use, and vice versa, if the declaration limits use to a particular category.²⁴

Irrespective of whether the rules are for a condominium or residential association, if you adopt or modify a rule, the rule must be recorded to be effective. Section 202.006 of the Texas Property Code, which applies to both condominium and non-condominium communities, provides that a “dedicatory instrument has no effect” until recorded.

V. CONCLUSION: THE NEED FOR FLEXIBILITY AND THE REALITY OF RULE CREATION AND MODIFICATION

Are rules made to be broken? Maybe, but if broken, the rules need to have been properly adopted and clearly written to be enforced. Just as important, in the author’s view, is the initial design of the governance system, or a redesign calculated to provide the developer and community leaders the ability to respond to changed circumstances. Who would have predicated 10 years ago that flying vehicles would be considered for delivery services, or short-term rentals would be a billion-dollar industry? What might the future hold and will the community have the means to address these new challenges?

When asked to modify rules, whether for the condominium or non-condominium community, the drafter would be well-advised to set expectations early and reinforce those expectations often. It is likely to take longer and cost more in time and resources than expected. It is difficult to overemphasize the politics of the rule modification process, especially for the mature community. Even assuming that the legal path to modification is clear and unequivocal, and assuming that the board or developer has the power to modify, the board or developer will have to confront settled expectations and entrenched attitudes. The risk of litigation is ever present. However, a well-defined process, the ability to clearly communicate the need for modification, and patience increases the likelihood of success.

²² Section 82.102 of the Texas Property Code is a provision that may be varied by the condominium declaration, so if the drafter is modifying existing condominium rules, the drafter is advised to confirm that the condominium declaration does not include constraints on these powers.

²³ Chapter 82 is effective for all condominiums created on or after January 1, 1994. Condominiums created prior to January 1, 1994, are governed by Chapter 81 of the Texas Property Code. However, Section 82.002 of the Texas Property Code provides that certain provisions of Chapter 82 apply to a condominium created prior to January 1, 1994. Section 82.102(a)(6) and (a)(7) are two provisions that apply to a condominium created prior to January 1, 1994.

²⁴ Note that Section 82.067 pertains to amendment to the condominium declaration as opposed to rules established by separate instrument. This is a compelling reason for including the authority to adopt rules in the condominium declaration and establishing those rules in an instrument other than the declaration.