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IN THE SUPERIOR COURT OF THE STATE OF ARIZONA

IN AND FOR THE COUNTY OF MARICOPA

COLETTE MCNALLY, an individual, Plaintiff, vs. SUN LAKES HOMEOWNERS ASSOCIATION #1, INC, an Arizona non-profit corporation, Defendant.	Case No. CV2014-009496 **DEFENDANT'S RESPONSE TO PLAINTIFF'S APPLICATION FOR PRELIMINARY INJUNCTION** (Assigned to the Honorable James Blomo)

Defendant Sun Lakes Homeowners Association #1, Inc. requests that the Court deny Plaintiff's Application for Preliminary Injunction. Plaintiff, a member of the Association's Board of Directors, seeks a preliminary injunction compelling the Association to grant her access to the confidential and sensitive information of the Association that is discussed during executive sessions of the Board. The Association has screened Plaintiff from receiving such information because she refuses to protect it against unauthorized disclosure, as required under applicable law. Plaintiff's unclean hands bar the extraordinary equitable remedy that she seeks.

Although Plaintiff asserts that she is entitled to a preliminary injunction because she is likely to succeed on the merits, this Court already has rejected Plaintiff's claim that the Association lacks authority to screen her from confidential and sensitive information or,

alternatively, that the ongoing nature of the screening is unreasonable *per se*. This Court denied Plaintiff summary judgment on these very grounds earlier this year.

Plaintiff's claim that the screening is causing her irreparable injury is controverted by the fact that, since the Association began screening her from executive sessions in September 2013, she has continued serving on the Association's Board of Directors, and was even re-elected to a second term. Plaintiff has stated that the screening has made her a more effective member of the Board, which may explain why she has waited nearly two years to seek an injunction.

Public policy, as embodied in A.R.S. §§ 33-1804(A) & -1805(B), favors protecting confidential and sensitive information against unauthorized disclosure. Because Plaintiff repeatedly has violated this statute during her service on the Board, and because she has stated – under oath – that she will not hesitate to do so again, the only way that the Association can prevent Plaintiff from disclosing such information is to ensure that she does not have access to it. Compelling the Association to grant Plaintiff access to confidential and sensitive information of the Association under these circumstances would expose the Association to a substantial risk of irreparable harm, and contravene both equity and public policy. Therefore, the Association respectfully requests that the Court deny Plaintiff's Application for Preliminary Injunction.

I. FACTUAL BACKGROUND

Plaintiff is a resident of a planned community known as Sun Lakes. Defendant is a non-profit Arizona corporation whose primary purpose is "to establish, own, operate, maintain, and manage community recreational and welfare facilities" for the residents of Sun Lakes. The Association is managed and controlled by a volunteer, seven-member Board of Directors comprised of Sun Lakes homeowners who are elected to staggered three-year terms at the Association's Annual Meeting. The Association's Bylaws authorize the Board of Directors "[t]o exercise all financial, legal, and other powers of the Board as are stated in these Bylaws, the Articles of Incorporation, and any other powers granted under the laws of

the State of Arizona." (*See* Restated Articles of Incorporation and Restated Bylaws of Sun Lakes Homeowners Association #1, Inc., attached as Exhibits B and C to Defendant's Response to Plaintiff's Statement of Facts in Support of Plaintiff's Motion for Summary Judgment to Restore Her Right to Participate in Executive Sessions filed 1/30/15 ("DSOF").) The Association employs various administrative personnel to carry out its day-to-day operations, including a General Manager and staff. The Association also employs many dozens of other people in positions that include golf course operations, restaurant operations, and maintenance. (*See* Declaration of Richard Schwartz, 1/26/15, attached as Exhibit D to DSOF.)

A. Plaintiff's Service on the Association's Board of Directors.

Plaintiff first began serving on the Association's Board of Directors in 2009, when she was appointed to fill a vacancy on the Board. At the conclusion of her appointed term, Plaintiff ran for election to the Board of Directors but was not elected. In 2010, Plaintiff was again appointed to fill a vacancy on the Board. However, Plaintiff was removed for cause before the end of her appointed term, after she disclosed confidential financial information of the Association to non-Board members. The Association incurred substantial attorneys' fees and costs associated with removing Plaintiff from the Board of Directors. After Plaintiff's removal, a former employee of the Association asserted a claim against the Association arising out of Plaintiff's breach of a confidentiality agreement between the Association and the former employee. The Association resolved the claim by paying the former employee a sum of money to settle the claim. The Association also incurred substantial attorneys' fees and costs in defending the former employee's claim.

Plaintiff ran for election in 2011 and was elected to the Board of Directors. The Board of Directors selected Plaintiff to serve as Secretary of the Board upon her election in 2011. However, Plaintiff served as Secretary for less than one year before the Board of Directors removed her from that position for cause. After her removal as Secretary, Plaintiff continued to serve as an elected member of the Board of Directors. Plaintiff's first term

ended in 2013, after which she was elected to a second term. Plaintiff's second term will end in February 2017. (*See id.*; *see also* Deposition of Colette McNally, 1/15/15, attached as Exhibit A to DSOF.)

B. Background of the Current Dispute.

On August 4, 2013, Plaintiff received an e-mail from Jeannie Martens, a former employee of the Association, in which Ms. Martens accused two of her former colleagues (General Manager Clint Warrell and Human Resources Manager Roberta Laird) of misconduct ("the Martens e-mail"). According to the Martens e-mail, the misconduct occurred two years earlier and involved the circulation of notes or correspondence that Ms. Martens discovered while cleaning out a "Board book" following a Board of Directors meeting. The notes and correspondence appeared to involve a plan by several members of the Board – including Plaintiff – to force the resignation of another member by publicizing that member's allegedly "illegal actions." Ms. Martens states in her e-mail that she brought the notes to the attention of General Manager Clint Warrell, who, together with Human Resources Manager Roberta Laird, decided to provide the notes anonymously to another Board member, Bill Hoyt, believing that Mr. Hoyt would circulate the notes throughout the community. Mr. Hoyt did in fact circulate the notes, and as a result, the actions of Plaintiff and her fellow Board members were publicized. Two years later, when Ms. Martens resigned her employment with the Association "under duress," she decided to send an e-mail to Plaintiff explaining how the notes had ended up in the hands of Mr. Hoyt. (*See* Exhibit A to DSOF, at Exh. 5.)

On August 5, 2013, Plaintiff forwarded the Martens e-mail to Rick Schwartz, President of the Association's Board of Directors, along with an e-mail authored by Plaintiff containing further accusations against Mr. Warrell and Ms. Laird, demanding that they resign or be dismissed, and demanding that the Board of Directors meet to address the matter. Mr. Warrell and Ms. Laird denied Ms. Martens' allegations. The President forwarded Plaintiff's e-mail to the remainder of the Board of Directors and asked for their input on how to handle

the situation. The President also called the Association's general counsel, Mr. Charles Maxwell, and sought legal advice concerning the handling of the Martens e-mail. (*See* Exhibit D to DSOF.)

The Board of Directors – including Plaintiff – met in a special executive session on August 14, 2013. The President reported that he had discussed the Martens e-mail with the Association's general counsel. The President reported that the employees named in the Martens e-mail denied the allegations of the e-mail. The President advised the Board that the Association should not act on the Martens e-mail because doing so could expose the Association to liability for defamation. Alone among the Board members, Plaintiff disagreed with the President's handling of the Martens e-mail. Plaintiff argued that the contents of the Martens e-mail should be disclosed to the Association's members and discussed by the Board of Directors in an open meeting. Following the August 14, 2013 executive session, the President sought further advice from the Association's general counsel concerning the matter. (*See id.*; *see also* Exhibit A to DSOF.)

On September 4, 2013, the Board of Directors – including Plaintiff – met in executive session prior to the Board's regularly-scheduled meeting. During the meeting, the President informed the Board that he would not allow the Martens e-mail to be discussed at any open meeting of the Association's Board of Directors because its contents were defamatory if false. In order to mitigate any potential liability to the Association arising out of the circulation of the Martens e-mail to the Board of Directors, the Board of Directors adopted a resolution disavowing any approval of or responsibility for the Martens e-mail and any of Plaintiff's e-mails maligning the Association's employees. With the sole exception of Plaintiff, the Board unanimously approved the resolution. Plaintiff made it clear that she did not approve of the President's handling of the Martens e-mail and demanded his resignation. (*See* Exhibit D to DSOF.)

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Following the executive session on September 4, 2013, the Board of Directors convened in open session. During the open session, a member of the Association attempted to address the matters raised in the Martens e-mail. Consistent with the Board's earlier resolution, the President refused to allow discussion of those matters during the Board meeting. After the President refused to allow the Board to discuss the Martens e-mail, Plaintiff began reading the Martens e-mail aloud to the members in attendance at the Board of Directors meeting. Because Plaintiff was out of order and refused to stop reading the Martens e-mail, the President adjourned the Board of Directors meeting and all of the Directors except Plaintiff left. Plaintiff continued to read the Martens e-mail aloud after the meeting adjourned. (*See id.*)

C. The Decision to Screen Plaintiff from Executive Sessions.

On September 11, 2013, the Association's general counsel sent Plaintiff a letter informing Plaintiff that her conduct during the open portion of the September 4, 2013 Board of Directors meeting violated her duties of confidentiality and loyalty to the Association, and informing Plaintiff of his recommendation that the Association screen Plaintiff from future executive sessions. (*See* Exhibit A to DSOF, at Exh. 8.) Plaintiff responded to the letter in writing, insisting that her conduct was completely appropriate and consistent with her obligations as a Board member. (*See id.*, at Exh. 9.) After receiving Plaintiff's response, the Board of Directors accepted the recommendation of the Association's counsel that Plaintiff should be screened from future executive sessions for the remainder of her term, which ended in February 2014. (*See* Exhibit D to DSOF.)

The Association employees identified in the Martens e-mail complained to the President that Plaintiff's conduct was creating a hostile work environment for them. The employees eventually retained separate legal counsel, who sent a letter to Plaintiff demanding that she stop defaming the Association's employees. The Association incurred substantial attorneys' fees and costs in addressing Plaintiff's conduct during the September 4, 2013 Board of Directors meeting. (*See id.*)

After Plaintiff was elected to a second term in 2014, the Board of Directors, through counsel, offered to allow Plaintiff to participate in executive sessions if she would agree to maintain as confidential all information that was discussed during executive sessions. Plaintiff refused, and continues to refuse. (*See id*.) On January 15, 2015, Plaintiff appeared for a deposition in this case and stated under oath that if allowed to participate in executive sessions she would disclose at open session any information she learned that, in her opinion, should be discussed in open session and not executive session. (*See* Exhibit A to DSOF at pp. 86-86.) As a result, the Association has continued screening Plaintiff from executive sessions and will do so until Plaintiff's current term ends in February 2017.

II. EQUITY FAVORS DENYING PLAINTIFF'S APPLICATION FOR A PRELIMINARY INJUNCTION

A preliminary injunction is an extraordinary remedy that may only be awarded upon a clear showing that Plaintiff is entitled to such relief. *See, e.g., Flexible Lifeline Sys., Inc. v. Precision Lift, Inc.*, 654 F.3d 989, 996-97 (9th Cir. 2011) (citing *Winter v. NRDC*, 555 U.S. 7, 22, 129 S. Ct. 365 (2008)). Plaintiff "is obligated to establish four traditional equitable criteria: 1) A strong likelihood that [s]he will succeed at trial on the merits; 2) The possibility of irreparable injury to h[er] not remediable by damages if the requested relief is not granted; 3) A balance of hardships favors h[er]self; and 4) Public policy favors the injunction." *Shoen v. Shoen*, 167 Ariz. 58, 63 (App. 1990). Preliminary injunctions are primarily issued to preserve the status quo. Mandatory preliminary injunctions, such as the one Plaintiff is seeking in this case, are particularly disfavored in the law, and should be denied unless the facts and law clearly favor the moving party. *See, e.g., Transwestern Pipeline Co. v. 17.19 Acres of Property Located in Maricopa County*, 550 F.3d 770, 776 (9th Cir. 2008). Plaintiff cannot meet her burden in this case.

A. Plaintiff's Unclean Hands Preclude Equitable Relief.

As an initial matter, before Plaintiff can be entitled to the extraordinary equitable remedy of a preliminary injunction, she must demonstrate that she herself "is free from fault; that h[er] own hands are clean." *Gibson v. Duncan*, 17 Ariz. 329, 332 (1915). Here, Plaintiff

freely admits that she disregarded the advice of the Association's general counsel, the direction of the President, and the consensus reached by a majority of her fellow Board members that the Martens e-mail should not be shared with the community and discussed at an open meeting of the Board of Directors. She did so with the knowledge that the employees named in the Martens e-mail denied its allegations, and that by circulating the Martens e-mail she could be exposing the Association to claims by those employees. She did so because she believed the allegations of Ms. Martens over the denials of Mr. Warrell and Ms. Laird, and because she believed that she was entitled to have the Martens e-mail circulated as vindication for the incident described in that e-mail, which involved the public outing in 2011 of "ethically questionable" conduct of Plaintiff and two other Board members. (*See* Exhibit A to DSOF, at Exh. 5 & 9. Plaintiff disregarded her duties of loyalty and confidentiality to the Association in favor of putting her own interests first. Equity does not lie with such conduct.

B. Plaintiff Is Unlikely to Succeed on the Merits of Her Claims.

Plaintiff's Application for Preliminary Injunction advances no new arguments and no new evidence beyond that which she presented in her Motion for Summary Judgment to Restore Plaintiff's Right to Participate in Executive Sessions (filed 12/12/14), which this Court denied. (*See* Minute Entry filed 2/25/15.) Plaintiff argues that the Association lacks the authority to screen Plaintiff's access to confidential and sensitive information of the Association, and that the screening is arbitrary, capricious, and unreasonable *per se* because it "has no time limit." (Plaintiff's Application for Preliminary Injunction, filed 4/29/15, at p. 5, l. 14.) These are the exact same grounds that Plaintiff advanced as the basis for her ill-fated Motion for Summary Judgment. (*See* Plaintiff's Motion for Summary Judgment at pp. 6-7 & 9.) These grounds are not sufficient to carry Plaintiff's burden – she must show that the facts and the law clearly entitle her to relief. They do not. (*See* Defendant's Opposition to Plaintiff's Motion for Summary Judgment to Restore Plaintiff's Right to Participate in Executive Sessions, filed 1/30/15, at pp. 9-12.)

For example, Plaintiff cites Arizona statutes as well as case law from other jurisdictions for the proposition that a community association or other non-profit may not remove a board member without putting the matter to a vote of its members. *See* A.R.S. §§ 33-1813(A)(2) (providing for removal of a member of the board of directors through a vote held at a special meeting); 10-3808 (providing for removal of a director of a nonprofit corporation); and cases from New York and Delaware cited in Plaintiff's Application at p. 5, ll. 7-9. Plaintiff's reliance on these authorities is misplaced, because the Association has not removed Plaintiff from her position as a Board member or interfered in any way with her ability to carry out her duties as a Board member. Instead, by screening Plaintiff from executive sessions, the Board of Directors has enabled Plaintiff to continue her service as a Board member without exposing the Association to liability arising out of Plaintiff's inappropriate handling of confidential and sensitive Association business. Contrary to Plaintiff's arguments, neither she nor any other member of the Association has an unfettered right to receive and disclose as she sees fit confidential and sensitive business information of the Association. (*See* Expert Affidavit of Scott B. Carpenter, 1/28/15, attached as Exhibit E to DSOF.) Information that falls within A.R.S. § 33-1805(B)[1] expressly is protected against disclosure. Further, Arizona law expressly authorizes an association's board of

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[1] Under A.R.S. § 33-1805(B), records relating to any of the following matters may be withheld from disclosure:

1. Privileged communication between an attorney for the association and the association.
2. Pending litigation.
3. Meeting minutes or other records of a session of a board meeting that is not required to be open to all members pursuant to section 33-1804.
4. Personal, health or financial records of an individual member of the association, an individual employee of the association or an individual employee of a contractor for the association, including records of the association directly related to the personal, health or financial information about an individual member of the association, an individual employee of the association or an individual employee of a contractor for the association.
5. Records relating to the job performance of, compensation of, health records of or specific complaints against an individual employee of the association or an individual employee of a contractor of the association who works under the direction of the association.

directors to meet in a closed or executive session for the purpose of discussing such information without publicly disclosing it. *See* A.R.S. § 33-1804(A). Plaintiff's argument that the Association lacks authority to prevent her from accessing and disclosing such information as she sees fit is controverted by the plain language of A.R.S. §§ 33-1804 and -1805.

Similarly, Plaintiff argues that, by screening Plaintiff from executive sessions, the Association has imposed a "sanction" that is "arbitrary and capricious on its face because it has no time limit and is therefore unreasonable per se." (Plaintiff's Application for Preliminary Injunction at p. 5, ll. 13-14.) The Association acknowledges that its Board of Directors has an obligation to act reasonably in the exercise of its powers. *See Tierra Ranchos Homeowners Ass'n v. Kitchukov*, 216 Ariz. 195, ¶ 25 (App. 2007); *see also* Exhibit E to DSOF. A board's exercise of its authority is "arbitrary and capricious" if it indulges in "unreasoning action, without consideration and in disregard for facts and circumstances." *Maricopa Cnty. Sheriff's Office v. Maricopa Cnty. Emp. Merit Sys. Comm'n*, 211 Ariz. 219, ¶ 17 (2005) (internal quotation and citation omitted). The evidence here demonstrates that the decision of the Board of Directors to screen Plaintiff from executive sessions was both reasoned and reasonable.

As for the decision to continue screening Plaintiff upon her election for a second term in 2014, the Board of Directors offered to allow Plaintiff to attend executive sessions if she would agree in writing to preserve the confidentiality of the matters discussed, but Plaintiff refused. At her deposition, Plaintiff affirmed under oath that she will publicly disclose any matter discussed in executive session that she does not agree should be kept confidential. Continued screening of Plaintiff's access to confidential and sensitive information of the Association is reasonable under these circumstances.

C. Plaintiff Is Not Suffering Any Harm.

Screening Plaintiff's access to the confidential and sensitive information of the Association that is discussed during executive sessions is not causing any harm to Plaintiff.

Plaintiff has continued to serve as a member of the Association's Board of Directors. She receives notice of all Board meetings and a "board packet" prior to each regular meeting. She is given the opportunity to ask questions and discuss fully in open session all non-confidential matters of the Association. Plaintiff herself has characterized this restriction as "minor," and has stated that it enables her to be more effective in carrying out her obligation to the community as an elected member of the Board of Directors. (*See* Exhibit A to DSOF, at Exh. 11.) Considering that she was re-elected for a second term after the screening began, Plaintiff's assessment that she is actually more effective as a screened member appears to be shared by the other members of the community. There is no evidence that Plaintiff is suffering any harm as a result of the screening, let alone irreparable harm.

D. Public Policy and the Balance of Hardships Weigh in Favor of Denying Plaintiff's Application for a Preliminary Injunction.

Public policy, as embodied in A.R.S. §§ 33-1804(A) & -1805(B), expressly favors protecting confidential and sensitive information against unauthorized disclosure. Because Plaintiff repeatedly has violated this statute during her service on the Board, and because she has stated – under oath – that she will not hesitate to do so again, the only way that the Association can prevent Plaintiff from disclosing such information is to ensure that she does not have access to it. Aside from screening, the only alternative available to the Association would be to undertake the expense of a special meeting to actually remove Plaintiff from the Board. The Association has already gone down that path and incurred that expense once, only to have Plaintiff successfully run for office the following year. Term limits prohibit Plaintiff from running for a third term, as long as she is allowed to complete her current term. Thus, the Association has employed screening as the least restrictive means of ensuring its interests in protecting the confidential and sensitive information of the Association against disclosure, while balancing Plaintiff's right as a member of the Association to serve on the Board of Directors.

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Conversely, compelling the Association to grant Plaintiff access to confidential and sensitive information of the Association under these circumstances would expose the Association to a substantial risk of irreparable harm. Once information protected under A.R.S. §§ 33-1804 and -1805 is disclosed, it cannot be "undisclosed;" the Association must instead deal with the ramifications of the disclosure, often at considerable expense to the Association.

Both public policy and the balance of the hardships weigh in favor of denying Plaintiff the extraordinary equitable remedy of a preliminary injunction.

III. CONCLUSION

For all the foregoing reasons, the Association respectfully requests that the Court deny Plaintiff's Application for Preliminary Injunction.

RESPECTFULLY SUBMITTED this 12th day of May, 2015.

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