A STUDY OF PROBLEMS IN THE CONDOMINIUM OWNER-DEVELOPER RELATIONSHIP

STUDY COMMITTEE

OFFICE OF CONSUMER PROTECTION

Walter T. Yamashiro, Director
Mitsuo Takayama, Chief Investigator
Gordon Uechi, Staff Attorney

OFFICE OF THE LEGISLATIVE REFERENCE BUREAU

Samuel B. K. Chang, Director
Stephanie M. Chang, Researcher
Nicholas B. Waite, Researcher

REAL ESTATE COMMISSION

Mary V. Savio, Vice Chairperson
Yukio Higuchi, Executive Secretary
John W. Reilly, Educational Consultant

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FOREWORD

This study of the condominium owner-developer relationship in Hawaii is presented by the Office of Consumer Protection, Office of the Legislative Reference Bureau, and the Real Estate Commission in response to Senate Resolution 439, Senate Draft 1, adopted during the 1976 legislative session.

This report presents the findings, analysis, and recommendations of the joint study committee following research, public hearings, and extensive discussion.

The report contains suggestions for legislative action, including a functional reorganization of the Horizontal Property Regimes Law.

WALTER T. YAMASHIRO
Director
Office of Consumer Protection

SAMUEL B. K. CHANG
Director
Office of the Legislative
Reference Bureau

AH KAU YOUNG
Chairperson
Real Estate Commission

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INTRODUCTION

In recent years, the number of condominium projects registered, developed, and sold in Hawaii has increased markedly to meet the rising demand for housing from both owner-occupants and investors. This remarkable growth, coupled with economic conditions reflected in the housing market at large and Hawaii's scarcity of land, suggest that the condominium may be destined to become Hawaii's basic housing unit of the future.

Originally enacted in 1961, Hawaii's Horizontal Property Regimes Law became a model for early condominium legislation in many jurisdictions. The law serves its purpose well, providing a technical legal framework within which rapid condominium development has proceeded in an efficient and orderly manner.

With this rapid increase in the number of condominium owners and a recently troubled economy has come an increase in consumer-type complaints arising from condominium owner-developer relationships. Such complaints have motivated legislative action, and the legislative sessions of 1975 and 1976 resulted in several amendments to the Horizontal Property Regimes Law of the consumer protection variety. During the 1976 session, in addition to the concern responsible for such amendments, concern arose regarding the organic effect of such amendments on the Horizontal Property Regimes Law itself. The law had been initially designed to regulate the creation and development of condominiums, and with the growing attention to condominium consumer matters, it was felt that the amendatory legislation surely to follow would encumber the technical operation of the law as it was originally intended.

On the basis of the foregoing it was suggested, as reflected in Standing Committee Report No. 605-76, that a review of reported condominium consumer problems be conducted, in conjunction with an inquiry into the possibility of formulating a code or horizontal property regimes law which separated the consumer protection provisions from those originally intended to govern creation and development of condominium projects. Senate Resolution 439, Senate Draft 1, and this study were the consequent result.

CHAPTER I

AN OVERVIEW OF THE STUDY

OBJECTIVES OF THE STUDY

The basic objectives of this study were:

(1) To determine what problems have been reported in the condominium owner-developer relationship.

(2) To determine whether such problems are amenable to solution by legislative action.

(3) To formulate a proposed condominium code or horizontal property regimes law, including suggested new legislation where appropriate, which functionally separates consumer protection provisions from those concerning creation and development of condominium projects.

LEGISLATIVE REQUEST

The specific request of S.R. 439, S.D. 1 (appears in its entirety as Appendix A) is as follows:

> *BE IT RESOLVED by the Senate of the Eighth Legislature of the State of Hawaii, Regular Session of 1976, that the Office of Consumer Protection, the Legislative Reference Bureau and the Real Estate Commission are requested to jointly study problems reported in the condominium, owner-developer relationship, to formulate a proposed condominium code in the same vein as the Residential Landlord-Tenant Code, designed to clearly define the legal relationships and establish methods for efficient and equitable resolution of disputes, and to report their findings and recommended legislation to the Legislature twenty days prior to the convening of the Regular Session of 1977;...*

Further guidance is provided by Standing Committee Report No. 605-76 (appears in its entirety as Appendix B), which states in part as follows:

> *As stated in the Resolution, condominiums may be destined to become the basic housing unit of the future. Although Hawaii has enacted relatively advanced laws regarding condominiums, the volume*

of consumer-type complaints arising from developer-owner relationships are steadily increasing and each year, the legislature considers additional legislation in a piece-meal attempt to alleviate these situations.

While the legislature is in accord with the intent of these measures, it has questioned their effect on existing law regarding horizontal property regimes, contained in Chapter 514, Hawaii Revised Statutes.

This concern was explicitly expressed on the Senate floor, this session, by the Vice-Chairman of your Committee on Judiciary as the Senate took final action on four amendments to the Horizontal Property Regimes Act as follows:

> *"This Act...was originally intended to be a highly technical, legal vehicle for placing certain lands in the horizontal property regimes. It is becoming through our actions... a consumer protection section of the law. Anyone trying to use it in its technical sense will have extreme difficulty...we will need to review this whole matter (and) the consumer protection aspects should be put into a separate code or chapter so that the initial intent of the law can still be accomplished."*

Your Committee on Judiciary, as stated in Standing Committee Report No. 605-76, has also recommended further study in this area:

> *"Your Committee is cognizant of the many problems arising in condominium living here in this State and is sympathetic to the needs of the condominium owner. Your Committee strongly recommends that the Real Estate Commission hold at least one public hearing not less than three months prior to the opening of the regular session of the legislature for the purpose of providing to the board of directors of the association of apartment owners and the individual apartment owners an opportunity to testify with regard to legislation recommended by them or the Commission as part of its function. This hearing shall be publicly announced by the Commission two weeks in advance thereof."*

Your Committee on Consumer Protection finds that the intent and purpose of the above-mentioned recommendations can be accomplished through the means proposed in S.R. No. 439.

LEGISLATIVE HISTORY

In 1961 Hawaii became the first state to adopt a Horizontal Property Regimes Law, Act 180, which was modeled after the condominium law of Puerto Rico. The stated purpose of the act was to establish the legal basis of condominiums as real estate entities, and provide a means of registration of condominium projects. It was divided into four parts. Part 1 defined terms applicable to horizontal property regimes, and set forth the substantive law relative to ownership of condominiums. Part 2 established recordation requirements for deeds, plans, and other documents evidencing creation of a condominium project. Part 3 provided some basic rules for internal administration of a condominium project, and Part 4 formalized regulation by the Real Estate Commission of condominium project creation and development.

In 1963 the Horizontal Property Regimes Law was enlarged by Act 101 to provide a more detailed means for the internal administration of a condominium project, and further defined the rights and obligations of apartment owners. These amendments were provisions recommended by the FHA Model Act, with modifications suggested by the New York Legislature. Division of the law into four parts was eliminated at that time.

Similar additions and amendments, Act 8 of 1964, Acts 190 and 212 of 1965, Act 244 of 1967, Act 16 of 1972, and Act 112 of 1973, pertaining mainly to creation, development and sale of condominium projects, were made to the Horizontal Property Regimes Law between 1964 and 1973.

In 1975 the Hawaii Legislature began to enact amendments to the Horizontal Property Regimes Law (Act 132) specifically designed to resolve problems between consumers and developers, and further consumer protection measures were added in 1976 (Acts 214, 215, 216, and 239). Because these measures were designed to address consumer problems, it soon became apparent that they did not readily fit within the 15-year old framework established originally to regulate the creation and development of condominium projects. Consequently, these measures were engrafted upon the old provisions, or inserted between them at the most plausible point.

SCOPE AND ORGANIZATION OF THE STUDY

The problems addressed by this study were selected from a series of public hearings held by the study committee[1] throughout the State, correspondence in connection therewith, the complaint files of the Office of Consumer Protection and Real Estate Commission, and written testimony submitted to legislative committees during the 1976 legislative session. The study committee hearings were held on June 26, 1976 at the State Capitol Auditorium in Honolulu (43 persons attended, of which 9 testified), on June 28 at the State Building in Lihue, Kauai (7 persons attended, of which 4 testified), on June 29 at the Kahului Library on Maui (27 persons attended, of which 5 testified), and on June 30 at Yano Hall in Kona (11 persons attended, of which 3 testified). A list of witnesses, and their status as owner, manager, or developer appears as Appendix C.

Consideration was limited, by the specifications of the resolution, to problems encountered in the developer-owner relationship, and insofar as possible, attention was focused on those problems potentially significant to the largest number of condominium owners and developers. The conclusions reached in this study were based on research, analysis, and lengthy discussions at study committee meetings, all of which were attended by representatives from each of the three agencies, and held at least weekly from May through November, 1976.

The study report is divided into five groups of problems: chapter 2 examines developer control, chapter 3 mixed uses, chapter 4 disclosure and consumer education, chapter 5 warranties, and chapter 6 consumer remedies. Within each chapter the problems are stated, possible approaches analyzed, and the study committee's recommendations set forth. A summary of these recommendations appears in chapter 9.

A proposed reorganization of the Horizontal Property Regimes Law is presented in chapter 7, which responds to the request for functional separation of consumer protection provisions from those pertaining to creation and development of condominium projects.

Finally, chapter 8 briefly examines the question of application of new condominium legislation to existing projects, and the input problem, which although not directly

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[1]*The panel at each hearing was composed of representatives from each of the three agencies. Chairpersonship of the hearings was rotated.*

within the scope of this study, are believed by the study committee to be of sufficient importance to warrant legislative scrutiny.

SUMMARY OF FINDINGS AND CONCLUSIONS

The study committee was directed by the Resolution to ascertain what problems have been reported in the condominium owner-developer relationship. In addition to examining its files and testimony from previous legislative hearings, the committee held a series of well-advertised public hearings throughout the State. The input taken and evidence compiled, while revealing the need for change or innovation in certain general areas, were composed mainly of isolated individual complaints or problems within a single project and did not reflect any pattern of prevalent or repeated major problems or abuse in the condominium community as a whole. In the judgment of the study committee, this does not warrant changes in the Horizontal Property Regimes Law which would significantly affect the legal and financial relationships of all condominium owners and developers in Hawaii.

Most of the problems presented to the committee, refined and analyzed by research and discussion, are treated by this report, and in certain cases proposals for legislation are recommended. These recommendations are summarized in chapter 9 and follow three general themes: making the government of condominium projects more democratic, increasing avenues of self-help for private resolution of owner-developer problems, and more extensive consumer education and disclosure. In the latter area, the committee also recommends the development and distribution of a standard consumer information sheet to each prospective purchaser, a sample of which is included in chapter 4 for purposes of illustration.

The committee recommends that the Horizontal Property Regimes Law be reorganized to separate the purchaser protection and governance provisions from those relating to creation and development of condominium projects. A proposed reorganization is submitted in chapter 7 of this study, which in the judgment of the committee more clearly defines the legal relationships and presents in a more orderly manner the methods for efficient and equitable resolution of disputes.

CHAPTER 2

DEVELOPER CONTROL PROBLEMS

This chapter examines problems reported by condominium owners when the developer retains some degree of control after responsibility for the project's affairs has officially passed to the owners' association. They can arise in connection with the allocation of votes to units, the method employed to elect the board of directors, and the vote required to amend the declaration and by-laws. Also examined are problems in connection with developer control of the board of directors by proxies, transfer of government of the project from developer to owners, composition and meetings of the board of directors, and election and removal of directors.

I. UNIT OWNERS

A. ALLOCATION OF VOTES TO UNITS

Reported problems arise where a developer retains a block of units or combines with investor blocks to achieve a majority of votes and control of the board of directors. In this situation, the owner of a single unit is virtually powerless under the present system where votes are allocated by percentage of common interest.

Possible Approaches to the Problem:

1. One vote per owner, regardless of the number of units or percentage of common interest owned in the project.

   Analysis: This approach provides each owner with an equal voice in the governance of the condominium project, and prevents a single owner or small group of multiple unit owners from controlling the board of directors simply because they own more units than others. This approach, however, raises possible constitutional problems by depriving owners with larger interests in the project of their proportionate power to determine the governance of their property. A further drawback is possible discouragement to investment by the many persons who own more than one unit.

2. By par value of unit. This approach allocates votes according to the original sales price of each unit.

   Analysis: While this approach might, at the outset, reflect each owner's interest at the time of purchase, over time it very probably would decreasingly reflect the owner's true property interest, due to external market factors, such as views and changing character of neighborhood structures, which might variably affect the value of each interest.

3. By market value of unit. This approach allocates votes according to the present market value of each unit. Those units with higher values would be accorded a larger percentage of voting power.

   Analysis: While this approach would most closely approximate each owner's actual property interest, practical considerations render it virtually unworkable. Reappraisal at regular intervals throughout the life of the project would be required, which would be prohibitively expensive.

4. By percentage of common interest. This is the present method of allocating votes. Section 514-11(6), *Hawaii Revised Statutes*. Percentage of common interest is determined primarily by the square footage of each unit.

   Analysis: This approach allows proportionate representation of the interest of each owner throughout the life of the project. As the power to vote is based on a property interest in the first instance, this approach equates voting power with the size of the property interest. While the voting power of a single unit owner is limited under this approach to his percentage of common interest, allocation of voting power greater than his property interest could lead to control by owners representing a minority of the property interest in a project.

Committee Recommendation:

The present system of allocating votes by percentage of common interest appears to most adequately protect the property interest of each owner in a practical, fair, and equitable manner.

B. VOTING FOR BOARD OF DIRECTORS

Problems reportedly arise when a group of owners is unable to cast enough votes to elect a member to the board of directors and is thus unrepresented. This reportedly can occur when a developer and/or investor block maintains a majority of the votes, and owner-occupants are unable to elect a representative to the board.

Possible Approaches to the Problem:

1. Cumulative voting. This system of voting is a common practice of corporate entities to facilitate minority representation on the board of directors. Each condominium owner would have a vote equal to his percentage of common interest multiplied by the number of directors to be elected at the meeting, and he could cast it all for one candidate, or divide it among several. The candidates receiving the highest number of votes would be elected. For example, if 3 directors are to be elected, and 6 candidates run, the top 3 vote-getters would be elected.

   The formula for determining the minimum number of votes a minority would need to elect one director is:

$$\frac{\text{number of votes X number of positions}}{\text{number of positions}} + 1$$

   For example, if there are 100 votes in the association, and 5 directors to be elected (500 possible votes under cumulative voting), a minority would need $\frac{100 \text{ X } 5}{5} + 1$, or 101 votes to assure election of one member of the board. Thus, if owners of 21 per cent of the common interest were to place all of their votes on one candidate, because they each have 5 votes under cumulative voting their candidate would have 105 votes, enough to ensure his election. His election would be assured even if the majority controlled all of the other 79 per cent of common interest, or 395 votes. If the majority distributed their votes among their 5 candidates equally, they would each receive only 79 votes, and the minority candidate would win first place handily. The best the majority could do would

be to cast 106 votes for three of their candidates, and 77 for a fourth. In this case, the minority candidate would place fourth, but still be elected.

Analysis: While this approach assures minority representation on the board in the above example, it does not so operate in every case. There must be, for cumulative voting to achieve this result, the proper combination of directors to be elected, and percentage of vote controlled by a minority. For example, in the previous illustration where 21 per cent of the vote could assure election of one director if 5 were to be elected, it could not if only 3 were to be elected. The minority would have 63 votes, and the majority 237. The majority could cast 79 votes for each of its three candidates, and win all three seats. On the other hand, if the minority controlled 26 per cent of the vote and there were three directors to be elected, the minority would have 78 votes and the majority 222. The majority could cast 79 votes for two of its candidates, but only 64 for the third, and the minority candidate would place third and be elected.

The fewer the number of directors to be elected, then, the greater the voting percentage a minority would need to elect one director using cumulative voting. As the number of directors to be elected each time is established by bylaw and varies from association to association, as well as the percentage of minority interest, it cannot and must not be said that cumulative voting would ensure minority representation on the board in every case. It can be said, however, that where the correct circumstances exist, cumulative voting could ensure minority representation in associations where none presently exists using the status quo method of voting. If cumulative voting was required, in these associations it would increase minority participation in the affairs of the project, and make the board of directors more democratic. For those associations where the correct circumstances do not exist for cumulative voting, the status quo method of voting would be retained.

2. Allocation of seats by type of owner. This approach would require that the board of

directors be comprised of owner-occupants, investor-owners, developer interests, and commercial owners in the proportion of each group's ownership of the condominium project.

Analysis: While this approach ensures proportionate representation on the board by type of unit ownership, practical considerations seem to render this proposal impractical, because of the constant change of ownership make-up which characterizes most projects.

3. Allocate a fixed number of directors to owner-occupants. This approach requires that a fixed number of seats on the board of directors be filled by owner-occupants.

Analysis: While this approach would ensure representation of owner-occupants, particularly in projects where the developer and/or investor block controls a majority of the votes, it may be overly broad and impractical in those condominium projects owned primarily or exclusively by investor-owners, or where there are insufficient owner-occupants willing to serve on the board to meet a statutory requirement.

Committee Recommendation:

Amend the Hawaii Revised Statutes to require cumulative voting for the board of directors only, with an adequate description of the process, thereby providing an opportunity for representation of cohesive minority interests on the board of directors where the correct circumstances exist.

C. NUMBER OF VOTES REQUIRED TO AMEND THE BYLAWS

The original declaration and bylaws of a condominium project are usually drawn up by the developer's attorney. These documents can reportedly be written in a manner which is advantageous to the developer, should he continue to participate in the project after the association is formed. Presently, under section 514-20(11), *Hawaii Revised Statutes*, the vote of 75 per cent of the condominium owners is required to amend the bylaws. Apathy of condominium owners and/or retainage of a 25 per cent voting interest by the developer and/or his allies reportedly can inhibit

amendment of the bylaws when a majority of owners wish to do so.

Possible Approaches to the Problem:

1. Reduce the number required to 67 per cent.

   Analysis: Lowering the statutory requirement to 67 per cent would make amendment of the bylaws easier for a majority of owners. A lower requirement would also require the developer, were he so inclined, to retain or amass a 33 per cent voting interest rather than 25 per cent to block such amendment.

2. Retain the number required at 75 per cent.

   Analysis: Conversely, a lower statutory requirement would make it easier for developers to enact amendments, that is, they would need only 67 per cent of the votes, say, in combination with investors, instead of 75 per cent to control. Lowering the statutory requirement would mean that fewer owners could determine the rules by which all the owners would have to abide.

Committee Recommendation:

A review of other jurisdictions reveals a fairly even split between the 67 per cent and 75 per cent requirement. As there are merits and drawbacks to both approaches, the decision appears to be one of policy. The committee makes no recommendation on this issue.

II. CONTROL OF BOARD BY PROXIES

Reported problems arise where the developer perpetuates his control of the condominium project after the association is formed by retaining units and obtaining proxies from absentee owners. This is apparently accomplished by including with the meeting announcement a proxy form which designates the president of the board as proxy. This is accomplished at association expense, while individual owners wishing to solicit proxies must do so at their own expense by separate mailings. Pursuant to section 514-20(17), *Hawaii Revised Statutes*, a standard proxy form authorized by the association may be sent with the notice of association meetings.

Possible Approaches to the Problem:

1. Require by statute a standard proxy form to be used by all associations which contains space to designate a proxy other than the management or board, with space to also limit the proxy to particular matters.

   Analysis: This approach sets minimum specifications for a proxy form to be used by associations, and would inform owners of their option not to place their proxy with the board or management unless they desire to do so, allowing them the opportunity to designate any individual as their proxy. Owners would also be accorded the opportunity, particularly if designating the board or management as their proxy, to limit such proxy to particular matters.

2. Allow a solicitation of proxies at association expense by any owner who can show a proper association purpose, and written support of not less than 10 per cent of the other owners, to be sent with the board or management's solicitation.

   Analysis: This approach enables any owner or group of owners to solicit proxies from absentee owners in support of their position on any proper matter to be before an association meeting. The 10 per cent and proper purpose requirements would help eliminate frivolous solicitations and wasted association expense.

Committee Recommendation:

The committee recommends that the Hawaii Revised Statutes be amended to include both of the foregoing proposals. Owners would have more access to the decision-making process, and use of the proxy would be less a tool of management and more a method of perpetuating a democratic vote on association matters.

III. TRANSFER OF GOVERNMENT OF PROJECT FROM DEVELOPER TO OWNERS

A. CONTRACTS

Problems reportedly arise when the developer, prior to formation of the association, or after formation if he retains control, makes contracts on behalf of the condominium project or developer-controlled association with others for operation

and maintenance of the condominium, i.e. management contracts, contracts for goods and services such as laundry, security, and gardening. These contracts may be for a lengthy period of time with incompetent, unreliable, or overpriced contractors, may be sweetheart agreements with a subsidiary, relative, or friend of the developer at inflated prices, or may simply be unreasonable or unnecessary under the circumstances or as circumstances evolve.

Possible Approaches to the Problem:

1. Require bids to be taken on all contracts or purchases over a certain minimum amount.

   Analysis: While this approach would enable a comparison to be made of market prices for goods and services contracted for by association, practical considerations make this unmanageable, as it would probably be difficult to get bids for certain contracts or jobs, and the actual mechanics of soliciting, receiving, and letting bids could prove cumbersome, costly, and time-consuming, especially in the case of essential services.

2. Require disclosure of the status of a contractor or seller as an employee, agent, director or officer of the developer, managing agent, any member of the board, or its subsidiary.

   Analysis: This approach gives notice to owners and prospective purchasers upon inquiry regarding the status of contractors or sellers involved with a condominium project. While this disclosure may discourage unreasonable contracts, it may not necessarily prevent them. At a minimum, however, the owner or purchaser has the opportunity to obtain such information.

3. Require newsletters at specified intervals from the board detailing contracts entered into on behalf of the association.

   Analysis: While this approach gives notice to owners of such contracts, it would not actually prevent unreasonable contracts, since the newsletter would be sent after the contract was finalized. Owners currently

have access to the books to obtain receipt and expenditure records if desired pursuant to section 514-21, *Hawaii Revised Statutes*.

4. Limit the length of all contracts entered into by the association or the developer on behalf of the project prior to formation of the association to a period of 5 years.

   Analysis: Section 514-20.5, *Hawaii Revised Statutes*, currently limits certain management contracts to one year. The five-year approach, applied to all contracts, would prevent excessive length yet allow sufficient time for recovery of investment costs by contractors where the contract involves initial expenditure of capital, as with a laundromat.

5. Where at least 51 per cent of the common interest is owned by parties other than the developer, including purchasers under agreements of sale, provide the association an option to rescind contracts entered into by the developer on behalf of the project prior to formation of the association. A majority vote among the nondeveloper interest would be required for rescission, and this right would be available even if the developer failed to include it in the particular contract.

   Analysis: By granting a unilateral right of rescission this approach would allow certain associations to free themselves from unreasonable contracts entered into by the developer on behalf of the project prior to the association's formation. This would not only provide a deterrent to the formation of such contracts, but free certain associations from unreasonable agreements not of their own making.

Committee Recommendation:

Amend the Hawaii Revised Statutes to provide that all contracts entered into by the association or the developer on behalf of the project be limited to 5 years, that the status of a contractor as an employee, agent, director, or officer of the developer, managing agent, member of the board or their subsidiaries be disclosed on the face of

each contract, and that certain associations be accorded the right of rescission as described in item 5 above.

B. TIME OF TRANSFER OF GOVERNMENT

Confusion reportedly arises concerning the time when the association should be formed, and government of the project thereby transferred. Section 514-20(12), *Hawaii Revised Statutes*, provides that the first meeting of the association shall be held not later than 180 days after a certificate of occupancy for the project has been issued by the appropriate county agency. As there are apparently several types of certificates of occupancy, which may vary as to time of issue, a firm benchmark for the operation of this requirement is reportedly sometimes difficult to establish.

Possible Approach to the Problem:

1. Require the first meeting to be held 180 days after conveyance of the first apartment is recorded.

   Analysis: This approach provides a benchmark which is firmly a matter of public record, the date of which cannot be subject to dispute.

Committee Recommendation:

Amend the Hawaii Revised Statutes to require the first meeting of the association to be held not later than 180 days following the first recordation of an apartment conveyance in a condominium project.

IV. COMPOSITION OF THE BOARD OF DIRECTORS

A. NUMBER OF DIRECTORS

The number of directors for a condominium project is specified by the developer in the original bylaws. Reportedly, a problem may occur if the bylaws do not require election of enough board members to adequately represent the owners.

Possible Approaches to the Problem:

1. Specify that condominium projects with 50 or more units be required to have a minimum of 6 members on their board of directors.

   Analysis: Presently the law requires a minimum of 3 members on the board of directors. Section 514-20(1), *Hawaii Revised Statutes*. While increasing this minimum for larger projects would ensure greater representation, as a mandatory requirement it might cause problems in those projects composed primarily of absentee owners, or where it is difficult to obtain participation.

2. Retain the statutory minimum of 3 directors.

   Analysis: This leaves the matter to each individual project, and allows each project to tailor the size of the board to its needs and participation level. Larger projects may increase the size of the board if they desire by amending the bylaws.

Committee Recommendation:

Retain the present statutory minimum of 3 directors.

B. PROPERTY MANAGER ON THE BOARD

Currently, section 514-20(15), *Hawaii Revised Statutes*, prohibits the resident manager of a condominium project from serving on the board of directors. Perhaps more serious problems might arise, however, when the property manager, or officers, directors, or agents of a property management firm or its subsidiary which has a contract with the project sit on the board. As the firm is under contract to the association and responsible for operation of the project, such a director would have an inherent conflict of interest which, because of the magnitude of the conflict, could not simply be handled by abstention from voting.

Possible Approaches to the Problem:

1. Require disclosure of any relationship with the property manager by candidates for the board.

Analysis: While this would inform the voting members of the association of the candidate's status, it would not always prevent the creation of such an absolute conflict of interest.

2. Preclude property managers, officers, directors, and agents of property management firms and their subsidiaries, but not employees of same, from serving on the board.

   Analysis: This approach would eliminate the potential conflict of interest. The ban would not extend to mere employees of the property manager or subsidiary, however, as many employees of large property management firms do not necessarily represent their employer's interest.

Committee Recommendation:

Amend the Hawaii Revised Statutes to preclude property managers, officers, directors, and agents of property management firms and their subsidiaries, but not employees, from serving on the board of directors. Require disclosure by an employee of his employment relationship with the property manager if a candidate for the board of directors.

C. TERM OF DIRECTORS

Problems reportedly arise because some directors serve virtually in perpetuity, becoming entrenched and unresponsive, and if they are linked to the developer or manager, or have contracts with the association, their presence perpetuates conflict of interest and prohibits injection of fresh thinking and increased owner participation.

Possible Approaches to the Problem:

1. Establish a maximum term or number of terms that a director may serve on the board.

   Analysis: While this would ensure new membership on the board, and avoid perpetuation of the above example, as a practical matter it is often difficult to get people who are willing to serve on the board, and in some cases the same few people giving time and service account for the successful operation of a project.

Committee Recommendation:

Pursuant to current law, section 514-20(1), Hawaii Revised Statutes, at least one-third of the board must be re-elected annually. To limit participation on the board, while possibly beneficial in those cases where abuse exists, would work a hardship on those associations where only a few persons are willing to serve on the board. No further requirement should be imposed.

V. ELECTION OF BOARD

A. QUALIFICATIONS OF CANDIDATES

In some cases the owners know nothing about the individuals running for the board of directors--qualifications, potential conflicts of interest, positions on issues. Reportedly, in this situation a developer or manager, if they have the votes, can unobtrusively place their candidates on the board.

Possible Approaches to the Problem:

1. Require a biographical sketch, statement of qualifications, disclosure of conflicts, and positions on issues to be filed in advance of the meeting and mailed with the notice of the meeting and proxies.

   Analysis: While desirable in theory, this approach would be difficult to implement in practice. In addition to the added time and expense of preparation, such a practice would necessarily preclude nominations from the floor at the meetings, of which owners voting by proxy would be unapprised.

Committee Recommendation:

This is a problem which associations should resolve themselves. The foregoing recommendations on proxy forms and disclosure of relationship to the property manager provide additional safeguards, while the current practice of nominating from the floor is undisturbed.

VI. REMOVAL OF DIRECTORS

A. UNAUTHORIZED REMOVAL

Reportedly some bylaws drawn by the developer authorize removal of a director by vote of the board. This presents the possibility that a director could be removed arbitrarily, probably enabling the board to proceed without a replacement until the next annual meeting of the association.

Possible Approach to the Problem:

1. Allow removal of a director only by vote of the association at a properly called association meeting.

   Analysis: This approach would eliminate the possibility of arbitrary removal of a director by the board. In the case of misconduct on the part of a director, a special association meeting could be held to consider removal pursuant to the association bylaws, and, if appropriate, to hold a special election to replace the director in question.

Committee Recommendation:

Amend the Hawaii Revised Statutes to provide that members of the board of directors may be removed only by the association at a properly called association meeting.

VII. BOARD OF DIRECTORS MEETINGS

Section 514-20(16), *Hawaii Revised Statutes*, provides that the board of directors shall meet at least once per year. Reportedly, bylaws in some cases require no more than the statutory minimum, and should the developer be in such a position, he has the opportunity to run the board for a year in the background without input from or disclosure to the association. Whether this abuse exists or not, some association members reportedly complain that they have no opportunity to present their problems to the board.

Possible Approaches to the Problem:

1. Require the directors to have a certain number of meetings per year which are open to all owners.

Analysis: While this would allow association members to be present when decisions affecting the condominium project are made, matters are often discussed at board meetings which should not be disclosed to the entire association, such as delinquencies, personal problems of owners, and allegations which are not substantiated.

2. Require the directors to have a certain number of meetings per year, and allow members of the association, by request, to attend, present problems and complaints, and remain present for discussion of the matter presented.

   Analysis: This approach enables owners to have greater communication with their board and gives opportunity for the airing of problems, while at the same time protects the privacy of those owners whose personal matters are being discussed.

Committee Recommendation:

Amend the Hawaii Revised Statutes to require the board of directors to meet at least twice per year, and to allow appearances of association members before the board by request to present problems, air complaints, and remain present for discussion of those matters.

CHAPTER 3

MIXED USE PROBLEMS

This chapter examines special problems reported by condominium owners living in projects devoted to both residential and commercial use, which include noise, allocation of maintenance fees, insurance costs, metering of utility lines, and repair or replacement of common areas.

I. MIXED RESIDENTIAL AND HOTEL USE

Problems reportedly occur when individuals purchase in a project which is intended for residential use, and subsequently a portion of the project is converted by the developer for use as a hotel.

Possible Approaches to the Problem:

1. Provide adequate disclosure and warning to prospective purchasers that a hotel operation is legally permitted and a future possibility.

   Analysis: Section 1 of Act 239 of 1976 currently requires developers to provide to prospective purchasers a statement of the proposed number of apartments to be used for residential or hotel use in a mixed use project, and projected hotel use must also be disclosed in the public report under restrictions on unit uses. While this information may not attract the attention of the prospective purchaser, it is available to him, and if all documents are proper and the required disclosures are made, the developer should not be required to do more.

Committee Recommendation:

Disclosure is required under current law. The effectiveness of such disclosure can be enhanced by further consumer education on the contents of condominium documents, and differences between residential and mixed use projects. Such education is recommended in chapter 4 of this report.

II. MAINTENANCE FEES

Reported problems involve the allocation of maintenance fees assessed in a mixed residential-commercial project. Residential owners in some cases complain that they pay and commercial areas receive a disproportionate amount of such moneys for maintenance, security, waste disposal, utilities, and the like.

Possible Approaches to the Problem:

1. Assess commercial areas maintenance costs proportionate to the amount expended in their areas.

   Analysis: While this approach would seem to reach an equitable result, the complexity of determining such an assessment and the variables existing between projects make detailed, workable legislation applicable to all projects virtually impossible.

2. Require commercial areas to be responsible for maintenance of their own areas.

   Analysis: This approach would require a separate governing organization for commercial areas solely to determine contribution rates for each owner, not to mention separation of this maintenance from the association budget, which would entail the same complexities and variables noted in approach #1.

Committee Recommendation:

Section 514-10, HRS, provides that in mixed use projects charges and distributions may be apportioned in any fair and equitable manner. Because the mixture of use in condominium projects varies from project to project, it would be virtually impossible to further detail legislative requirements applicable to all situations. This matter must thus be resolved by individual associations and private legal action.

III. INSURANCE COSTS

Insurance costs to residential owners are sometimes increased due to the presence of commercial enterprises in the condominium project. Reportedly, mixed use projects are given a mercantile rating, which often results in higher insurance costs throughout the project.

Possible Approaches to the Problem:

1. Provide adequate disclosure that the presence of commercial areas in mixed use projects may have an effect on insurance rates.

   Analysis: This approach would apprise purchasers of possible higher insurance costs in mixed use projects, allowing them to consider this factor when deciding to purchase.

2. Allocate increased insurance costs experienced by residential owners to the commercial use responsible for the increase.

   Analysis: While residential owners would pay only that portion of the insurance cost allocable to residential use, it would in fact penalize the commercial owners for engaging in commercial use. Further, insurance rates are reportedly determined by a variety of factors in addition to use, and an accurate allocation would be difficult, if not impossible, to obtain.

Committee Recommendation:

Provide adequate disclosure that mixed commercial and residential use in a project may result in increased insurance costs to residential owners. Rather than a specific warning for each mixed use project, which might place those projects at a competitive disadvantage, the disclosure should be provided through consumer education on the possible differences between residential and mixed use projects. Consumer education of this type is recommended in chapter 4 of this report.

IV. METERING OF COMMERCIAL SPACE UTILITY LINES

Commercial and residential utility use in some mixed use projects is recorded on the same meter. Problems might arise when total utility costs are assessed in such a manner that residential owners pay an amount disproportionate to their actual use, which in effect subsidizes commercial areas.

Possible Approaches to the Problem:

1. Require that commercial areas be metered separately and/or individually.

Analysis: While this would assure that residential owners would not subsidize commercial enterprises, in some projects overall higher rates would result, as additional commercial use of utilities reportedly entitles the project to bulk utility rates which reduce the overall cost to individual owners.

2. Assess commercial enterprises for their actual proportionate share of utility costs based on usage.

   Analysis: While this would prevent subsidies by residential owners, an accurate assessment of commercial utility use is very difficult to obtain when metered together with residential use. Further, a combination of commercial and residential use on one utility meter could be detrimental in the future, should utility companies alter their rate schedules to encourage lower consumption.

Committee Recommendation:

Decisions regarding utility metering should be left to the individual associations, due to the foregoing analysis and the variety of considerations involved in each individual project.

V. REPAIR AND REPLACEMENT OF COMMON AREAS

Problems reportedly arise in determining who should pay for the repair and replacement of those common areas which deteriorate at a faster rate due to heavier use by patrons of commercial areas.

Possible Approaches to the Problem:

1. Require repair and replacement by owners of those commercial areas responsible for faster deterioration.

2. Assess all or part of repair and replacement cost to commercial areas responsible for faster deterioration.

3. Require contribution by commercial areas at a fixed rate to the association's general reserve for repairs and replacement.

4. Require contribution by commercial areas at a fixed rate to a special reserve for repairs and replacement of those common areas used by the commercial enterprises.

Analysis: While each of these approaches would relieve residential owners of these costs, such allocations and rate determinations must be based on the difficult assumption either that residential owners never make use of these areas, or that the extent of such use can be determined. Further, allocation of costs among commercial owners would require data difficult to obtain, and any formula developed for one project would be difficult to apply to all mixed use projects.

Committee Recommendation:

In mixed use projects, exactly who uses common areas is very difficult to determine, and allocation of the cost of their repair is thus very difficult. Because of the variable factors involved in each project, no solution by legislation is feasible, and resolution should be left to the individual associations.

VI. NOISE

Resident owners in mixed use projects reportedly complain of increased noise attributable to commercial areas.

Possible Approaches to the Problem:

1. Provide adequate disclosure that mixed use projects may experience additional noise due to the presence of commercial areas.

2. Seek relief through noise ordinances. There are currently certain requirements regarding noise, and private remedies at law are available.

Committee Recommendation:

Provide disclosure of possible increased noise in mixed use projects due to the presence of commercial areas through consumer education on the possible differences between residential and mixed use projects.

CHAPTER 4

DISCLOSURE AND CONSUMER EDUCATION

This chapter examines problems of awareness and comprehension on the part of condominium owners and buyers, and consumer education.

I. LACK OF AWARENESS AND COMPREHENSION

It appears that a prevailing attitude among many consumers is that the law does not afford condominium purchasers adequate protection, that lengthy condominium documents cannot be understood because of complex legal language, and that many purchasers are unaware of their rights and obligations as condominium owners. It is also reported that in actual practice many condominium purchasers do not read and are not familiar with the public report, declaration, by-laws, house rules and protective provisions of the Horizontal Property Regimes Law, nor do they seek assistance in understanding these documents. Furthermore, many condominium owners living in a condominium for the first time are apparently unaware of particular facets of condominium life which differ from single family home ownership or apartment living, oftentimes resulting in dissatisfaction and unfulfilled expectations.

Possible Approaches to the Problem:

1. Require the Real Estate Commission to prepare, the developer to distribute, and the purchaser to receipt for a standard consumer information sheet containing a general description of condominium living, a summary of the major documents involved in a condominium purchase, and the highlights of the Horizontal Property Regimes Law. This information sheet would be issued to encourage the consumer to inquire further into his condominium purchase prior to legally binding himself to a contract. It would be printed on distinctively colored paper, be distributed to the prospective purchaser at the same time, but detached from, the public report, and be receipted for on the same receipt form as the public report. For purposes of illustration, a draft of a consumer information sheet appears at the end of this chapter, following the committee recommendation.

Analysis: This approach would provide to the condominium buyer in digested form the most important information needed to make an informed condominium purchase. For the first-time condominium buyer, the information sheet would serve not only as a reference document, but fulfill an educational purpose as well, and at the very least hopefully provide the impetus for further inquiry regarding the documents, rights, duties, obligations, and statutory provisions involved in condominium living.

2. Request the Real Estate Commission to develop a comprehensive pamphlet, written in laymen's terms, which outlines and describes the particulars of condominium life, including a checklist of pertinent items to consider in making a purchase, and a review of the various documents in that connection. In addition to making this pamphlet available to both prospective purchasers and the general public, the Real Estate Commission should also develop a long-range program to educate the public on condominium living, utilizing all forms of media distribution, including newspapers, seminars, radio and television.

   Analysis: This approach provides a long-range program to educate the public and condominium owners about the particulars of condominium life and its legal basis, benefits and obligations. In the long run this should foster increased awareness on the part of all concerned in the condominium community, which could greatly reduce misunderstanding, dissatisfaction, and would help to alleviate many of the problems reported in this study.

Committee Recommendation:

Request the Real Estate Commission to develop and distribute the comprehensive pamphlet outlined in approach #2 above, and to design and implement the described long-range program to educate the public on condominium living. Funding could be provided by legislative appropriation, or the Real Estate Commission could be requested to fund these recommendations by grant from the Real Estate Education Fund.

As an immediate measure to foster consumer education and increased disclosure, amend the Hawaii Revised Statutes to require the Real Estate Commission to develop, and developers to distribute to prospective purchasers the standard consumer information sheet described in approach #1 above, a draft of which follows for purposes of illustration.

CONDOMINIUM CONSUMER INFORMATION SHEET

IMPORTANT - READ THIS INFORMATION SHEET BEFORE BUYING.

THIS INFORMATION SHEET IS NOT AN APPROVAL OR DISAPPROVAL OF THIS CONDOMINIUM PROJECT NOR DOES IT REPLACE THE REAL ESTATE COMMISSION'S PUBLIC REPORT WHICH MUST BE GIVEN TO ALL PURCHASERS AND SHOULD BE READ IN ITS ENTIRETY BEFORE YOU SIGN THE PURCHASE CONTRACT.

This information sheet is designed to provide you with a general overview of condominium ownership to make you more aware of your rights and obligations as a condominium owner.

It is by no means a complete discussion of the subject and should not be treated as a substitute for sound professional advice before you sign a legally binding contract.

GENERAL. Modern condominium ownership has filled a need for apartment ownership that has all the benefits and protections of typical single family home ownership. In its simplest terms, condominium ownership is a situation in which many people each own a fraction of a piece of property, not as tenants in common of the whole, but each one owning his own individual portion of the building himself plus a certain proportionate interest in the common areas. Each individual portion may be mortgaged, taxed, sold or otherwise transferred in ownership, separately and independently of all other units in the structure. Each condominium owner has exclusive ownership of his individual unit, but must, nevertheless, comply with the requirements of certain legal documents such as the Declaration, Bylaws and House Rules set up for the protection and comfort of all condominium owners. As you can imagine, with many separate owner-occupants living together, there have to be rules and regulations to insure harmony and agreement among the many people living so close to each other.

You may find these definitions helpful in understanding the concept of condominium ownership:

COMMON ELEMENTS. Parts of the property which are necessary or convenient to the existence, maintenance and safety of the condominium, or are normally in common use by all of the condominium residents. All condominium owners have an undivided ownership interest in the common elements. Maintenance of the common elements is paid for by the condominium association, and each owner must pay a monthly maintenance assessment, prorated according to his individual common interest. Typical examples of common elements are elevators, load bearing walls, hallways, swimming pool, and the like.

COMMON INTEREST. The percentage of undivided ownership in the common elements belonging to each condominium apartment, as established in the condominium declaration. The applicable percentage is usually computed as the ratio of the square footage of a particular apartment to the total square footage of the building, or as the ratio of the apartment's purchase price to the total sales price of all of the apartment units. The ratio is expressed as a percentage, such as 1.47 per cent or .0147. The percentage of common interest is used in determining an owner's interest in the common elements, the amount an owner will be assessed for maintenance and operation of the common properties, the real estate tax levied against an individual unit and the number of votes an owner has in the condominium association.

LIMITED COMMON ELEMENTS. That special class of common elements in a condominium reserved for the use of a certain apartment(s) to the exclusion of other apartments. This would include assigned parking stalls, storage units, or certain common areas and facilities.

Any amendment of the declaration affecting the limited common elements requires the unanimous consent of all those to whom the use is reserved. Additions to or alterations of a limited common element require prior approval of the Board of Directors on behalf of the Association of Owners.

MAINTENANCE FEE. An amount of money each owner must pay, usually monthly, to cover his share of the costs of operating and maintaining the common areas. This amount can increase or decrease depending on the types of services provided (for example, 24-hour guard service), and the effect of inflation in the economy (utility rate increase).

It is important that you examine and understand the various rules regulating the use of your condominium BEFORE you bind yourself to a contract to purchase. Let us briefly outline the contents of the major documents involved in a condominium transaction. You may examine these documents by notifying your sales agent.

DECLARATION. The formal document which the developer records to create a condominium under the Horizontal Property Act. The declaration must contain a precise description of the land, whether leased or fee; description of the materials used to construct the building; description of the common elements and limited common elements; percentage of undivided interest in the common elements, which is the basis for voting, maintenance and assessments; use of the building and apartment (residential, hotel, commercial, etc. or combination of uses) including restrictive uses such as number of occupants, and other technical requirements. Many of the important provisions of the Declaration are summarized in the Horizontal Property Regimes Public Report you must receive and receipt for before signing the purchase contract.

BYLAWS. A most important set of regulations for the management and administration of the condominium apartment and common elements. It sets forth the method of electing a Board of Directors from among the apartment owners and the method for calling meetings and adopting decisions. Bylaws may also provide for the authority to hire a managing agent to run the day-to-day operations. Other provisions of the bylaws as required by law include the method of assessing common expenses for the operation, maintenance and repair of common elements and collection of same (especially important where the condominium has mixed residential and commercial use); restrictions on the use of apartments (such as whether pets are permitted) and common elements in addition to those set forth in the declaration. The bylaws can only be amended or modified with a 75 per cent vote of the apartment owners.

HOUSE RULES. The administrative rules and regulations governing the details of the everyday operation and use of the common elements such as use of trash chutes, swimming pools, etc.

A thorough reading of the above-described documents will point out the central role played by the Board of Directors in managing and controlling the use and enjoyment of your condominium. Those elected to the Board of Directors are usually knowledgeable and practical people but are not necessarily active practitioners in the field of real estate. Nor do they often have the time and facilities to devote to the daily problems of the apartment building. Consequently, it usually is more practical for the association of owners to employ competent managing agents who have personnel trained in building operation and administration. The Board establishes policy for the operation of the building and the management attempts to implement these policies.

Because of the many responsibilities charged to the Board, you should take an interest in the selection of a qualified Board. Among other things, the Board you elect has the power to modify and adopt the house rules, to decide whether you can make certain alterations and additions to your apartment, and to determine additional charges and assessments against owners for common expenses as provided in the bylaws. Whether you agree with these charges or not, common maintenance expenses properly assessed must be paid and any unpaid share constitutes a lien on the apartment which could result in a forced sale of your apartment.

You should also recognize the importance of actively participating in the government of the condominium through the Association of Owners. If you have complaints about the management and operation of the building, you should contact the managing agent and the Board. Your voting power in the association is determined by the amount of your "common interest". If you are unable to attend a certain meeting, it may be necessary for you to send a proxy so that there is a quorum to conduct the meeting. Be sure the proxy will vote in accordance with your wishes. Remember that if 75 per cent of the apartment owners desire to amend the bylaws this can be done even though you personally object. This is part of the concept of living together.

The Horizontal Property Act contains many provisions which affect the ownership and use of your condominium. Among the highlights of this law are:

1. Association of Owners.

- The first meeting of the association of apartment owners shall be held within 180 days of the date of the county's certificate of occupancy. Note that your financial obligations and common expenses may be triggered by this date, even though the project may still require minor work to be fully completed.

- Notices of association meetings must be sent to each association member at least 14 days prior to the meetings.

- Proxies of meetings are only valid for the meeting for which the proxy is sent.

- The association meetings must be held at the condominium project, or elsewhere within the State as determined by the Board.

- The purchaser of an apartment under an agreement of sale shall have all the rights of an apartment owner, including the right to vote. The seller, however, may retain the right to vote on matters substantially affecting his security interest in the apartment.

- No apartment owner can do any work which might jeopardize the safety or value of the property nor add any material structure without the unanimous consent of all other apartment owners. However, additions to and alterations of an apartment or a limited common element can be made by an owner provided he has the consent of the Board and such percentage of owners as may be required by the declaration or bylaws.

2. Board of Directors.

- All members of the board of directors must be owners and no director shall vote on any issue in which he has a conflict. A resident manager may not serve on the board.

- A vendee under an agreement of sale can serve on the board.

- The board has access to each apartment during reasonable hours as may be necessary for the operation of the property or for making emergency repairs.

- The board must meet at least once a year.

- The board must provide insurance to cover the common elements and, whether or not part of the common elements, all exterior and interior walls, exterior glass, floors, and ceilings against damage by fire or other hazard. You should still check with your insurance agent and procure all necessary insurance to protect your own personal property and to protect yourself against general liability. You should also inquire about protection for any additions, alterations and improvements in your own unit, as these may not be protected by the building policy.

3. Developer.

- If the developer acts as the first managing agent the term of contract shall not exceed one year and it may be terminated by either the developer or the association on 60 days notice.

- A developer must provide in writing to each prospective unit purchaser a breakdown of the annual maintenance fees and a description of all warranties for the individual

apartments and the common elements. Also, the developer must give notice to the owners 90 days prior to expiration of the normal one-year warranty period and set forth specific methods to seek remedies for defects, if any. The warranties given may vary from condominium to condominium. If you are not satisfied with the warranty offered, you are legally entitled to bargain and negotiate for the warranty that you want.

4. Owner.

- Each owner must comply with the by-laws, the house rules and with the covenants, conditions and restrictions set forth in the declaration.

- Condominium owners can transfer their parking stalls among owners by following the prescribed rules.

- Allows the apportionment of charges and distribution of common profits in a mixed use project containing apartments for both residential and commercial use, in any fair and equitable manner as set forth in the declaration.

- If there are material changes in the building plans requiring county approval, purchaser can obtain refund of monies paid unless purchaser consents in writing to the changes or 90 days has elapsed since he has accepted the apartment in writing or he has first occupied the apartment.

SPECIAL NOTICE. If you have any questions concerning the purchase of the condominium or the material contained in this document or the public report, you should discuss these questions with your sales agent prior to signing the contract. If you are relying on a specific statement or representation, it is in your best interest to reduce the statement to writing. REMEMBER, DO NOT RELY ON ORAL PROMISES OR AGREEMENTS. ALWAYS HAVE THEM IN WRITING.

The Horizontal Property Act (Chapter 514, *Hawaii Revised Statutes*) provides remedies for you in the event you feel you have been wronged. Copies of this law are available at the Department of Regulatory Agencies at a nominal cost.

NOTE: THIS INFORMATION SHEET IS BASED ON THE PROVISIONS OF THE HORIZONTAL PROPERTY ACT AS OF _____, 19__.

CHAPTER 5
WARRANTY PROBLEMS

This chapter examines problems encountered by condominium owners when a developer fails to repair warranty defects, or because of insolvency or bankruptcy is financially unable to repair them. Also examined is the question of existence and coverage of express warranties, their initiation, duration, and parties to whom they run.

I. FAILURE TO REPAIR

Complaints have been reported that developers fail in certain instances to honor their warranties by refusing or neglecting to repair or correct structural, appliance and fixture defects after proper notification by the owner. The developer may promise to comply and fail to do so, or refer the owner to the contractor, who in turn may refuse to make repairs because of a dispute with the developer. In either case, the repairs are not made, or the owner may suffer long delays in getting his problems resolved.

Possible Approaches to the Problem:

1. Require developers to repair or correct warranty defects within a prescribed period of time following proper notification.

   Analysis: While this would clarify some violations, as a practical matter it probably would not provide a workable solution where a developer chooses to ignore warranty obligations. Failure to repair in most cases constitutes a breach of warranty, and making it a statutory violation as well in all probability would not decrease or deter future failures. Further, developers probably refer warranty work to their contractors, who most likely wait until enough repair work accrues in one project to justify cost-efficient deployment of crews to correct all reported defects at one time. Placing a statutory time limit on repairs would, for those developers who honor their warranty obligations, probably increase the number of call-back trips by the contractor, increase costs, and decrease efficiency. Currently section 514-26.5, *Hawaii Revised Statutes*, requires the

developer to notify the owner ninety days before the warranty expires, and to set forth specific methods which owners may pursue in seeking remedies for defects, if any, prior to expiration of the warranty. Although a specific time limit on repairs is not prescribed, section 514-26.5 does establish a date from which a reasonable time can be calculated, while allowing the contractor the opportunity to correct defects in the most cost-efficient manner.

2. Require the developer to retain, in an interest-bearing escrow account or fund (interest accruing to developer), an amount equal to a certain percentage of the purchase price or construction cost of each condominium unit. Should the developer fail to repair a warranty defect within a certain (reasonable) period of time after notification by the owner, the latter would be entitled to withdraw this certain amount, i.e. a proportionate share of the escrow fund based on the purchase price or construction cost of his unit, to initiate repair of the warranted defect. Should the cost of such repair exceed the amount of the escrow fund to which the owner is entitled, the owner could at that point initiate private legal action.

   Analysis: This approach would make available to each owner a certain sum of money to initiate warranty repairs where the developer fails to comply with the terms of his warranty. While legal action may be necessary in some cases to fully correct the problem, the owner under this approach has an avenue short of legal action to afford at least partial relief within a reasonable time.

   On the other hand, such a provision may impose cash flow restrictions on developers, perhaps sufficiently detrimental to small developers to create a competitive disadvantage. Further, the cost of such a retainage would in all probability be passed on to the consumer in the form of higher condominium prices throughout the market. The approach may also be overly broad, as it no doubt would include developers with whom owners have experienced no problems concerning warranty repairs. Consideration must also be given to immunizing the escrowed funds from the creditors of the developer.

A determination must be made of the method to be used in allocating to each owner his share or potential share of the escrowed moneys. If each owner is entitled to withdraw only that amount proportionate to the purchase price or construction cost of his unit, the situation may arise where there are few claims and little use of the escrowed money, but one owner has a large claim in excess of his allocated share. An unfair result would occur if this owner is limited only to his proportionate share and is forced to sue the developer for the balance, while the escrowed moneys remaining in the account continue to draw interest for the developer. However, if this owner is allocated more than his proportionate share, an equally unfair result would occur if similar claims depleted the amount available and other legitimate claims went unsatisfied. Equity might better be served if each owner with a valid claim were entitled to withdraw his proportionate share, then when all warranties or the statute of limitations expire, any amount remaining could be divided proportionately to satisfy claims which exceeded the original proportionate share.

In addition, certain technical and procedural matters must be resolved, such as determining whether the escrow accounts should be opened with private financial institutions or a government agency, establishing procedures and identifying individuals or agencies to process claims, certify legitimate warranty items, determine when each account may be drawn upon, disburse moneys and keep records.

3. Require the developer, prior to conveying any unit, to post a bond in an amount equal to a percentage of the construction cost of the project to serve as surety against any failure on his part to repair warranty defects.

Analysis: This approach makes available to the owners a solvent third party to whom they can turn for satisfaction should the developer fail to fulfill his warranty obligations. In so doing, uniformity of expectation and predictability of satisfaction would, at least arguably, be substantially increased. Section 4-104(b) of the October 1, 1976 draft of the Uniform Condominium Act, circulated for discussion by the National Conference of Commissioners on Uniform State

Laws[1] requires the developer, before conveying any unit, to post a surety bond with the unit owners association in the sum of 5 per cent of the estimated construction cost of the condominium to remedy defects against which the developer is required to warrant.

On the other hand, in addition to the same cost, market, procedural and technical problems considered above in connection with the escrow approach, consideration must be given, particularly with small repairs, to the time and expense involved in filing claims. Also to be considered is the possibility that legal action may be required against bonding companies, which could possibly dispute the validity and repair cost of at least some claimed warranty defects.

4. Require assignment by the developer to the owners of all rights the developer may have under any warranty and/or performance bond furnished to him by the contractor.

   Analysis: Owners may encounter the same problems in obtaining warranty repairs by the contractor as were encountered with the developer. The problems referenced above concerning bonds would also remain the same. This approach would provide, however, a remedy for owners directly against the contractor, without having to deal with the developer as intermediary. Blanket assignments might produce conflict, however, among owners and the association over priorities and order of repair. Intra-association conflicts of this type may prove debilitating to any effort to establish a viable association during the formative years of the project.

5. Require all developers of condominium projects to be licensed by the Department of Regulatory Agencies. Failure to make warranty repairs within a reasonable time could be made a ground for revocation of a developer's license.

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[1] *The ideas and conclusions set forth in the draft, including drafts of proposed legislation, have not been passed upon by the Commission on Uniform State Laws, and do not necessarily reflect the views of the committee, staff, advisors, or commissioners.*

Analysis: This approach relies upon the deterrent effect of such a provision, but would protect only future condominium owners from disreputable developers who may, in fact, plan to develop no more projects. Unresolved would be the problems of owners who in fact face unrepaired warranty defects. In addition, as license revocation is a serious matter, rules and procedure would have to be carefully developed, accompanied by the hiring and training of administrative and investigative staff, all of which would require appropriation of additional public funds.

6. Provide for arbitration of warranty repair disputes within each project by a panel composed of representatives of the developer, owners, and an independent party.

   Analysis: While such an approach could possibly lead to amicable resolution of disputes regarding warranty repairs, in addition to its time and cost, it is unlikely that parties who reached the point of arbitration would accept the decision as legally binding, or agree to such arbitration if it were. The alternative of professional arbitration is reported to be prohibitively expensive, especially when small claims are involved.

7. Provide condominium owners with a statutory remedy whereby they can bring an action against the developer and/or contractor for failure to make warranty repairs, and if successful, to recover costs and reasonable attorney fees.

   Analysis: This approach would, at least in the case where the developer and/or contractor is solvent, afford to the condominium owner an avenue by which he could obtain complete relief. By allowing costs and reasonable attorney fees to the successful owner, such an approach would greatly reduce the reportedly high cost of such an action, which currently constitutes the main deterrent to bringing them. By according such relief only to successful owners, the measure should discourage frivolous lawsuits and insure the litigation of only bona fide warranty claims.

Committee Recommendation:

The possible approaches considered above involve potentially significant legal, financial, and economic ramifications for the condominium market and community in its entirety. While the study committee received a

number of warranty repair complaints, it is the judgment of the committee that the limited breadth of the sample received does not constitute a sufficient basis upon which to recommend action which may have such a widespread impact. Consequently, it is the recommendation of the committee that before legislative action is taken in this area, a determination be made of the actual extent and nature of warranty repair problems in the condominium community as a whole. In this connection, it is recommended in chapter 8 of this report that a specific mechanism for obtaining data and receiving complaints be established. It is further recommended that prior to enactment of a particular proposal, estimates of the potential legal, financial, and economic impact on the condominium market and community should be made with the assistance of those best qualified to make them.

With respect to the private remedy outlined in the final approach to this problem, such a provision is recommended in chapter 6 of this report.

II. INSOLVENCY OF DEVELOPER - INABILITY TO REPAIR

Complaints have been reported that following completion of a project and conveyance of some or all units to buyers, the developer has become insolvent or filed for bankruptcy, thereby rendering himself unable to make repairs pursuant to his warranty. Further, should the owner obtain a judgment for the cost of warranty repairs, satisfaction of such a judgment against an insolvent or bankrupt developer is highly improbable.

Possible Approaches to the Problem:

1. Require the developer to retain, in an interest-bearing escrow account or fund (interest accruing to developer), an amount equal to a certain percentage of the purchase price or construction cost of each condominium unit. Should the developer be unable to repair a warranty defect within a certain (reasonable) period of time after notification by the owner because he is insolvent or has filed for bankruptcy, the owner would be entitled to withdraw this certain amount, i.e. a proportionate share of the escrow fund based on the purchase price or construction cost of his unit, to defray or partially defray the expense of making warranty repairs.

2. Require the developer, prior to conveying any unit, to post a bond in an amount equal to a percentage of the construction cost of the project, to serve as surety against inability on his part to repair warranty defects due to insolvency or bankruptcy.

3. Require assignment by the developer to the owners of all rights he may have under any warranty and/or performance bond furnished to him by the contractor.

Analysis: As these approaches are identical to approaches 2, 3, and 4 above for failure to repair, consideration must be given to all the factors discussed in connection with those approaches. In addition, it is necessary to consider the effect in each case that insolvency or bankruptcy would have on the funds or rights involved, particularly vis-a-vis the trustee in bankruptcy or creditors of the developer. Further, in considering the approaches to this problem, account must be given to the fact that the developer in this situation is both insolvent and virtually judgment-proof. Any recovery obtained will thus probably constitute the only amount recouped by the condominium owner, and he will have to bear the loss for the balance. The complexities and problems previously outlined for the approaches presented may thus appear less formidable in a context where the only alternative is probably no recovery whatsoever.

Committee Recommendation:

For the same reasons and considerations, the recommendations here are identical to those advanced for the previously discussed problem of failure to repair.

III. EXPRESS WARRANTIES

Act 239 of 1976 requires a developer to provide to each prospective initial purchaser an abstract which contains a description of all warranties for the individual apartments and the common elements, including the date of initiation and expiration of any such warranties. The developer is also required by section 514-26.5, *Hawaii Revised Statutes*, (enacted in 1975), to give notice by certified mail at the appropriate time that the "normal one-year warranty period" will expire in ninety days, and set forth specific methods which apartment owners may pursue in seeking remedies for defects, if any, prior to expiration.

These are the only provisions of the Horizontal Property Regimes Law which address warranties, and as they were recently enacted, it is difficult at this point to determine their effectiveness or the connected problems which may occur or be occurring. There has, however, in the study of warranty problems in general been a great deal of concern and discussion in Hawaii as well as other jurisdictions regarding potential problems in connection with express warranties on condominium units, much of which is reflected in the following examination.

A. EXISTENCE AND COVERAGE OF EXPRESS WARRANTIES

At no point does the Horizontal Property Regimes Law actually require the developer to give a "normal one-year warranty", nor does it specify what such a warranty, if given, must cover, to whom it should run, when it should commence, and when it should terminate. Notwithstanding any theory of implied warranty, which would require a lawsuit for assertion, it appears that unless the developer in fact gives such a written warranty expressly covering certain items, under current law it is possible that he could give no express warranty whatsoever, or state such a warranty in such nebulous terms as to render it virtually meaningless. Although the current disclosure and notification provisions provide information to the consumer, they do not assure any minimum warranty standards upon which he can depend.

Possible Approaches to the Problem:

1. Maintain the status quo of disclosure to prospective purchasers and notification of expiration.

   Analysis: This approach provides the consumer with information sufficient to make an informed purchase decision on the warranty issue. If the prospective purchaser is not satisfied with the warranty, its length or coverage, he is free to negotiate with the seller for a longer or more comprehensive warranty. Further, the overall effect of requiring all developers to give a written express warranty to specified dimensions may be an increase in the cost of condominiums.

2. Require the developer to give each unit a written express warranty for a certain period of time, to cover certain expressly designated

items. For example, the October 1, 1976 Draft of the Uniform Condominium Act of the National Conference of Commissioners on Uniform State Laws provides at section 4-104(a) that the developer shall warrant against structural defects, which are defined as defects in components constituting any unit or common element which reduce the stability or safety of the structure below commonly accepted standards, or which restrict the normal intended use of all or part of the structure, and which require repair or replace-- ment.

Analysis: This approach would assure each purchaser of a condominium that certain items are under warranty by the developer. In addition to providing protection to the buyer, this approach would establish certain minimum standards for the industry, create uniformity of expectation, and heighten consumer awareness regarding their rights, as with appliance and automobile warranties. On the other hand, as previously indicated, the overall effect of requiring all developers to give a written express warranty of specified dimensions may be an increase in the cost of condominiums.

B. INITIATION AND DURATION OF WARRANTIES

Problems may occur because the warranty given by a developer commences on the date a project is ready for occupancy, and not the date the unit is actually conveyed to, or occupied by, a condo-minium owner. Thus, it is possible, especially in a slow market, that a consumer could purchase a unit upon which the warranty has expired or has a brief time to run.

Possible Approaches to the Problem:

1. Maintain the status quo of disclosure to prospective purchasers and notification of expiration.

Analysis: While this approach does not provide for a basic minimum and establish uniformity of expectation on the part of condominium buyers, it does provide the consumer with the information necessary to make an informed purchase decision insofar as length of warranty is concerned, and establishes

the opportunity for purchasers to bargain for a longer warranty on a unit by unit basis.

2. Require that if a warranty is given, it must run for a certain period following the date a unit is conveyed. The October 1, 1976 Draft of the Uniform Condominium Act requires the warranty to run for one year from the date each unit is first conveyed to a bona fide purchaser.

Analysis: This approach would create uniformity of expectation for purchasers of new condominiums insofar as the length of warranty is concerned. In addition, the date of conveyance provides a clear benchmark from which to determine the expiration date of the warranty. Developers, however, reportedly receive a warranty from the contractor which runs from the date of completion of the project. If the warranty the developer gives the purchaser begins at a later date and runs beyond his warranty from the contractor, the developer would then be directly responsible for repairs which may have been occasioned by poor workmanship on the part of the contractor. It could be argued, however, that the developer has the ability to negotiate a warranty for potential additional periods with the contractor, and if he fails to protect himself it is the developer, and not the consumer, who should bear the loss.

C. TO WHOM THE WARRANTY RUNS

Regardless of when a warranty commences to run, there are situations where problems could arise in determining who can avail himself of its coverage. For example, if an owner-occupant sells his unit before the end of the warranty period, does the warranty extend to his successor? In the case of an investor-owner who never lives in the apartment, when does the warranty period commence? What if an apartment is used only for investment purposes, and is conveyed several times before a tenant actually lives in the unit?

Possible Approaches to the Problem:

1. Maintain the status quo of disclosure to prospective purchasers and notification of expiration.

Analysis: While uniform rules are not provided, the purchaser under this approach is provided with information regarding the limitations of the warranty offered, and can, if desired, negotiate the terms of his choice. On the other hand, the initial purchaser is not likely to be concerned about the warranty rights of those who succeed him, and thus has little motive to negotiate protection for them. Further, subsequent purchasers, although they probably don't expect to be covered by a warranty, are not protected by the disclosure rules and may not be aware of the warranty limitations that do exist.

2. Require the developer to warrant the unit for a specified period following conveyance to the first bona fide purchaser, regardless of whether the purchaser intends to live in the unit, or how many actual owners there are following the first conveyance. A successor to the original bona fide purchaser would thus have standing under the warranty during the warranty period.

   Analysis: This approach establishes uniform rules to govern most possible situations, including those stated above. In each case, the responsibility for discovering warranty defects and pursuing redress rests with the owner of the unit. The approach also holds the developer responsible on the warranty for a certain period, regardless of change of ownership of the apartment, which period is probably necessary for at least some defects to become apparent. However, in the case of multiple successive changes, problems may arise as to causation of alleged defects, i.e. the developer may claim that abuse by one of the tenants in the unit was really the cause of the damage.

Committee Recommendation:

As previously indicated, the warranty disclosure and notification provisions of the Horizontal Property Regimes Law were enacted so recently that it is not yet possible to clearly discern their effectiveness, or to establish any pattern of problems in this connection which require legislative resolution. Consequently it is the recommendation of the study committee that no legislative action be taken at this time, but that the operation of the disclosure and notification provisions

be monitored, and their effectiveness determined over a period of time. In this connection, it is recommended in chapter 8 of this report that a specific mechanism be established for obtaining data and receiving complaints.

CHAPTER 6
CONSUMER REMEDIES

This chapter examines problems encountered by condominium owners in obtaining legal redress for grievances in connection with the purchase and ownership of a condominium unit.

I. ABSENCE OF EFFECTIVE REMEDY

Complaints have been expressed by individual owners that there exists no rapid, economical, and effective means by which they may obtain legal relief against the developer or others for misrepresentation in connection with purchase of the unit, on warranty items, in connection with control or operation of the condominium project, or against any person for violation of the Horizontal Property Regimes Law, declaration, bylaws or house rules. Government agencies reportedly do not have the authority, staff, or budget to fully accommodate many such condominium cases, and thus the consumer is usually relegated to private legal action, which is reported to be prohibitively expensive for the average condominium owner.

Possible Approaches to the Problem:

1. Assign to a government agency the reponsibility for screening, investigating, and taking legal action if necessary on complaints filed by condominium owners.

   Analysis: This approach to be effective would require the appropriation of money for the hiring and training of administrative, investigative, and legal staff, with no assurance that it would be sufficient to efficiently accommodate a growing caseload and satisfy the majority of the consumer public. Additionally, because such a governmental service would be without charge, a certain amount of time and expense would necessarily be misallocated to frivolous claims and personality conflicts.

2. For actions concerning condominium warranty repairs, increase the jurisdictional limit of the small claims division of the district courts sufficiently to allow owners with relatively minor

complaints to obtain, where appropriate, direct, speedy, and personal relief.

Analysis: This approach is best suited to the frustrated owner seeking legal redress for a relatively minor warranty repair, who is presently deterred by the expense of the judicial process. The reported success of such a system in the landlord-tenant area, particularly with regard to security deposits, in providing judicial arbitration and fact finding is an encouraging precedent for the warranty repair area.

3. Provide a statutory remedy whereby a condominium owner may bring legal action for damages and/or injunctive relief against a developer, property manager, owners association, board of directors of the owners association, an individual director, or other person for misrepresentation in connection with the purchase of his apartment, or violation of consumer protection provisions of the Horizontal Property Regimes Law, declaration, bylaws, house rules, or the like, and if successful, recover costs and reasonable attorney fees.

   Analysis: This approach would provide condominium owners with an avenue by which they could obtain affordable judicial relief for most legitimate grievances or problems which might arise in connection with purchase and ownership of a condominium unit. By allowing the court to award costs and attorney fees if the owner is successful, the deterrent effect of the high cost of legal action would be greatly lessened. By according such relief only to successful owners, the measure would discourage frivolous lawsuits and insure that only bona fide claims are litigated. While court dockets are already crowded and the process may sometimes be lengthy, the provision for injunctive relief would afford to the condominium owner an opportunity, where appropriate, to obtain quick temporary relief.

Committee Recommendation:

Provide a statutory remedy whereby a condominium owner may bring legal action for damages and/or injunctive relief, and if successful, to recover costs and reasonable attorney fees. Amend the Hawaii Revised Statutes to increase the jurisdictional limit of the small claims division of district courts in cases involving condominium warranty repairs.

CHAPTER 7

PROPOSED REORGANIZATION OF THE HORIZONTAL PROPERTY REGIMES LAW

The proposed reorganization of the Horizontal Property Regimes Law which follows separates on a functional basis the purchaser protection and condominium governance provisions from those pertaining to creation and development of condominium projects. Equally, another objective is to restate the Horizontal Property Regimes Law, in the same vein as the Residential Landlord-Tenant Code, to more clearly define legal relationships and methods for efficient and equitable resolution of disputes.

For purposes of clarity and functional organization, this proposal, like the Residential Landlord-Tenant Code, is divided into several parts. The proposed reorganization retains all sections of the current Horizontal Property Regimes Law in their existing form, but reorders those sections and places them into one of the following five parts:

Part I: General Provisions and Definitions

Part II: Creation, Alteration, and Termination of Condominiums

Part III: Registration and Administration

Part IV: Protection of Purchasers

Part V: Condominium Management

This division, as well as the part headings, has as its basis the October 1, 1976 draft of the proposed Uniform Condominium Act, recently submitted for discussion by the National Conference of Commissioners on Uniform State Laws. In the judgment of the study committee the clarity, organization, and simplification which accompany division of the law into functional parts will be of great value in the future to the legislature and judiciary, as well as the consumer public.

Part I of the proposed reorganization includes general provisions and definitions pertinent to the entire chapter, while Part II reflects the intention to bring together all those provisions of the current law relating to creation, alteration and termination of condominium projects.

Part III first separates and then combines, in functional order, those provisions of the current law pertaining to registration of condominium projects with, and administration of condominium development by the Real Estate Commission, including the duties, procedures, and powers of the latter.

Part IV assembles those provisions, some of which were recently enacted, directly concerned with protection of the consumer-purchaser from fraud, financial mismanagement, or faulty construction in connection with the purchase of a condominium unit. Included also are remedies available to the individual consumer in the instance of abuse or dissatisfaction.

Part V is devoted to the governance and management of condominium projects, including the rights, duties, liabilities, and obligations of individual owners and the owners association, procedure and governmental structure for operation and maintenance of the project, and avenues of recourse should the need arise.

The points at which proposals for legislation recommended by the study committee would be inserted are noted in the proposed reorganization. Existing section 514-20 would be amended, two new sections added to Part IV, and one to Part V.

HORIZONTAL PROPERTY REGIMES

New Section Numbering	Existing Section (Source)	Section Title
		PART I. GENERAL PROVISIONS AND DEFINITIONS
514-1	514-1	Title.
514-2	514-55	Chapter not exclusive.
514-3	514-2	Definitions.
514-4	514-4	Status of apartments.
514-5	514-5	Ownership of apartments.
514-6	514-23	Separate taxation.
		PART II. CREATION, ALTERATION, AND TERMINATION OF CONDOMINIUMS
514-11	514-11	Recordation and contents of declaration.
514-12	514-13	Copy of floor plans to be filed.
514-13	514-6	Common elements.
514-14	514-	Parking stalls. (Act 239 of 1976)

New Section Numbering	Existing Section (Source)	Section Title
514-15	514-10	Common profits and expenses.
514-16	514-9	Liens against apartments; removal from lien; effect of part payment.
514-17	514-12	Contents of deeds or leases of apartments.
514-18	514-16	Blanket mortgages and other blanket liens affecting an apartment at time of first conveyance or lease.
514-19	514-13.5	Merger of increments.
514-20	514-3	Horizontal property regimes.
514-21	514-17	Removal from provisions of this chapter.
514-22	514-18	Removal no bar to subsequent resubmission.

PART III. REGISTRATION AND ADMINISTRATION

514-31	514-29	Notification of intention.
514-32	514-30	Questionnaire and filing fee.
514-33	514-31	Inspection.
514-34	514-32	Inspection expenses.
514-35	514-33	Waiver of inspection.
514-36	514-34	Public reports and issuance fees.
514-37	514-35	Preliminary public report.
514-38	514-44	Request for public report or hearing by developer.
514-39	514-36	Filing with commission required.
514-40	514-15	Issuance of final reports prior to completion of construction.
514-41	514-42	Supplementary public report.
514-42	514-43	True copies of public report.
514-43	514-54	Automatic expiration of public reports.
514-44	514-51	Deposit of fees.
514-45	514-52	Supplementary regulations governing a horizontal property regime.
514-46	514-48	Investigatory powers.
514-47	514-49	Cease and desist orders.
514-48	514-50	Power to enjoin.
514-49	514-46	Penalties.
514-50	514-53	Limitation of action.

PART IV. PROTECTION OF PURCHASERS

514-60	514-	Disclosure requirements. (Act 239 of 1976)
514-61	514-41	Copy of public report to be given to prospective purchaser.
*514-62	None	*Standard consumer information sheet.*

Proposal for legislation recommended by the study committee.

New Section Numbering	Existing Section (Source)	Section Title
514-63	514-38	Enforceability of sales.
514-64	514-37	Changes in building plans.
514-65	514-40	Escrow requirement.
514-66	514-14	Financing construction.
514-67	514-45	Misleading statements and omissions.
514-68	514-47	Remedies; sales voidable when and by whom.
*514-69	None	*Remedies; action for damages or injunction.*
514-70	514-26.5	Warranty against structural and appliance defects; notice of expiration required.

PART V. CONDOMINIUM MANAGEMENT

514-80	514-19	By-laws.
**514-81	514-20	Content of by-laws.
514-82	514-28.5	Purchaser's right to vote.
514-83	514-20.5	Management contracts; developer and its affiliates.
*514-84	None	*Limitation on contracts; disclosure of status; right of rescission.*
514-85	514-21	Books of receipts and expenditures; availability for examination.
514-86	514-26	Insurance.
514-87	514-28	Personal application.
514-88	514-7	Compliance with covenants, by-laws and administrative provisions.
514-89	514-8	Certain work prohibited.
514-90	514-24	Priority of lien.
514-91	514-25	Joint and several liability of grantor and grantee for unpaid common expenses.
514-92	514-22	Waiver of use of common elements; abandonment of apartment; conveyance to board of directors.
514-93	514-27	Actions.
514-94	514-	Attorney's fees and expenses of enforcement. (Act 239 of 1976)

**Proposal for legislation recommended by the study committee.*

***This section would be amended by proposals for legislation recommended by the study committee: cumulative voting, standard proxy form, proxy solicitation, time of transfer of control, exclusion of property managers from board and disclosure by their employees, removal of directors by association, two meetings of board per year, and association members appearing at such meetings.*

CHAPTER 8
RELATED MATTERS

I. APPLICATION OF CONDOMINIUM LEGISLATION TO EXISTING ASSOCIATIONS

During the course of this study, a legal issue emerged for consideration by the study committee, which although not directly within the scope of the study's specifications, is believed by the committee to be of sufficient importance to warrant brief treatment.

When problems relating to governance of existing condominium associations are examined, and proposals for legislation considered as they are in this report, it is desirable in the committee's view that uniformity of expectation exists among consumers, developers, other interest groups and legislators with respect to the legal and constitutional limits within which the legislature will act.

It is well settled that the constitution, rules, and bylaws of an unincorporated association constitute a contract between members which the courts will enforce.[1] Article I, section 10, of the United States Constitution prohibits a state from passing a law impairing the obligations of existing contracts. The obligation of a contract is impaired by a statute which alters its terms by imposing new conditions or dispensing with existing conditions, or which adds new duties, releases or lessens any part of the contract obligation, or substantially defeats its end.[2]

Based on the foregoing, it therefore appears that while the legislature may enact laws applicable to the declaration and bylaws of condominium associations formed after the effective date of such laws, and require existing associations which voluntarily amend their bylaws or declarations in specific substantive areas to amend them in conformance with such laws, in general the legislature may not enact new laws which

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[1] *Martinez v. Parado, 35 H. 149 (1939); 6 Am Jur. 2d Associations and Clubs, sec. 8 (1964, Supp. 1976).*

[2] *16 Am Jur. 2d Constitutional Law, sec. 445 (1964, Supp. 1976).*

would require existing associations to conform their declarations or bylaws thereto. Such would probably constitute impairment of existing contracts, in this case, the declarations and bylaws of the respective associations.[3]

To minimize misunderstanding and achieve uniformity of expectation among interested parties, the study committee recommends that consumers, developers, and other interest groups be apprised in advance of the legal and constitutional limits within which the legislature must act in addressing problems within existing condominium associations.

II. THE PROBLEM OF INPUT

As noted elsewhere in this report, a major problem with a study of this nature is obtaining input of sufficient significance to warrant a recommendation for legislative action. This is particularly true in an area such as warranties, where legislation could have economic, financial, and legal significance for the entire condominium community.

In certain areas examined by this study, problems were noted and complaints received, but because they were few in number or localized, they could not be designated as prevalent for the condominium community as a whole. In those instances, particularly with warranties, the study committee recommended that more representative data be obtained before legislative action is taken.

Because of this problem, the study committee recommends that a method be developed to enable the legislature to obtain data and receive complaints from condominium owners at large over a certain period of time, such as one year. Insofar as it is familiar with the situation, the committee which conducted this study could be requested to develop a condominium owner complaint sheet, publicize its availability, make distribution on request through consumer groups, property managers, etc., and serve as a centralized collection agent.

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[3]*For a definite ruling, an official legal opinion should be requested from the Department of the Attorney General.*

When the complaint sheet is distributed, it should be emphasized that its purpose is to obtain input from the condominium community for the legislature, and not to service complaints or assist with individual problems. Confidentiality should also be emphasized, and provision made for receipt of complaint sheets, analysis, and investigation of the data received, and a report of results to the legislature.

CHAPTER 9

SUMMARY OF RECOMMENDATIONS

Page of Report

CHAPTER 4 - DISCLOSURE AND CONSUMER EDUCATION

18. Require the Real Estate Commission to prepare, the developer to distribute, and the purchaser to receipt for a standard condominium consumer information sheet containing a general description of condominium living, a summary of the major documents involved in a condominium purchase, and the highlights of the Horizontal Property Regimes Law..... 28

19. Request the Real Estate Commission to develop a comprehensive pamphlet, written in laymen's terms, which outlines and describes the particulars of condominium life, including a checklist of pertinent items to consider in making a purchase, and a review of the various documents in that connection..... 28

20. Request the Real Estate Commission to develop a long-range program to educate the public on condominium living, utilizing all forms of media distribution, including newspapers, seminars, radio, and television..... 28

CHAPTER 5 - WARRANTY PROBLEMS

21. Before legislative action is taken in this area, determine the actual extent and nature of warranty repair problems in the condominium community as a whole, and prior to enactment of a particular proposal, ascertain the potential legal, financial, and economic impact on the condominium market and community..... 39

22. Monitor the effectiveness over a period of time of the warranty disclosure and notification provisions of the Horizontal Property Regimes Law..... 45

CHAPTER 6 - CONSUMER REMEDIES

23. Provide a statutory remedy whereby a condominium owner may bring legal action for damages and/or injunctive relief, and if successful, recover costs and reasonable attorney fees..... 48

(To be made one and twelve copies)

THE SENATE
EIGHTH ..... LEGISLATURE, 19 76
STATE OF HAWAII

S.R. NO. 439 S.D. 1

SENATE RESOLUTION

REQUESTING A STUDY OF PROBLEMS IN THE CONDOMINIUM DEVELOPER-OWNER RELATIONSHIP AND FORMULATION OF A PROPOSED CONDOMINIUM CODE.

WHEREAS, in recent years the number of condominiums in this State has increased markedly; and

WHEREAS, in view of recent economic and housing trends, the condominium is becoming and may become the basic housing unit in Hawaii, for residents of this State and vacationers alike; and

WHEREAS, by virtue of its ownership characteristic, the legal relationships surrounding construction and operation of condominium projects are complex and significant, more so than a landlord-tenant residential rental situation; and

WHEREAS, although Hawaii has a relatively advanced horizontal property regimes law, the number of complaints arising from the developer-owner relationship in condominium projects are steadily increasing; and

WHEREAS, in the landlord-tenant area, the legislature recently enacted the comprehensive Residential Landlord-Tenant Code, which clearly and thoroughly defines the legal relationships between the parties and establishes efficient and equitable methods for the resolution of disputes; and

WHEREAS, with the proliferation of condominiums, the proposal has often been made for a condominium code similar to the landlord-tenant code, to clearly define legal relationships and identify methods to swiftly and equitably resolve disputes; now, therefore,

BE IT RESOLVED by the Senate of the Eighth Legislature of the State of Hawaii, Regular Session of 1976, that the Office of Consumer Protection, the Legislative Reference Bureau and the Real Estate Commission are requested to jointly study problems reported in the condominium, owner-developer relationship, to formulate a proposed condominium code in the same vein as the Residential Landlord-Tenant Code, designed to clearly define the legal relationships and establish methods for efficient and

equitable resolution of disputes, and to report their findings and recommended legislation to the Legislature twenty days prior to the convening of the Regular Session of 1977; and

BE IT FURTHER RESOLVED that the Office of Consumer Protection, the Legislative Reference Bureau and the Real Estate Commission, provide all interested parties the opportunity for input while formulating the proposed code, and that these agencies collectively report on the progress and status of this investigation every sixty days following adoption of this resolution, to the Chairpersons of the Senate Committees on Consumer Protection, Housing and Hawaiian Homes and Judiciary; and

BE IT FURTHER RESOLVED that certified copies of this Resolution be transmitted to the Director of the Office of Consumer Protection, the Director of Legislative Reference Bureau and the Chairperson of the Real Estate Commission.

S-709

STANDING COMMITTEE REPORT NO. 939-76

Honolulu, Hawaii
April 13, 1976

Honorable John T. Ushijima
President of the Senate
Eighth Legislature
Regular Session of 1976
State of Hawaii

Sir:

RE: S.R. No. 439

Your Committee on Consumer Protection to which was referred S.R. No. 439 entitled:

"SENATE RESOLUTION REQUESTING A STUDY OF THE PROBLEMS IN THE CONDOMINIUM DEVELOPER-OWNER RELATIONSHIP AND FORMULATION OF A PROPOSED CONDOMINIUM CODE.",

begs leave to report as follows:

The purpose of this Resolution is to request the Office of Consumer Protection and the Real Estate Commission to examine difficulties relating to the legal relationships between condominium developers and owners and to formulate a proposed condominium-consumer protection code.

As stated in the Resolution, condominiums may be destined to become the basic housing unit of the future. Although Hawaii has enacted relatively advanced laws regarding condominiums, the volume of consumer-type complaints arising from developer-owner relationships are steadily increasing and each year, the legislature considers additional legislation in a piece-meal attempt to alleviate these situations.

While the legislature is in accord with the intent of these measures, it has questioned their effect on existing law regarding horizontal property regimes, contained in Chapter 514, Hawaii Revised Statutes.

This concern was explicitly expressed on the Senate floor, this session, by the Vice-Chairman of your Committee on Judiciary as the Senate took final action on four amendments to the Horizontal Property Regimes Act as follows:

"This Act...was originally intended to be a highly technical, legal vehicle for placing certain lands in

the horizontal property regimes. It is becoming through our actions...a consumer protection section of the law. Anyone trying to use it in its technical sense will have extreme difficulty...we will need to review this whole matter (and) the consumer protection aspects should be put into a separate code or chapter so that the initial intent of the law can still be accomplished."

Your Committee on Judiciary, as stated in Standing Committee Report No. 605-76, has also recommended further study in this area:

"Your Committee is cognizant of the many problems arising in condominium living here in this State and is sympathetic to the needs of the condominium owner. Your Committee strongly recommends that the Real Estate Commission hold at least one public hearing not less than three months prior to the opening of the regular session of the legislature for the purpose of providing to the board of directors of the association of apartment owners and the individual apartment owners an opportunity to testify with regard to legislation recommended by them or the Commission as part of its function. This hearing shall be publicly announced by the Commission two weeks in advance thereof."

Your Committee on Consumer Protection finds that the intent and purpose of the above-mentioned recommendations can be accomplished through the means proposed in S.R. No. 439.

Your Committee amended the Resolution by including the Legislative Reference Bureau as a participant in this study. Your Committee finds that the technical expertise and research capabilities of the Bureau will be of great importance in examining the problems and proposing enabling legislation to alleviate the situation.

Your Committee also amended the Resolution by stipulating that the Office of Consumer Protection, the Real Estate Commission and the Legislative Reference Bureau provide public input in the formulation of the proposed code, and that they report on the progress and the status of the investigation, at least every two months, to the Chairpersons of your Committees on Consumer Protection, Housing and Hawaiian Homes and Judiciary.

Your Committee on Consumer Protection is in accord with the intent and purpose of S.R. No. 439, as amended herein, and recommends its adoption in the form attached hereto as S.R. No. 439, S.D. 1.

SMA 896-865

Appendix C

WITNESSES TESTIFYING AT STUDY COMMITTEE HEARINGS

Oahu - June 26, 1976

Sunhild Hampson - Condominium owner
Ali Mohammed - Condominium owner
Elizabeth Miyamoto - Condominium owner
Louise Hewett - Condominium owner
Jean Minton - Condominium owner
Thomas Oshiro - Condominium owner
James Rowland - Condominium owner
Lois Yoder - Condominium owner
Dean Reid - Realtor

Kauai - June 28, 1976

George Schulze - Resident manager
Bill Smith - Realtor
Elizabeth Hammond - Condominium owner
Jane Hines - Realtor

Maui - June 29, 1976

Andy Freitas - Condominium owner
Jack Snipes - Condominium owner
Les Hill - Condominium owner
John Schiebelhut - Property manager
Willis Kemp - Developer

Kona - June 30, 1976

A.L. Draeger - Condominium owner
Kim Whitman - Property manager
Kaliko Chun - Property manager

Appendix D

LETTER TO WAIKIKI RESIDENTS ASSOCIATION

December 7, 1976

Dear Sir:

In response to your previous interest and participation in the input phase of the condominium owner-developer relationship study being conducted by the Office of Consumer Protection, Legislative Reference Bureau, and Real Estate Commission, please find enclosed an advance confidential copy of the report for your review and comment.

The enclosed advance copy is not for general distribution, as it is preliminary to the final report and thus subject to change. The report remains the property of the study committee and is intended solely for confidential review and comment by designated representatives of condominium owners, property managers, and developers who have previously participated in this study. The contents of the draft are to remain confidential until the final draft is approved by the study committee and submitted to the legislature in final form.

The study committee would appreciate a review of this report by you or appropriate members of your group, and invites you to submit written comments concerning the report. In order to allow for possible incorporation of your comments, they must be in single-spaced typewritten form and be received by the study committee no later than 4:30 p.m. on December 17, 1976. Comments should be addressed and delivered to: Study Committee, c/o Mr. Walter T. Yamashiro, Office of Consumer Protection, 250 South King Street, Honolulu, Hawaii 96813.

Thank you for your cooperation and assistance.

Very truly yours,

WALTER T. YAMASHIRO
Director
Office of Consumer Protection

SAMUEL B. K. CHANG
Director
Office of Legislative Reference Bureau

MARY V. SAVIO
Vice Chairperson
Real Estate Commission

Enc.

Note: This letter was also sent to the Hawaii Council of Associations of Apartment Owners, Institute of Real Estate Management, Honolulu Board of Realtors, Mr. Douglas E. Prior, Esq., Mr. Dwight M. Rush, Esq., Mr. Hiroshi Sakai, Esq., and Mr. Alfred M. K. Wong, Esq. Copies were made available on Maui, Kauai, and Hawaii through the Office of Consumer Protection, and previous participants there were so notified. As of December 21, 1976, no comments had been received from these parties.

Appendix E

RESPONSE FROM THE WAIKIKI RESIDENTS ASSOCIATION

16 December, 1976

Study Committee
c/o Mr. Walter T. Yamashiro
Office of Consumer Protection
250 S. King Street
Honolulu, Hawaii 96813

Dear Mr. Yamashiro:

Thank you for your invitation to comment on the "Confidential Draft-Study of Problems in the Condominium Owner-Developer Relationship," dated 2 December, 1976.

Our group has mixed reactions to the Draft Study. We find some of the proposals analyzed thoroughly and thoughtfully, while on the other hand, other proposals seemed to be studied superficially. The study stated that the input taken, and evidence complied, were composed mainly of isolated individual complaints or problems. Perhaps this accounts for the wide divergence in the quality of the proposals. Our experience is that most of the problems discussed in the Study are more widespread than realized. You may be interested to know that on 1 December and 8 December, 1976, our Waikiki Residents Association conducted meeting-workshop sessions attended by a total of about 300 persons and all of the complaints and recommendations which the Study raises were discussed. All districts of Oahu, where condominiums now exist, were represented. Incidentally, six State Representatives and one City Councilman also attended. Most of our comments below were derived from the results of these two meetings and they are:

1. We found the first paragraph of the Introduction especially important with its emphasis on the condominium as destined to become an important housing unit of the future in Hawaii. Therefore, we might add that basic improvements in condominiums today could be an important factor in improving the quality of life in Hawaii in the years ahead.

2. To the second paragraph of the Introduction, however, we would add at the end "... but which neglected, to some extent, the operational period of condominiums."

3. On page 2, under Objectives of the Study #(3), it is suggested that before the word "consumer," the words home-ownership be added. This is necessary in order to distinguish condominium owners as being much more than pure consumers; they are home-ownership families, property-tax-paying citizens. This should be kept in mind when discussing the Declaration and By-Laws Sections.

4. Since the Study Committee has recommended basic changes to the Law, it is not clear to us what the concluding statement of the first paragraph of the Summary (page 6) means. Furthermore, some proposals for change may be necessary based on the Study's conclusion in the second paragraph of the Summary which refers to the need for more democracy, more self-help, and more education and disclosure in condominium projects.

5. As to the allocation of votes to units, we regret you didn't explore the idea of one vote per one residential owner when voting for the Board. We would recommend this change. (The allocation of votes by percentage of common interest for all economic questions could remain as is.) The basis for this proposal is that in a democratic society or organization (such as a condominium), any person, irrespective of his wealth, receives one vote in electing officials. This is a basis of our Constitution. This is true of the President, the Governor of Hawaii, et. al. Consequently, one owner owning 10 apartments should have only one vote in the election of Officers. Also, "apartment" should mean residential apartment only. An owner of a commercial property would vote if he also owned a residential apartment. However, a commercial owner not owning an apartment could become a Board Member if elected where his economic vote is more meaningful to him. His democratic vote of course would be counted in the condominium in which he lives. Incidentally, on page 8, the Study implies that "voting by percentage of common interest" is the Law. Actually, the developer has the right to declare any system he desires.

6. The use of cumulative voting, as proposed on page 11, is not a part of our democratic system for electing officials; this method of voting is an economic-corporation method and since condominiums are home-ownership oriented, as indicated in the Introduction, this method of voting is not appropriate for residential condominiums. We feel there are better methods of protecting the minority.

7. Page 11, "By-Laws." The word "reportedly" is used to infer that the developer could write the By-Laws to disadvantage himself. We doubt he would do this, so the word should be eliminated. Also the Study should point out that for the owners to amend the By-Laws, the Declaration must also be changed. The cost of doing this is estimated to be $400-$2,000, depending on the attorney fees. Also, in this section a more in-depth study is needed, we feel. An analysis should be made of the relationship between the Declaration and the By-Laws. They are separate kinds of documents as implied in S.R.439, S.D.I. and S.C.R. 605-76. The Declaration is a detailed description of the Project, prepared by the developer for the Real Estate Commission and the buyers. It is a seller-buyer document. On the other hand, the By-Laws are the day-to-day rules and regulations for the home-owners to operate the condominium. The Study could also investigate the use of Interim By-Laws prepared and used by the developer until the date when the home-owners take over the operations. At this time, the owners should prepare their own By-Laws, with the necessary checks and balances.

8. As to "By-Laws" (page 12). The home-owners, through their Boards, rather than the developer should determine the percentage required to amend <u>their</u> By-Laws. Also the participation of commercial areas in the Association should be determined by the home-owners.

9. As to "Proxies," again the home-owners should decide this, with provisions that any owner can solicit proxies at any time provided a standard form is used. This form should not indicate any name such as "President," Managing Agent," etc. on the form. Other home-owners should not pay for any such solicitations except for quorum purposes.

10. "Contracts" (page 15). Our understanding of the analysis is that contracts should be limited to a maximum of 5 years subject to rescission by the home-owners. We feel this is especially important and should be applied to all contracts, especially those entered into by the developer. The home-owners, through the democratically-elected Board, must have authority over all operations that affect all residents; otherwise, their management is compromised.

11. Page 16, "Transfer of Government." It is suggested that a phrase be added: "<u>and when 25% of the resident home-owners call for such a meeting.</u>"

12. As to "Property Manager on the Board," (page 18), we agree with the recommendation that he should not be on the Board, but would add that it is equally wrong to have an employee of the Manager on the Board because threats to his freedom of actions might arise related to his job security. We don't feel this threat would be conducive to rational decisions affecting other home-owners.

13. "Term of Directors" (page 19). We feel a six-year limitation is not detrimental but instead creates a healthy approach to democratising condominiums. Also, a really good Board member can become an Adviser to the Board for one year, and then run again for election, if he or she desires.

14. "Election of Board" (page 19) refers to the issuance of a biographical sketch for each candidate. Condominiums already doing this find it essential and useful. The Study indicates that proxy voters would be unapprised of nominations from the floor. We don't feel this is as big a problem as the need for the biography. One solution is to send the new nominations from the floor to absentee owners who then re-vote, with a recount made at the next Board Meeting at an "open" meeting. Again, we feel each Board can resolve this problem; however, biographies should be provided and investigated before the vote.

15. "Board Meetings" (page 21). The Sunshine Law, applied so successfully in Hawaii, should be used at all Board meetings. Notices and agenda should be sent to every homeowner. In condominiums that now have open meetings, the problem of "very personal matters" is handled by setting aside, on the agenda, the necessary 5-15 minutes for these matters. This has proven to be workable.

16. "Mixed Uses," (page 22), should be, we feel, analyzed in greater depth. The problem is not just "residential" vis-a-vis "hotel," but all mixed uses as defined in the Zoning Laws and Codes. Therefore restaurants, night clubs, time-sharing, etc. should be analyzed as to the economic, social, quality, aesthetics, noise and pollution effects. The Declaration plus other necessary documents should clearly state these uses and their zoning effects. Disclosure and education should be a simultaneous occurrence.

17. Again, on "Mixed Uses," especially as to maintenance fees, insurance costs, metering, common areas, and noise related to commercial areas (pages 23-26), there is a need to clearly state in the Declaration how all common costs are allocated and a need to state that the homeowners (through their Boards) can assess these costs in an equitable manner. The problems posed in the Study are not as difficult to overcome as the analysis indicates.

18. We agree that a pamphlet (page 28) on Condominiums is needed; however, we feel that the Real Estate Board should prepare only a "model" pamphlet with each Association required to modify the document to fit its own situation, with approval of the final document by the Consumer Protection Office.

19. The proposed "information sheet" (page 29). While we agree in principle with the need, we feel that the present draft uses a number of over-stated words such as "protection and comfort," "competent managing agents," and a number of derogatory ideas such as "Board Members do not have time and facilities..." Also, the dangers of management, such as "sweetheart" deals, padding, corruption are not discussed. These are "real life." Actually the information sheet should be rewritten as a "model," with each condominium being required to issue an approved sheet to every buyer - not just the "first buyer." All the pros and cons should be given, names of all developers, agents and apartment-owners should be shown. Under By-Laws, accurate statements should be required: such as, "amendments under the present law require an amendment of the Declaration also," etc. Input for the "model" information sheet should be obtained from discussions with resident-owners in Hawaii.

20. "Consumer Remedies" (page 48). It should be pointed out that the small claims division of district courts handle only cases up to a maximum of $300. Therefore additional limits would be needed.

In conclusion, you may be interested to know that as a result of our meetings and workshops, we have drafted a number of proposed law changes covering all of the issues raised in your much-needed Study. There are a number of other issues for which we are also drafting legislation such as warranties, definitions, time-sharing, etc.

Again, thank you for this opportunity to comment on the draft Study document. We have been offered a rather short time to gather all the comments of our 300-plus workshop participants, and we have probably not elaborated on all the points as much as we would have wanted. However, we hope you will be able to schedule some time for discussion with us in the near future.

Sincerely,

Donald R. Hanson

and for

Jean Minton
Polly Yoder
Witnesses at Study Committee Hearings

Appendix F

LETTER TO WAIKIKI RESIDENTS ASSOCIATION

December 21, 1976

Mr. Donald R. Hanson
President
Waikiki Residents Association
1860 Ala Moana Boulevard
Honolulu, Hawaii 96815

Dear Mr. Hanson:

The Study Committee is in receipt of the comments submitted by your group on the "Study of Problems in the Condominium Owner-Developer Relationship", and we wish to thank you for your interest and participation. Your comments will be included as an appendix to the final report of the Study Committee, which will be submitted to the legislature in January.

In general response to your comments, while it appears from your proposals and constructive criticism that your group is concerned almost exclusively with residential owner-occupants, the Study Committee of necessity had to consider not only residential owner-occupants, but all condominium owners in Hawaii. In analyzing the problems of the residential owner-occupant and formulating recommendations, it was necessary to consider the ramifications and equities for the condominium community as a whole, including residential owners, investor owners, commercial owners, and developer owners.

Sincerely,

WALTER T. YAMASHIRO
Director
Office of Consumer Protection

SAMUEL B. K. CHANG
Director
Office of Legislative Reference Bureau

MARY N. SAVIO
Vice Chairperson
Real Estate Commission