PRESENTATION OF THE
REAL ESTATE COMMISSION

TO THE HOUSE COMMITTEE ON
CONSUMER PROTECTION AND COMMERCE

TWENTY-FIFTH LEGISLATURE
Regular Session of 2010

Monday, January 25, 2010
2:00 p.m.

TESTIMONY ON HOUSE BILL NO. 2033 – RELATING TO CONDOMINIUMS.

TO THE HONORABLE ROBERT N. HERKES, CHAIR, AND
MEMBERS OF THE COMMITTEE:

My name is Michele Loudermilk and I serve as the Chairperson of the Real Estate Commission's ("Commission") Condominium Review Committee. We thank you for the opportunity to provide testimony expressing concerns with House Bill No. 2033, which proposes to clarify that any condominium developed after July 1, 2006 is subject to chapter 514B, HRS, and to limit condominium maps to two dimensional renderings.

The Commission believes the current statute, section 514B-21, HRS, already makes clear that chapter 514B, HRS, applies to all condominiums created after July 1, 2006 and that the provisions of chapter 514A, HRS, do not apply to condominiums created after July 1, 2006. The proposed amendments therefore seem unnecessary.

As to the proposed amendments in Section 2 of the bill, the Commission is unsure as to their intent and purpose. However as background for the Committee, in 2006 when the current condominium law was overhauled, the issue over spatial units was discussed at length. On one side consumers needed notice of the potential development of spatial units to make an informed decision on whether to purchase within a registered condominium project. On the other side, developers needed to

preserve their right to build other units as allowed by the county. Moreover, a review of other states' experience with spatial units included the option of three dimensional spatial coordinates. The Commission is concerned that the proposed new subsection (b) for section 514B-33, may have negative unintended results, namely that, a purchaser or prospective purchaser may be misled as to the scope of the condominium project and the size, placement, or location of the unit being purchased. We also note that there are other sections in chapter 514B, HRS, that contain substantially similar requirements relating to spatial units and should this bill move forward, these sections must also be amended.

Thank you for the opportunity to present testimony.

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January 25, 2010

The Honorable Robert N. Herkes, Chair
House Committee on Consumer Protection and Commerce
State Capitol, Conference Room 325
Honolulu, Hawai'i 96813

Re: H.B. 2033 – Relating to Condominiums

Dear Chair Herkes and Committee Members:

I am Gordon Arakaki, former Condominium Law Recodification Project Attorney for the Hawai'i Real Estate Commission, testifying in support of what I believe to be the intent of H.B. 2033, with suggestions for amendments.

Proposed Amendment to HRS §514B-21

While the amendment to HRS §514B-21 making it even clearer that all condominiums developed after 7/1/06 are subject to the provisions of HRS Chapter 514B is nice, it would be even better if HRS §514B-22 were amended to make all of HRS Chapter 514B applicable to pre-existing condominiums (unless, as already set forth in the section, application would impair developers' reserved rights or be considered an unconstitutional impairment of contract rights). This would have the added benefit of allowing the Legislature to *repeal* HRS Chapter 514A and eliminate the confusion over the applicability of HRS Chapter 514A.

For example, amending HRS §514B-22 to make all of HRS Chapter 514B applicable to pre-existing condominiums would make it clear that existing condominium associations cannot "elect" to remain governed by HRS Chapter 514A, as was inaccurately stated by the Real Estate Commission in testimony last session. (*See*, Real Estate Commission testimony on SB 1107, SD2, dated 3/16/09, at page 3.)

No condominium association can "elect" to "*remain* governed" by HRS Chapter 514A. Put another way, the Commission appeared to be saying, incorrectly, that condominium associations may choose to have HRS Chapter 514A apply to the association even for things that

have happened after 7/1/06. Pursuant to HRS §514B-22, all of the "Management of Condominium" provisions of the new condominium law (and a number of other provisions that affect the management of condominiums) apply to ***all*** condominiums in the State "with respect to events and circumstances occurring on or after July 1, 2006."

The second proviso of HRS §514B-22 does not have anything to do with a condominium association continuing to be governed by HRS Chapter 514A. It simply recognizes that certain contractual rights may exist under a condominium project's constituent documents, and ***IF*** invalidating a provision in the project's constituent documents would: (i) invalidate the developer's reserved rights (i.e., rights specifically reserved in the project's declaration or other constituent document), or (ii) be an ***unreasonable impairment*** of contract (i.e., the constitutional standard, which is high), ***THEN*** the provision(s) of the condominium project's constituent documents would not be invalidated by the new condominium law.

Therefore, I respectfully suggest that HRS §514B-22 be amended as follows:

> **§514B-22 Applicability to preexisting condominiums.** [~~Sections 514B-4, 514B-5, 514B-35, 514B-41(e), 514B-46, 514B-72, and part VI, and section 514B-3 to the extent definitions are necessary in construing any of those provisions~~] This chapter, and all amendments thereto, shall apply to all condominiums created in this State before July 1, 2006; provided that [~~those sections~~] the provisions of this chapter:
>
> (1) Shall apply only with respect to events and circumstances occurring on or after July 1, 2006; and
>
> (2) Shall not invalidate existing provisions of the declaration, bylaws, condominium map, or other constituent documents of those condominiums if to do so would invalidate the reserved rights of a developer or be an unreasonable impairment of contract.
>
> For purposes of interpreting this chapter, the terms "condominium property regime" and "horizontal property regime" shall be deemed to correspond to the term "condominium"; the term "apartment" shall be deemed to correspond to the term "unit"; the term "apartment owner" shall be deemed to correspond to the term "unit owner"; and the term "association of apartment owners" shall be deemed to correspond to the term "association".

Proposed Amendment to HRS §514B-33

I do not believe that the proposed amendment to HRS §514B-33 regarding spatial units actually resolves the issues surrounding spatial units. The proposed amendment seeks, I believe, to clarify and correct the Real Estate Commission's non-binding opinions regarding spatial units.

(Such clarification and correction is definitely needed; *see* my letter to the Commission, through one of its condominium consultants, dated November 29, 2007, a copy of which is attached for your reference.) Since, however, the Real Estate Commission is currently in the process of amending its administrative rules governing condominiums, it may be more appropriate to clarify and correct its "non-binding" opinions regarding spatial units in the administrative rules. The statutory language regarding spatial units in HRS Chapter 514B appears to be clear enough.

Thank you for this opportunity to present written testimony and for your long-standing support of the Hawaii condominium law recodification.

Sincerely,

CLAY CHAPMAN IWAMURA PULICE & NERVELL

Gordon M. Arakaki

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November 29, 2007

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Subject: Spatial Units

Hi Ken:

Hope you had a safe and happy Thanksgiving!

I understand that the Real Estate Commission's condominium consultants will be meeting during the first week of December, and would appreciate it if you would share my comments regarding spatial units (aka "air space condos") with the consultants, Commission staff, and any Commissioners who might be attending. As explained in more detail below, I believe that the Commission's December 15, 2006 informal non-binding interpretation of "spatial units" is incorrect. Having served for nearly fours years as the Commission's Condominium Law Recodification Attorney, I hope my comments will help clarify the intent of relevant sections of the new condominium law (i.e., Chapter 514B of the Hawaii Revised Statutes ("HRS")) and how those sections should be interpreted.

Background

Since January 2, 2007, I have served as the Chief of Staff of the Hawaii State Senate Committee on Ways and Means and am no longer taking private clients. Recently, however, a former client contacted me with questions and concerns about the Commission's December 15, 2006 interpretation of "spatial units" requiring, among other things, that all spatial units:

- Have boundaries indicated in accordance with §514B-35 (citing HRS §514B-3);
- Have dimensions – horizontal and vertical boundaries (citing HRS §514B-32(a)(7));
- Include spatial coordinates – a beginning and an end point (citing HRS §514B-32(a)(7));
- Comply with county requirements (citing HRS §514B-32(a)(13)); and
- Not exceed the dimensions, heights, set backs, and other requirements mandated by the county (citing HRS §514B-32(a)(13)).

Even before my former client contacted me, a number of developer's attorneys had contacted me with similar questions and concerns.

Analysis

When drafting provisions related to "spatial units," the Commission, through its Blue Ribbon Recodification Advisory Committee, contemplated two distinct situations: (1) Actual spatial units with non-physical boundaries (e.g., certain parking stalls and boat slips), as well as spatial building envelopes where unit owners have the right to build within those envelopes, but the units remain spatial even after the structures are built; and (2) Spatial units meant to override the requirements of In re: The Krieg Condominium, REC-DR-93-1 (2/10/95), and do away with the need to create "tool shed" condominiums.

I do not believe that any developers have a problem with using specific spatial coordinates to describe spatial units of the first type ("Type 1 spatial units"). The problem is with the Commission's unfounded requirement that specific spatial coordinates that are somehow in compliance with non-existent county requirements be used to describe spatial units of the second type ("Type 2 spatial units"). For Type 2 spatial units (again, meant to replace the "tool shed" condominium fiction required by Krieg), the Commission's December 15, 2006 informal non-binding interpretation of "spatial units" is incorrect for the following reasons:

- HRS §514B-35 defines unit boundaries, but is prefaced with the phrase: "*Except* as provided by the *declaration* ..." (emphasis added). The provision, which is meant to protect against inartful drafters,[1] clearly allows unit boundaries to be defined differently in actual declarations. In the case of Type 2 spatial units, the unit boundaries are not important for title purposes, defining maintenance responsibilities, or anything but serving notice that a physical unit is intended to replace the Type 2 spatial unit. Other provisions in declaration should very specifically define what can be built. And other provisions of the law (e.g., HRS §514B-5) make it clear that any physical structures that are built in a condominium property regime must comply with County and State land use laws, and declarations generally echo the law.[2]

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[1] In its 12/31/03 final report to the Legislature on the recodification of the condominium law, the Real Estate Commission commented as follows regarding HRS §514B-35:

> As noted in the official comments to UCIOA: "It is important for title purposes, for purposes of defining maintenance responsibilities, and other reasons to have a clear guide as to precisely which parts of a condominium constitute the units and which parts constitute the common elements. This section fills the gap left when the declaration merely defines unit boundaries in terms of floor, ceilings, and perimetric walls."

[2] Declarations I have drafted contain at least the following clauses:

> [*Regarding use and occupancy restrictions, generally*]: "The Units and their appurtenant Limited Common Elements shall be occupied and used only in accordance with lawful zoning allowances and for no other purpose. Each Unit Owner and occupant shall at all times comply with all applicable County, State, and Federal laws. In addition, each Unit Owner and occupant shall comply with each of the provisions of this Article; provided, however, that in the event of any conflict between the provisions set forth below and any applicable law(s), the most restrictive provision or law shall control."
>
> [*Regarding site development and use*]: "No structure shall be permitted except in conformance with HRS Chapter 205, [*name of specific county*] law, building and zoning regulations, and the Design Standards set forth herein."

- HRS §514B-32(a)(7) states that "[t]o the extent *not shown* on the *condominium map*," a declaration shall contain "a description of the location and dimensions of the horizontal and vertical boundaries of any unit." (Emphasis added.) In other words, the declaration needs to describe the horizontal and vertical boundaries of a unit only to the extent it is not shown on the condominium map. For Type 2 spatial units, the simplest description makes the most sense, since the spatial unit is meant to be replaced by a physical structure. In declarations I have drafted, I described such units as follows:

  > For purposes of creation of the condominium property regime, Units 1, 2, 3, (etc.) are created as air space units. The dimensions, area, and location of each air space unit are described herein and shown graphically on the Condominium Map.
  >
  > Notwithstanding any other provision herein, each air space unit shall be comprised of the entire volume of space in an imaginary twenty-five foot by twenty-five foot by twenty-five foot cube situated on the surface of the Limited Common Element land area appurtenant to the Unit.
  >
  > Each of the respective Unit Owners of Units 1, 2, 3, (etc.) has the right to alter or replace its air space unit and build a single-family detached unit and other appurtenant improvements pursuant to Article ___ ("Alteration of Project").

  I believe that such a description is entirely consistent with the letter and intent of HRS Chapter 514B.

  Of course, in the case of projects containing Type 2 spatial units, each spatial cube unit is located on an area of land designated as a limited common element (i.e., a yard surrounding the unit), and it is important that the limited common element yard boundaries are defined by a map, metes and bounds, or other coordinates that allow them to be definitively located, unless there's a fence, wall or other structure defining those boundaries. This would essentially be the same approach as existed under HRS Chapter 514A, and it serves a legitimate purpose. It might be appropriate for the Commission to require that, once a structure is built that replaces the Type 2 spatial unit, the owner must file a declaration or condominium map amendment reflecting the conversion of the unit from spatial to structural.

  Finally, please note that HRS §514B-32(a)(7) also states that "[u]nit boundaries *may* be defined by physical structures or, if a unit boundary is not defined by a physical structure, by spatial coordinates." (Emphasis added.) Clearly, HRS §514B-32(a)(7) does *not require* that Type 2 spatial units be described by spatial coordinates. Furthermore, the horizontal and vertical boundaries of Type 2 spatial units may be described in declarations as I did in the example above and represented on condominium maps as simple cubes.

  Again, the cubes of air space described above are meant to replace the physical "tool shed" condominiums required by Krieg. The Commission's December 15, 2006 informal

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[*Regarding alteration of projects*]: "All changes shall conform to applicable [*name of specific county*] building and zoning laws and regulations ("County Laws") and other applicable State of Hawaii laws and regulations ("State Laws")."

non-binding decision has caused many developers to simply throw up their hands and go back to using the "tool shed" condominium fiction. Such an interpretation is clearly contrary to the intent of HRS Chapter 514B.

- There are no county requirements that I am aware of regarding the boundaries of Type 2 spatial units (or any other spatial units). Therefore, requiring Type 2 spatial unit boundaries to somehow comply with the requirements of HRS §514B-32(a)(13) by following county zoning and building code requirements applicable to structures makes no sense and is contrary to general principles of statutory construction.

  If the Commission's December 15, 2006 interpretation of "spatial units" requires that all spatial unit boundaries follow the setbacks, height restrictions, etc., set forth for physical structures in zoning and building codes, it makes even less sense. As noted above, any physical structures constructed in a spatial unit must comply with those zoning and building requirements, but there is absolutely no requirement that spatial unit boundary descriptions follow requirements for physical structures. To the contrary, such a requirement would create practical problems because things like setback and height restriction are often variable.

  For example, it is very common to have multiple height restrictions, such as 30 feet for structures but 40 feet for antennas and chimneys. You can also have exceptions to setbacks that allow certain structures closer to a lot boundary than others. In either case, it is not possible to draw a fixed, legal spatial unit boundary that is tied to a variable height restriction or setback, and it is wrong for the Commission to impose a requirement that is impossible to comply with.

Conclusion

Based on the discussion above, I hope that the Hawaii Real Estate Commission will reconsider its December 15, 2006 interpretation of "spatial units" and approve condominium declarations that comply with the true intent of HRS Chapter 514B, particularly those containing provisions meant to replace the "tool shed condo" fiction (i.e., Type 2 spatial units).

My suggestions above are consistent with key principles of the new condominium law, i.e., clearly disclosing what is being sold to purchasers (and necessarily, therefore, what title insurers and other insurers are insuring), and allowing maximum flexibility and creativity to condominium declaration/bylaws drafters while still complying with land use and development laws.

Thank you for sharing my concerns at the Commission's condominium consultants' meeting, Ken. If anyone has questions, please have them e-mail me at gordon.arakaki@gmail.com or call me on my cell at (808)542-1542.

Sincerely,

Gordon M. Arakaki

Gordon M. Arakaki