

JAN 28 2009

A BILL FOR AN ACT

RELATING TO CONDOMINIUMS.

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF HAWAII:

1 SECTION 1. The legislature finds that many condominium
2 owners, especially those that are retired and on fixed incomes,
3 are struggling with increases in their monthly maintenance fees.
4 One source of these constant increases appears to be the
5 estimated replacement reserves that are required to maintain the
6 property based on a reserve study performed by the unit owners
7 association.

8 The purpose of this Act is to require, at the request of at
9 least ten per cent of the owners of a condominium or condominium
10 property regime, an independent audit of any replacement reserve
11 study prepared by a board of directors in the preparation of its
12 annual budget.

13 SECTION 2. Section 514A-83.6, Hawaii Revised Statutes, is
14 amended to read as follows:

15 "**§514A-83.6 Associations of apartment owners; budgets and**
16 **reserves.** (a) The board of directors of each association of
17 apartment owners shall prepare and adopt an annual operating



1 budget and distribute it to the apartment owners. At a minimum,
2 the budget shall include the following:

- 3 (1) The estimated revenues and operating expenses of the
4 association;
- 5 (2) Information as to whether the budget has been prepared
6 on a cash or accrual basis;
- 7 (3) The total replacement reserves of the association as
8 of the date of the budget;
- 9 (4) The estimated replacement reserves the association
10 will require to maintain the property based on a
11 reserve study performed by the association[+] along
12 with a copy of the reserve study;
- 13 (5) A general explanation of how the estimated replacement
14 reserves are computed;
- 15 (6) The amount the association must collect for the fiscal
16 year to fund the estimated replacement reserves; and
- 17 (7) Information as to whether the amount the association
18 must collect for the fiscal year to fund the estimated
19 replacement reserves was calculated using a per cent
20 funded or cash flow plan. The method or plan shall
21 not circumvent the estimated replacement reserves



1 amount determined by the reserve study pursuant to
2 paragraph (4).

3 (b) The association shall assess the apartment owners to
4 either fund a minimum of fifty per cent of the estimated
5 replacement reserves or fund one hundred per cent of the estimated
6 replacement reserves when using a cash flow plan; provided that a
7 new association created after January 1, 1993, need not collect
8 estimated replacement reserves until the fiscal year ~~[which]~~ that
9 begins after the association's first annual meeting. For each
10 fiscal year, the association shall collect the amount assessed to
11 fund the estimated replacement for that fiscal year reserves, as
12 determined by the association's plan, except:

13 (1) The commission shall adopt rules to permit an existing
14 association to fund its estimated replacement reserves
15 in increments after January 1, 1993, and prior to
16 January 1, 2000; and

17 (2) The commission shall adopt rules to permit an
18 association to fund in increments, over three years,
19 estimated replacement reserves that have been
20 substantially depleted by an emergency.

21 (c) The association shall compute the estimated replacement
22 reserves by a formula ~~[which]~~ that is based on the estimated life



1 and the estimated capital expenditure or major maintenance
2 required for each part of the property. The estimated replacement
3 reserves shall include:

4 (1) Adjustments for revenues [~~which~~] that will be received
5 and expenditures [~~which~~] that will be made before the
6 beginning of the fiscal year to which the budget
7 relates; and

8 (2) Separate, designated reserves for each part of the
9 property for which capital expenditures or major
10 maintenance will exceed \$10,000. Parts of the
11 property for which capital expenditures or major
12 maintenance will not exceed \$10,000 may be aggregated
13 in a single designated reserve.

14 (d) No association or apartment owner, director, officer,
15 managing agent, or employee of an association who makes a good
16 faith effort to calculate the estimated replacement reserves for
17 an association shall be liable if the estimate subsequently proves
18 incorrect.

19 (e) At the request of at least ten per cent of the apartment
20 owners of an association of apartment owners, the board of
21 directors shall engage an independent consultant to perform an
22 audit of any reserve study incorporated into any annual budget.



1 If the audit discloses that there is a surplus or a projected
2 surplus in the replacement reserve, the audit shall contain
3 recommendations to equitably either refund to each apartment owner
4 a pro rata share of the surplus or reduce future maintenance fees
5 to reflect a gradual reduction of the surplus over a period of one
6 year.

7 ~~[(e)]~~ (f) The commission may request a copy of the annual
8 operating budget of the association of apartment owners as part of
9 the association's registration with the commission under section
10 514A-95.1.

11 ~~[(f)]~~ (g) A board may not exceed its total adopted annual
12 operating budget by more than twenty per cent during the fiscal
13 year to which the budget relates, except in emergency situations.
14 Prior to the imposition or collection of an assessment under this
15 paragraph, the board shall pass a resolution containing written
16 findings as to the necessity of the extraordinary expense involved
17 and why the expense was not or could not have been reasonably
18 foreseen in the budgeting process, and the resolution shall be
19 distributed to the members with the notice of assessment.

20 ~~[(g)]~~ (h) The requirements of this section shall override
21 any requirements in an association's declaration, bylaws, or any
22 other association documents relating to preparation of budgets,



1 calculation of reserve requirements, assessment and funding of
2 reserves, with the exception of:

3 (1) Any provisions relating to the repair and maintenance
4 of property;

5 (2) Any requirements in an association's declaration,
6 bylaws, or any other association documents [~~which~~]
7 that require the association to collect more than
8 fifty per cent of reserve requirements; or

9 (3) Any provisions relating to upgrading the common
10 elements, such as additions, improvements, and
11 alterations to the common elements.

12 [~~(h)~~] (i) Subject to the procedures of section 514A-94 and
13 any rules adopted by the commission, any apartment owner whose
14 association board fails to comply with this section may enforce
15 compliance by the board. In any proceeding to enforce compliance,
16 a board [~~which~~] that has not prepared an annual operating budget
17 and reserve study shall have the burden of proving it has complied
18 with this section.

19 [~~(i)~~] (j) The commission may adopt rules to implement this
20 section.

21 [~~(j)~~] (k) As used in this section:



1 "Capital expenditure" means an expense that results from the
2 purchase or replacement of an asset whose life is greater than one
3 year, or the addition of an asset that extends the life of an
4 existing asset for a period greater than one year.

5 "Cash flow plan" means a minimum twenty-year projection of an
6 association's future income and expense requirements to fund fully
7 its replacement reserves requirements each year during that
8 twenty-year period, except in an emergency; provided that it shall
9 not include a projection of special assessments or loans during
10 that twenty-year period, except in an emergency.

11 "Emergency situation" means any extraordinary expenses:

- 12 (1) Required by an order of a court;
- 13 (2) Necessary to repair or maintain any part of the
14 property for which the association is responsible
15 where a threat to personal safety on the property is
16 discovered;
- 17 (3) Necessary to repair any part of the property for which
18 the association is responsible that could not have
19 been reasonably foreseen by the board in preparing and
20 distributing the annual operating budget;
- 21 (4) Necessary to respond to any legal or administrative
22 proceeding brought against the association that could



1 not have been reasonably foreseen by the board in
2 preparing and distributing the annual operating
3 budget; or

4 (5) Necessary for the association to obtain adequate
5 insurance for the property [~~which~~] that the
6 association must insure.

7 "Major maintenance" means an expenditure for maintenance or
8 repair that will result in extending the life of an asset for a
9 period greater than one year.

10 "Replacement reserves" means funds for the upkeep, repair, or
11 replacement of those parts of the property, including but not
12 limited to roofs, walls, decks, paving, and equipment, that the
13 association is obligated to maintain."

14 SECTION 3. Section 514B-148, Hawaii Revised Statutes, is
15 amended to read as follows:

16 "[+] §514B-148 [+] Association fiscal matters; budgets and
17 reserves. (a) The budget required under section 514B-144(a)
18 shall include at least the following:

19 (1) The estimated revenues and operating expenses of the
20 association;

21 (2) Information as to whether the budget has been prepared
22 on a cash or accrual basis;



- 1 (3) The total replacement reserves of the association as
2 of the date of the budget;
- 3 (4) The estimated replacement reserves the association
4 will require to maintain the property based on a
5 reserve study performed by the association[+], along
6 with a copy of the reserve study;
- 7 (5) A general explanation of how the estimated replacement
8 reserves are computed;
- 9 (6) The amount the association must collect for the fiscal
10 year to fund the estimated replacement reserves; and
- 11 (7) Information as to whether the amount the association
12 must collect for the fiscal year to fund the estimated
13 replacement reserves was calculated using a per cent
14 funded or cash flow plan. The method or plan shall
15 not circumvent the estimated replacement reserves
16 amount determined by the reserve study pursuant to
17 paragraph (4).
- 18 (b) The association shall assess the unit owners to either
19 fund a minimum of fifty per cent of the estimated replacement
20 reserves or fund one hundred per cent of the estimated
21 replacement reserves when using a cash flow plan; provided that
22 a new association need not collect estimated replacement



1 reserves until the fiscal year [~~which~~] that begins after the
2 association's first annual meeting. For each fiscal year, the
3 association shall collect the amount assessed to fund the
4 estimated replacement for that fiscal year reserves, as
5 determined by the association's plan.

6 (c) The association shall compute the estimated
7 replacement reserves by a formula that is based on the estimated
8 life and the estimated capital expenditure or major maintenance
9 required for each part of the property. The estimated
10 replacement reserves shall include:

11 (1) Adjustments for revenues [~~which~~] that will be received
12 and expenditures [~~which~~] that will be made before the
13 beginning of the fiscal year to which the budget
14 relates; and

15 (2) Separate, designated reserves for each part of the
16 property for which capital expenditures or major
17 maintenance will exceed \$10,000. Parts of the
18 property for which capital expenditures or major
19 maintenance will not exceed \$10,000 may be aggregated
20 in a single designated reserve.

21 (d) No association or unit owner, director, officer,
22 managing agent, or employee of an association who makes a good



1 faith effort to calculate the estimated replacement reserves for
2 an association shall be liable if the estimate subsequently
3 proves incorrect.

4 (e) At the request of at least ten per cent of the unit
5 owners in an association, the board of directors shall engage an
6 independent consultant to perform an audit of any reserve study
7 incorporated into any annual budget. If the audit discloses
8 that there is a surplus or a projected surplus in the
9 replacement reserve, the audit shall contain recommendations to
10 equitably either refund to each unit owner a pro rata share of
11 the surplus or reduce future maintenance fees to reflect a
12 gradual reduction of the surplus over a period of one year.

13 ~~[-(e)]~~ (f) Except in emergency situations or with the
14 approval of a majority of the unit owners, a board may not
15 exceed its total adopted annual operating budget by more than
16 twenty per cent during the fiscal year to which the budget
17 relates. Before imposing or collecting an assessment under this
18 subsection that has not been approved by a majority of the unit
19 owners, the board shall adopt a resolution containing written
20 findings as to the necessity of the extraordinary expense
21 involved and why the expense was not or could not have been
22 reasonably foreseen in the budgeting process, and the resolution



1 shall be distributed to the members with the notice of
2 assessment.

3 ~~[(f)]~~ (g) The requirements of this section shall override
4 any requirements in an association's declaration, bylaws, or any
5 other association documents relating to preparation of budgets,
6 calculation of reserve requirements, assessment and funding of
7 reserves, and expenditures from reserves with the exception of:

8 (1) Any requirements in an association's declaration,
9 bylaws, or any other association documents which
10 require the association to collect more than fifty per
11 cent of reserve requirements; or

12 (2) Any provisions relating to upgrading the common
13 elements, such as additions, improvements, and
14 alterations to the common elements.

15 ~~[(g)]~~ (h) Subject to the procedures of section 514B-157
16 and any rules adopted by the commission, any unit owner whose
17 association board fails to comply with this section may enforce
18 compliance by the board. In any proceeding to enforce
19 compliance, a board that has not prepared an annual operating
20 budget and reserve study shall have the burden of proving it has
21 complied with this section.

22 ~~[(h)]~~ (i) As used in this section:



1 "Capital expenditure" means an expense that results from
2 the purchase or replacement of an asset whose life is greater
3 than one year, or the addition of an asset that extends the life
4 of an existing asset for a period greater than one year.

5 "Cash flow plan" means a minimum twenty-year projection of
6 an association's future income and expense requirements to fund
7 fully its replacement reserves requirements each year during
8 that twenty-year period, except in an emergency; provided that
9 it does not include a projection of special assessments or loans
10 during that twenty-year period, except in an emergency.

11 "Emergency situation" means any extraordinary expenses:

- 12 (1) Required by an order of a court;
- 13 (2) Necessary to repair or maintain any part of the
14 property for which the association is responsible
15 where a threat to personal safety on the property is
16 discovered;
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18 the association is responsible that could not have
19 been reasonably foreseen by the board in preparing and
20 distributing the annual operating budget;
- 21 (4) Necessary to respond to any legal or administrative
22 proceeding brought against the association that could



1 not have been reasonably foreseen by the board in
2 preparing and distributing the annual operating
3 budget; or

4 (5) Necessary for the association to obtain adequate
5 insurance for the property [~~which~~] that the
6 association must insure.

7 "Major maintenance" means an expenditure for maintenance or
8 repair that will result in extending the life of an asset for a
9 period greater than one year.

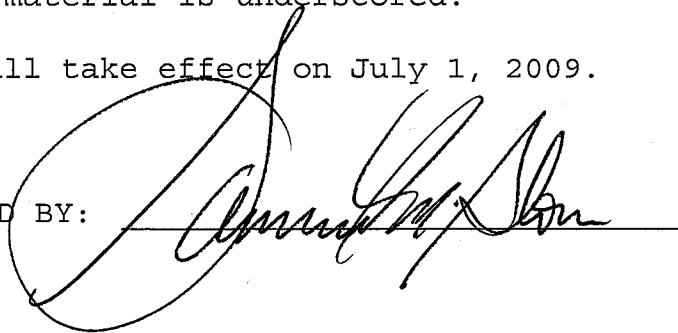
10 "Replacement reserves" means funds for the upkeep, repair,
11 or replacement of those parts of the property, including but not
12 limited to roofs, walls, decks, paving, and equipment, that the
13 association is obligated to maintain."

14 SECTION 4. Statutory material to be repealed is bracketed
15 and stricken. New statutory material is underscored.

16 SECTION 5. This Act shall take effect on July 1, 2009.

17

INTRODUCED BY:



Report Title:

Condominiums; Replacement Reserve Study

Description:

Upon request of 10% or more owners, requires board of directors of associations of apartment owners to have independent audit of replacement reserve study and if audit reveals a surplus or future surplus, requires Board to either refund surplus pro rata or reduce future maintenance fee to reflect reduction in the surplus.





H.I.C.C.O.

HAWAII INDEPENDENT CONDOMINIUM & COOPERATIVE OWNERS
1600 ALA MOANA BLVD. - APT. 3100 - HONOLULU - HAWAII 96815

February 24, 2009

Senator Rosalyn H. Baker, Chair
Committee on Commerce and
Consumer Protection

Testimony on SB 1145 Relating to Condominiums

Dear Senator Baker:

Thank you for this opportunity to testify on the various sections of SB 1145 on behalf of the Hawaii Independent Condominium and Co-op Owners (HICCO).

In Section 2 of the bill, our organization supports the amendment included in lines 11 & 12 on page 2.

Also in Section 2(e) on pages 3 & 4, we do not object to the request by owners regarding the engagement of independent consultants to perform an audit of any reserve study; however, our experience is that the reserves of condominium associations are dramatically underfunded.

We appreciate your committee's consideration of our comments.

Sincerely,

Richard Port

Richard Port, Chair
Legislative Committee



SENATE COMMITTEE ON COMMERCE AND CONSUMER PROTECTION,
REGARDING SENATE BILL 1145

Hearing Date : Tuesday, February 24, 2009
Time : 8:30 a.m.
Place : Conference Room 229

Chair Baker and Committee Members,

My name is John Morris, and I am testifying on behalf of the Community Associations Institute Hawaii Chapter Legislative Action Committee ("CAI"). CAI Hawaii is the local chapter of a national organization dedicated to improving the management and operation of community associations nationwide. CAI has over 200 members in Hawaii and over 14,000 nationwide.

CAI opposes Senate Bill 1145. The reserves law was established in 1991 to put the burden on the board of directors to properly fund reserves for the association. Prior to that time, it was not uncommon for large special assessments because an association had inadequate reserves.

The concern was that if owners could veto the process, they might prevent the board from establishing adequate reserves to protect everyone. The concern was not simply for the present owners in the building but also for those who might buy into the building in the future and be completely unaware that the reserves were underfunded. The Legislature decided it would be easier to supervise board members than to try to supervise the whole association, hence the obligation imposed on the board of directors to collect reserves. The scheme established by the Legislature has worked reasonably well for more than 15 years. Therefore, before altering that scheme, CAI hopes the Legislature will consider the following:

- Given the uncertainties of predicting the future, very few condominium associations seem to have surplus reserve funds. In fact, more often, the reverse is true, the associations have a shortfall that must be made up by specially assessing the owners or borrowing the money.
- SB 1145 seems to be unfair in that it proposes to take authority away from the board while still making the board responsible for collecting adequate reserves.
- The cost of employing an independent consultant to conduct a research study could be very high for a small building. Even in a large building, the bill would allow a small group of owners to force the association to incur a large expense.
- In addition, since there are no specific State standards established for reserve study preparers, there is no confirmation that the "independent consultant" required by the

CAI Testimony Regarding SB 1145
February 23, 2009
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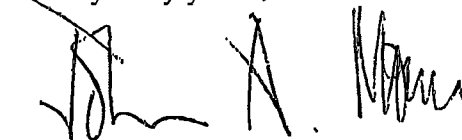
bill will do an accurate reserve study.

- If that occurs, the so-called "surplus" may turn out to be illusory and the association may refund the money only to have to specially assess the owners again for additional reserves that were mistakenly refunded.

In summary, this bill seems to address a problem that affects very few associations. In doing so, it undermines the scheme established by the Legislature to help present and future owners avoid unnecessary and expensive special assessments. Therefore, CAI requests that this committee hold the bill.

Thank you for this opportunity to testify.

Very truly yours,

A handwritten signature in black ink, appearing to read "John A. Morris", written over a horizontal line.

John A. Morris
Hawaii Legislative Action Committee
of the Community Associations Institute

JAM:alt