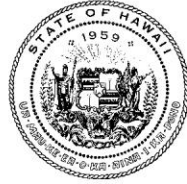


NEIL ABERCROMBIE  
GOVERNOR

SHAN TSUTSUI  
LT. GOVERNOR



STATE OF HAWAII  
**DEPARTMENT OF TAXATION**  
P.O. BOX 259  
HONOLULU, HAWAII 96809  
PHONE NO: (808) 587-1530  
FAX NO: (808) 587-1584

FREDERICK D. PABLO  
DIRECTOR OF TAXATION

JOSHUA WISCH  
DEPUTY DIRECTOR

To: The Honorable Angus L.K. McKelvey, Chair  
and Members of the House Committee on Consumer Protection and Commerce

Date: Wednesday, March 12, 2014  
Time: 2:10 p.m.  
Place: Conference Room 325, State Capitol

From: Frederick D. Pablo, Director  
Department of Taxation

Re: S.B. No. 2483 S.D. 1, Proposed H.D. 1, Relating to Condominium Associations

The Department of Taxation (Department) opposes the proposed amendment to subsection (a)(1), as set forth in section 2 of S.B. No. 2483, Proposed H.D. 1. The Department takes no position regarding the other proposed amendments in this measure.

S.B. 2483, S.D. 1, Proposed H.D. 1, amends subsections (a) and (g) of §514B-146, Hawaii Revised Statutes (HRS), as well as subsections (b) of HRS §514B-106. The Department's testimony only pertains to the proposed amendment to subsection (a) of HRS § 514B-146, which would amend the rule governing priority of liens in the event a condominium association places a lien on an owner's unit for unpaid maintenance fees. Under current law, liens for all taxes have priority over liens for maintenance fees. This measure amends the law to provide that only liens for real property taxes have such priority. The measure has a defective effective date of July 1, 2050.

As a matter of policy, the State and counties have a vested interest in protecting claims for amounts owed to them. Repealing lien priority for State taxes will seriously weaken the State's ability to collect money owed, if the asset that can be collected from is a condominium subject to Chapter 514B.

It has also been brought to the Department's attention that the reason this amendment has been proposed is due to a belief that, as a matter of practice, only real property tax liens would ever attach to condominium units. However, this is not the case. The Department and the IRS may seek to attach a lien to a condominium or any other real property interests in an effort to collect on any unpaid tax, including income tax, general excise tax, or any other kind of tax. Without the super-priority of liens established under this section, the Department's liens will be

less effective and will negatively impact the Department's ability to collect tax amounts owed to the State.

The Department notes that there is an identical sister provision to § 514B-146(a), located in Chapter 514A, HRS, (which governs condominiums established before July 1, 2006 which have not opted into the new rules under Chapter 514B). An examination of the different versions of S.B. 2210 (2004), which became Act 164, Session Laws of Hawaii 2004 (Condominium Property Act), show that the current statutory language is reflected in all drafts. The Department interprets this consistency throughout the various drafts to indicate that the drafters intended to prioritize all tax liens, not just real property tax liens. Since the relevant provisions in Chapter 514A and Chapter 514B are identical, the Department believes that all tax liens should continue to have statutory priority.

Furthermore, the Department notes that if subsection (a) is amended as proposed, the net result is that Internal Revenue Service (IRS) will have priority in all collection matters of tax debts. Federal tax liens will not be affected by this measure, since federal law controls federal matters, including the collection of tax liens, a conflicting state law notwithstanding. Under Internal Revenue Code (IRC) § 6321, a very broad lien is created upon it's the filing of a notice of federal tax lien which encompasses all of the taxpayer's property or rights to property. This lien acts as security for the federal tax liability.

State law is significant only in determining whether or not a taxpayer has property and rights to property. The federal government will look to state law to determine a taxpayer's interest in a particular piece of property. However, once it is determined that a taxpayer has an interest in property, federal law determines whether such interests qualify as property or rights to property to which the federal tax lien attaches and how that lien is collected. "[One] look[s] to state law to determine what rights the taxpayer has in the property the Government seeks to reach, then to federal law to determine whether the taxpayer's state-delineated rights qualify as 'property' or 'rights to property' within the compass of federal tax lien legislation." United States v. Craft, 535 U.S. 274 (2002); Drye v. United States, 528 U.S. 49, 58 (1999).

After notice and demand for payment, the federal tax lien arises and relates back to the assessment date. IRC § 6323 governs the priority of liens in collection matters where a federal tax lien has been filed. IRC § 6323(a) provides, in part, that "the lien imposed by §6321 shall not be valid as against any purchaser, holder of a security interest, mechanic's lienor, or judgment lien creditor until notice thereof has been filed." Once a Notice of Federal Tax Lien (NFTL) has been filed, the IRS generally follows a "first in time, first in line" rule in order to determine the distribution priority of various creditors.

Under IRC § 6323(b), however, special protection is granted for a limited set of interests which come into existence after the filing of a NFTL by giving them priority over the federal tax lien even though the interests. These special interests are called "super priorities." With respect to real property, the only super priority provided for is under § 6323(b)(6), and only covers real

property taxes and special assessments issued by a taxing authority, and charges for utilities or public services provided by a governmental unit.

All other interests are junior to that of the IRS if they are filed after the NFTL. If this measure is adopted, the federal tax lien will continue to have priority over any lien by a condominium association while the State tax lien will be junior to such lien. For these reasons, the Department strongly requests that subsection (a) remain unamended, and that all tax liens continue receiving statutory priority.

Thank you for the opportunity to provide comments.



P.O. Box 976  
Honolulu, Hawaii 96808

March 11, 2014

Honorable Angus L.K. McKelvey, Chair  
Honorable Derek S.K. Kawakami, Vice Chair  
Consumer Protection and Commerce  
415 South Beretania Street  
Honolulu, Hawaii 96813

Re: **SB 2483, SD1 / SUPPORT**

Dear Chair McKelvey, Vice Chair Kawakami and Committee Members:

I am the Chair of the Community Association Institutes Legislative Action Committee ("CAI"). **CAI supports SB 2483, SD 1 for reasons noted below.**

First, §514B -146, HRS, was amended during the 2013 Legislative Session so that association's 6-month "super priority lien" or special assessment would be paid upon closing of a foreclosure sale. Although the intent was clear when the language was revised for this purpose, a word – "purchaser" – was dropped from the final language.

This has created a problem in that one or more title companies are taking the position that an association's 6-month special assessment right or super priority lien rights only apply to a lender foreclosing on a property and being the highest bidder, but if a third-party is the successful bidder the 6-month special assessment is "wiped out" and not paid.

The proposed revisions seek to correct this error; therefore, CAI supports this.

Second, the proposal to add to §514B-146 (a)(1), HRS, the word "real property" before "taxes" does *clarify* that the only taxes that have priority over an association's lien are "real property taxes" which is *the intent of the law*. This clarification will assist with avoiding some taxing authorities attempting to argue from time-to-time that "all taxes" have priority over an association's lien. The correct legal position as affirmed by a number of courts in this State is that only "real property taxes" have priority over an association lien.

Lastly, we respectfully submit that the effective date of this Bill needs to be July 1, 2014 and not July 1, 2050.

Honorable Angus L.K. McKelvey, Chair  
Honorable Derek S.K. Kawakami, Vice Chair  
March 11, 2014  
Page 2 of 2

CAI represents the association industry, and **supports the passage of SB 2483, SD1 with the effective date to be July 1, 2014.** Thank you.

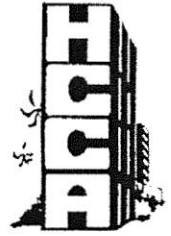
Very truly yours,

A handwritten signature in black ink, appearing to read 'CP', with a long horizontal flourish extending to the right.

Christian P. Porter



**Hawaii Council of Associations  
of Apartment Owners**  
**DBA: Hawaii Council of Community Associations**  
1050 Bishop Street, #366, Honolulu, Hawaii 96813



March 10, 2014

Rep. Angus McKelvey, Chair  
Rep. Derek S. K. Kawakami, Vice-Chair  
House Committee on Consumer Protection & Commerce

Re: SB2483, SD1 RELATING TO CONDOMINIUM ASSOCIATIONS  
Hearing: Wed., March 12, 2014, 2:10 p.m. , Conf. Rm. #325

Chair McKelvey, Vice-Chair Kawakami and Members of the Committee:

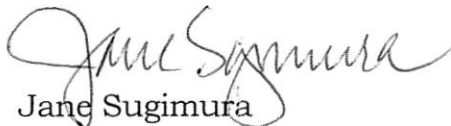
I am Jane Sugimura, President of the Hawaii Council of Associations of Apartment Owners (HCAAO dba HCCA).

HCAAO agrees with the intent and purpose of the SB2483 and agrees with the clarifications that are being sought by the bill and the revisions in SD1.

HCAAO is also in favor of a proposed revision at Part II of this bill that clarifies that condominium boards may only fill board vacancies with persons who will serve until the next annual meeting or duly noticed meeting. Attached to this testimony is proposed language for Part II of the bill for the Committee's consideration and this proposed revision reflects the collaborative efforts of HCAAO, CAI and the Hawaii State Association of Parliamentarians.

Accordingly, based on all of the above, we ask that you pass out this bill as revised as described herein.

Thank you for the opportunity to testify on this matter.

  
Jane Sugimura  
President

“(b) The board may not act on behalf of the association to amend the declaration or bylaws (sections 5143-32(a) (11) and 5143-108 (b) (7)), to remove the condominium from the provisions of this chapter (section 514B-47) , or to elect members of the board or determine the qualifications, powers and duties, or terms of office of board members (subsection (e)); provided that nothing in this subsection shall be construed to prohibit board members from voting proxies (section 5143-123) to elect members of the board; and provided further that **notwithstanding anything to the contrary in the declaration or bylaws**, the board may **only** fill vacancies in its membership to serve until the next annual or **duly noticed** special association meeting, **provided that the notice of the special meeting shall include notice of the election to fill said vacancy and that the meeting date shall be set on a date that allows sufficient time for owners to declare their intentions to run for election and to solicit proxies for that purpose**”

**Revisions are in bold and underscored.**



## Collection Law Section

**Chair:**  
Steven Guttman

**Vice Chair:**  
William J. Plum

**Secretary:**  
Thomas J. Wong

**Treasurer:**  
Arlette S. Harada

**Directors:**  
Lynn Araki-Regan  
Marvin S.C. Dang  
David C. Farmer  
Christopher Shea Goodwin  
Steven Guttman  
Arlette S. Harada  
James Hochberg  
Elizabeth A. Kane  
William J. Plum  
David B. Rosen  
Andrew Salenger  
Mark T. Shklov  
Yuriko J. Sugimura  
Thomas J. Wong  
Reginaid K.T. Yee

*Reply to:* STEVEN GUTTMAN, CHAIR  
220 SOUTH KING STREET SUITE 1900  
HONOLULU, HAWAII 96813  
TELEPHONE: (808) 536-1900  
FAX: (808) 529-7177  
E-MAIL: sguttman@kdubm.com

March 11, 2014

Representative Angus L. K. McKelvey, Chair  
Representative Derek S. K. Kawakami, Vice Chair  
Committee on Consumer Protection & Commerce

**RE: Senate Bill 2483, SD1, Proposed HD1  
Hearing Relating to Condominium Associations on  
Wednesday, March 12, 2014 at 2:10 PM in  
Conference Room 325**

My name is Arlette Harada and I am testifying in favor of Senate Bill 2483 on behalf of the Collection Section of the Hawaii State Bar Association. **The comments and recommendations submitted herein reflect the position of the Collection Section of the HSBA. The position has not been reviewed or approved by the HSBA Board of Directors, and is not being endorsed by the Hawaii State Bar Association.**

The Collection Section urges you and your colleagues to vote in favor of: 1) clarifying the provision of the condominium act setting forth the priority of liens so that only **real property tax** liens on the property which is the subject of the foreclosure and mortgages of record recorded prior to the condominium association's notice of lien would have a senior lien status against the condominium association's lien; and 2) allowing condominium associations to collect six (6) months of assessments against both mortgagee purchasers and third party purchasers in foreclosure. The Collection Section takes no position regarding the amendment proposed in HD1 regarding election of directors.

My practice is in the area of collection and foreclosure for condominium and homeowner associations. One of the areas that has been up in the air for several years has been whether other types of tax liens not for the property itself but recorded against the property being foreclosed, such as for income, withholding or general excise taxes, are senior or junior to recorded condominium notices of lien. Thus far, we have been able to work out such issues with the deputy attorney generals for the State tax office. However, I can foresee a dispute arising where we may not be able to work out the distribution of the sales proceeds. SB 2843 will clarify that only real



Testimony on Senate Bill 2483, SD 1, Proposed HD1

March 11, 2014

Page 2

property taxes against the property have senior lien status along with prior recorded mortgages of record. Unlike state tax liens, real property taxes, like association assessments, add value to condominium properties by providing services or improvements to the project and surrounding neighborhood.

The second issue addressed by the bill would change the provisions of Hawaii Revised Statutes 514B-146(g), (h) and (i) to apply to third party purchasers as well as mortgagee purchasers at foreclosure. The law prior to the 2013 changes required payment of six (6) months of the delinquent assessments at the time of purchase of the unit by third party purchasers and at the time of resale for mortgagee purchasers. The 2013 changes eliminated the time condominium associations needed to wait to obtain the six months of assessments for mortgagee foreclosures. However, due to last minute changes in the bill, the need for third party purchasers to pay the six months of assessments was eliminated. SB 2483 would put back the requirement that third party purchasers, like mortgagee purchasers, pay the six months of assessments.

The application of the language in the 2013 amendment only to mortgagees purchasing in foreclosure means that when a third party purchases at a mortgagee foreclosure and the highest bid is not enough to even pay the mortgagee in full, the condominium association may not recover the six months of assessments. An anomalous situation results where the association can recover only when the mortgagee is the purchaser in foreclosure although in both situations, the association has not been paid for months or years by the delinquent owner. Hawaii Revised Statutes 514B-146(g), (h) and (i) were enacted to provide condominium associations with some recovery of the unpaid assessments given that the associations provide services for the foreclosed unit and maintain the project, which benefits any purchaser of the unit in foreclosure.

For the above reasons, the Collection Section urges the Committee to vote in favor of Senate Bill 2483. If you have any questions, I would be happy to answer them or you may reach me at 523-0702.

Very truly yours,



Arlette S. Harada

Treasurer

Collection Law Section of the  
Hawaii State Bar Association

cc: Steven Guttman, Chair, Collection Law Section  
Patricia Mau, Executive Director, Hawaii State Bar Association

888 Mililani Street, 2<sup>nd</sup> Floor  
Honolulu, Hawaii 96813-2918  
Telephone: (808) 523-0702  
March 11, 2014

HOUSE COMMITTEE ON CONSUMER PROTECTION AND COMMERCE  
REGARDING SENATE BILL 2483

Hearing Date: WEDNESDAY, March 12, 2014  
Time : 2:10 p.m.  
Place : Conference Room 325

Chair McKelvey, Vice Chair Kawakami, and Members of the Committees,

My name is John Morris and I work as an attorney representing condominium and other homeowner associations. I am testifying in support of SB2483, SD1, Proposed HD1, which makes worthwhile changes to the condominium law relating to liens. I question, however, the benefit of section 3 of the bill.

Section 2, item 1 of the bill clarifies decades of confusion by making it clear that only real property tax liens, not all tax liens, are prior to a condominium association's lien. The priority of the association's lien exists because the association pays for the maintenance and many of the services (e.g., elevators, landscaping, cleaning, etc.) that add value to the unit against which the association claims its lien. The priority given to real property taxes recognizes a similar principle: real property taxes provide many of the services (roads, fire, police, etc.) that add value to the property that pays the real property taxes. In fact, real property tax liens are given priority over the association's lien for that reason.

In contrast, other taxes, such as income taxes, sales taxes, etc., do not have the same connection to the unit/property against which the association and county real property tax departments claim their liens. Therefore, those other types of taxes should not have priority over the association's lien.

Section 2, item 2 of the bill makes a worthwhile change by clarifying that, anyone, not just a mortgagee, who purchases a unit at a foreclosure auction is responsible for paying the association's six-month priority lien. That priority lien guarantees payment of at least six months of maintenance fees to an association in any foreclosure, even if the lender is not paid in full. That priority lien recognizes that the

TESTIMONY REGARDING SENATE BILL 2483, SD1, Proposed HD1

March 11, 2014

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association provides significant value in maintaining and properly repairing the unit that is the subject of the foreclosure and should therefore have a guaranteed recovery of six months of maintenance fees in any foreclosure.

Associations previously lobbied long and hard for that six-month priority lien. Unfortunately, a change in the 2013 legislative session indicated that the association could only claim the six-month priority lien from a mortgagee who purchased a unit in foreclosure, not from anyone else who purchased the unit. Section 2, item 2 of the bill restores the former wording of the law to confirm that anyone who purchases a unit in foreclosure is liable for the association's six-month priority lien.

Section 3 of the bill may create more problems than it solves. There seems to be a valid purpose in amending section 514B-106(b) to clarify that the law permits boards of directors to appoint directors to fill vacancies only until the next association meeting. The words "duly noticed" seem to have little benefit.

Many bylaws of associations permit the board to appoint directors to fill a vacancy for the remainder of the term of the vacancy. Nevertheless, it seems advisable that the owners, rather than the board, should make that decision for the long term. For that reason, since 2006, section 514B-106(b) has permitted boards to appoint directors until the next association meeting, so the owners can make that choice.

Despite the clear wording of that section, since 2006 there seems to have been some confusion on this point. Therefore, adding the word "only" to that section helps confirm the legislative intent.

In contrast, adding the words "duly noticed" may only create confusion. Special meetings are not common, especially special meetings just to appoint a new director, whereas annual meetings occur at least once a year. Therefore, it seems more than likely that, in the typical case, the board will appoint a director until the next annual meeting but will not call a special meeting just to have the owners vote on a replacement director.

Moreover, the law and Robert's Rules are already clear that the notice of a special meeting must state the subjects for the meeting and no other subjects can be considered at that special meeting. Therefore, adding the words "duly noticed" seems to add very little to the equation and will probably create confusion.

TESTIMONY REGARDING SENATE BILL 2483, SD1, Proposed HD1

March 11, 2014

Page 3

Please contact me at 523-0702 if you have any questions. 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