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September 19, 1995

MEMORANDUM

TO: Condominium Apartment Owners

FROM: Real Estate Commission

SUBJECT: Budget and Reserves Law for Condominium AOA and  
Increased Maintenance Fees

The condominium law is based on self-governance, owner enforcement, and majority rule. With respect to condominium reserves, it is important to note that condominium associations require that all condominium owners share in the expense of the common elements, as they share in the ownership and use of the common elements which generally includes roofs, exterior walls of units, grounds, roadways, buildings, parking lots or garages, and the like, unlike single family dwellings.

In the past, many associations failed to set aside funds for future repairs. That failure is why the Legislators passed the condominium budget and reserve laws (Act 132, SLH 1991). In years past and less presently, many owners complained to the Legislature and to the Real Estate Commission about large special assessments for major replacement and repairs because of either no or inadequate reserves. The record special assessment reported is \$42,500 per condominium owner, although most have been in the range of \$5,000 to \$20,000 per condominium owner. Payment for these special assessments by each condominium owner had to be accomplished in a short period of time, with two years the maximum period reported. In addition, many owners complained about damage to their individual apartments and its contents (example: water infiltration and termites) because of their association's lack of funds to repair or replace the common elements that caused the damage.

All condominium associations face the problem of high and ever increasing Costs to maintain a condominium project, including reserves. To compound the problem, a number of condominium boards cannot, or will not, make "hard and unpopular" decisions of raising maintenance fees to meet this problem and facing any criticism.

The law requires condominium association boards to study the project's particular maintenance and replacement needs of the common elements and to collect and establish reserves so that funds will be on hand when repairs and replacements are needed as well as emergencies. The law was enacted to provide relief for the vast majority of condominium associations, although a good number of well-managed condominium associations were already providing for reserves. If the reserves are properly calculated, each owner's share should only be what the owner ought to be putting aside each month for the true cost for repairs and replacements. The law tries to prevent owners from taking value out of a condominium property by underfunding reserves, selling out, and leaving subsequent purchasers to pay for the underfunding.

in response to complaints by some condominium owners that they could not afford the increase in monthly maintenance fees due to the reserves law, the Legislature passed Act 189, SLH 1992. The Act allowed a minimum 50' funding of reserves instead of \$100, extended the time period to fund the reserves to the end of 1999, and extended the time period to fund reserves depleted by an emergency to three years.

Based on information received, it appears that some of the key factors that influence budget and reserves problems and increased maintenance fees are as follows:

1. The condominium project is old and/or is a high-maintenance project. Twenty years is about the time period that most well maintain projects face major repairs and replacements.

2. The condominium project has accumulated very little in reserve balance or had unexpected emergency expenditures. Emergency expenditures include court orders, legal fees that could not be foreseen, insurance premium increases that could not be foreseen, and repairs or maintenance that could not be foreseen.

3. The condominium project's construction costly to maintain and replace. Usually wood construction are considered costly to maintain, repair and replace, especially if coupled with termite and dry rot problems.

4. The design of the structure and common elements may be costly to maintain, repair and replace, especially if the project consists of a good number of apartments in numerous separate structures, townhouse style, numerous walkways, stairwells, driveways, recreational areas, large or multiple parking areas, trash receptacle areas, and/or large square footage of land. As an example: a high-rise condominium with the same number of

apartments of identical size would normally require less reserve funds for the roof and the common areas than a townhouse-type project on a number of acres of land.

5. If the funding for the reserves was started (and continued) from the condominium project's first year of occupancy, then the monthly portion of the maintenance fees for reserves would be substantially less than a project who started reserve funding in its tenth year. It should be noted, that a number of condominium associations have reported collecting reserves for fifteen years and more.

6. Any delay in confronting and controlling reserve situations will not change the condominium association's need for repair or replacement or the common elements nor the need for funds. The Commission's research reflects that those condominium associations deciding on 50% funding of reserves and/or are substantially underfunded, especially if they face major common area repairs and replacements in the near future, will have to dramatically increase maintenance fees, make special assessments and/or take out a loan.

Should you have any questions, please call a Condominium Specialist at (808) 586-2646.