SCWC-17-0000145

IN THE SUPREME COURT OF THE STATE OF HAWAI'I

GILBERT V. MALABE and DAISY D. MALABE, Petitioners / Plaintiffs-Appellants, vs. ASSOCIATION OF APARTMENT OWNERS OF EXECUTIVE CENTRE, by and through Its Board of Directors; DOE DEFENDANTS 1-10, Respondent / Defendant-Appellee.	CIVIL NO. 16-1-2256 (Declaratory Relief and Damages) **PETITIONERS/PLAINTIFFS - APPELLANTS' SUPPLEMENTAL BRIEF RE: SB 551, CD 1; APPENDICES "A" – "G"; CERTIFICATE OF SERVICE**

PETITIONERS/PLAINTIFFS-APPELLANTS' SUPPLEMENTAL BRIEF RE SB 551, CD 1; APPENDICES "A" – "G";
CERTIFICATE OF SERVICE

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Table of Contents

Table of Authorities

Supreme Court Cases

Federal Cases

State Cases

Federal Statutes

Hawaii Revised Statutes

Other

PETITIONER / PLAINTIFFS-APPELLANTS' SUPPLEMENTAL BRIEF

I. INTRODUCTION

In 2010, Defendant Association of Apartment Owners of Executive Centre ("AOAO") enforced its lien on the condominium apartment owned by Petitioners/Plaintiffs-Appellants Gilbert V. Malabe and Daisy D. Malabe ("Malabes") by conducting a nonjudicial foreclosure using *Hawaii Revised Statutes* ("HRS") § 667-5 ("Part I").[1] Prior to its repeal in 2012, Part I's plain language permitted a nonjudicial foreclosure only where a mortgage expressly contained a power of sale. *Santiago v. Tanaka*, 137 Hawai'i 137, 154-55, 366 P.3d 612, 629-30 (2015); *Lee v. HSBC Bank USA*, 121 Hawai'i 287, 289-90, 218 P.3d 775, 777-78 (2009). AOAO is not a mortgagee of the Malabes' property and never held a mortgage containing a power of sale. Accordingly, the Intermediate Court of Appeals ("ICA") correctly held that the complaint filed by the Malabes sufficiently stated a claim for wrongful foreclosure against AOAO. SB 551 CD1, which became law as Act 282 on July 10, 2019 ("Act 282"), does not change this outcome because it does not give AOAO, or any other condominium association, a mortgage containing a power of sale as is required by Part I.[2] Moreover, to the extent Act 282 retroactively eliminates the requirement for a mortgage or eliminates the Malabes' claim for wrongful foreclosure, it is unconstitutional.

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[1] All references herein to HRS § 667-5 or to Part I are to HRS § 667-5, as amended in 2008, unless otherwise indicated.

[2] Act 282 was first introduced as SB 551 on January 18, 2019. On March 5, 2019, it was received by the House as SB 551, SD 1, and on March 12, 2019, it was passed by the House Committee on Consumer Protection with amendments as SB 551, HD1. On April 5, 2019, it was passed by the House Committee on Judiciary as SB 551, HD2. That version was rejected by the Senate, and on April 25, 2019, a conference committee consisting of members of the House and Senate passed the version designated SB 551, CD 1, which became law as Act 282. Prior to the version that became Act 282, no version of SB 551 mentioned Part I or attempted to retroactively approve the use of Part I by condominium associations. For the Court's convenience, copies of all of the aforesaid versions of SB 551 are attached as Appendices "A" – "D" to this Supplemental Brief.

Until 1998, condominium associations like AOAO could enforce their liens for unpaid common expenses only through judicial action. HRS § 514A-90, the condominium statute applicable to association liens for unpaid common expenses, only authorized enforcement of such liens "by action … in like manner as a mortgage of real property." Additionally, although Part I provided a nonjudicial or power of sale foreclosure process, by its express terms, it could be used only "'when a power of sale is contained in a mortgage,'" which associations did not have.

In 1998, the legislature recognized associations' desire to conduct cost-effective nonjudicial foreclosures, but also a need to create consumer safeguards that Part I did not provide.[3] Accordingly, in 1998, the legislature enacted HRS §§ 667-21 to 42, known as Part II, giving associations the ability to conduct a "[a] power of sale foreclosure" so long as several enumerated consumer protection safeguards were followed. The legislature explained its intent: "[T]his measure provides an alternate nonjudicial foreclosure process which reduces the time and cost of the current foreclosure process and contains additional safeguards not required in the current power of sale foreclosure law [Part I] that are needed to protect the interests of consumers."[4] Consistent with Part II's creation, the next year the Legislature amended HRS § 514A-90 of the condominium statute to expressly allow an association lien to be foreclosed "by action or by non-judicial or power of sale foreclosure procedures set forth in chapter 667 … in like manner as a mortgage of real property."[5]

The 1998 and 1999 legislative changes gave AOAO the right to conduct a nonjudicial foreclosure under Part II. Part I remained unavailable to AOAO because AOAO did not hold a

[3] In 2012, Part I was repealed due to creditor abuse.
[4] Conf. Com. Rep. 75 on H.B. No. 2506 at p. 979.
[5] Act 236, SB 36 (1999) at 727.

mortgage on the Malabes' property, much less a mortgage containing a power of sale. Yet, rather than follow the consumer protection safeguards laid out in Part II, AOAO conducted a Part I nonjudicial foreclosure of the Malabes' apartment. Act 282 does not change the illegality of AOAO's conduct or the ICA's ruling below.

At most, Act 282 responds to the ICA's recent decision in *Sakal v. Ass'n. of Apt. Owners of Hawaiian Monarch*, 143 Hawai'i 219, 426 P.3d 443 (2018), which held that an association could conduct a Part II nonjudicial foreclosure only if a written document (e.g., the association's governing documents) provided a power of sale. Because many associations' governing documents do not contain such a provision, Act 282 incorporates by statute a power of sale into those documents so associations may properly conduct Part II and Part VI nonjudicial foreclosures. However, Parts II and VI are not at issue in this case. Part I is at issue, and Part I expressly requires that the power of sale be "contained in a mortgage." Act 282 does not (because it cannot) retroactively give associations a mortgage necessary to use Part I. Accordingly, despite Act 282's passage, AOAO's use of Part I remains unlawful and the ICA's decision sound. To the extent, Act 282 is found to eliminate the Malabes' claims, it is unconstitutional and unenforceable.

II. LEGAL STANDARD

When construing the meaning of a statute, the Court must start with the language of the statute. If the plain language is unambiguous, the Court must give effect to that language. *Hungate v. Law Office of David B. Rosen*, 139 Hawai'i 394, 401, 391 P.3d 1, 8 (2017). "'[I]mplicit in the task of statutory construction is our foremost obligation to ascertain and give effect to the intention of the legislature, which is to be obtained primarily from the language contained in the statute itself.'" *Id.* (quoting *Citizens Against Reckless Dev. v. Zoning Bd. of*

Appeals, 114 Hawai'i 184, 193, 159 P.3d 143, 152 (2007)). It is only when the words of a statute are ambiguous that the Court "'may resort to extrinsic aids in determining legislative intent, such as legislative history, or the reason and spirit of the law.'" *Id.* Courts must construe a statute in a manner consistent with its purpose and with reference to other laws regarding the same issue, rejecting interpretations that are absurd, unjust or clearly inconsistent with the purposes and policies of the statute. *Haole v. State*, 111 Hawai'i 144, 149, 140 P.3d 377, 382 (2006); *State v. McKnight*, 131 Hawai'i 379, 389, 319 P.3d 298, 308 (2013) (citation omitted).

Additionally, the Court generally does not hear questions raised for the first time on appeal that were not presented to the trial court. *Miller v. Leadership Hous. Sys.*, 57 Haw. 321, 325, 555 P.2d 864, 867 (1976). The Court should adhere to that general rule "unless and until justice otherwise requires." *Earl M. Jorgensen Co. v. Mark Constr., Inc.*, 56 Haw. 466, 476, 540 P.2d 978, 985 (1975). In determining whether justice otherwise requires, the Court should consider (1) whether the question requires additional facts, (2) whether resolution of the question will affect the findings of fact of the trial court, and (3) whether the question is of great public import. *Fujioka v. Kam*, 55 Haw. 7, 9, 514 P.2d 568, 570 (1973).

The Legislature just recently passed Act 282 into law, and therefore no court has reviewed its applicability to Part I nonjudicial foreclosures or the constitutionality of its potential retroactive effect. This Court may hear this issue as a question of first impression if it determines that it is a question of great public import. To the extent factual questions are raised, the Court should remand for further proceedings by the trial court.[6]

[6] For example, in its answering brief to the ICA, AOAO suggested that there may be a factual dispute as to whether the association bylaws gave AOAO a power of sale. Those governing docs are not part of this appeal. ICA Order at 7 n.7. Additionally, even if the bylaws give AOAO a power of sale, they cannot give AOAO the ability to use Part I to conduct a nonjudicial foreclosure because AOAO never had a mortgage.

III. STATEMENT OF THE CASE

A. Factual Background and Procedural History

In or around May of 2005, the Malabes purchased an apartment for $225,000 in the condominium project known as Executive Centre. ¶¶ 5-7.[7] To purchase the apartment, the Malabes obtained a loan from a bank for $180,000 secured by a mortgage on the apartment. ¶ 8. Sometime prior to December 2010, the Malabes fell behind on their common assessments to AOAO, prompting AOAO to file a lien for the delinquent amounts.

On December 17, 2010, to enforce its lien, the AOAO conducted a nonjudicial foreclosure of the Malabes apartment using HRS § 667-5, Part I, and sold the apartment to itself for an amount that did not constitute adequate consideration. ¶¶ 20-22. On January 4, 2011, AOAO executed a quitclaim deed as both the grantor and grantee. ¶ 22. The result of AOAO's foreclosure was that the Malabes lost their apartment but remained liable for the mortgage. ¶ 24. As of July 2016, AOAO still owned the Malabes' apartment. ROA at 74. After discovering that AOAO's conduct was unlawful in or around July 2016, the Malabes filed suit, alleging wrongful foreclosure and violation of Hawaii's unfair and deceptive practices act, HRS §§ 480 et seq. ("UDAP"). ¶¶ 30-44.

On February 17, 2017, the Circuit Court for the First Circuit ("Circuit Court") dismissed the Malabes' complaint and entered final judgment in favor of AOAO. ROA at 89-92. On March 9, 2017, the Malabes appealed. ROA at 97-98.

On November 29, 2018, the ICA reversed judgment on the wrongful foreclosure claim, finding that "the Malabes stated a cognizable claim for wrongful foreclosure against the AOAO for which some relief may be granted." ICA Opinion at 6. The ICA however, upheld the

[7] All "¶" cites are to the complaint, filed December 13, 2016, contained in the original Record on Appeal ("ROA").

dismissal of the Malabes' UDAP claim based on the four-year statute of limitations. *Id.* at 10. As to the wrongful foreclosure claim, the ICA held that under *Santiago*, *Lee*, and *Sakal*, AOAO could conduct a nonjudicial foreclosure under Part I only if it had a mortgage containing a power of sale. *Id.* at 3-6. Because the Malabes alleged AOAO did not have a mortgage containing a power of sale, they properly alleged a claim for wrongful foreclosure.

On May 9, 2019, this Court accepted the Malabes' petition for review of the UDAP claim, and on May 23, 2019, this Court accepted AOAO's petition for review of the wrongful foreclosure claim. On July 10, 2019, the Governor allowed Act 282 to become law without his signature. The Court subsequently granted the Malabes' request for supplemental briefing on the application of Act 282 to this case.

B. Hawaii's Foreclosure Laws

When AOAO foreclosed on the Malabes' apartment in December 2010, the authority of an association to foreclose a lien for unpaid assessments was governed by HRS Chapters 514A, 514B and 667. Chapter 514A, enacted in 1977 as the Condominium Property Act, applied to condominiums that were created prior to July 1, 2006. Chapter 514B, enacted in 2004, replaced Chapter 514A as the Condominium Property Act as of July 1, 2006.[8] Chapter 667 governed foreclosures and in 2010 consisted of Part I (HRS §§ 667-1 to 667-10) and Part II (HRS §§ 667-21 to 667-42).

Part I was originally enacted in the 19th century, long before condominiums existed. HRS § 667-1 of Part I permitted foreclosure by action, and HRS § 667-5 provided a nonjudicial foreclosure process where a mortgage contained a power of sale. By its express terms, HRS § 667-5 could only be used "when a power of sale is contained in a mortgage" and required the

[8] HRS § 514A-1.5 and § 514B-21.

foreclosing party to "give any notices and do all acts as are authorized or required by the power contained in the mortgage." Section 667-5 also required the mortgagee to "give notice of the … intention to foreclose the mortgage and of the sale of the mortgaged property" by publishing notice of public sale once a week for three successive weeks. The mortgagee could then hold a public sale no less than fourteen days after the final notice was published, allowing a nonjudicial foreclosure to take place in as little as 36 days.[9]

When Chapter 514A of the condominium statute was enacted in 1977, HRS § 514A-90, authorized associations to enforce a lien for unpaid common assessments only "by action by the manager or board of directors, acting on behalf of the apartment owners, in like manner as a mortgage of real property."[10] This meant that associations could only enforce their liens by judicial action pursuant to HRS § 667-1 and could not use the nonjudicial process available to mortgagees in HRS § 667-5.

In 1998, the legislature passed Act 122, the "Alternate Power of Sale Foreclosure Process," codified at HRS §§ 667-21 through 667-42 (Part II), to provide associations a nonjudicial foreclosure process.[11] Because of concerns regarding the rights of homeowners, the legislature included substantial consumer protection safeguards in Part II that were not contained in Part I.[12] They included: (1) at least sixty days for the homeowner to cure any default (HRS §667-22(a)(6)); (2) actual service of the notice of default on the homeowner in the same manner as service of process (HRS §667-22(c)); (3) at least sixty days advance notice before the public sale (HRS § 667-25); (4) at least two open houses of the mortgaged property (HRS § 667-26); (5) signature by the homeowner of the conveyance document (HRS § 667-31(a) [1998]); and (6)

[9] HRS § 667-5.
[10] HRS §514A-90 (1998).
[11] H.B. 2506, H.D. 1, 19th Leg., Reg. Sess. (1998).
[12] *Id.*

a bar against deficiency judgments (HRS § 667-38). The nonjudicial foreclosure process set out in Part II was specifically made available to condominium associations where "a law or a written document" provided the association with a power of sale:

> A power of sale foreclosure under this part may be used in certain non-mortgage situations where a law or a written document contains, authorizes, permits, or provides for a power of sale, a power of sale foreclosure, a power of sale remedy, or a nonjudicial foreclosure. These laws or written documents are limited to those involving time share plans, condominium property regimes, and agreements of sale.[13]

When the legislature enacted Part II, it failed to change HRS § 514A-90 of the condominium laws, which continued to provide that the lien for unpaid assessments had to be foreclosed "by action… in like manner as a mortgage of real property."[14] To bring the statutes into harmony, the legislature sought to "clarify that associations of apartment owners may enforce liens for unpaid common expenses by non-judicial and power of sale foreclosure procedures, as an alternative to legal action."[15] In 1999, pursuant to Act 236, the legislature amended HRS § 514A-90 to provide that the lien of an association could be foreclosed "by action or non-judicial or power of sale procedures set forth in chapter 667."[16] In addition, Act 236 added HRS § 514A-82(b)(13), by which the bylaws of all condominium projects existing as of January 1, 1988, or created thereafter were deemed to include the following language:

> A lien created pursuant to section 514A-90 may be enforced by the association in any manner permitted by law, including nonjudicial or power of sale foreclosure procedures authorized by chapter 667.[17]

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[13] HRS § 667-40.
[14] HRS § 514A-90 (1998).
[15] 1999 Act 236, §1.4.
[16] Hereafter, HRS § 514A-90 refers to HRS § 514A-90 (1999), which remained unchanged between 1999 and 2010.
[17] When Chapter 514B became the Condominium Property Act in 2004, it included HRS § 514B-146(a), which repeated verbatim the language of HRS § 514A-90.

This provision was intended to provide the "law or written document" that HRS § 667-40 required for associations to use Part II's nonjudicial foreclosure process. It was not intended to give associations a mortgage containing a power of sale for the use of Part I.

In 2012, after an extensive review by the Mortgage Foreclosure Task Force, the legislature repealed HRS § 667-5 in its entirety due to mortgagees' abusive use of Part I's nonjudicial process to strip consumers of their homes. This left Part II as the only process for a power of sale or nonjudicial foreclosure and added an alternative power of sale process specifically for associations, known as Part VI (HRS §§ 667-91 to 667-104), which contains many of the consumer safeguards that originated in Part II.[18] Nonetheless, before its repeal in 2012, associations, including AOAO, conducted hundreds of nonjudicial foreclosures under Part I even though Part II was expressly available to them. The associations used Part I because they did not want to follow the consumer safeguards required under Part II.

C. The Passage of Act 282

On July 10, 2019, SB 551, CD 1 became law as Act 282. In enacting Act 282, the legislature found "it is crucial that condominium associations be able to secure timely payment of dues to provide services to all residents of a condominium community."[19] The legislature further recognized that since 1999, when it amended HRS § 514A to clarify its intent that associations could conduct judicial and nonjudicial foreclosures consistent with HRS § 667, associations "have been authorized to conduct nonjudicial foreclosures regardless of the presence or the absence of power of sale language in an association's governing documents."[20] To this

[18] House Bill No. 1875; HRS §§ 667-91 – 667-101.
[19] Act 282 at 2.
[20] *Id.*

end, the legislature found that the court in *Sakal* misread the statutes by holding that to use Part II an association's governing documents had to have an express power of sale.[21]

To clarify its intent, Act 282 confirms "that condominium associations should be able to use nonjudicial foreclosure to collect delinquencies regardless of the presence or absence of power of sale language in an association's governing documents."[22] Accordingly, Act 282 amends HRS § 514B-146 to state that an association's lien "may be foreclosed by action or by nonjudicial or power of sale foreclosure, regardless of the presence or absence of power of sale language in an association's governing documents…."[23] Act 282 also "provides an additional consumer protection by requiring the foreclosing association to offer mediation with any notice of default and intention to foreclose and the procedures when mediation is chosen by the consumer."[24]

While Act 282 states that it "shall be applied retroactively to any case, action, proceeding, or claim arising out of a nonjudicial foreclosure under section 667-5 (repealed June 28, 2012), Hawai'i Revised Statutes, and parts II and VI of chapter 667," Act 282 also continues to recognize the difference between powers of sale that arise in a mortgage and powers of sale applicable to associations, and does not expressly provide associations with a mortgage containing a power of sale.[25] In amending the definition of "power of sale" under HRS § 667-1, the legislature maintained the definition applicable to mortgagees – power of sale means "[t]he mortgage contains, authorizes, permits, or provides for a power of sale, a power of sale foreclosure, a power of sale remedy, or a nonjudicial foreclosure" – but added a definition

[21] *Id.* at 6.
[22] *Id.*
[23] *Id.* at 11.
[24] *Id.* at 6.
[25] *Id.* at 13.

applicable to associations – power of sale also means, "[f]or the purposes of part VI, an association enforces its claim of an association lien, regardless of whether the association documents provide for a power of sale, a power of sale foreclosure, a power of sale remedy, or a nonjudicial foreclosure."[26] Thus, while Act 282 writes into an association's governing documents an express power of sale, it does not (and cannot) create a mortgage containing a power of sale for the association.

Indeed, the legislature expressly stated that Act 282 should not be applied so as to impair any contract existing as of the effective date of this Act in a manner violative of either the Hawaii State Constitution or Article I, section 10, of the United States Constitution.[27] The legislature also provided a severability clause providing that if any provision is held invalid, it will not affect the validity of other provisions.[28]

On July 9, 2019, Governor Ige issued a press release indicating that he would allow SB 551, CD 1 to become law without his signature, stating: "Although there are concerns with the retroactivity [of SB 551], the prospective application has utility and value. The severability clause in this measure will allow appropriate judicial review."[29] The next day, Governor Ige wrote a letter to the legislature stating that while he has "concerns because the bill expressly states that it will apply retroactively, we recognize the need for foreclosing associations to have clarity after Sakal."[30]

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[26] *Id.* 12-13.
[27] *Id.* at 13.
[28] *Id.*
[29] https://governor.hawaii.gov/newsroom/latest-news/office-of-the-governor-news-release-governor-ige-vetoes-18-measures-two-will-become-law-without-his-signature/, attached as Appendix "F".
[30] A copy of the July 10, 2019 letter from Governor Ige to the legislature is attached as Appendix "G".

IV. LEGAL ARGUMENT

A. Act 282 Does Not Eliminate the Malabes' Claim for Wrongful Foreclosure

1. Part I Requires a Mortgage that AOAO Does Not Have

The Malabes alleged that AOAO conducted a nonjudicial foreclosure of their apartment using Part I. ¶ 20. Part I permits a nonjudicial foreclosure "[w]hen a power of sale is contained in a mortgage, and where the mortgagee, the mortgagee's successor in interest, or any person authorized by the power to act in the premises, desires to foreclose under power of sale…." HRS § 667-5(a).

This Court has long recognized that Part I's plain language does not give a statutory right to mortgagees to foreclose. Rather, Part I creates a right to conduct a nonjudicial foreclosure only when the contractual provisions of a mortgage permit it. In *Santiago,* the Court explained:

> Prior to its repeal in 2012, HRS § 667-5 authorized the non-judicial foreclosure of mortgaged property only "[w]hen a power of sale is contained in a mortgage." HRS § 667-5(a). This court examined HRS § 667-5 in *Lee v. HSBC Bank USA*, 121 Hawai'i 287, 218 P.3d 775 (1999), and found that it "authorize[d] nonjudicial foreclosure under power of sale clause contained in a mortgage." *Id.* at 289, 218 P.3d at 777 (emphasis added). In *Lee*, the plaintiffs argued, and this court agreed, that "no state statute creates a right in mortgagees to proceed by non-judicial foreclosure; the right is created by contract." *Id.* at 292, 218 P.3d at 780.
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> Thus, this court has held that HRS § 667-5 does not provide the nonjudicial power of foreclosure but only allows its creation, if the parties choose to do so, within the four corners of a contract. *See id.*; *see also Apao v. Bank of N.Y.*, 324 F.3d 1091, 1096 (9th Cir. 2003) (finding that HRS § 667-5 "did not confer the power of sale, but merely authorized the parties to contract for the express terms of foreclosure upon default").

137 Hawai'i at 154-55, 366 P.3d at 629-30; *see also Mount v. Apao*, 139 Hawai'i 167, 176, 384 P.3d 1268, 1277 (2016) (holding that a nonjudicial foreclosure under HRS § 667-5 "is in the nature of a contractual self-help remedy … and is not 'an action in law or a suit in equity'").

Based on this reasoning, the Court in *Santiago* invalidated a Part I nonjudicial foreclosure conducted by a mortgagee because the mortgage did not expressly give the mortgagee the right to conduct a nonjudicial foreclosure. 137 Hawai'i at 155, 366 P.3d at 630. The *Santiago* court held: "As written, HRS § 667-5 is the only source from which the Mortgage's power to foreclose may be derived. However, HRS § 667-5 does not independently provide for a power of sale, and, as noted, it only authorizes a sale where such a power is contained in a mortgage. *Lee*, 121 Hawai'i at 289, 218 P.3d at 777. Thus, the Mortgage does not provide for a power of sale that would have authorized [defendant]'s nonjudicial foreclosure." *Id.* (emphasis in original).

Similarly, when AOAO foreclosed on the Malabes' apartment using Part I, AOAO did not hold a mortgage containing a power of sale. ¶ 13. Relying on the express language of Part I and this Court's prior decisions in *Santiago* and *Lee*, the ICA below properly concluded that the Malabes stated a claim for wrongful foreclosure because "HRS § 667-5 (repealed 2012) did not grant a power of sale but merely authorized use of certain nonjudicial *procedures* in order to effect a foreclosure only '[w]hen a power of sale [was] contained in a mortgage.'" ICA Order at 5-6 (quoting HRS § 667-5 (repealed 2012) and citing *Santiago*, 137 Hawai'i at 154, 366 P.3d at 629; *Lee*, 121 Hawai'i at 289, 218 P.3d at 777).

The legislative history supports the ICA's conclusion that without a mortgage containing a power of sale, AOAO could not use Part I to foreclose. The legislature viewed Part I negatively and never intended for associations to use it to conduct nonjudicial foreclosures. As discussed above, when the legislature enacted Part II for express use by associations, the legislature included substantial safeguards to protect consumers from abusive collection practices that were

occurring under Part I. The legislature believed that these safeguards were "needed to protect the interests of consumers."[31]

The legislature viewed Part I as "one of the most draconian (nonjudicial foreclosure statutes) in the country" that "was originally designed to make it easy to take land away from Native Hawaiians."[32] When the legislature repealed HRS § 667-5 in 2012, its stated intent was to "provide a single nonjudicial foreclosure process under Part II of [chapter 667]."[33] Given the legislature's desire to protect homeowners, it is illogical to conclude that after enacting Part II in 1998, the legislature intended that condominium associations could bypass the safeguards in Part II and instead use HRS § 667-5 under Part I. The legislature created Part II with consumer safeguards because it intended that associations use Part II – not Part I.

Accordingly, it is clear from the express language of HRS § 667-5, the holdings in *Santiago* and *Lee*, and the legislative history, that AOAO did not have a right to conduct a nonjudicial foreclosure of the Malabes' apartment pursuant to Part I because it did not have a mortgage containing a power of sale.

2. Act 282 Does Not Give AOAO a Mortgage

Act 282 does not change the conclusion arrived at by the ICA in this case. The only way for AOAO to properly use Part I is if it had a mortgage that contained a power of sale. While

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[31] *Aames Funding Corp. v. Mores*, 107 Hawai'i 95, 102, 110 P.3d 1042, 1049 (2005) (*quoting* Conf. Com. Rep. No. 75, in 1998 House Journal, at 979).

[32] 2011 House Journal – 59th Day, Conf. Com. Rep. No. 133 and S.B. No. 651, SD 2, CD 1. Representative Herkes is on record as stating that "And in the last 10 to 15 years [HRS § 667-5] had been the mechanism to non-judicially foreclose on homeowners, often without their knowledge and without providing them a fair opportunity to save their homes. In Act 48, we just put a stop to it. Now we've gotten rid of it." Conf. Com. Report No. 63-12, in 2012 House Journal, at 817.

[33] Conf. Com. Rep. 63-12, in 2012 House Journal, at 1631.

Act 282 may give AOAO a statutory grant of a power of sale in its governing documents to use Parts II and VI, Act 282 does not give AOAO a mortgage to use Part I.

Mortgages are contracts which transfer interests in real property as security for the performance of an act or subject to defeasance upon the payment of an obligation. HRS § 506-1; *Lpp Mortg. Ltd. v. Doctolero*, 142 Hawai'i 209, 416 P.3d 930 (Haw. App. 2018) (citing *Beneficial Hawaii, Inc. v. Kida*, 96 Hawai'i 289, 312, 30 P.3d 895, 918 (2001)). Liens for unpaid common expenses, by contrast, are created by HRS § 514A-90 or HRS § 514B-146(a), and are not contracts or mortgages. *United States Bank National Association v. AOAO of Makaha Valley Plantation*, 133 Hawai'i 512, 331 P.3d 490 (2014 Haw. App.) ("the AOAO's lien pursuant to HRS § 514B-146 is not based on a mortgage, but rather outstanding common expenses owed on the Unit."). Act 282 does not give associations mortgages or change their liens into mortgages. The AOAO's lien for the Malabes' unpaid common expenses is not the same thing as a mortgage, and Act 282 does not and cannot convert that or any other lien into a mortgage.

Indeed, in Act 282, the legislature continues to expressly recognize the difference between powers of sale contained in mortgages and powers of sale arising by virtue of other documents related to associations. Act 282 defines power of sale as:

> "Power of sale" or "power of sale foreclosure" means a nonjudicial foreclosure when:
>
> (1) The mortgage contains, authorizes, permits, or provides for a power of sale, a power of sale foreclosure, a power of sale remedy, or a nonjudicial foreclosure; or
>
> (2) For the purpose of part VI, an association enforces its claim of an association lien, regardless of whether the association documents provide for a power of

> sale, a power of sale foreclosure, a power of sale remedy, or a nonjudicial foreclosure.[34]

Therefore, the legislature did not intend to change the mortgage requirements of Part I. Instead, by definition, Act 282 gives an association the right to conduct a nonjudicial foreclosure, either through a mortgage giving the association a power of sale, or under Part II or Part VI with a statutory right to conduct that power of sale. AOAO did not have a mortgage containing a power of sale in 2010 at the time of the Malabes' foreclosure and still does not have one today, despite the passage of Act 282. The Malabes' claim for wrongful foreclosure based on AOAO's use of Part I, therefore, remains alive.

B. To the Extent Act 282 Retroactively Eliminates the Malabes' Claims under Part I, Act 282 is Unconstitutional

If the Court finds that Act 282 retroactively gives AOAO a mortgage containing a power of sale to use Part I, then the Court must assess whether such retroactive application is constitutional. *Landgraf v. USI Film Prods.*, 511 U.S. 244, 267-68. If a particular provision of Act 282 is found to be unconstitutional, it may be severed from the remainder of the statute. *State v. Pacquing*, 139 Hawai'i 302, 319, 389 P.3d 897, 913 (2016).

1. Act 282 Violates the Contracts Clause of the U.S. Constitution

The Contracts Clause of the U.S. Constitution provides, "no state shall . . . pass any . . . Law impairing the Obligation of Contracts." U.S. Const. art. I, § 10, cl. 1. This restriction "must be accommodated to the inherent police power of the State 'to safeguard the vital interests of its people.'" *Energy Reserves Group, Inc. v. Kansas Power & Light Co.*, 459 U.S. 400, 410 (1983) (quoting *Home Bldg. & Loan Assn. v. Blaisdell*, 290 U.S. 398, 434 (1934)). Thus, the Court must first determine "whether the state law has, in fact, operated as a substantial impairment of a

[34] Act 282 at 12-13.

contractual relationship." *In re Seltzer*, 104 F.3d 234, 236 (9th Cir. 1996). "This inquiry has three components: whether there is a contractual relationship, whether a change in law impairs that contractual relationship, and whether the impairment is substantial." *Id.* (quoting *Gen. Motors Corp. v. Romein*, 503 U.S. 181, 186 (1992)); *Anthony v. Kualoa Ranch*, 69 Haw. 112, 118-19, 736 P.2d 55, 60 (1987). "Total destruction of contractual expectations is not necessary for a finding of substantial impairment." *Energy Reserves Group*, 459 U.S. at 411.

"If the state regulation constitutes a substantial impairment, the State, in justification, must have a significant and legitimate public purpose behind the regulation,… such as remedying a broad and general social or economic problem." *Id.* at 411-412. "The requirement of a legitimate public purpose guarantees that the State is exercising its police power, rather than providing a benefit to special interests." *Id.* at 212.

In *Anthony*, the Court found that a Hawai'i statute violated the Contracts Clause because it substantially changed the contractual obligations of the parties under an existing lease agreement. The parties in *Anthony* had entered into a 30-year lease that allowed the lessee to remove all buildings erected on the leased property at his own cost at the termination of the lease. This contractual language reflected the law at the time the lease was signed. During the pendency of the lease, the Hawai'i legislature amended the law, requiring all lessors to pay fair market value to the lessee for leasehold improvements if the lessee did not remove them from the property. The purpose of the amended law was to "break[] up the oligopolistic landownership, and the inequality of bargaining power resulting therefrom." *Id.* at 118. In striking down the law as unconstitutional as applied to the facts in *Anthony*, the Court found that the statute created a substantial change in the contractual obligations of the parties and concluded: "This statute, as applied to leases already in effect, purely and simply, is an attempt by the legislature to change

contractual remedies and obligations, to the detriment of all lessors and to the benefit of all lessees, without relation to the purposes of the leasehold conversion act." *Id.*

Act 282 is similarly unconstitutional because it attempts to substantially change the Malabes' contractual rights as a mortgagor. A mortgage is a contract that transfers interests in real property as security for the performance of a contractual obligation for payment. HRS § 506-1; *Lpp Mortg.*, 142 Hawai'i 129. A mortgage cannot be created by statute.

The only mortgage contract the Malabes agreed to was with the mortgage bank. The Malabes did not agree to a mortgage with AOAO. To the extent the Malabes had a contractual relationship with AOAO it was as an association, not a mortgagee. By giving AOAO a mortgage containing a power of sale that did not exist, Act 282 significantly changes the Malabes' contractual relationship with AOAO. Indeed, as Part I contemplates, any mortgage that contains a power of sale should contain specified notice and other requirements to be followed in the event of a nonjudicial foreclosure. But the legislature makes no effort in Act 282 to include such additional contractual provisions. That is because its intent is not to create a mortgage for associations for use of Part I, but rather, simply to clarify associations' use of Parts II and VI.

Additionally, Act 282's retroactive application to Part I is not based on a legitimate public purpose. Part I has not existed since 2012 and therefore, is no longer used to conduct any nonjudicial foreclosures. The only purpose of Act 282's retroactive application to Part I is to eliminate AOAO's and other associations' liability in ongoing litigation to the detriment of homeowners and for the benefit of those associations. That is not a legitimate purpose. Given the language of Part I and this Court's prior decisions interpreting Part I's requirement that the power of sale must be contained in a mortgage - including Lee, which was decided in 2009, one year prior to the foreclosure in this case - associations were on notice that they could not use Part

I to conduct nonjudicial foreclosures. Act 282 is unconstitutional to the extent it applies retroactively to nonjudicial foreclosures brought by associations under Part I where no mortgage containing a power of sale existed.

2. Act 282 Violates the Separation of Powers Doctrine

On its face, Act 282 seeks to address the ICA's decision in *Sakal* by retroactively authorizing associations to conduct nonjudicial foreclosures under Parts II and VI "regardless of the presence or absence of powers of sale language in an association's governing documents."[35] To the extent it is designed to retroactively abolish the claims for wrongful foreclosure that homeowners presently have against associations that unlawfully used Part I, Act 282 violates the separate of powers doctrine.

In this regard, Section 5 of Act 282 declares that "this Act shall be applied retroactively to any case, action, proceeding, or claim arising out of a nonjudicial foreclosure under section 667-5 (repealed June 28, 2012), Hawaii Revised Statutes . . . that arose before the effective date of this Act." While the purpose of this provision is unclear, it cannot retroactively give associations a mortgage containing a power of sale sufficient to allow the use of Part I to conduct a nonjudicial foreclosure.

Act 282 is disingenuous. Its preamble implies that the intent of the 1998 and 1999 legislatures was to give associations authority to use any nonjudicial foreclosure process that existed, including Part I. It does this by selectively quoting only a portion of the enabling statute, which was HRS § 667-40. The preamble states:

> Additionally, the legislature finds that condominium associations, since 1999, have been authorized to conduct nonjudicial foreclosures regardless of the presence or the absence of power of sale language in an association's governing documents. Beginning in 1998 with the passage of Act 122, Session Laws of

[35] SB 551 at 13.

> Hawaii 1998, and codified in section 667-40, Hawaii Revised Statutes, condominium associations were authorized to conduct nonjudicial foreclosures if a "**law or a written document contains, authorizes, permits, or provides for a power of sale, a power of sale foreclosure, a power of sale remedy, or a nonjudicial foreclosure**."

The aforesaid passage, however, deliberately leaves out the words, "**A power of sale foreclosure under this part may be used in certain non-mortgage situations,**" which appear in the full text of HRS § 667-40 immediately before the underscored words in bold type in the passage quoted above. This language that is missing from Act 282's quote makes it clear that the 1998 legislature intended to authorize associations to use only the process contained in Part II , and not Part I. By deliberately leaving out the phrase that begins with "**A power of sale foreclosure under this part in certain non-mortgage situations,"** Act 282 falsely implies that the 1998 legislature authorized associations to use any and all nonjudicial foreclosure processes that existed, including Part I , when in fact the 1998 legislature did not.

To the extent this is an attempt by the current legislature to negate the prior decisions of this Court limiting the use of Part I to creditors holding mortgages containing powers of sale, Act 282 violates the separation of powers of doctrine. Under the federal and state constitutions, it is the function of the courts to determine legislative intent, and once that is done the legislature cannot attempt to set aside the judicial ruling through retroactive legislation. *Plaut v. Spendthrift Farm*, 514 U.S. 211 (1995); *Alakai Na Keiki, Inc. v. Matayoshi*, 127 Hawai'i 263, 296, 277 P.3d 988, 1021 (2012) (dissent); *State v. Brantley*, 99 Hawai'i 463, 483 (2002) (dissent) (cannot overrule by legislative enactment a prior authoritative Supreme Court opinion construing a statute). Clearly, SB 551 runs afoul of this principle.

In *Santiago*, the Court ruled that Part I, prior to its repeal, could only be used where a mortgage contains a power of sale. In *Lee*, the Court said that no statute creates a power of sale.

Pursuant to *Santiago* and *Lee*, therefore, the ICA ruled that AOAO was not authorized to use Part I to foreclose the lien on Malabes' apartment. To the extent Act 282 seeks to retroactively overturn these decisions, it is unconstitutional. *State v. Bani*, 97 Hawai'i 285, 291 n.4, 36 P.3d 1255, 1261 n.4 (2001) (citing *Del Rio v. Crake*, 87 Hawai'i 297, 304, 955 P.2d 90, 97 (1998) ("[T]he question as to the constitutionality of a statute is not for legislative determination, but is vested in the judiciary, and a statute cannot survive constitutional challenge based on legislative declaration alone.")

3. Act 282 Violates the Malabes' Rights to Due Process and Equal Protection

Act 282 also violates the due process and equal protection clauses of the Fourteenth and Fifth Amendments to the U.S. Constitution and Article 1, §§ 4, 5 and 20 of the Hawai'i State Constitution.

It is settled that due process must be provided before citizens can be stripped of their homes. *KNG Corp. v. Kim*, 107 Hawai'i 73, 80, 110 P.3d 397, 404 (2005). By its terms, and to provide even minimal protections against wrongful loss of property, Part I required that there be a breach of condition of the mortgage and that the creditor "give any notices and do all acts as are authorized or required by the power contained in the mortgage." *Lee*, 121 Hawai'i at 291. This included a notice of default and the amount needed to cure. *Matrix Fin. Servs. v. Campbell*, No. 24412, 2003 Haw. App. LEXIS 5, at *17 (App. Jan. 15, 2003). Moreover, that obligation is not satisfied merely by publishing notice of the foreclosure sale. *Klinger v. Kepano*, 64 Haw. 4, 635 P.2d 938 (1981).

Procedural due process requires that a party be given "notice and opportunity to be heard at a meaningful time and in a meaningful manner. *Ek v. Boggs*, 102 Hawai'i 289, 298, n75 P.3d 1180, 1189 (2003). Where mortgage foreclosures under Part I are involved, it is the mortgage

rather than any statute that provides for how notice of default is to be given, where such notices are to be sent, and what the debtor is required to do to cure the default. *Santiago*, 137 Hawai'i at 155; *Lee*, 121 Hawai'i at 289-92. Since they do not hold mortgages, therefore, AOAO and other associations could not and did not provide the notice of default and opportunity to cure that Part I and the federal and state constitutions required. Instead, AOAO and other associations did nothing more than to publish notice of their intent to sell their homeowners' apartments, which does not constitute the notice required by Part I "to protect the mortgagor from a wrongful loss of property." *Lee*, 121 Hawai'i at 291-92.

To the extent Act 282 retroactively permits AOAO and other condominium associations to use Part I without a mortgage, therefore, it does so without a mechanism for providing homeowners with the notice that Part I and due process requires. *Boddie v. Connecticut*, 401 U.S. 371, 376-78 (1971) (Due process of law requires notice and a right to be heard.); *Cleveland Bd. Of Education v. Loudermill*, 470 U.S. 532, 542 (1985) ("An essential principle of due process is that a deprivation of life, liberty, or property 'be preceded by notice and opportunity for hearing appropriate to the nature of the case.'"); *Mullane v. Central Hanover Bank & Trust Co., 339 U.S. 306, 313 (1950); Minton v. Quintal*, 131 Hawai'i 167, 185, 317 P.3d 1, 19 (2013) ("The requirement of procedural due process exists to protect individuals against the state's deprivation of liberty and property interests.") Act 282, therefore, is unconstitutional. *United States v. James Daniel Good Real Property*, 510 U.S. 43 (1993) (Forfeiture of real property without notice is unconstitutional). Act 282, therefore, is unconstitutional.

Generally, state action has to be involved before a violation of the right to due process can be found. *Flagg Bros. Inc. v. Brooks*, 436 U.S. 149 (1978). Here, it is the very act of the legislature in passing a law that deprives homeowners of their right to due process that is being

scrutinized. Accordingly, the requirement for state action is met. *Lugar v. Edmondson Oil Co.*, 457 U.S. 922 (1982). (Title 42 U.S.C. § 1983 provides remedy for deprivation of constitutional rights under color of state law.) In addition, state action is also implicated because the associations that benefit from Act 282 are deemed to have acted both under state law and the imprimatur of the state. *Burton v. Wilmington Parking Authority*, 365 U.S. 715 (1961) (Symbiotic relationship between state and private entity sufficient to constitute state action). Thus, there is no impediment to finding that Act 282 violates due process.

Furthermore, Act 282 also violates the right to equal protection guaranteed by the federal and state constitutions because it discriminates against two classes of individuals. First, it treats associations differently from all other lien holders as it allows associations to use Part I even though they do not hold mortgages containing powers of sale, while denying that right to other lien holders, such as holders of mechanic's and materialman's liens. *Shibuya v. Architects Hawaii*, 65 Haw. 26, 647 P.2d 276 (1982). Second, it improperly grants immunity to AOAO and other associations that committed wrongful foreclosures while discriminating against homeowners by arbitrarily, capriciously and unreasonably depriving them of their property rights. *Fujioka v. Kam*, 55 Haw. 7, 514 P.2d 568 (1973) (citing *Truax v. Corrigan*, 257 U.S. 312 (1921)); *Shibuya v. Architects Hawaii, Ltd.*, 65 Haw. 26, 43, 647 P.2d 276, 288 (1982) ("Equal protection is a requisite "both in the privileges conferred and the liabilities imposed.")

In *Truax v. Corrigan*, a restaurant sought to enjoin picketing employees and their union from threatening and harassing other employees and patrons of the restaurant. The lower court dismissed the complaint because a state statute prohibited issuance of injunctive relief in a labor dispute. On appeal, the United States Supreme Court ruled that the state statute violated the equal protection clause of the United States Constitution because it carved out a specific class of

people for protection while failing to protect the property rights of the restaurant owner. The Supreme Court said:

> Immunity granted to a class, however limited, having the effect to deprive another class, however limited, of a personal or property right, is just as clearly a denial of equal protection of the laws to the latter class as if the immunity were in favor of, or the deprivation of right permitted working against, a larger class.

Truax, 257 U.S. 312, 333.

Here, applying Act 282 retroactively to Part I nonjudicial foreclosures by associations wrongfully deprives homeowners like the Malabes of their property rights while providing immunity to associations. This violates the right to equal protection.

4. Act 282 Impermissibly Allows Property to be taken without Adequate Compensation

Act 282 also eliminates the claims of former homeowners without providing them just compensation as the Fifth Amendment of the U.S. Constitution and Article 1, § 20 of the Hawai'i State Constitution require. *Lugar*, *supra Louisville Joint Stock Land Bank v. Radford*, 295 U.S. 555 (1935) (If public interest requires and permits the taking of private property, resort must be had to proceedings by eminent domain so the burden of the relief afforded the public interest may be borne by the public); *Ketchum v. Alameda County*, 811F.2d 1243, 1245 (9th Cir. 1987); *Resolution Trust Corp. v. Fleischer*, 257 Kan. 360, 892 P.2d 497 (1995) (Retroactive legislation abolishing vested right to pursue claims for negligence and breach of fiduciary duty unconstitutional). Retroactive application of a law that changes the substantive vested rights of a party is prohibited. *Kaho'Ohanohano v. Dep't of Human Servs.*, 117 Hawai'i 262, 312, 178 P.3d 538, 588 (2008) (constitutionality of retroactive elimination of tort claim).

This Court has long held that Part I can only be used by a mortgagee holding a mortgage containing a power of sale. Additionally, state and federal courts, including the ICA, have

already ruled that it was unlawful for creditors who did not hold mortgages containing powers of sale to use Part I and that their victims are entitled to restitution and damages. To the extent Act 282 eliminates those claims without providing adequate compensation in exchange, Act 282 is unconstitutional.

V. CONCLUSION

The Court should deny AOAO's petition for review because Act 282 does not eliminate the Malabes' claim for wrongful foreclosure. To the extent, the Court finds that Act 282 applies to the Malabes' claims, the Court should find that its retroactive application is unconstitutional.

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