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# LEGAL ALERT

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# Santiago v. Tanaka: The Hawaii Supreme Court Increases Disclosure Requirements for Commercial Property Sellers

By Christopher J.I. Leong

In an opinion issued just before the end of 2015, the Hawaii Supreme Court gave what many regarded as an unexpected complete win to the buyers in a commercial property transaction. In this case, the main issue was whether the seller could be held liable for not disclosing material facts to the buyer during the sale negotiations regarding the true nature and amount of monthly sewer fees for the property.

Here is what happened. Seven years into their twenty-year commercial lease of the Nawiliwili Tavern on Kauai, the Santiagos submitted a purchase offer to owner Ruth Tanaka. After an initial offer and several counteroffers, the Santiagos agreed to purchase the property; while the Santiagos agreed to an "as is" condition addendum, the addendum kept Tanaka obligated to disclose all material facts about the property to them. Tanaka then prepared a disclosure statement, which noted that the Tavern was connected to a private sewer line. Tanaka also disclosed a 1995 agreement she had made with James Jasper Enterprises, LLC providing for the Tavern's connection to the line and Jasper's maintenance and operation of the line. The agreement required Tanaka to pay Jasper a one-time $300 deposit, $150 in monthly maintenance, and $150 for cleanout of the line every other month. Jasper reserved the right to adjust the deposit annually, up to a twenty percent increase of the previous year's deposit amount. The Santiagos therefore relied on Tanaka's representation that these were the total sewer costs. The parties closed the sale in August 2006.


In October 2006, the Santiagos received a bill from Jasper for $3,467.43 for August and September sewer maintenance fees. When the Santiagos inquired about the high amount, Jasper responded that the fees had increased twenty percent annually every year since 1995 and that Tanaka had always paid the fees. Jasper suggested that the Santiagos could choose an alternative method of sewage disposal for the Tavern but would have to pay under the agreement until they did so. The Santiagos' attorney then contacted Tanaka, inquiring as to why Tanaka did not disclose that the sewer fees could—and did—increase by twenty percent every year. The attorney also contacted Jasper, suggesting that the agreement between Jasper and Tanaka had not been assigned

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to the Santiagos and that the Santiagos could pay a prorated amount based on their actual usage of the system. Jasper maintained that Tanaka had agreed to pay the fees and the agreement did not provide for prorated payments. Jasper gave the Santiagos three options: (1) pay the full amount owing under the agreement; (2) pay a reduced amount and try to sue Tanaka for damages to cover the balance; or (3) disconnect the Tavern from the Jasper sewer system and construct their own.

The Santiagos ultimately sued Tanaka for, among other things, negligent misrepresentation and nondisclosure regarding the sewer agreement. The circuit court concluded after a trial that Tanaka had provided timely and appropriate disclosures indicating that the sewer fees could increase by twenty percent annually, and therefore the Santiagos received enough information to calculate the current fees. The court also concluded that the Santiagos acknowledged these disclosures and did not conduct due diligence with respect to the sewer system, and it entered judgment for Tanaka. After the Intermediate Court of Appeals affirmed the circuit court's judgment, the Hawaii Supreme Court accepted the case.

The Hawaii Supreme Court discussed the negligent misrepresentation and nondisclosure claims together, noting that they essentially argued the same thing: misrepresentation of the true amount of the sewer fees on one hand and a failure to disclose the true amount of the fees on the other. Under either theory, the court held that Tanaka had a duty to disclose all material facts about the property to the Santiagos and failed to disclose the true amount of the sewer fees. It therefore vacated the circuit court's entry in favor of Tanaka and directed judgment in favor of the Santiagos on the negligent misrepresentation and nondisclosure claims.

The court looked to the specific language of the DROA to establish Tanaka's duty of disclosure with respect to the property: it required Tanaka to "fully and accurately disclose in writing to [the Santiagos] any fact, defect, or condition, past or present, that would be expected to measurably affect the value of the Property to a reasonable person." Further, the "as is" condition addendum and the disclosure statement prepared by Tanaka also obligated her to disclose in writing all material facts concerning the property.


Based on the facts presented, the court concluded that Tanaka's disclosures led the Santiagos to believe the sewer fees were $150 per month for maintenance and $150 every other month for cleanout charges, and that only the amount of the deposit to Jasper—not the actual fees—could increase each year. The evidence also showed that Tanaka had paid the increased fees every year, knew what they were, knew that the fees were the largest expense for the Tavern, knew that the Santiagos would have to disconnect from the sewer system if they did not agree to the agreement with Jasper, and could have informed the Santiagos of all of this. The court noted that the Santiagos' decision to purchase the property might have been influenced had these facts been fully disclosed.

Generally, parties to a commercial transaction are not afforded any special protection by the courts and by statutory law. This differs from situations where the parties have an imbalance in their negotiating power, such as between a tenant and a landlord, or between a buyer and a seller of residential property. Here, although the Santiagos had the opportunity and ability to perform their due diligence before closing on the sale, the Hawaii Supreme Court nevertheless ruled in their favor. *Santiago v. Tanaka* is thus a warning to commercial property sellers that they should not hold back in their disclosures, because they might be the liable party if things go wrong.

**For more information on this article, please call Christopher at 531-8031 ext 623 email him at cjil@hawaiilawyer.com or scan the code with your smartphone.**

# The BE-13 Foreign Direct Investment Survey: Am I Subject to Mandatory BEA Reporting Requirements?

By Kelly Y. Morikone

Does a foreign person, either individual or entity, own at least ten percent of your U.S. business enterprise's voting securities? If so, your U.S. business enterprise may be subject to a recently reinstated mandatory survey tracking foreign direct investment ("FDI") in the U.S. by the U.S. Department of Commerce's Bureau of Economic Analysis ("BEA"). This mandatory survey, known as the "BE-13", was discontinued in 2009 and recently brought back by the BEA towards the end of 2014.

The BE-13 was created by rules promulgated under the authority of the International Investment and Trade in Services Survey Act of 1976 to gather data on new FDI in the United States. Any U.S. business enterprise, including a holding or shell company, that has at least ten percent of its voting securities owned directly or indirectly by a foreign person is called a "U.S. affiliate" by the BEA. A BE-13 is required to be filed by the U.S. affiliate when it is first created or if an existing U.S. affiliate establishes a new U.S. legal entity, expands its U.S. operations, or acquires a U.S. business enterprise. These events are referred to as "reportable transactions" and a BE-13 must be filed within forty-five days after the date of the transactions. Failure to file may result in civil penalties ranging from $2,500 up to $32,500. The information itself is kept confidential by the BEA and used only for statistical and analytical purposes.

Depending on what type of "reportable transaction" occurs, one of five alphabetized BE-13 forms (BE-13A through BE-13E) or a BE-13 Claim for Exemption form will need to be filed. The threshold distinction between the BE-13 Claim for Exemption and the other five BE-13 forms turns on whether the total amount of the acquisition, establishment, or expansion of or by the U.S. affiliate exceeds $3 million. If the amount is less than $3 million, then a BE-13 Claim for Exemption must be filed. The BE-13 Claim for Exemption requests information related to the name and mailing address of the U.S. business enterprise, reason for filing the exemption, the type of transaction that occurred, certain financial and operating information, and contact information of the person to consult about the form.

The alphabetized BE-13 forms range from BE-13A to BE-13E. The category of BE-13 filed depends on what type of transaction occurred. The varied transactions include situations when a U.S. affiliate acquires a new U.S. business enterprise, including the purchase of U.S. real estate intended for lease or sale without significant added construction, to the instance of merger between an existing U.S. affiliate and a newly acquired business enterprise. Generally, the alphabetized BE-13 forms require more information than the BE-13 Claim for Exemption, including equity or debt components of the foreign parent funding, whether the new U.S. operation will involve research and development activities, whether the new U.S. operation is still under construction, employment projections, and actual or projected construction expenditures by type and by year.

If requested by the BEA, you may need to file the BE-605, Quarterly Survey, or the BE-15, Annual Survey. These only need to be filed if you are contacted by the BEA. There is also a mandatory BE-12 benchmark survey that is conducted once every five years. As with the BE-13, depending on various triggering events, a different alphabetized BE-12 will need to be filed. A BE-12 Claim for Exemption may be filed in certain circumstances.

**For more information on this article, please call Kelly at 531-8031 ext 614 email her at kym@hawaiilawyer.com or scan the code with your smartphone.**

# U.S. Supreme Court Considering Who Counts in "We The People"

*by Robert H. Thomas*

## "We the People."

The familiar opening of the U.S. Constitution, the foundational document announcing our most cherished principles. The Hawaii Constitution begins on a similar note: "We, the people of Hawaii … reserve the right to control our destiny, to nurture the integrity of our people and culture, and to preserve the quality of life that we desire."

Big words, for sure. But just who are *"We the People?"*

In December, the United States Supreme Court heard oral arguments in an election law case that could have a major impact on the way we choose the Hawaii State Legislature. The case involves the process of reapportionment – the drawing of boundary lines between state Senate and House districts. Reapportionment is based on population, and under the U.S. Constitution's Equal Protection Clause, each district must contain a roughly equal number of people as every other district.

In *Evenwel v. Abbott*, a case originating in Texas, the Court is wrestling with the question of who can be counted – and who must be counted – when determining the "population." In that case, Hawaii's decades-long exclusion of active-duty military and families from the body politic is front and center.

In 1964, the Supreme Court ruled that state legislatures must be reapportioned according to the "one-person, one-vote" principle, meaning that under the Equal Protection clause of the Fourteenth Amendment, each legislative district must contain a roughly equal number of people. But the Supreme Court avoided explaining what "population" must be counted. All persons? U.S. citizens? Something else?

Two years later, in *Burns v. Richardson*, a case originating in Hawaii, the Supreme Court held that states need not count everyone, but may measure one of three alternate "populations"—either the total number of Census-counted residents, U.S. citizens, or state citizens. The court also noted that "aliens, transients, short-term or temporary residents, or persons denied the vote for conviction of crime" need not be counted. This is because "one-person, one-vote" is not meant literally, but protects two competing principles. "Voting equality" protects voters' equal opportunity to elect representatives, while "representational equality" protects every person's right—regardless of their ability to vote—to equally access those officials. After all, they represent everyone in their districts, not just voters.

Last year, a diverse coalition of civilian and military Hawaii residents represented by Damon Key attorneys Robert Thomas, Anna Oshiro, and Mark Murakami, challenged the exclusion of active-duty military residents and their families from our reapportionment process. Systematically excluding them from Hawaii's body politic violated one-person, one-vote's representational equality principle, and resulted in many districts having unequal numbers of people. It should not matter that many of Hawaii's military residents do not pay state income taxes, or vote locally. Hawaii automatically counts everyone else regardless of whether they pay Hawaii taxes, or can or do vote, such as aliens, minors, and felons.

The federal court disagreed. Excluding them was fine, because the *Burns* ruling allowed Hawaii to count state citizens. Service members and families are not "Hawaii citizens" because they report on a federal form they pay taxes to another state. But Hawaii never asked anyone but service members where (or if) they pay taxes. This resulted in aliens and other non-U.S. citizens being considered Hawaii citizens, while military residents are not. Despite this surreal outcome, the U.S. Supreme Court summarily affirmed.

In *Evenwel*, the Supreme Court is revisiting that ruling. Texas draws its legislative districts to equalize its Census population, which includes undocumented immigrants. Voters challenged that, arguing Texas

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should have also considered whether districts contain an equal number of voters. The court will decide whether states must count everyone (including noncitizens, non-voters, and military), only those eligible to vote, or some other population. The question posed by the case is straightforward: what "population" must be counted, and if less than everyone is included, what one-person, one-vote principle must states protect when determining whom to eliminate?

A ruling requiring counting everyone would bring Hawaii's reapportionment practice in line with 48 other states and with Congressional apportionment, which, like Texas, is based on the Census count of all persons present, regardless of their citizenship, taxpaying, or voting status. It wasn't always so, and prior to adoption of the Fourteenth Amendment, African-Americans counted as three-fifths of a person in Congressional reapportionment. It took a civil war and amendments to our Constitution to exorcise the demon of not counting everyone equally.

While the situation here is much less dramatic, the stakes are no less important, and excluding service members and their families is no less repugnant. Military and families are counted by the Census only as Hawaii residents. Under federal law, they are counted nowhere else but in Hawaii's legislature, and not counting them here means they are not represented anywhere.

*Evenwel* is vitally important because the Supreme Court's decision may finally force Hawaii to stop excluding service members and their families from "We the People."

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Robert H. Thomas attended the Supreme Court oral arguments in December 2015. The Court is expected to issue a ruling before June 2016.

**For more information on this article, please email Robert at rht@hawaiilawyer.com or scan the code with your smartphone**

# Damon Key Attorneys Headline at National Eminent Domain Conference in Austin

In January, Damon Key lawyers Robert Thomas and Mark Murakami attended the American Law Institute - Continuing Legal Education's annual conference on eminent domain and property law, "Eminent Domain and Land Valuation Litigation." This year's conference was held in Austin, Texas, the first time the conference visited that city.

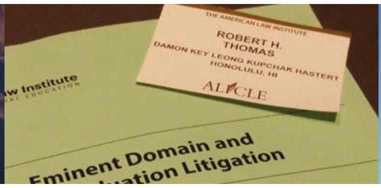
Robert – along with colleague Joe Waldo of Norfolk, Virginia – is the co-planning Chair of the Conference, and is on the faculty. Mark is also a regular member of the faculty. Robert presented a session on the latest eminent domain court decisions, while Mark (pictured below) spoke on a panel of experts about motions practice in eminent domain cases.

This premier national conference brings together over 200 of the country's most prominent eminent domain and condemnation lawyers, appraisers, judges, and legal scholars for three days of presentations on subjects such as property rights, the ability of the government to take property, and valuation and just compensation in condemnation.

In addition to Mark's session on motions practice, some of the highlights of the agenda were a keynote presentation by law professor Ilya Somin about the infamous 2005 U.S. Supreme Court decision in *Kelo v. City of New London* (in which the Court permitted the city to take a home so the land could be used as a hotel), and a talk by retired Minnesota Supreme Court Justice Paul Anderson about the view of eminent domain from his side of the bench.

Robert also had the opportunity to interview Ted Balaker, the producer of the upcoming feature film about the *Kelo* case, "Little Pink House." Listen to excerpts of their talk here: http://tinyurl.com/zu25wsq.

It wasn't all business, of course, and Mark and Robert were able to partake of some of Austin's other attractions such as the live-music scene, and central Texas' famous barbecue.



# All About ADU's?

By Ikaika B. Rawlins

On September 14, 2015, Mayor Kirk Caldwell signed into law Ordinance 15-41 (the "Ordinance"), which allows for the creation of "accessory dwelling units" ("ADU") in certain zoning districts within the City & County of Honolulu (the "City"). An ADU is defined as a second dwelling unit, including its own kitchen, bedroom, and bathroom facilities, which may be attached or detached from the primary dwelling unit on the zoning lot. The purpose of the Ordinance is to encourage the development of ADU's in permitted zoning districts to increase the number of affordable rentals and, consequently, to help alleviate the City's housing shortage.

An ADU may be created in a number of ways. A property owner can alter an existing structure, build a new structure (attached or detached), recognize an existing structure that was built without a building permit (provided the owner receives after-the-fact permits), or convert an existing structure that exceeds the maximum floor area and/or cannot meet the off-street parking requirements in the Ordinance described further below (provided the applicant applies for and receives a zoning adjustment).

Property owners who may be considering adding an ADU to their property or converting an existing structure to an ADU should be aware of the strict regulations on development, parking, rental terms, and rental advertising contained in the Ordinance. Below is a summary of the key regulations:


1. The subject property must be located in either the Residential or Country zoning district.
2. There must be sufficient sewer and water capacity to support the ADU.
3. The minimum lot size for creation of an ADU is 3,500 square feet. If a lot is between 3,500 – 4,999 square feet in land area, the maximum size of the ADU is 400 square feet. If the lot is 5,000 square feet in land area or greater, the maximum size of the ADU is 800 square feet.
4. The lot must not have more than one existing dwelling unit on the date of application.
5. Either the primary dwelling unit or the ADU (but not both) must be occupied by the property owner(s), the owner's family, or designated authorized representative.
6. There must be at least one off-street parking stall provided for the ADU.
7. The property owner must agree not to "CPR" or "condominiumize" the subject property[1] in an attempt to legally separate the primary dwelling unit from the ADU. Accordingly, the ADU cannot be sold separately from the primary dwelling unit.
8. The ADU or, if applicable, the primary dwelling unit may only be used for "long term rentals," i.e., rentals for a period of six months or longer.
9. If the ADU is advertised for rent as a "bed and breakfast home" or a "transient vacation unit" (generally defined in the City's Land Use Ordinance as rentals to transient occupants for a period of 30 days or less), the Ordinance provides that this will be considered as evidence that the property owner is illegally operating a bed and breakfast home or transient vacation unit on the property, and the burden will be on the property owner to prove otherwise.

If you or someone you know needs assistance navigating through the complex ADU permitting process, Damon Key's real estate attorneys are here to help.

[1] Or, in legal terms, to subject the property to a condominium property regime under Chapter 514B, Hawaii Revised Statutes.

**For more information on this article, please call Ikaika at 531-8031 ext 605 email him at ibr@hawaiilawyer.com or scan the code with your smartphone.**

# 2016 Best Lawyers and Super Lawyers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## Attorneys in the News

**Clare M. Hanusz** will be featured in the Q&A section on the topic of immigration in Hawaii in the UH Magazine, a new general interest publication for the University of Hawaii alumni and general audience readers.

**Christine A. Kubota** volunteered as an event judge at the Family Career and Community Leadership of America event, where public school students competed to go to the nationals. She spent the day judging over eight groups of students from intermediate to seniors in high schools about their FCCLA projects, and judging them on their written, oral and presentation skills. She also volunteers for the Honolulu Japanese Junior Chamber of Commerce to assist the Cherry Blossom Festival contestants with their speaking and presentation skills. The Festival Ball will be held March 26, 2016, at the Sheraton Waikiki, when the Queen will be crowned.

She will also be a speaker at a joint Hawaii State Bar Association/Daichi Tokyo Bar Association Conference Seminar in Tokyo in April, highlighting estate plan issues of Japanese investors in Hawaii.

**Gregory W. Kugle** will be a judge for the 64th Cherry Blossom Festival on March 26, 2016, at the Sheraton Waikiki.

**Kelly Y. Morikone** & **Megumi Honami** presented a seminar in February to the Hawaii Senior Life Enrichment Association. HISLEA is a Hawaii/Japan non-profit organization with 800+ members mostly 55+ retired seniors that travel back and forth between Japan and Hawaii. The 2-hour session focused on long term stays in Hawaii.