

STATE OF HAWAII
DEPARTMENT OF LAND AND NATURAL RESOURCES
Land Division
Honolulu, Hawaii 96813

May 23, 2014

Board of Land and Natural Resources
State of Hawaii
Honolulu, Hawaii

Hawai'i

Request for Consent to Extension of Lease Term Pursuant to Act 207, Session Laws of Hawaii 2011, General Lease No. S-3606, The Food Basket Inc., Waiakea, South Hilo, Hawaii Tax Map Key: (3) 2-2-50:96.

APPLICANT:

Improvements to leasehold property financed by Lessee, The Food Basket, Inc., pursuant to Act 207, Session Laws of Hawaii and Sections 171-36(b) in the amount of approximately \$170,000.00.

In order for Lessee to amortize this expenditure, the Lessee is requesting an extension of General Lease No. S-3606 of 10 years, commencing on January 16, 2016 and expiring on January 15, 2026 for an aggregate term (initial 55 year term plus extension) of 65 years.

LEGAL REFERENCE:

Act 207, Session Laws of Hawaii 2011
Sections 171-36(b)(3), Hawaii Revised Statutes, as amended.

LOCATION:

Portion of Government lands of Lot 28, Kanoelehua Industrial Lots, situated at Waiakea, South Hilo, Hawaii, identified by Tax Map Key: (3) 2-2-50:96, as shown on the attached map labeled Exhibit A.

AREA:

15,000 square feet, more or less.

ZONING:

State Land Use District: Urban
County of Hawaii CZO: ML-20 Limited Industrial Use

TRUST LAND STATUS:

Section 5(b) lands of the Hawaii Admission Act
DHHL 30% entitlement lands pursuant to the Hawaii State Constitution: NO

CHARACTER OF USE:

Proposed uses allowed under the County of Hawaii zoning code, ML-20, limited industrial.

LEASE TERM:

Original term of 55 years, commencing on January 16, 1961 and expiring on January 15, 2016.
Requested extension of 10 years commencing on January 16, 2016 and expiring on January 15, 2026.

ANNUAL RENT:

Current rent is \$17,100, due in semi-annual installments of \$8,550.00 on January 16 and July 16 of each year.

RENTAL REOPENINGS:

Reopening's in the original term were at the end of the 20th, 30th, 40th and 50th years of the term. The last rental reopening occurred on January 16, 2011.

Staff is recommending the rent for the extended term be determined by an immediate appraisal that will project rent for the period January 16, 2016 through January 15, 2026. The appraiser shall be selected by the State and paid for by Lessee. As a condition of the Board's discretionary approval of the lease extension, the appraised rent for the extension period will be determinative and not subject to arbitration.

PROPOSED IMPROVEMENTS:

The Lessee has made substantial improvements to the property. These improvements include major repairs and renovations to the warehouse. The cost of these improvements is estimated to be in excess of \$170,000.00.

DCCA VERIFICATION:

Place of business registration confirmed:	YES <u>X</u>	NO <u>__</u>
Registered business name confirmed:	YES <u>X</u>	NO <u>__</u>
Applicant in good standing confirmed:	YES <u>X</u>	NO <u>__</u>

APPLICANT REQUIREMENTS:

Applicant shall be required to pay for an appraisal for the immediate rental reopening.

REMARKS:

On January 13, 1961 General Lease No. S-3606 was issued to Hilo Equipment and Manufacturing Co., Ltd. as a result of Act 4, First Special Session, 1960 which authorized the leasing or leasing with option to purchase of public lands to victims of natural disaster through direct negotiation for other than residential or agricultural purposes.

At its meeting of May 27, 1961, under Agenda Items F-1-c, the Board of Land and Natural Resources approved the assignment of GL S-3606 from Honolulu Iron Works Company, successor in interest to Hilo Equipment and Manufacturing Co., Ltd., Assignor, to Hilo Kala, Inc., Assignee. On September 23, 1966, the Chairperson consented to the sublease of a portion of the property to Truck & Trailer Service, Inc.

The previous Lessee had been utilizing the property for the same purpose for which the lease was issued (wholesaling and retailing of truck and trailer parts and body manufacturing). Staff recommended the Board consent to the change in the character of use from 'truck and trailer parts and body manufacturing' to the proposed uses allowed under the County of Hawaii zoning code, ML-20, limited industrial.

At its meeting of June 23, 2011, under agenda item D-3, the Board consented to the assignment of lease from Hilo Kala, Inc., Assignor to The Food Basket Inc., Assignee, and to the change in character of use to limited industrial.

The Lessee, The Food Basket Inc. is an island wide, supplemental food network that collects and distributes nutritious, quality food to low income households, the working poor, the disabled, the ill, senior citizens, children programs and other charitable organizations that serve this population. Supplemental food is provided regardless of religious beliefs, gender or ethnicity. The Lessee's current operation utilizes the subject property for warehouse, storage and distribution purposes. This use is consistent with the current county zoning, industrial use.

The Lessee has not had a lease, permit, easement or other disposition of State lands terminated within the last five years due to non-compliance with such terms and conditions. The proposed use is allowable in the county zoning. The Lessee is in compliance with all the lease terms and conditions.

LEASE EXTENSION:

The Lessee's current 55 year lease is set to expire on January 15, 2016. They are requesting a 10 year extension pursuant to Act 207, Session Laws of Hawaii 2011¹ in order to amortize the cost of improvements made to the property. These improvements include major renovations to the exterior and interior of the building including the replacement of the roof along with significant interior office renovations and the installation of a walk-in refrigeration storage facility all at a cost in excess of \$170,000.00. An appraisal evaluation performed by a certified appraiser (Exhibit B) has determined that the economic life of the proposed improvements will exceed the ten year extension period requested to amortize the refurbishments.

Staff additionally notes that The Food Basket, Inc. has made substantial repairs and improvements to the premises in the course of the lease. The warehouse structures are well maintained and in good condition. Such maintenance demonstrates the Lessee's continuing efforts to keep the buildings in good order and repair.

The subject parcel is located in an area served by aging and/or substandard infrastructure. The area also includes numerous other DLNR parcels currently encumbered by long term leases that are also scheduled to expire between 2016 and 2021. Most of the DLNR leases in this area were established pursuant to Act 4, First Special Session of 1960 resulting from the destruction of the Hilo bay front caused by the 1960 tsunami. Businesses that were severely impacted by the tsunami were given the opportunity to relocate to the newly created industrial area of Kanoelehua. The act provided lessees with an option to purchase the land within two years. Several businesses exercised this option creating an industrial area of mixed DLNR leases and fee simple properties².

Since the implementation of Act 207, SLH 2011, there have been several leases within the Kanoelehua Industrial area that have been granted ten year extensions. Three of these leases are in the immediate vicinity of GL S-3606 and are direct leases awarded as a result of Act 4. The Other leases, although in the Kanoelehua Industrial area are located along Railroad Ave. and were initially awarded through the public auction process.

The East Hawaii economic region is unique in that a majority of the available land suitable for commercial and/or industrial use is under the management of a government agency³ (Exhibit C). As one of the largest stake holders of commercial/industrial land in the Hilo area, the Department of Land and Natural Resources understands the need for a comprehensive analysis

1 Act 207, Session Laws of Hawaii 2011 amends Section 171-36(b) of the Hawaii Revised Statutes by allowing the Lessee to: Extend or modify the fixed rental period of the lease: provided that the aggregate of the initial term and any extension granted shall not exceed sixty-five years.

2 There are currently twenty six (26) leases and fifteen (15) fee simple properties within the area set aside as a result of Act 4 First Special Session 1960. The area borders are Kawili St., Makaala St., Pookela St. (both sides) and Wiwoole St.

3 The Department of Land and Natural Resources (DLNR) and the Department of Hawaiian Home Lands (DHHL) are the two major land holders in the industrial area of East Hawaii.

of the area in order to develop an economic strategy that will encourage new enterprises in addition to supporting the established businesses.

With this concept in mind, the Land Division has retained the services of the consulting firm Munekiyo & Hiraga, Inc. for the purpose of providing a feasibility study and analysis of the Kanoelehua Industrial Area in order to determine the future direction of this very important economic area of East Hawaii.

Key elements of the study/analysis will be:

- Determine the market demand for the KIA properties, particularly the demand for industrial-commercial use or some other use for long-term leasing (30 years or more)
- Determine whether some properties should be consolidated and reconfigured to maximize the utility of the land in view of the results from the above findings.
- Assess the feasibility and desirability of placing management of the leasehold properties (or clusters of properties) under a master lease (or multiple master leases for each cluster) from the State for industrial, commercial or other uses permitted by the applicable zoning.

The results of this study will be used to assist the department in determining the future of the Kanoelehua Industrial Area and create an economic region that will benefit not only the people of East Hawaii, but the State as well.

The Lessee, a non-profit 501 (C) 3 corporation, had previously submitted a request for a new direct lease at minimum rent for the existing property.

When considering lease dispositions to eleemosynary organizations or religious organizations, the Board may issue the lease by public auction at fair market rent, or by direct negotiation at an amount below fair market rental (i.e., nominal rent). On May 13, 2005, the Land Board established a Minimum Rent Policy that stated, among other things, that the Minimum Rent for lease be no less than \$480 per year. Land Division generally issues leases at fair market rental value as determined by an appraiser or via public auction. Staff believes “nominal rent” under section 171-43, Hawaii Revised Statutes ought to be anywhere between fair market rent, or lower, but not lower than the minimum rent of \$480.

At its meeting of December 13, 2013, under agenda item D-12, staff recommended the Board deny the Lessee’s request for a direct lease at nominal rent. Staff explained to the Board that the Lessee acquired the industrial lease with less than 5 years remaining on it and made substantial improvements while acknowledging there would be no guarantee of a new lease being granted. The location of the property is in a prime industrial area with a combination of leasehold and fee simple lots. Staff indicated that granting a long term lease prior to the results of the above-mentioned feasibility study would not be in the best interest of the State. It was suggested that the Lessee return to the Board for an extension of the current lease under Act 207.

There should be a reasonable and fair market annual rent for all Land Division non-profit tenants. However, as the location of the subject property is in an established industrial district,⁴ staff is of the opinion that this extension request warrants a lease rent above the nominal rent amount discussed above and is recommending an extension of lease at fair market value as determined by an independent appraiser.

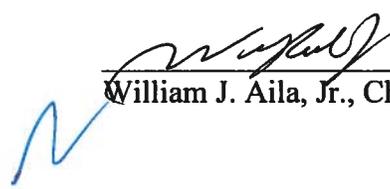
RECOMMENDATION: That the Board:

1. Authorize the extension of General Lease No. S-3606 under the terms and conditions cited above, which are by this reference incorporated herein and further subject to the following:
 - A. The standard terms and conditions of the most current lease extension form, as may be amended from time to time;
 - B. Applicant shall be required to pay for an appraisal for the immediate rental reopening;
 - B. Review and approval by the Department of the Attorney General; and
 - C. Such other conditions as may be prescribed by the Chairperson, which are in the best interests of the State.

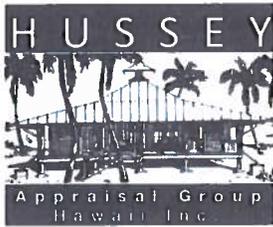
Respectfully Submitted,


Gordon C. Heit
District Land Agent

APPROVED FOR SUBMITTAL:


William J. Aila, Jr., Chairperson

⁴ The Kanoelehua Industrial Area (KIA) was developed as an industrial park to relocate businesses damaged or destroyed by the 1960 tsunami that devastated the Hilo Bay front. The KIA is a mixture of fee simple, DHHL and DLNR properties. It has been the industrial and commercial center for East Hawaii since its development in the mid 1960's. The subject property is located among several State leases. Most of these leases are set to expire in 2016.



Hussey Appraisal Group Hawaii, Inc.

FKA, Lawrence Appraisal Group Hawaii, Inc.

308 Kamehameha Avenue, PH-3
Hilo, HI 96720
Tel. (808) 935-6081
Fax (808) 935-6147

April 18, 2014

The Food Basket, Inc.
40 Holomua Street
Hilo, HI 96720

Attention: En Young, Executive Director (email: en.young.foodbaskethi@gmail.com)

Re: Report on the Economic Life of Building Improvements in connection with a Request for Extension of Hawaii General Lease No. S-3606. Property identified as Lot 28, Por. Waiakea House Lots Extension, Hilo, Hawaii; TMK (3) 2-2-50: 96, Located at 40 Holomua Street, Hilo, HI 96720. Our File No. CCOO3A002E4.

Dear Mr. Young,

Per your request, here is my report regarding the remaining estimated economic life of building improvements on the above property. My estimate is as of the date of inspection of the subject property, which was March 7, 2014.

I understand that the Intended Use of this Appraisal Report is to provide an independent valuation of the remaining economic life of building improvements in connection with an application for a lease extension. Intended Users are identified as you, the DLNR Land Division and the Board of Land and Natural Resources. All substantial improvements were completed prior to the date of inspection.

Extraordinary Assumptions

An Extraordinary Assumption is defined as "An assumption, directly related to a specific assignment, which, if found to be false, could alter the appraiser's opinions or conclusions. Extraordinary assumptions presume as fact otherwise uncertain information about physical, legal, or economic characteristics of the subject property; or about conditions external to the property such as market conditions or trends; or about the integrity of data used in an analysis."¹

No Extraordinary Assumptions were necessary for this analysis.

¹ Page 73, The Dictionary of Real Estate Appraisal, 5th Edition, Appraisal Institute, Chicago, Ill.

Hussey Appraisal Group Hawaii, Inc.

EXHIBIT B

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Hypothetical Conditions

A Hypothetical Condition is “That which is contrary to what exists but is supposed for the purpose of analysis. Hypothetical conditions assume conditions contrary to known facts about physical, legal, or economic characteristics of the subject property’ or about conditions external to the property, such as market conditions or trends; or about the integrity of data used in an analysis.”²

No Hypothetical Conditions were used in this report.

Scope of Work

To determine the estimated remaining economic life of substantial additional improvements, the appraiser made a complete inspection of the subject’s improvements, reviewed actual receipts and expenditures by the lessee, and then consulted the Marshall & Swift Cost Estimator Program to determine an estimate of the effective age of improvements after consideration of all renovations. From this, an estimate of the remaining useful economic life of building improvements was derived.

Description of Building and Costs of Substantial Improvements

County tax map key records indicate that the subject’s steel warehouse was built in 1963 and consisted of an 8,466 square foot steel warehouse that included 660 square feet of office space, and 1,360 square feet of mezzanine sales display areas. Public records (Bureau of Conveyances) indicate that the lease was assigned from HILO KALA, INC, a Hawaii corporation, to THE FOOD BASKET INC, a Hawaii Nonprofit Corporation. This Assignment of Lease was recorded on September 27, 2011. Consent to assign this general lease was granted by the Board of Land and Natural Resources at its meeting of June 23, 2011, and recorded by the Bureau of Conveyances on September 27, 2011.

Since taking possession of the subject property less than three years ago, the lessee has spent about \$180,000 on building improvements. (Another \$57,200 was spent to acquire the leasehold interest; but that cost is not relevant to this assignment). The building was essentially gutted and transformed from a “plain vanilla” unfinished steel warehouse into a first class customer service facility. Renovations include a new customer reception area, handicapped restrooms, finished offices on the main floor and on the mezzanine, a conference room, and food preparation areas that meet Department of Health requirements for cleanliness, etc. Other new amenities include dropped fluorescent lighting in all offices and food preparation areas, and a split system air conditioning system for the entire first floor and mezzanine offices. The building has also been wired for internet and computer services and has a full security system. All work was permitted by the County of Hawaii, and completed in a quality manner that is consistent with County of Hawaii building codes. To make the above improvements as cost effective as possible, much of the labor was donated by qualified community volunteers. The above improvements were all verified by the appraiser’s complete physical inspection (please see subject photographs).

² Ibid, page 97

Estimate of the Economic Life of Subject's Building Improvements

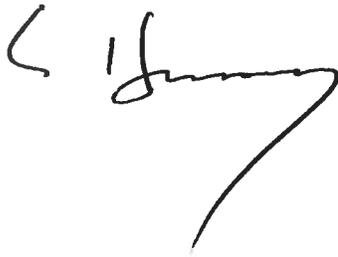
From the Marshall & Swift Commercial Cost Estimator program, an average quality industrial steel-framed storage warehouse would have a nominal total economic life expectancy of 40 to 45 years. However, it has been the appraiser's experience in this market that such warehouses in fact have typically had substantially longer economic lives—especially if they receive regular maintenance. This is true in part because in Hilo, temperature ranges are not subject to the extremes in harsher climates that cause contraction, expansion and deterioration of building components. Thus, I anticipate that the total economic life of the subject's improvements "as is," and as of the date of inspection should range from a minimum of 40 years to 55 years or more.

Photographs & Records of Payment for Significant Building Improvements

Photographs of the subject's substantial refurbishment, and records of payment are described in the appendices to this letter.

Thank you again for the opportunity to be of service. If you have any questions, please don't hesitate to call me.

With Aloha,

A handwritten signature in black ink, appearing to read "Stewart H. Hussey". The signature is fluid and cursive, with a long, sweeping tail that extends downwards and to the right.

Stewart H. Hussey
President
Certified General Appraiser #540
License Expires 12-31-2015

**Summary of Costs for Significant Building Improvements (By Vendors
Other than HPM)**

The Food Basket--Significant Renovation Costs (Exclusive of HPM Costs)	
40 Holomua Construction Costs (From September 2011 to Present)	
Vendor	Amount Paid
Airgas	\$53
Alumside Products, Incorporated	\$1,178
AMAZON	\$277
American Savings Bank	\$1,707
BAYLIGHT	\$2,739
CARPET ISLE	\$100
Central Supply	\$338
Cornerstone Welding	\$708
COSTCO WHS POSPUR 11/19/12	\$83
Curtis Mamone	\$5,910
Dale Mayotte dba Eastside Painting	\$500
Ferguson Enterprises Inc.	\$321
Fukushima, Glenn	\$5,465
GARDEN EXCHANGE	\$68
HD	\$62
HD White Cap	\$6
Hilo Mechanical, Inc.	\$19,549
HILO STEEL	\$1,606
Hirayama Bros. Electric, Inc.	\$6,179
HOME DEPOT	\$5,007
honsador Lumber	\$2,952
HPM	\$34,308
ICO	\$418
Ivan Mochida Contracting	\$6,586
JBL HAWAII	\$96
Joe L Hawthorne	\$3,100
John Pratt Construction Services	\$7,718
Jo's Computer Services	\$11,885
Kona Coast Office Supply	\$516
LOWES	\$35
Mana Christian Ohana	\$389
Mehmet Boysal	\$10,146
Rodney Yonemura	\$11,000
SEARS POSPUR 11/30/12	\$77
Sport Authority	\$417
White Cap Construction Supply	\$1,422
WRC Refrigeration Engineering Contractor	\$2,582
Yamada and Sons, Inc.	<u>\$4,200</u>
Grand Total	\$149,701
	Rounded to: \$150,000
 Purchase of Building	 \$57,160

Summary of Costs for Significant Building Improvements (By HPM)

<p>The Food Basket Inc Summary HPM Construction Invoices Significant Refurbishment Costs (Jan 2012 thru May 2013)</p>		
Invoice Numbers	Dates	Amount
Various	(As above)	29,297.96
Rounded		\$29,300

(Detailed breakdown of HPM invoices held in file)

* * * * *

Summary of TOTAL Costs for Significant Building Improvements

<p>The Food Basket Inc. Summary of All Significant Refurbishment Invoices (Jan 2012 thru May 2013)</p>	
Vendors	Amount
Construction (Other than HPM)	\$149,701.25
HPM	<u>\$29,297.96</u>
Totals	\$178,999.21
Rounded	\$179,000

Invoices for construction vendors other than HPM are attached. For the sake of brevity, 153 HPM invoices are held in the appraiser's files.

Kanoelehua Industrial Leases

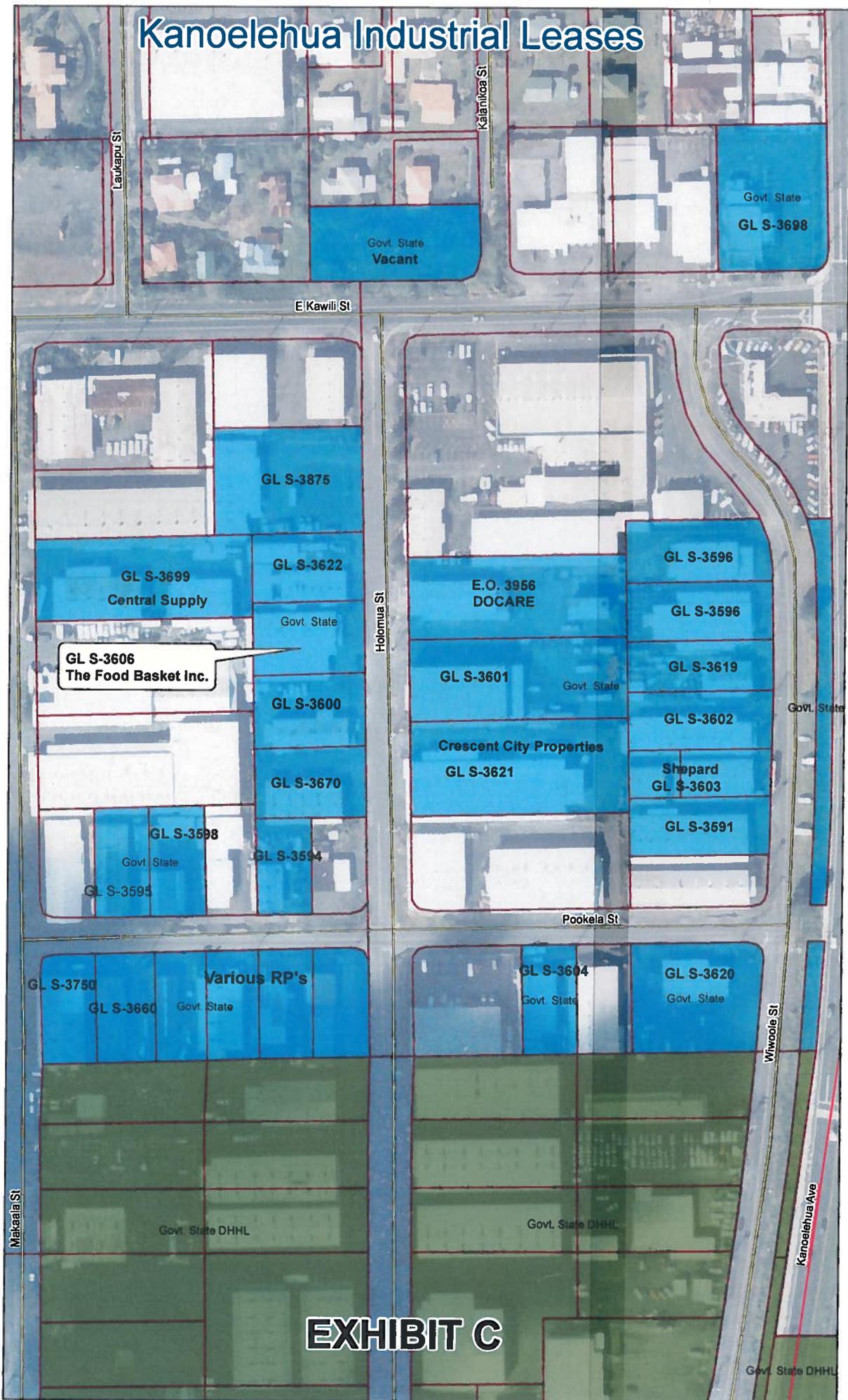


EXHIBIT C