

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

August 14, 2015

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

Ref. No.: GLS-5187

HAWAII

Amend Prior Board Action of May 9, 2014, Item D-2, Term Extension of General Lease No. S-5187; Aloha Petroleum, Ltd., Lessee, Waiakea, South Hilo, Hawaii, Tax Map Key: (3) 2-1-009:042.

The purpose of the amendment is to change Condition 1.B. by including “improvements required by applicable law or regulations” as a permissible basis of the lease extension, and extending the due date from December 31, 2015 to December 31, 2016, for submitting receipts of the expenditures of the proposed improvements.

BACKGROUND:

At its meeting of May 9, 2014, under agenda Item D-2, the Board of Land and Natural Resources approved a 10-Year Term Extension of General Lease No. S-5187; Aloha Petroleum, Ltd., Lessee, Waiakea, South Hilo, Hawaii, Tax Map Key: (3) 2-1-009:042. The extension is contingent upon Aloha Petroleum, Ltd. (Lessee) performing a minimum of \$297,500 worth of improvements upon the demised premises. (Exhibit A)

Under Condition 1.B., Lessee is to submit receipts for a minimum of \$297,500 worth of repairs by December 31, 2015.

REMARKS:

By letter dated July 16, 2015, Nathan T. Okubo, an attorney with Cades Schutte, on behalf of Lessee, notified staff that it recently lost its fuel supply contract with Costco's gas station on the Big Island. This resulted in a decrease of 40% of Lessee's annual gross revenue on the Big Island, making it impracticable for Lessee to commit to complete \$297,500 in proposed improvements by the December 31, 2015 deadline. In addition, due to new government regulations applicable to Aloha, in the event Lessee continues as lessee under the lease, Lessee will be required to make substantial improvements to the

property to comply with such government regulations. (Exhibit B)

Given the foregoing changes in circumstances, Lessee proposes that condition 1.B. be amended and restated in its entirety as follows:

“B. Aloha shall complete a minimum of \$297,500 in improvements, which can be in the form of; (i) new containment permitting, design and construction, (ii) conducting the inspections and repairs recommended in the Powers Engineering & Inspection, Inc., report dated March 31, 2014, or (iii) improvements required by applicable law or regulations, or a combination of (i), (ii) and/or (iii), and submit to the Hawaii District Land Office receipts for expenditures by December 31, 2016, or the lease extension shall be subject to cancellation.”

RECOMMENDATION: That the Board:

1. Amend its prior Board action of May 9, 2014, under agenda item D-2, by deleting and replacing Condition 1.B. with the following:

“B. Aloha shall complete a minimum of \$297,500 in improvements, which can be in the form of; (i) new containment permitting, design and construction, (ii) conducting the inspections and repairs recommended in the Powers Engineering & Inspection, Inc., report dated March 31, 2014, or (iii) improvements required by applicable law or regulations, or a combination of (i), (ii) and/or (iii), and submit to the Hawaii District Land Office receipts for expenditures by December 31, 2016, or the lease extension shall be subject to cancellation.”

2. All terms and conditions listed in its May 9, 2014 approval to remain the same.

Respectfully Submitted,



for Wesley T. Matsunaga
Land Agent

APPROVED FOR SUBMITTAL:



Suzanne D. Case, Chairperson

AMENDED

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

May 9, 2014

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

Ref. No.: GLS-5187

HAWAII

Approval of Term Extension of General Lease No. S-5187; Aloha Petroleum, Ltd., Lessee, Waiakea, South Hilo, Hawaii, Tax Map Key: (3) 2-1-009:042.

APPLICANT AND REQUEST:

Aloha Petroleum, Ltd., a Hawaii corporation.

Improvements to leasehold property financed by Lessee, Aloha Petroleum, Ltd. (Lessee), pursuant to Section 171-36(b), Hawaii Revised Statutes, and Act 207, Session Laws of Hawaii 2011, in an amount of at least \$595,000.00.

In order for Lessee to fully amortize its expenditures, the Lessee is requesting an extension of General Lease No. S-5187 of 20 years, commencing on May 19, 2014 and expiring on May 18, 2034 for an aggregate term (initial 25-year term, plus 20-year extension currently being requested) of 45 years. Lessee additionally seeks the right to cancel the lease at the end of the tenth year of the extension.

LEGAL REFERENCE:

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

LOCATION:

Portion of Government lands, Waiakea, South Hilo, Hawaii, identified by Tax Map Key: (3) 2-1-009:042, as shown on the attached map labeled Exhibit A.

AREA:

2.66 acres, more or less.

as amended
APPROVED BY THE BOARD OF
LAND AND NATURAL RESOURCES
AT ITS MEETING HELD ON

May 9, 2014 *UO*

EXHIBIT A

TRUST LAND STATUS:

Section 5(b) lands of the Hawaii Admission Act

DHHL 30% entitlement lands pursuant to the Hawaii State Constitution:

YES _____ NO x

LEASE CHARACTER OF USE:

Solely for bulk storage and distribution of petroleum products purposes.

TERM OF LEASE:

Original lease was for 25 years, commencing on May 19, 1989 and expiring on May 18, 2014. Last rental reopening occurred on May 9, 2004. No additional rental reopening is scheduled.

Request a 20-year extension under Section 171-36(b), HRS, commencing on May 19, 2014 and expiring on May 18, 2034 for an aggregate term (initial 25-year term plus 20-year extension) of 45 years.

RENTAL REOPENINGS:

The reopening in the original term was at the end of the 15th year of the term. Last rental reopening occurred on May 19, 2004.

Rent for the extended term shall be determined by an immediate appraisal that will project rent for the period of May 19, 2014 through May 18, 2024. The appraiser shall be selected by the State but paid for by Lessee.

IMPROVEMENTS:

Aloha Petroleum is proposing two improvement options:

Option 1: Containment of Tank #2602 and 2603 on the South East Corner of the Terminal, which will consist of an estimated area of 6,500 square feet (130' x 50') at a cost of \$595,000.00.

Option 2: Containment for the Entire Tank Farm, consisting of an estimated 41,340 square feet (260' x 159') at a cost of \$1,595,000.00.

Lessee contracted Powers Engineering & Inspection, Inc. to provide an assessment using visual test of components at the East Terminal of the Aloha Petroleum facility in Hilo. The resulting report dated March 21, 2014 is based on field inspection and evaluation in accordance with the American Petroleum Institute (API) 653/650 Standard. The purpose

of the assessment was to determine the current condition of the components in question and assess, if possible, the economic life of the components. The report indicated that the economic life of all components may extend beyond 20 years if periodic maintenance and inspection are performed.

ANNUAL RENTAL:

\$50,760.00.

DCCA VERIFICATION:

Place of business registration confirmed:	YES <u>x</u>	NO
Registered business name confirmed:	YES <u>x</u>	NO
Good standing confirmed:	YES <u>x</u>	NO

APPLICANT REQUIREMENTS:

Applicant shall:

1. Be required to pay for an appraisal for the rental reopening for the first ten years of the 20-year extension term of the lease, scheduled for May 19, 2014. The appraisal shall not be subject to arbitration.
2. Provide a performance bond in an amount equal to twice the annual rental amount for the extended period of the lease.
3. By May 31, 2015, complete a minimum of \$595,000.00 worth of improvements to the lease premises and provide the Hawaii District Land Office (HDLO) with copies of receipts for the improvements made.

REMARKS:

General Lease No. S-5187 was sold at public auction on May 19, 1989 to Texaco Refining and Marketing, Inc., a Delaware corporation for an annual rent bid of \$49,400. The premises are now the site of Aloha Petroleum, Ltd.'s Hilo East Terminal property – a gasoline storage terminal and distribution facility that receives gasoline, diesel and ethanol via marine delivery, with upgrades reflecting the modernization of loading rack arms, the addition of an ethanol load arm, and drainage improvements which include grading, paving and the installation of drainage structures (drywells, piping, catch basins). The site includes a warehouse, utility shed, canopy, asphalt parking and driveway areas, perimeter fencing, seven storage and refining tanks, piping, load arm, load rack, and related components. There were a number of lease assignments prior to Aloha Petroleum, Ltd.'s acquisition of 100% of the leasehold interest in the property, as summarized below.

Effective December 29, 1989, as part of an internal realignment of various Texaco subsidiaries, Texaco Refining and Marketing, Inc. changed its name to TRMI Holdings Inc. (THI). Thereafter, a new subsidiary of THI called Texaco Refining and Marketing, Inc. was formed. At its meeting of February 8, 1991, Item F-1-d, the Board of Land and Natural Resources consented to the assignment of the lease from Texaco Refining and Marketing, Inc., now known as TRMI Holdings, Inc., as assignor, to the new Texaco Refining and Marketing, Inc., as assignee.

At its meeting of September 27, 1996, Item D-14, the Board approved the assignment of the lease from Texaco Refining and Marketing, Inc., as assignor, to Texaco Refining and Marketing, Inc. and Aloha Petroleum, Inc., assignee, as tenants in common in equal shares. At its meeting of August 13, 1999, Item D-12, the Board approved the assignment of the lease from Texaco Refining and Marketing, Inc. and Aloha Petroleum, Inc., as assignor, to Equilon Enterprises LLC and Aloha Petroleum, Inc., as assignee, as tenants in common. At its meeting of August 12, 2010, Item D-2, the Board consented to the assignment of the lease from Equilon Enterprises LLC, and Aloha Petroleum, Ltd., as assignor, to Aloha Petroleum, Ltd., as assignee. Since that time, Aloha Petroleum, Ltd. (Lessee), has been the sole lessee under the lease.

By letter dated, April 9, 2014, Mr. Robert Fong, Lessee's General Counsel, requested up to a 40-year term extension of General Lease No. S-5187 pursuant to Act 207, Session Laws of Hawaii 2011.¹ The subject lease is scheduled to expire on May 18, 2014. Lessee explains that it is considering two improvement option packages to the premises. Option 1, in the amount of \$595,000, consists of construction and containment work in an area around two petroleum tanks on the premises, and Option 2, in the amount of \$1,595,000, is for construction and containment work for the entire tank farm. This work involves permitting, grading and installation of a polyurethane liner as required by the Environmental Protection Agency for containment purposes in the event of a spill. The two options of scope of services were proposed in an effort to give Lessee flexibility in implementing the work for the entire property in phases. If granted the extension, Lessee would like to include a special provision giving it the right to early cancellation of the lease by providing the State with a written notice of such cancellation at least one hundred eighty (180) days prior to the following dates:

- a. May 18, 2024
- b. May 18, 2034; and
- c. May 18, 2044.

The cancellation would only be effective upon the dates listed above, and not at any other time.

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.

The subject lease was issued through a public auction, and not pursuant to Act 4, First Special Session of 1960 relating to the 1960 tsunami.

Staff reviewed the file and can report that Lessee is in compliance with all terms and conditions of the lease. Liability and fire insurance are current, with an expiration date of April 1, 2015. Surety Bond No. 105441120, for \$101,520 is through Travelers Casualty and Surety Company of America, will expire on May 18, 2015. The Lessee has never been cited for any illegal or unlawful activity on the State property.

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 last rental reopening occurred on May 18, 2004.

General Lease No. S-5187 is an older form lease that lacks any Phase I environmental site assessment (ESA) requirement upon lease termination. Staff would like to see a Phase I ESA requirement included in the lease as well as greater indemnity protection to the State for hazardous materials, but because the lease was issued at public auction, staff understands the lease terms cannot be amended.

Although Lessee has requested a 40-year term extension, it has not provided staff with a report justifying that long of an extension. Rather, the March 21, 2014 report by Powers Engineering & Inspection, Inc. (PEII) states that with periodic inspection, maintenance and repairs,² the useable economic life of the facility may be extended beyond 20 years. Accordingly, staff feels constrained to recommend that only a 20-year extension be approved at this time. The recommendation below is to allow Lessee approximately one year to expend at least \$595,000 in improvements to the premises, which can be in the form of: (i) new containment permitting, design and construction, or (ii) conducting the inspections and repairs recommended in the PEII report, or a combination of (i) and (ii). Lessee is required to submit proof of expenditures to HDLO by May 31, 2015.

There is only one other DLNR lease in the vicinity of the subject premises. That lease, General Lease No. S-4323, is now held by Kalaniana'ole Real Estate Investments and expires on November 9, 2035. See Exhibit B. Most of the lands surrounding the Aloha Petroleum site are privately owned or under the jurisdiction of the Department of Transportation – Harbors Division.

RECOMMENDATION: That the Board:

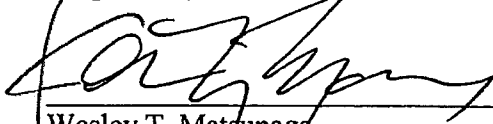
1. Subject to the Lessee fulfilling the Applicant requirements listed above, authorize

² The inspections and repairs in the PEII report generally relate to isolated coating failures and corrosion on piping, anchors, supports and other components, and the condition of a seal at the base of the ethanol tank.

a 20-Year Term Extension of General Lease No. S-5187, under the terms and conditions cited above, which are by this reference incorporated herein and further subject to the following:

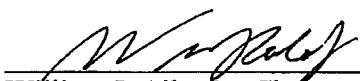
- A. The standard terms and conditions of the most current lease extension form, as may be amended from time to time; provided that the Lessee shall have the right of early termination of the extension effective as of May 18, 2024 if Lessee notifies the Board in writing of its intention to terminate the lease at least 180 days prior to May 18, 2024;
- B. Lessee shall complete a minimum of \$595,000 in improvements which can be in the form of: (i) new containment permitting, design and construction, or (ii) conducting the inspections and repairs recommended in the Powers Engineering & Inspection, Inc. report dated March 21, 2014, or a combination of (i) and (ii), and submit to the Hawaii District Land Office receipts for expenditures by May 31, 2015, or the lease extension shall be subject to cancellation;
- C. Provide a performance bond/security deposit, equal to twice the annual rental amount within 30 days of issuing the Extension;
- D. Review and approval by the Department of the Attorney General; and
- E. Such other conditions as may be prescribed by the Chairperson which are in the best interests of the State.

Respectfully Submitted,



Wesley T. Matsunaga
Land Agent

APPROVED FOR SUBMITTAL:



William J. Aila, Jr., Chairperson

Land Board Meeting: May 9, 2014; D-2:
Approved as amended. See attached
page.

Land Board Meeting: May 9, 2014; D-2: Approved as amended.

Approved as amended. With the agreement of the Lessee, who was represented by Nathan Okubo, Esq., the Board approved: (1) an extension of ten (10) years commencing May 19, 2014 through May 18, 2024 on the condition that lessee provide receipts of expenditures of at least \$297,500 by December 31, 2015; and (2) a provision in the extension document committing the lessee to performing at least a phase I environmental site assessment for the premises upon the expiration or early termination of the lease¹.

The specific amendments to the staff submittal are as follows:

- Page 3, no. 1 of applicant requirements changed 20-year extension to 10-year extension
- Page 3, no. 3 to read: “By December 31, 2015 complete a minimum of \$297,500 worth of improvements...”
- Page 6, recommendation section change 20-year extension to 10-year extension
- Page 6, recommendation section 1B to read in its entirety:
“B. Lessee shall complete a minimum of \$297,500 in improvements which can be in the form of: (i) new containment permitting, design and construction, or (ii) conducting the inspections and repairs recommended in the Powers Engineering & Inspection, Inc. report dated March 21, 2014, or a combination of (i) and (ii), and submit to the Hawaii District Land Office receipts for expenditures by December 31, 2015, or the lease extension shall be subject to cancellation.”

¹ A Departmental sample standard provision for the Department of Attorney General and counsel to work with is as follows:

Phase I environmental site assessment. Prior to termination or revocation of the subject lease or the assignment of the leasehold, Lessee shall conduct a Phase I environmental site assessment and conduct a complete abatement and disposal, if necessary, satisfactory to the standards required by the Federal Environmental Protection Agency, the Department of Health, and the Department of Land and Natural Resources. Failure to comply with the provisions of this paragraph shall not extend the term of this lease or automatically prevent termination or revocation of the lease. The Board, at its sole option, may refuse to approve termination, revocation, or assignment unless this evaluation and abatement provision has been performed. In addition or in the alternative, the Board may, at its sole option if Lessee does not do so, arrange for performance of the provisions of this paragraph, all costs and expenses of such performance to be charged to and paid by Lessee.

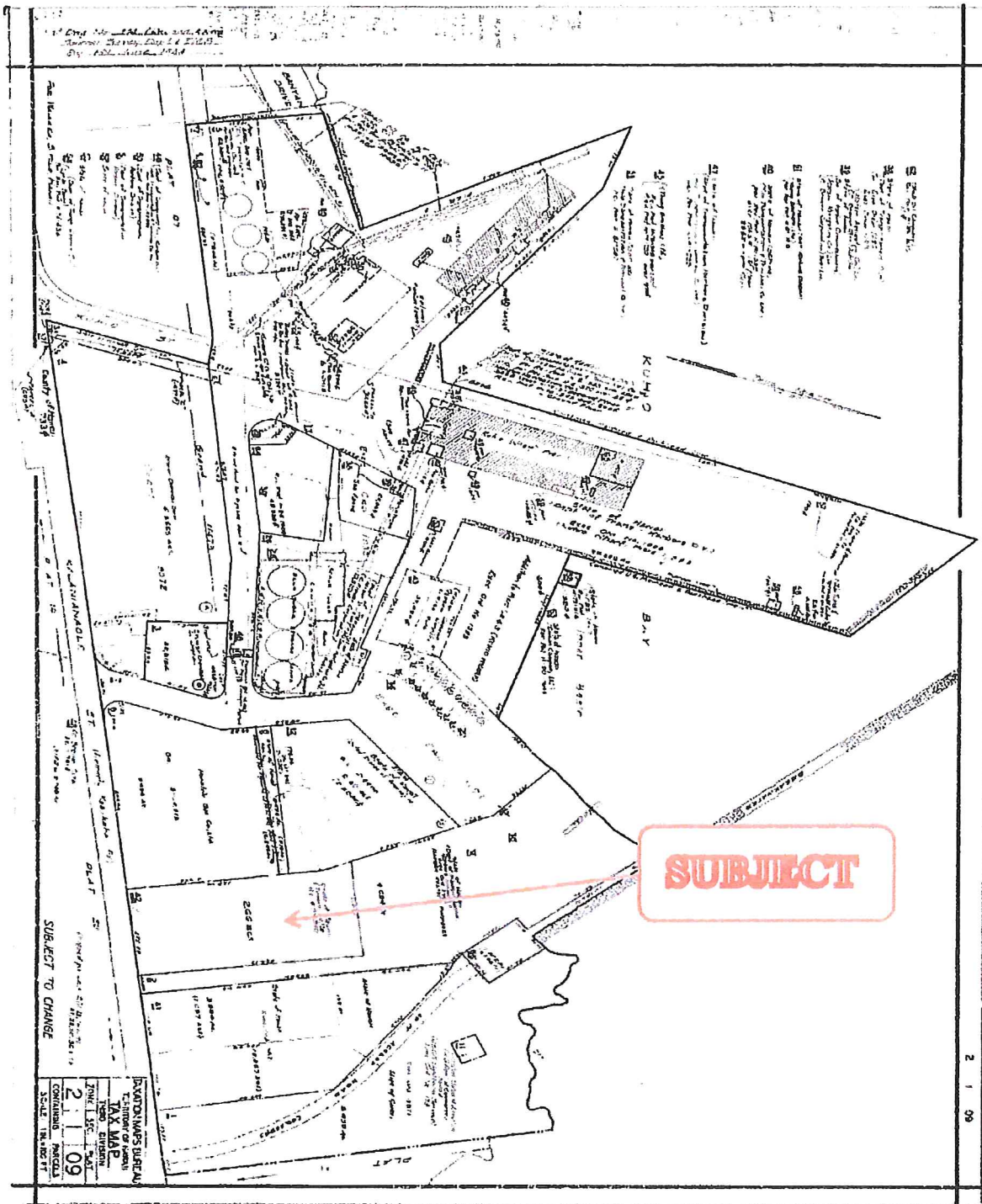


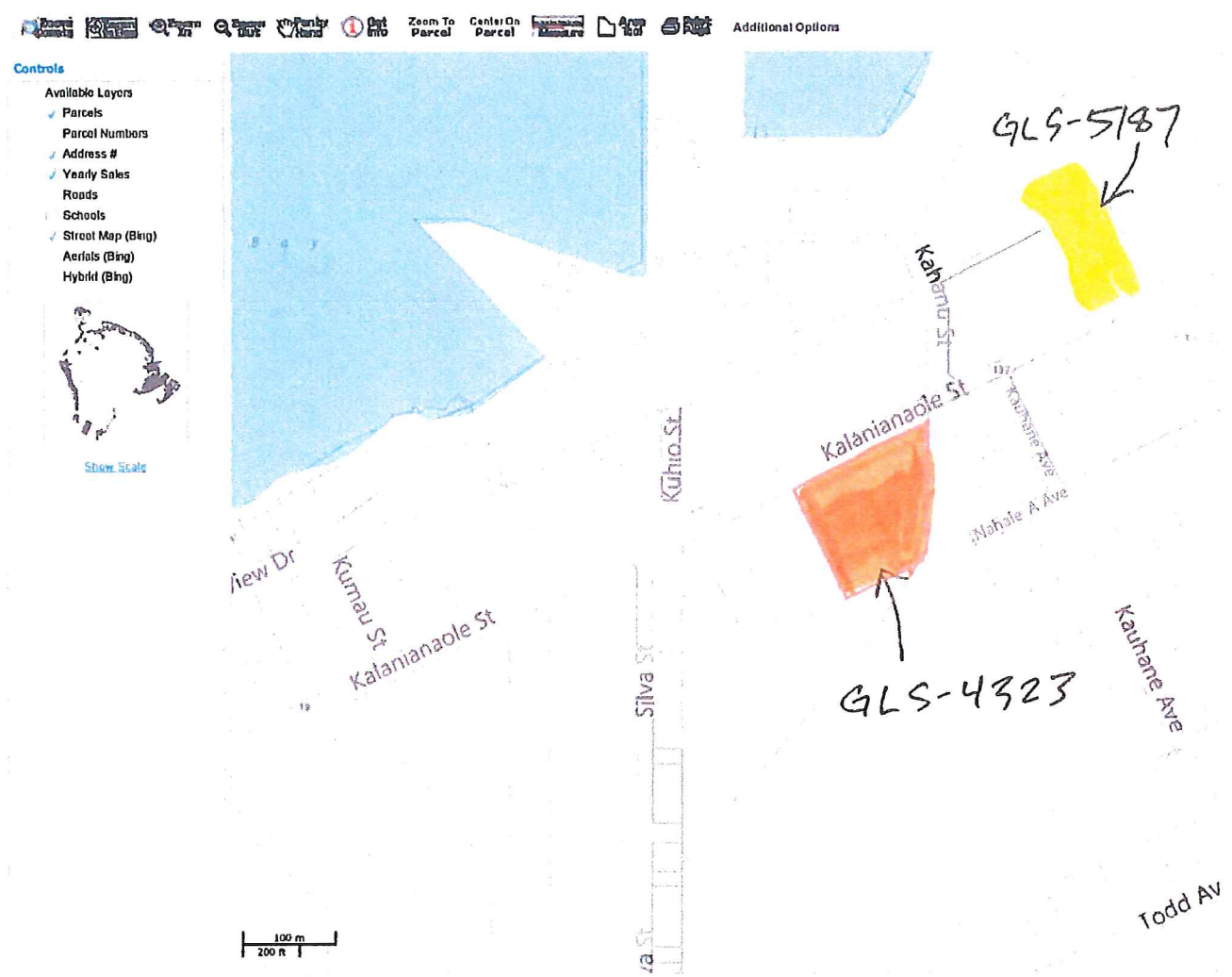
EXHIBIT A



To see all the details that are visible on the screen, use the "Print" link next to the map



SUBJECT



*Hawaii County makes every effort to produce the most accurate information possible. No warranties, expressed or implied, are provided for the data herein, its use or interpretation. The assessment information is from U intended to be used for visual purposes only and should not be used for boundary interpretations or other spatial analysis beyond the limitations of the data. The 'parcels' data layer does not contain metes and bounds des layers that may not have used this layer as a base may not produce precise results. GPS and imagery data will not overlay exactly.

EXHIBIT B

Nathan T. Okubo
Direct Line: (808) 521-9256
Fax: (808) 540-5026
E-mail: nokubo@ca des.com

July 16, 2015

BY EMAIL ONLY TO:
Russell.Y.Tsuji@hawaii.gov
Kevin.E.Moore@hawaii.gov

Department of Land and Natural Resources,
Land Division
Kalanimoku Building
1151 Punchbowl Street, #220
Honolulu, HI 96813
Attn.: Mr. Russell Tsuji and Mr. Kevin Moore

Re: General Lease No. S-5187 dated December 18, 1989 by and between State of Hawaii ("State"), as lessor, and Aloha Petroleum, Ltd. ("Aloha"), as lessee, regarding the proposed extension of lease term

Dear Mr. Tsuji and Mr. Moore:

Per our phone discussion, I represent Aloha in connection with the proposed extension of lease term for the above-entitled lease (the "Lease"). The Lease expired by its terms on May 19, 2014.

As you know, on May 9, 2014, the Board of Land and Natural Resources ("BLNR") approved the extension of the Lease term for ten (10) additional years, commencing May 19, 2014, subject to the following conditions:

(1) Aloha shall pay for an appraisal for the rental re-negotiation for the ten-year period, commencing May 19, 2014;

(2) Aloha shall provide a performance bond/security deposit in an amount equal to twice the annual rental amount for the extended period of the Lease; and

(3) Aloha shall complete a minimum of \$297,500 in improvements, which can be in the form of: (i) new containment permitting, design and

EXHIBIT B

C S

ImanageDB:3165141.2

Cades Schutte Building
1000 Bishop Street, Suite 1200
Honolulu, Hawaii 96813
Tel: 808.521-9200
Fax: 808.521-9210
www.cades.com

Kona Office
75-170 Hualalai Road, Suite B-303
Kailua Kona, Hawaii 96740
Tel: 808.329-5811
Fax: 808.326-1175

Maui Office
444 Hana Highway, Suite 204
Kahului, Hawaii 96732
Tel: 808.871-6016
Fax: 808.871-6017

"Subject" property should be (3) 2-1-009-042 for a land area of approximately 115,870 square feet. Tax Map Key Number (3) 2-2-50-96 refers to another State lease for a property with a land area of approximately 15,002 square feet. Consequently, with an incorrect Tax Map Key Number referencing a substantially smaller property in size and not the correct "Subject" property encumbered by the Lease in Table 1, the DLNR Appraisal either (i) did not make appropriate size adjustments based on the comparable properties referenced in the document, or (ii) did not utilize the appropriate comparable properties based on the correct characteristics of the "Subject" property; and

(2) On Page 16 of the DLNR Appraisal, "Transaction Number 2" makes reference to a 16,000 square-foot site, Tax Map Key Number (3) 2-1-10: Parcels 28 and 35. However, Parcels 28 and 35 collectively only cover a land area of approximately 10,501 square feet (5,501 square feet and 5,000 square feet, respectively). On the contrary, the Tax Map Key Map in Exhibit II, Market Data Land Transactions, for Transaction Number 2 highlights three (3) parcels in yellow, Parcels 28, 34 and 35. Parcel 34 reflects a property with a land area of approximately 5,501 square feet, which is located next to Parcel 28. With the inclusion of Parcel 34, Transaction Number 2 now collectively covers a land area of approximately 16,002 square feet, which is a closer square footage number referenced on Page 16 of the DLNR Appraisal. However, with the inclusion of Parcel 34 in Transaction Number 2 and with Parcel 34 being a corner parcel, a location adjustment was not made for this corner parcel in the DLNR Appraisal.

We believe the foregoing corrections and adjustments should be made to the DLNR Appraisal. Please let us know if the DLNR will agree to make such corrections and adjustments. If the DLNR is willing to make such corrections and adjustments, we would appreciate the opportunity to discuss the DLNR Appraisal with the DLNR and Mr. Conboy.

Thank you for your time and attention to this matter.

Very truly yours,



Nathan T. Okubo, Esq.

for

CADES SCHUTTE

A LIMITED LIABILITY LAW PARTNERSHIP

cc: Client (via e-mail)