

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

September 11, 2015

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

PSF: 15HD-046

Hawai'i

**Lessee's Request for Discretionary Approval for Lease Term Extension, Act 207, Session Laws of Hawaii 2011, General Lease No. S-3742, JH Moku Ola, LLC, Lessee; Amendment of Terms and Conditions Regarding Allowed Use, Assignment and Sublease Provisions for General Lease No. S-3742; Lot 29, Waiakea Industrial Lots, Waiakea, South Hilo, Hawaii, Tax Map Key: (3) 2-2-058:014.**

APPLICANT AND REQUEST:

JH Moku Ola, LLC, a Hawaii Limited Liability Company, lessee.

Improvements to leasehold property financed by lessee pursuant to Act 207, Session Laws of Hawaii 2011 and Section 171-36, Hawaii Revised Statutes in an amount of approximately \$37,064.00.

In order for the Lessee to amortize this expenditure, Lessee is requesting an extension of General Lease No. S-3742 of 10 years, commencing on November 12, 2018 and expiring on November 11, 2028 for an aggregate term of 65 years (initial 55 year term plus the 10 year extension).

LEGAL REFERENCE:

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

LOCATION:

Portion of Government lands of Lots 8 to 13 inclusive, Waiakea Industrial Lots situated at Waiakea, South Hilo, Hawaii, identified by Tax Map Key: (3) 2-2-058:014, as shown on the attached map labeled Exhibit A.

AREA:

2.165 acres, more or less.

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:

For the first 5 years of term, for same business use which Lessee was engaged at time of natural disaster; provided that Lessee may use for uses other than manufacturing of trailers, bodies and unloaders, with prior written consent of Board. Additional use of automotive repair and engine and part sales allowed.

TERM OF LEASE:

Original term of 55 years, commencing on November 12, 1963 and expiring on November 11, 2018.

Requested extension of 10 years commencing on November 12, 2018 and expiring on November 11, 2028.

ANNUAL RENTAL:

Current rent is \$70,700.00, due in quarterly installments of \$17,675.00 on February 12<sup>th</sup> May 12<sup>th</sup>, August 12<sup>th</sup> and November 12<sup>th</sup> of each year.

RENTAL REOPENINGS:

Rental reopenings in the original term were at the end of the 20<sup>th</sup>, 30<sup>th</sup>, 40<sup>th</sup> and 50<sup>th</sup> years of the term. The last rental reopening occurred on March 20, 2011, therefore, staff is recommending the rent for the extended term be determined by an appraisal that will project the rent for the extension period of November 12, 2018 through November 11, 2028.

PROPOSED IMPROVEMENTS:

The lessee proposes to replace the existing metal roof with 24 gauge, zincaluminum, 4-rib roofing material. The lessee will also replace the existing gutter and downspout. The cost of the roof and gutter replacement is estimated to be \$37,000.00

DCCA VERIFICATION:

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

APPLICANT REQUIREMENTS:

Pay for an appraisal of the projected rent payable during the 10-year extension, from November 12, 2018 to November 11, 2028.<sup>1</sup>

Complete approximately \$37,000.00 worth of improvements to the lease premises by September 30, 2016, and provide the Hawaii District Land Office (HDLO) with copies of receipts for the improvements made.

REMARKS:

As a result of Act 32, Sessions Laws of Hawaii 1962, the direct lease of public lands to victims of natural disasters, General Lease No. S-3742 was issued to Hilo Trailer Ltd. for a period of 55 years effective November 12, 1963. A condition of the direct lease was that for the first five years, the character of use be consistent with the business being relocated. Hilo Trailer, Ltd. was in the business of manufacturing trailers, truck bodies and un-loaders.

On October 26, 1966 the lease was assigned from Honolulu Iron Works Company, Successor of Hilo Trailers, Ltd., as surviving corporation under merger agreement dated 10/31/1965 as Assignor, to Edward R. Kuwaye, James R. Kuwaye, Yasuo Kuwaye and Yoshinobu Kuwaye, doing business as co-partners under the firm name of Edward R. Kuwaye & Company. At its meeting of March 10, 1967, under agenda item F-12, the Board consented to the change in character of use to include automotive repair and engine and parts sales.

The Board, at its meeting of January 12, 1979 under agenda item F-1-a, consented to the assignment of lease from Edward R. Kuwaye, James R. Kuwaye, Yasuo Kuwaye and Yoshinobu Kuwaye, dba co-partners under the firm name of Edward R. Kuwaye & Company as Assignors, to Yasuo Kuwaye husband of Hanako Kuwaye, as Assignee.

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<sup>1</sup> At the Board meeting of June 12, 2015, Item D-2 (regarding an extension request for a different lease), the Board directed staff to request an opinion from the Department of the Attorney General as to: (i) who should bear the cost of the appraisal report, (ii) whether there is an option to split the cost between the State and the lessee, and/or (iii) whether the Board has discretion to determine who bears the cost. Accordingly, staff is including a recommendation below that the appraisal report for the extension period be held in abeyance until the Department of the Attorney General has made findings on opinion request.

At its meeting of April 12, 1990, under agenda item F-1-e, the Board consented to the assignment of lease from Yasuo Kuwaye husband of Hanako Kuwaye, as Assignor to Yasuo Kuwaye, Trustee under that Revocable Trust Agreement of Yasuo Kuwaye dated April 9, 1986 and American Trust Co. of Hawaii, Inc., Corporate Trustee under that certain Revocable Trust Agreement of Yasuo Kuwaye dated April 9, 1986, as Assignees.

Further, at its meeting of July 8, 1994 under agenda item F-1-d, the Board consented to the assignment of lease from Yasuo Kuwaye, Trustee under that Revocable Trust Agreement of Yasuo Kuwaye dated April 9, 1986 and American Trust Co. of Hawaii, Inc., Corporate Trustee under that certain Revocable Trust Agreement of Yasuo Kuwaye dated April 9, 1986, as Assignor to Yasuo Kuwaye, Trustee under that certain unrecorded Revocable Trust Agreement of Yasuo Kuwaye dated April 9, 1986, as amended by Amended Revocable Trust Agreement of Yasuo Kuwaye (Self-Trusted Trust) dated March 23, 1993, as Assignee.

At its meeting of February 11, 2005 under agenda item D-8, the Board consented to the assignment of lease from Yasuo Kuwaye, Trustee under that certain unrecorded Revocable Trust Agreement of Yasuo Kuwaye dated April 9, 1986, and amended by Amended Revocable Trust Agreement of Yasuo Kuwaye (Self-Trusted Trust) dated March 23, 1993, as Assignor to JH Moku Ola, LLC, as Assignee, who, at the time of the assignment, was a tenant subleasing a portion of the property<sup>2</sup>.

LEASE EXTENSION:

The Lessee’s current 55 year lease is set to expire on November 11, 2018 and the Lessee is requesting a 10 year extension pursuant to Act 207, Session Laws of Hawaii 2011<sup>3</sup> in order to amortize the cost of improvements to the property. These improvements include the replacement of the roof along with other minor renovations to the property at a cost in excess of \$37,000.00. An appraisal evaluation performed by a certified appraiser has determined that the economic life of the proposed improvements will exceed the twelve-plus year period necessary to amortize the refurbishments.

Staff additionally notes that JH Moku Ola, LLC 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.

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<sup>2</sup> Paragraph 22 of the lease states “that the Lessee shall not assign, sublease or mortgage the whole of the leasehold premises without the prior written approval of the Board, provided, further, that the Lessee may sublet a part of the leasehold premises without approval of the Board”.

<sup>3</sup> 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 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 and Act 32, Sessions Laws of Hawaii 1962 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. These acts provided the 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 properties.

Since the implementation of Act 207, SLH 2011, there have been several leases within the Kanoelehua Industrial Area that have been granted a ten year extension. Eight of these leases are direct leases awarded as a result of Act 4. The other leases although in the Kanoelehua Industrial Area, are along Railroad Avenue and were 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 agency. As one of the largest stakeholders of commercial/industrial land in the Hilo area, the Department of Land and Natural Resources understands the need for a comprehensive analysis of the area in order to develop an economic strategy that will encourage new enterprises in addition to supporting the established businesses.

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 department’s commercial leases in 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:

- Determine the market demand for the KIAA lease properties, particularly the demand for commercial/industrial 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 under a master lease from the State for commercial, industrial or other uses permitted by the applicable zoning.

The results of the 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.

There are no outstanding rental reopening issues. Staff is of the opinion that an expenditure of \$37,000.00 in improvements does justify a 10-year extension, as permitted under Act 207, SLH 2011. The Lessee is current with rent, insurance and performance bond.

AMEND LEASE TERMS:

Because the lease was issued by direct negotiation instead of public auction, the Board has authority to amend the lease to change the character of use provision and make other amendments. An amendment to the character of use provision is recommended in this case because the Lessee’s use of the premises is potentially inconsistent with the use restriction in the lease.<sup>4</sup> The lease originally provided in part that:

“use the leased land for the first five (5) years of the term of the lease for the same business use or undertaking in which the Lessee was engaged at the time of the natural disaster or a use designated by the Board; provided, however, that the Lessee may devote or place said demised premises to a use or uses other than manufacturing of trailers, bodies and unloaders in character,<sup>[5]</sup> with the prior written consent of the Board, which consent shall not be unreasonably or arbitrarily withheld; provided, further, that should the Lessor consent to a change in the character of the use, it shall be upon such terms and conditions as set by the Lessor.”

The lease was amended with Board approval of March 10, 1967, to expand the allowed use to include “automotive repair and engine parts and sales”.

The Lessee, JH Moku Ola, LLC manufactures high quality, custom made wood cabinets for homes throughout the state. A change in the character of use to “uses allowed under the County of Hawaii zoning code, ML-20, limited industrial”, would allow for the existing use and additionally benefit the State by opening the door to a wider range of uses, thereby making the property more appealing/valuable for future leasing.<sup>6</sup>

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4 Although the use restriction in the lease only applied to the first five years of the lease, it is unclear what the allowed use was intended to be after the first five years. Amending the character of use provision will resolve this ambiguity.

5 At the time the lease was issued, localized manufacturing of truck and trailer equipment was a more economical and practical method of supplying the trucking industry with finished goods than importation. However, the need for this type of specialized industry is no longer necessary as finished products can be brought in at a much lower cost resulting in less demand for the type of service the lease was initially issued for.

6 Changing the character of use should not have an impact on the determination of fair market rent charged under the lease. The lease went through a rent reopening arbitration in 2013. No adjustments to rent were made in the course of that process based on the use restrictions contained in the lease.

Also, the lease contains language which allows the Lessee to sublease portions of the property without Board approval, consent or knowledge. There are currently three subleases on the property.<sup>7</sup> Staff believes the better practice is to require prior Board consent for all subleases. Therefore, Staff is recommending the assignment/sublease provision in the lease be amended to reflect the current language for assignments and subleases.

No agency comments were solicited on the request because it involves a lease extension, not a new disposition.

**RECOMMENDATION:**

That the Board, subject to the Applicant fulfilling the Applicant requirement listed above:

1. Authorize the extension of General Lease No. S-3742 to JH Moku Ola, LLC 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. JH Moku Ola, LLC shall complete the proposed improvements as described above and submit to Land Division staff, receipts verifying payment for the improvements by September 30, 2016, or be subject to cancellation;
  - C. At the Board meeting of June 12, 2015, Item D-2 (regarding an extension request for a different lease), the Board directed staff to request an opinion from the Department of the Attorney General as to: (i) who should bear the cost of the initial appraisal report, (ii) whether there is an option to split the cost between the State and the lessee, and/or (iii) whether the Board has discretion to determine who bears the cost. Accordingly, the appraisal report for the extension period shall be held in abeyance until the Department of the Attorney General has made findings on the opinion request, and staff has returned to the Board to report on the same;
  - 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.

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<sup>7</sup> Miranda Country Store (ranch and farm supplies), Big Island Toyota (parking), and Hertz Car Rental (service and maintenance).

2. Authorize the amendment of General Lease No. S-3742 to change the character of use from “manufacturing of trailers, bodies and unloaders” to “uses allowed under the current County of Hawaii Zoning Code, ML-20, limited industrial”, and to update the lease provision titled “Assignments, etc.” (par. 22 of the lease) with the current language used by the Department of the Attorney General for assignment and subleasing provisions. The amendment of the lease shall further be subject to the following:
  - A. The standard terms and conditions of the most current consent to change in character of use and amendment of lease document forms, as may be amended from time to time;
  - B. Review and approval by the Department of the attorney general; and
  - C. Such other terms and conditions as may be prescribed by the Chairperson to best serve the interests of the State.

Respectfully Submitted,

  
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Gordon C. Heit  
District Land Agent

APPROVED FOR SUBMITTAL:

  
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Suzanne D. Case, Chairperson





