

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

June 24, 2016

Ref. No.: 16HD-065
GLS-5619

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

HAWAII

Consent to Mortgage of Sublease K-4 with Estoppel Certificate, General Lease No. S-5619, Natural Energy Laboratory of Hawaii Authority, Lessee, Cyanotech Corporation, Sublessee/Mortgagor, First Foundation Bank, Mortgagee, Kalaoa 1st-4th, North Kona, Hawaii, Tax Map Key: (3) 7-3-043: 063.

APPLICANT AND REQUEST:

Cyanotech Corporation, requesting Consent to Mortgage of Sublease K-4 with Estoppel Certificate from First Foundation Bank, Mortgagee, in an amount not to exceed \$2,000,000.00.

LEGAL REFERENCE:

Section 171-22, Hawaii Revised Statutes, as amended.

LOCATION:

Portion of Government lands situated at Kalaoa 1st-4th, North Kona, Hawaii, identified by Tax Map Key: (3) 7-3-043: 063 as shown on the attached map labeled Exhibit A.

AREA:

90.067 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:

YES ___ NO X

SUBLEASE CHARACTER OF USE:

The commercial production of various microalgal products including, but not limited to, *spirulina*, natural beta-carotene, astaxanthin, natural biopesticides, and *Chlorella*.

TERM OF LEASE:

65 years, commencing on July 3, 2001 and expiring on July 2, 2066. Last reopening was on July 3, 2011. Next rental reopening is scheduled for July 3, 2021.

SUBLEASE TERM:

40-years, commencing on January 1, 1996 and expiring on December 31, 2035.

ANNUAL LEASE RENTAL:

\$480.00 Per Annum Plus Fifty Percent (50%) of the Net Operating Income for the Period July 3, 2011 to July 2, 2021.

The inclusion of a \$480.00 per annum rent in addition to the annual rent of fifty percent of the net operating income is due to the Board of Land and Natural Resource's minimum rent policy established in May 2005.

Annual rental shall be fifty percent (50%) of the net operating income (NOI)¹.

SUBLEASE RENTAL:

\$24,932.82 per month

The fixed rental fee is calculated at a rate of \$246.78 per acre, per month, for unimproved lands (83.13 acres), \$2,200.00 per pond for two ponds, and \$18.00 for tanks, for periods covering 2/1/2012 to 1/31/2017.

USE OF LOAN PROCEEDS:

An itemized breakdown of the loan proceeds will be disbursed as follows:

\$2,000,000.00 Revolving working capital line of credit to support operations
\$2,000,000.00 Total loan distribution

¹ NOI is the actual net income remaining after all adjusted operating expenses are deducted from the effective gross income including a reserve for replacement and for major repairs not covered in the operating budget. This does not include federal funds and grants.

REMARKS:

At its meeting of April 26, 1996, the Board of Land and Natural Resources, under Agenda Item D-14, approved the Cancellation of Sublease K-2 and Facilities Use Agreement and Consent to Sublease K-4 of General Lease No. S-4717, Natural Energy Laboratory of Hawaii Authority (NELHA), Sublessor, to Cyanotech Corporation, a Nevada corporation, as Sublessee. Sublease commenced on January 1, 1996 and will expire on December 31, 2026, for a term of thirty (30) years.

The NELHA Board approved Supplemental Agreement No. 1 of Sublease K-4, dated November 21, 1996, which modified the Primary Agreement by:

1. Adding Parcels H1 (4.412 acres) and H2 (8.587 acres), which increased the sublease area to 90.067 acres, more or less.
2. Increasing the fixed rental fee from \$9,360.00 per month to \$12,313.00 per month.

At its meeting of November 19, 1999, the Board of Land and Natural Resources, under Agenda Item D-20, approved as amended, the cancellation of General Lease No. S-4717 and S-5157; Cancellation of Governor's Executive Order No. 3282; and Direct Issuance of a New Lease, General Lease No. S-5619 to the NELHA.

On April 18, 2000, the Chairperson of the Board of Land and Natural Resources approved the Consent to Mortgage of Sublease K-4 and Estoppel Certificate in favor of B & I Lending. Loan proceeds with an aggregate principal amount of \$3,500,000.00 was under the United States Department of Agriculture, Rural Development guaranteed loan program.

At its meeting of May 23, 2008, Agenda Item D-8, the Board of Land and Natural Resources approved consent to mortgage of Sublease K-4 to Bridgeview Capital Solutions, Mortgagee, in an amount not to exceed \$ 1,078,400.00 for working capital.

The NELHA Board, at its meeting of January 31, 2012, approved Supplemental Agreement No. 2 of Sublease K-4, which included the following:

1. Term extension of Sublease K-4 for ten (10) years, commencing on January 1, 1996, and expiring on December 31, 2035.
2. Adjust the fixed monthly rental fee of \$12,313.00 (11/21/1996-1/31/2012) to \$24,932.82, which is calculated at a rate of \$246.78 per acre, per month for 83.13 acres of unimproved land, \$2,200.00 per pond per month for two ponds, and \$18.00 per month for tanks. The fixed rental fee shall commence on February 1, 2012.

3. Insert the standard Hazardous Waste (Level 1) Evaluation clause.

At its meeting of May 11, 2012, under agenda Item D-2, the Land Board approved consent to mortgage of Sublease K-4 through Pacific Rim Bank for \$5,500,000.00. Loan proceeds of \$1,878,000.00 were distributed for the purchase of machinery & equipment, and \$622,000.00 for building improvements. Additional funds required for the \$7,482,000.00 project was financed through a Cyanotech Equity Loan for \$1,982,000.00.

By email, dated April 5, 2016, Ms. Ann Tanouye, Vice President, First Foundation Bank, on behalf of Cyanotech Corporation, requested Consent to Mortgage of Sublease K-4 with Estoppel Certificate² of General Lease No. S-5619, NELHA, Lessee, Cyanotech Corporation, Sublessee/Mortgagor, in favor of First Foundation Bank, as Mortgagee. The subject consent is for a revolving working capital letter of credit in the amount of \$2,000,000.00.

The NELHA Board reviewed and approved Cyanotech's request for consent to mortgage of Sublease K-4, which will be a third mortgage, used as a line of credit for \$2,000,000.00. Cyanotech is the largest client of NELHA and leases approximately 90 acres for microalgae production.

NELHA 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.

Staff reviewed the file and can report that for the past two (2) years, Lessee has been in compliance with all lease terms and conditions. The Lessee has never been cited for any illegal or unlawful activity on the State property.

The next rental reopening is scheduled for July 3, 2021.

Staff has no objections to the request.

² An Estoppel Certificate, which accompanies the Consent to Mortgage of a Lease, confirms the current status of the Tenant and Landlord rights on the existing lease. In general, it assures the Mortgagee that all terms and conditions of the lease is in compliance at time of financing the mortgage.

RECOMMENDATION: That the Board:

- A. Consent to the Mortgage of Sublease K-4 of General Lease No. S-5619, NELHA, Lessee, between Cyanotech Corporation, Sublessee/Mortgagor, and First Foundation Bank, Mortgagee, subject to the following:
1. The standard terms and conditions of the most current consent to mortgage form, as may be amended from time to time;
 2. The loan proceeds shall be used for the purposes as stated in "Use of Loan Proceeds" above. The Lessee shall maintain records of loan expenditures which may be inspected by the Department;
 3. Review and approval by the Department of the Attorney General; and
 4. Such other terms and conditions as may be prescribed by the Chairperson to best serve the interests of the State.
- B. Authorize the execution of an Estoppel Certificate subject to the following:
1. The standard terms and conditions of the most current estoppel certificate form, as may be amended from time to time;
 2. Review and approval by the Department of the Attorney General; and
 3. Such other terms and conditions as may be prescribed by the Chairperson to best serve the interest of the State.

Respectfully Submitted,



Wesley T. Matsunaga
Land Agent

APPROVED FOR SUBMITTAL:



Suzanne D. Case, Chairperson

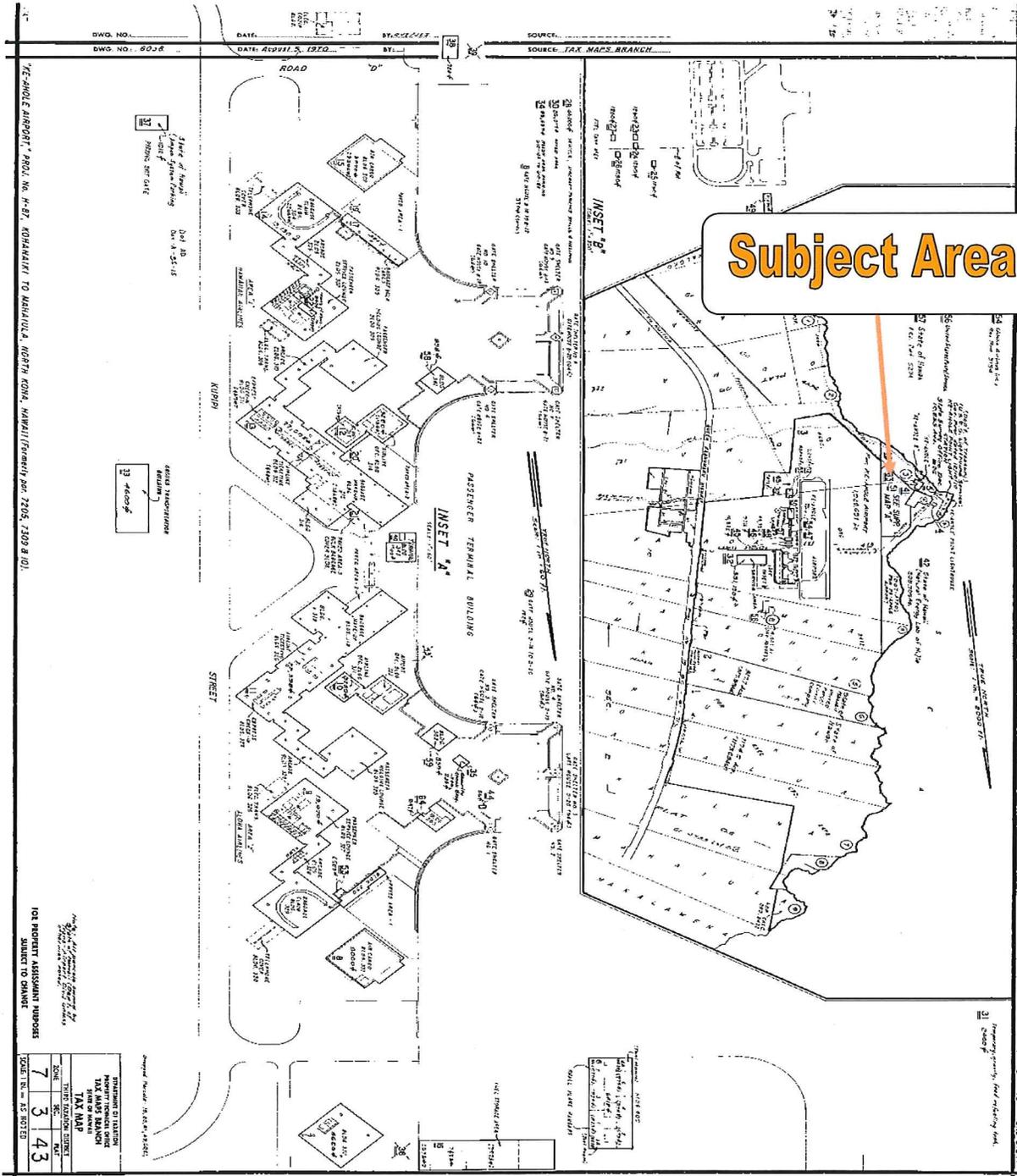


EXHIBIT A

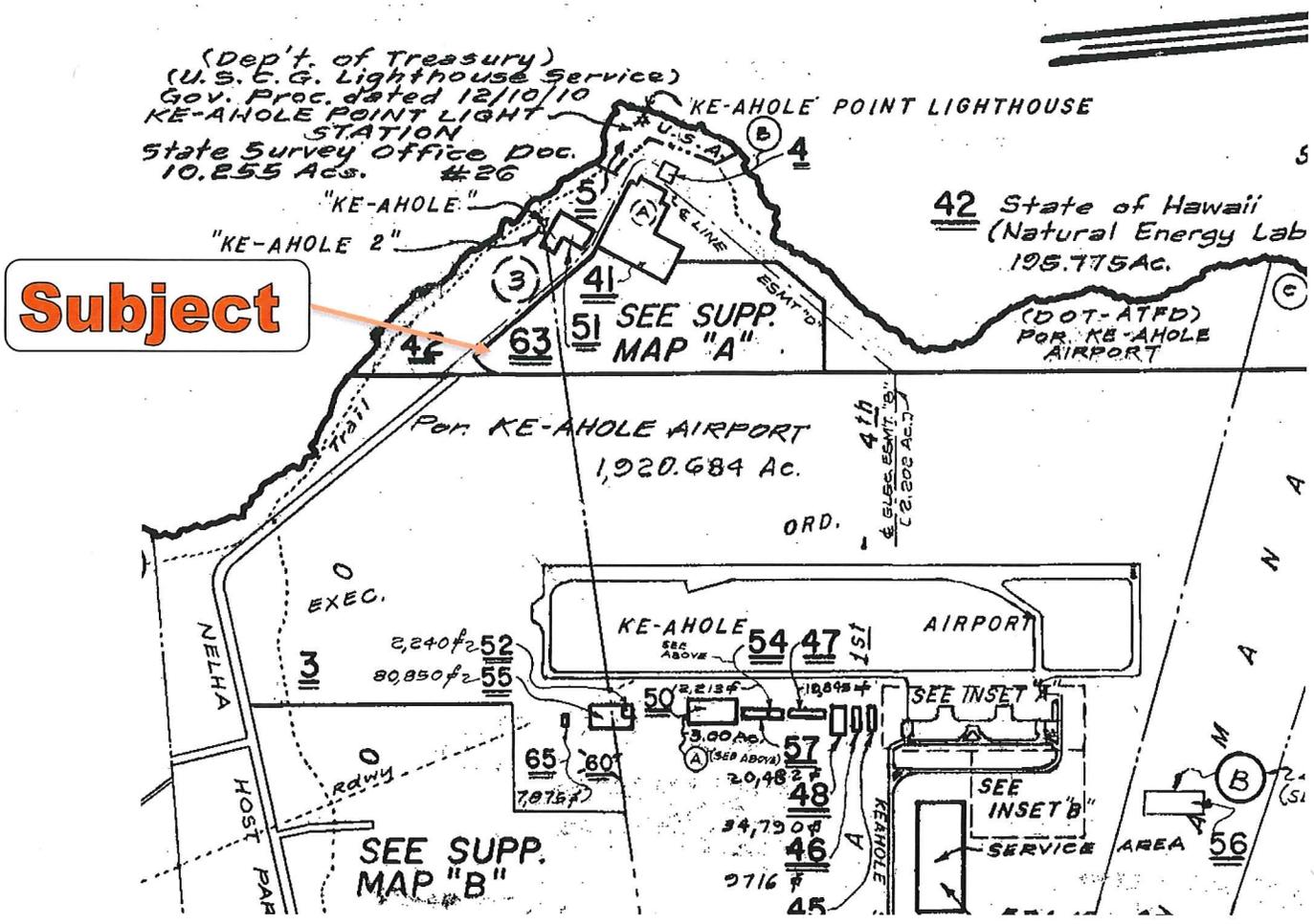


EXHIBIT A