

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

December 9, 2016

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

Hawaii

Approve a 3-Year Term Extension of General Lease No. S-3698, Bank of Hawaii, Lessee, Pursuant to Act 207, Session Laws of Hawaii 2011; Lot 7, Waiakea House Lots Extension, Waiakea, South Hilo, Hawaii, Tax Map Key: (3) 2-2-049:022.

APPLICANT AND REQUEST:

Bank of Hawaii, lessee, a Hawaii for-profit corporation.

Proposed improvements to the leasehold property will be financed by the lessee pursuant to Act 207, Session Laws of Hawaii 2011 and Section 171-36, Hawaii Revised Statutes in an amount of approximately \$20,776.00.

In order for the Lessee to fully amortize its expenditures, Lessee is requesting an extension of General Lease No. S-3698 for a period of 3 years, commencing on January 26, 2017 and expiring on January 26, 2020 for an aggregate term of 58 years (initial 55 year term plus the 3 year extension).

LEGAL REFERENCE:

Sections 171-36, Hawaii Revised Statutes, as amended.

LOCATION:

Portion of Government lands of Waiakea House Lots Extension situated at Waiakea, South Hilo, Hawaii, identified by Tax Map Key: (3) 2-2-049:022, as shown on the attached map labeled Exhibit A.

AREA:

29,912 square feet, 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:

Business purposes

TERM OF LEASE:

Original term of 55 years, commencing on January 26, 1962 and expiring on January 25, 2017.

Request for an extension of 3 years commencing on January 26, 2017 and expiring on January 25, 2020.

ANNUAL RENTAL:

Current rent is \$46,800.00, due in quarterly installments of \$11,700.00.

RENTAL REOPENINGS:

Rental reopenings in the original term were at the end of the 15th, 25th, 35th and 45th years of the term. The last rental reopening occurred on January 25, 2007, therefore, staff is recommending the rent for the extended term be determined by an appraisal that will establish the rent for the extension period of January 26, 2017 through January 25, 2020.

PROPOSED IMPROVEMENTS:

The lessee proposes to replace the metal supporting structure of the air conditioning system and perform roof renovations to the 740 sf east wing roof of the building that is currently leaking at the drain areas. The cost of the air conditioning system and roof improvements is estimated to be \$20,776.00.

DCCA VERIFICATION:

Place of business registration confirmed:	YES
Registered business name confirmed:	YES
Good standing confirmed:	YES

APPLICANT REQUIREMENTS:

Applicant shall be required to:

1. Complete approximately \$20,776.00 of proposed improvements to the lease premises

by August 1, 2017, and provide the Hawaii District Land Office with copies of receipts and photographs of the improvements made prior to September 1, 2017.

BACKGROUND:

General Lease No. S-3698 (GLS-3698) was sold to Bank of Hawaii by way of public auction. The lease was issued for a term of 55 years commencing on January 26, 1962 and expiring January 25, 2017. The property was part of a resubdivision of the Waiakea House Lots, but being located on the corner of Kanoiehua and Kawili streets, is now both functionally and spatially more associated with the Kanoiehua Industrial Lots.

The current 55-year lease is set to expire on January 25, 2017 and the lessee is requesting a 3 year extension pursuant to Act 207, Session Laws of Hawaii 2011¹ to amortize the cost of proposed improvements to the property estimated at \$20,776.00.

A site inspection on September 21, 2016 (inspection report attached as Exhibit B) revealed the property is well maintained and in good condition. Roof leaks were noted in the east wing of the building where there is a flat top roof. After inspection by a roofing contractor, the cause was determined to be inadequate operation of two roof drains resulting in ponding of water (refer to attached Exhibit C). Lessee has proposed to cure this condition and in addition, replace rooftop counter flashings and flash and seal all duct work penetrations. The work will be warranted for 5 years with prepaid contractor annual inspections for the duration of the warranty. Further, the metal support structure for the air conditioning unit has sustained considerable corrosion in the Hilo climate. Lessee proposes to have supports fabricated for the frame and condenser coils.

On November 15, 2016, R.W. Spangler LLC, lessee consultant, tendered its report regarding the economic life and value of the proposed improvements to the leasehold premises (refer to attached Exhibit D). The report assesses that the proposed improvements will extend the useful life of the improvements by approximately 5 years and will add value approximating the anticipated costs of the project of \$20,776.00.

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 2026. 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 Kanoiehua. 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.

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 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 either the Department of Land and Natural Resources (DLNR) or the Department of Hawaiian Home Lands (DHHL). As one of the largest stake holders of commercial/industrial land in East Hawaii, DLNR recognizes the need for a comprehensive analysis of land use in 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, DLNR-Land Division retained the services of the consulting firm, Munekiyo & Hiraga, Inc., for the purpose of providing a feasibility study and land use planning analysis for the KIA.

Key elements of the study/analysis was to:

- 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 under a master lease from the State for industrial, commercial or other uses permitted by the applicable zoning.

The results of the study will be used to assist DLNR in formulating a use strategy for the future of the KIA and create an economic region that will benefit both the public and private sectors. However, good planning does not happen overnight; Departmental reviews, revisions and approvals may extend the timeframe for a well-conceived final plan. Many of the key elements aforementioned require lengthy administrative processes which could take several years to accomplish.

The Lessee is in compliance with the terms and conditions of the lease. The Lessee is current with rent, insurance and performance bond. A recent inspection showed good maintenance of the property and existing structures.

Staff is recommending that the rent payable for the 3-year extension period commencing January 26, 2017 be determined by immediate appraisal.

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

RECOMMENDATION:

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

1. Authorize the extension of General Lease No. S-3698 to Bank of Hawaii 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. Bank of Hawaii shall complete the proposed improvements as described above by August 1, 2017 and submit to the Hawaii District Land Office copies of receipts verifying payment for the improvements and photographs of the work by September 1, 2017, or be subject to cancellation.
- C. Review and approval by the Department of the Attorney General; and
- D. Such other conditions as may be prescribed by the Chairperson which are in the best interests of the State.

Respectfully Submitted,



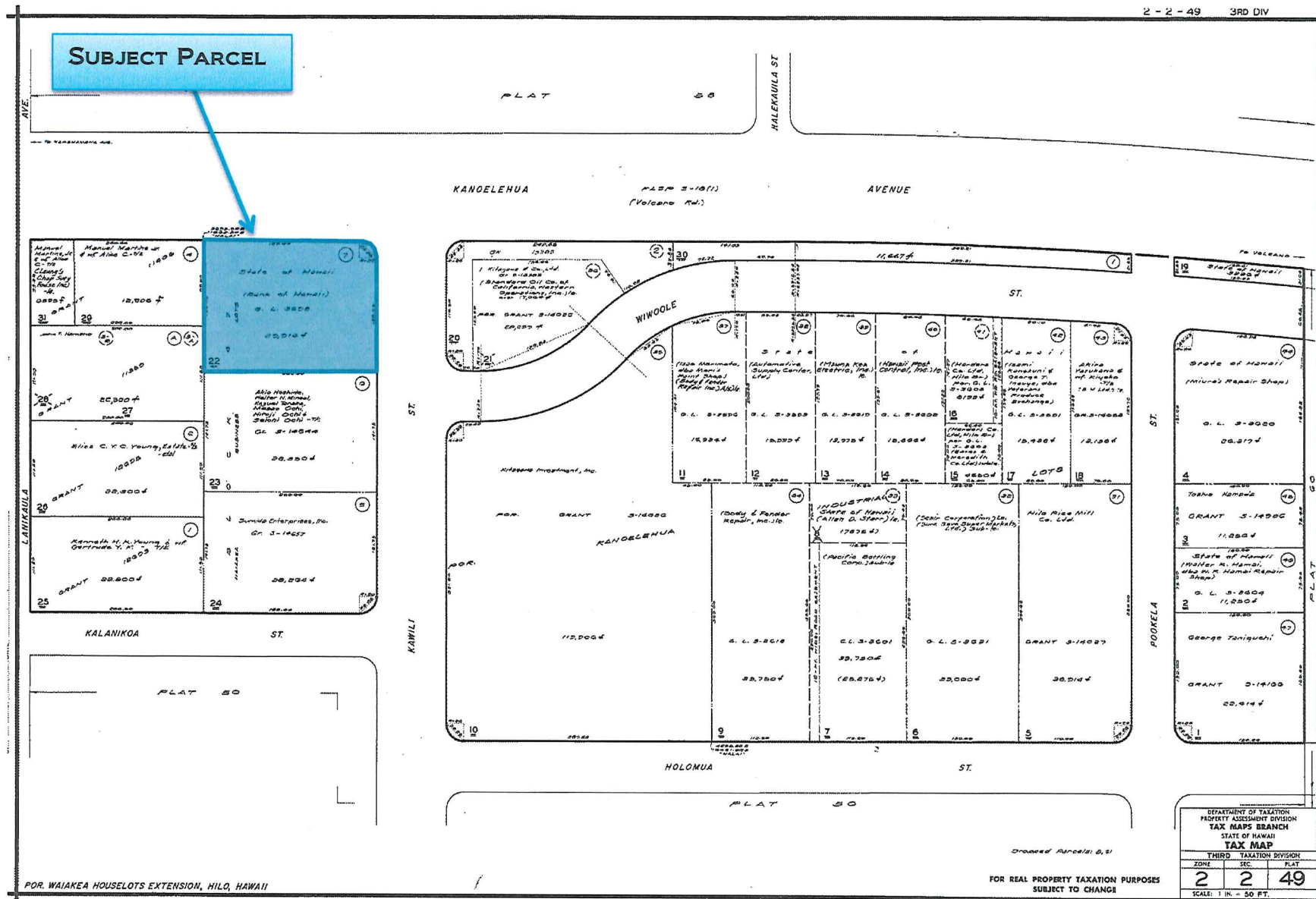
Candace Martin
Land Agent

APPROVED FOR SUBMITTAL:



Suzanne D. Case, Chairperson

2 - 2 - 49 3RD DIV



INSPECTION REPORT
Commercial/Industrial/Resort/Other Business**General Information**Document Number: GLS 3698 or RPS _____Character of Use Commercial/IndustrialInspection Date: 09/21/2016 Inspection Time: 9:00 amLand Agent: Candace Martin**TENANT INFORMATION**Name: Bank of HawaiiHome Phone: N/AAddress: 417 E. Kawili StreetBusiness Phone: (808) 961-0681Hilo, HI 96720Fax: N/AContact Person: Roxann IkedaContact Phone: (808) 854-2082**SITE INFORMATION**TMK: (3) 2-2-049:022Area: 29,912 square feetSite Address: 417 E. Kawili Street, Hilo, Hawaii 96720**FISCAL INFORMATION**

ITEM	N/A	CURRENT= COMPLIANCE	DEFAULT = NON-COMPLIANCE	COMMENTS
Rent		X		Due quarterly. Next due in October 2016.
Liability Insurance		X		1M/2M expires 6/1/2017
Fire Insurance		X		10M expires 3/1/2017
Bond		X		2x annual rent expires 1/25/2017

FIELD INSPECTION RESULTS (refer to Field Inspection Worksheet)

ITEM	N/A	COMPLIANCE	NONCOMPLIANCE	COMMENTS
Subleases	X			
Improvements		X		
Premises		X		
Character of Use		X		

Field Inspection Worksheet
Commercial/Industrial/Resort/Other Business**File Review****LICENSES/PERMITS/CONSENTS**

ITEM	DLNR Approval Docs in File			COMMENTS/NOTES/LISTS
	N/A	YES	NO	
Subletting	X			attach copy of list or map if applicable
Improvement Construction Buildings		X		note deadlines for % completion
Improvement Construction Other structures/misc.		X		note deadlines for % completion

Field Inspection

ITEM	SATISFACTORY?			COMMENTS/NOTES
	N/A	YES	NO	
SUBLEASES	X			
Consents approved				
Use adheres to lease purpose	X			
IMPROVEMENTS		X		*The east wing roof has some leaking. The gutter on that section appears to be leaking and is missing a downspout. The fixed windows on that section need to be resealed. The edges of the two mansard roofs on the west side are peeling back and in need of repair. The drive thru window mechanism is no longer functional and parts are not available so it is not in use.
<u>Buildings/Residences:</u> roof		X		
paint		X		
exterior		X		
interior		X		
<u>Structures:</u> roads		X		The parking lot area needs to be resealed. The two driveways are unidirectional with a right-in right-out only traffic pattern onto Kawili St. No access is permitted from Kanoelehua. During the inspection, the air conditioner company informed BoH that the condenser & compressor units of the airconditioning system needed replacement.
walkways		X		
fencelines	X			
others		X		
PREMISES		X		
clean, sanitary, orderly appropriate storage/use of hazardous materials		X		
CHARACTER OF USE		X		
adheres to lease purpose				

ITEM	SATISFACTORY?			COMMENTS/NOTES
	N/A	YES	NO	
Other:				

9/21/2016 – Inspection walk-thru was led by Joe Francher of the Corporate Facilities Division, Bank of Hawaii. He indicated that the roof of the east wing would be repaired/replaced as necessary, the gutter and windows would of that same section would be repaired, and the air-conditioning unit would have the necessary parts replaced.

*See attached photos

09/21/2016 Photos of GL S-3698 Bank of Hawaii

417 E. Kawili St., Hilo, Hawaii, TMK: (3) 2-2-049:022.



Eastside (Kanoelehua Ave) from corner of Kanoelehua Ave and Kawili St.



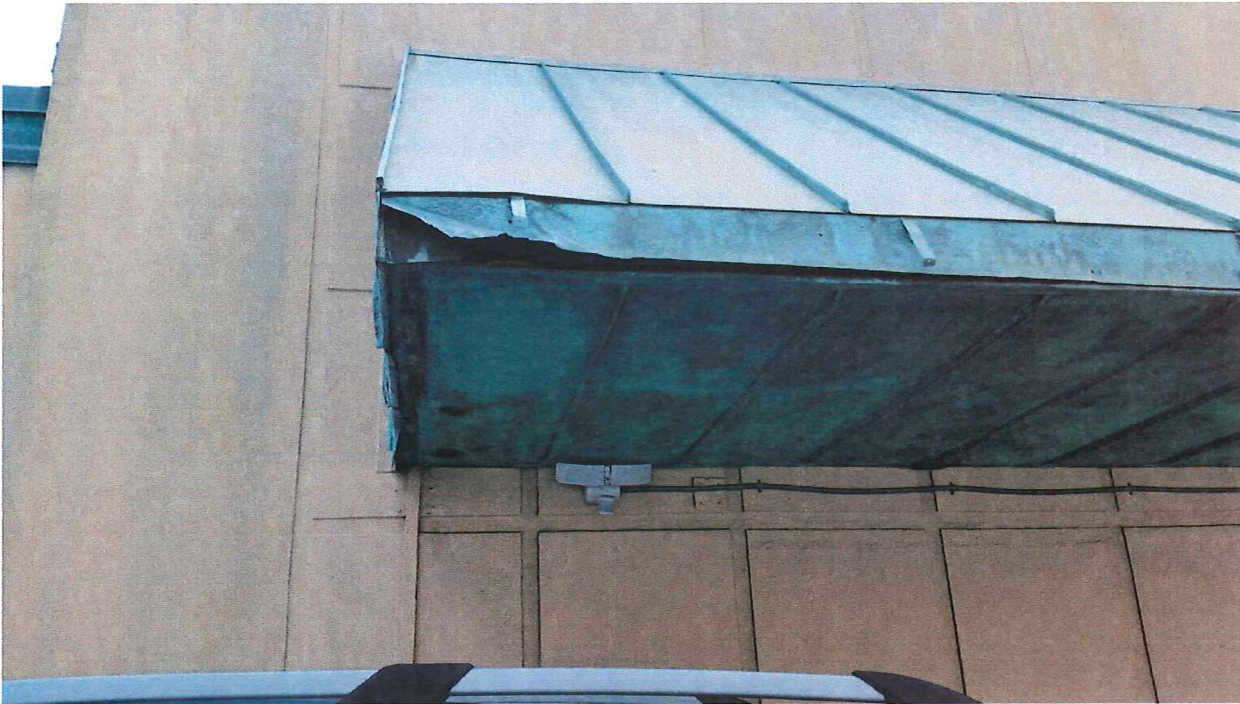
Eastside and rear of building from Kanoelehua Ave.



Southside (front) of building fronting Kawili St.



Westside of building with unidirectional exit driveway on left. Note: Drive-thru teller not in operation.



Peeling edge of mansard roofs located over drive-thru teller lane.



Northside (rear) of building looking south down exit lane. Enclosure in center houses mechanical equip.



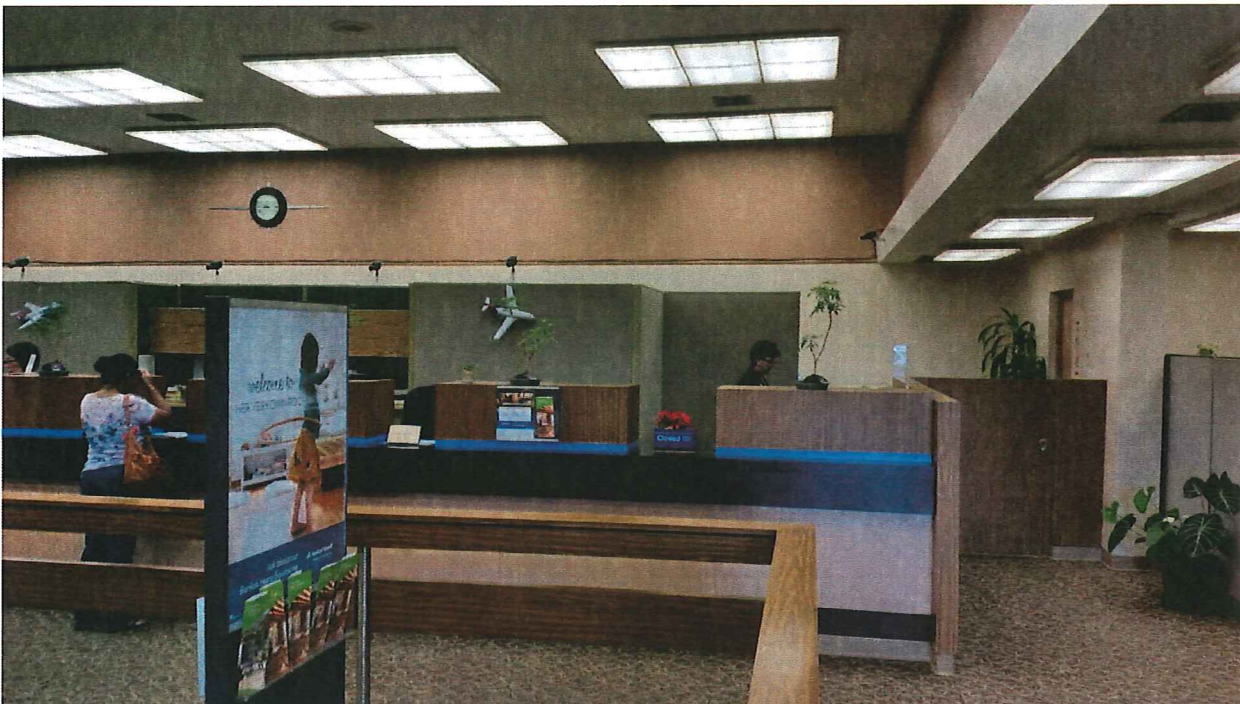
Northside looking west.



Eastside of mechanical equipment enclosure.



Lobby area from eastside entry.





Lobby area from eastside entry.



Southside entrance (on left) with vault area on right.



East wing on left (arrows indicate areas of following pictures).



East wing (arrows indicate areas of following pictures).



Photo of area A. Substantial leak on southwest end of east wing.



Photo of area B. Leak damage to southeast end of east wing.

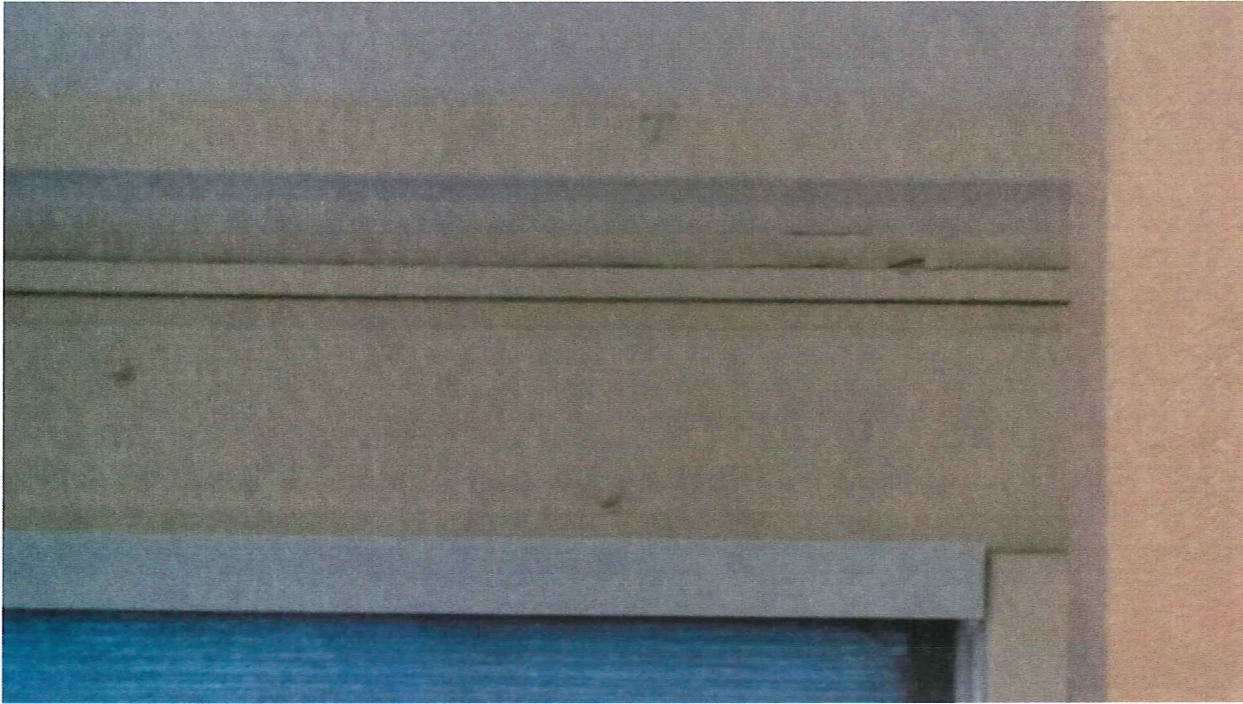


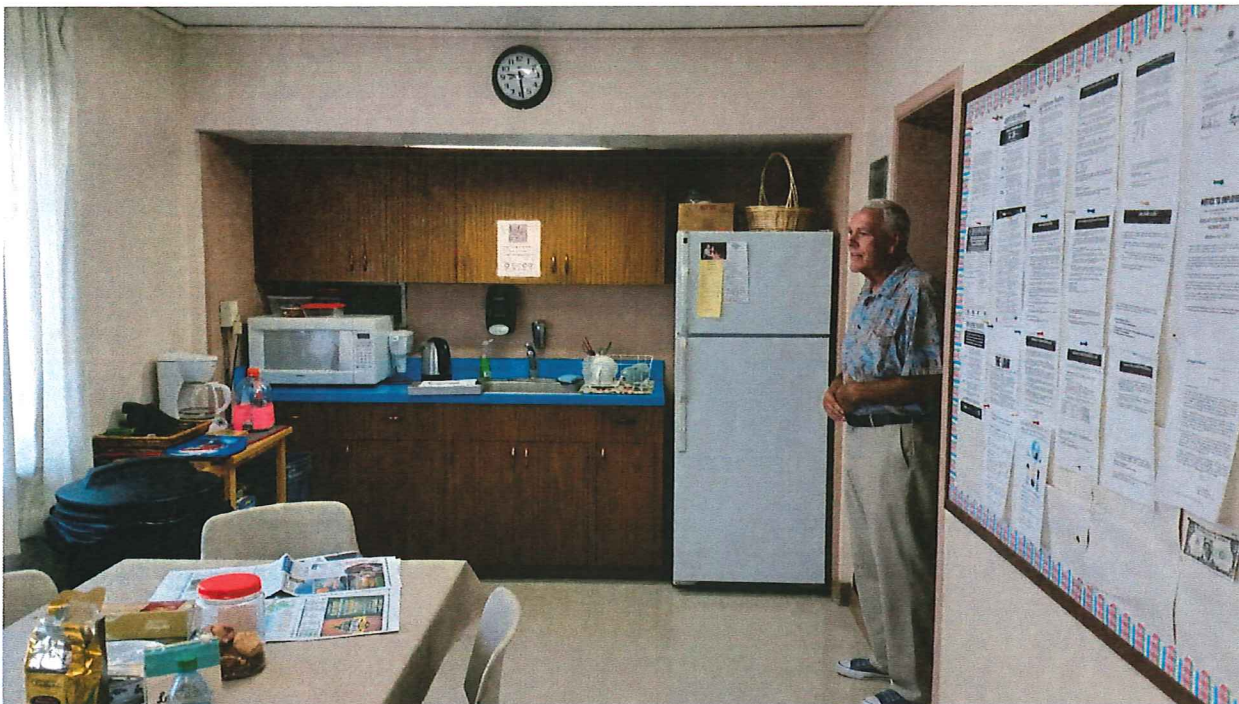
Photo of area C. Leak damage from water behind wall on eastside wall of east wing. Suspect gutter problem.



Photo of area D. Leak damage located at Northeast end



Non-public section behind tellers looking south along west wall of building.



Breakroom/Lunchroom

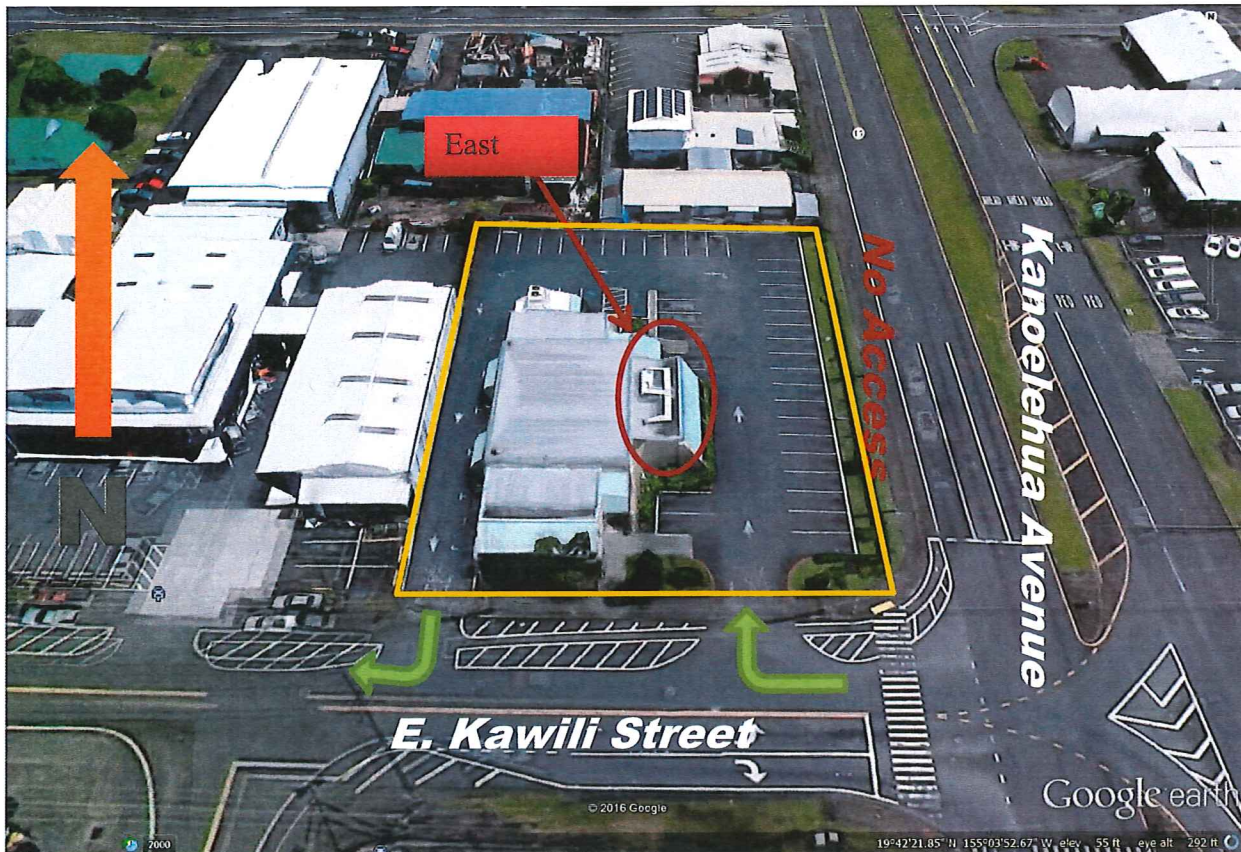


Restroom door in locker room area off of breakroom/lunchroom.



2 stall restroom with sink (out of frame on left).

Google aerial image of GL S-3698



Note: One-way traffic pattern with right turn only both in and out (left turn from E. Kawili St not permitted). No access from Kanoelehua.

EXHIBIT C

Photo below shows current conditions of ponding water:



Photo below shows current conditions of roof drain:



Photo below shows current conditions:



Aerial photo below of project location:



R.W. SPANGLER LLC
Real Estate Analysis

11.15.16

Gordon C. Heit
District Land Agent, State of Hawaii
Department of Land and Natural Resources
Hawaii District Land Office
75 Aupuni Street, Room 204
Hilo, Hawaii 96720
808.961.9590 tel
808.961.9599 fax
gordon.c.heit@hawaii.gov

RE: Value added improvements
427 East Kawili Street, Hilo, Island and County of Hawaii, Hawaii 96720
TMK: (3) 2-2-49-22

Dear Mr. Heit:

Based on my review, the proposed air conditioning and roof improvements at the Bank of Hawaii Branch located at 427 East Kawili Street, Hilo will add value to the property approximating the anticipated cost of the project of \$20,776 (see allocation below and contractor quotes attached) and extend the useful life of the building by approximately five years.

Air conditioning improvements	\$8,751
Roof improvements	<u>\$12,025</u>
TOTAL	\$20,776

The roofing contractor identified that the existing roofing is in poor condition, is in excess of 15 years old and has active leaks. The active leaks serve to disrupt occupancy and represent a material form of deferred maintenance that any prospective buyer would identify and correct in a similar or more extensive manner as proposed.

The roofing improvements bid consists of:

- Repair leaks at two drain areas
- Perimeter counterflashing caulking replacement
- Seal three duct penetrations with fabric and Silicone coating
- Annual inspection for 5 years

The improvements will only be made to the roofing with the HVAC.

District Land Agent, State of Hawaii
Department of Land and Natural Resources
Attn: Mr. Heit
11.15.16
Page two

The proposed work will remediate defects to the property and extend the useful life of the building by approximately five years. Importantly, the roof is not failing universally. Rather, the ponding areas near the drains on the HVAC portion are the primary isolated source of the leaks. A prudent buyer would likely opt to extend the useful life by five years (with support of the annual inspections over the five-year period) by addressing the problem areas at this point rather than opting for a premature roofing coating replacement on the entire building.

The air conditioning improvements represent a correction of corrosive deferred maintenance related to the air conditioning frame. While a relatively simple materials and labor improvements, failure of the frame would preclude functional air conditioning of the building and potentially cause roofing damage. Accordingly, the proposed improvements will facilitate the necessary function of the building mechanical systems and serve as a preventative measure against potential collateral damage from a frame failure.

The proposed improvements and related costs would be identified by a prudent buyer and the purchase price adjusted downward by the magnitude of the estimated cost of the improvements consistent with the market value definition. A separate value before and after the improvements was not necessary given the relatively minor amount of costs along with the nature of and identifiable status of the improvements. Buyers often attempt to re-trade during escrow related to these types of deferred maintenance issues discovered during due diligence. The adjustment in price is tied to the cost to cure. Accordingly, if the improvements are conducted pro-actively, the form of deferred maintenance will not exist during due diligence and not corresponding price reduction will be in play.

Respectfully submitted,



Robert W. Spangler, MAI
R.W. Spangler LLC
P.O. 137
Wailuku, HI 96793
808-446-4129
Hawaii State Certified General Appraiser, CGA-967
Expiration Date December 31, 2017