

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

October 26, 2018

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

PSF: 18HD-113

Hawaii

**Consent to Assign Sublease K-26 under General Lease No. S-5619,
CELLANA LLC, Assignor, to CYANOTECH CORPORATION, Assignee,
Kalaoa 1st, North Kona, Hawaii, Tax Map Key: (3) 7-3-043:102.**

APPLICANT:

Cellana LLC, a Delaware limited liability company, as Assignor
Cyanotech Corporation, a Nevada corporation, as Assignee.

LEGAL REFERENCE:

Section 171-36(a)(5), Hawaii Revised Statutes, as amended.

LOCATION:

Portion of Government lands of the Natural Energy Laboratory of Hawaii Authority
situated at Kalaoa 1st, North Kona, Hawaii, identified by Tax Map Key: (3) 7-3-043:102,
as shown on the attached map labeled Exhibit A.

AREA:

6.216 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

ENCUMBRANCE:

Subject parcel is a portion of State land encumbered under General Lease No. S-5619 to
the Natural Energy Laboratory of Hawaii Authority

CHARACTER OF USE:

The Lessee shall use or allow the premises leased to be used solely to develop, maintain and operate an ocean-related high technology industrial park in accordance with Chapter 206M, Hawaii Revised Statutes, and to allow for ancillary and accessory uses that will assist the development to become self-sufficient, and for telecommunication purposes.

SUBLEASE CHARACTER OF USE:

Current: Biofuels demonstration facility from photosynthetic microbes.
Amended: Production of marine microalgae products.

TERM OF LEASE:

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

TERM OF SUBLEASE:

30 years, commencing on December 15, 2007 and expiring on December 14, 2037. Rental reopenings every 5 years. Last rental reopening was scheduled to occur on December 15, 2017, but has been on hold due to default of rent payments.

ANNUAL LEASE RENTAL:

\$480.00 per annum, plus fifty percent (50%) of the net operating income.

ANNUAL SUBLEASE RENTAL:

Current:

Fixed Rental Fee: \$1,800 per acre, per month based on 6.216 acres = \$11,188 per month (\$134,265 per annum).

Amended:

Fixed Rental Fee: \$500 per acre, per month based on 6.216 acres = \$3,108 per month (\$37,296 per annum).

Both the current and amended lease include the following provision for percentage rent:

If 2% of Sublessee's gross sales for any calendar year exceeds the amount of fixed rental fees already paid by Sublessee for such period, then Sublessee shall pay percentage rent equal to 2% of Sublessee's gross sales less the amount of fixed rental fees already received by Sublessor for said calendar year.

CONSIDERATION:

\$495,000.00.

RECOMMENDED PREMIUM:

Not applicable as the lease does not allow for a premium.

DCCA VERIFICATION:

ASSIGNOR: CELLANA LLC

Place of business registration confirmed: YES

Registered business name confirmed: YES

Good standing confirmed: YES

ASSIGNEE: CYANOTECH CORPORATION

Place of business registration confirmed: YES

Registered business name confirmed: YES

Good standing confirmed: YES

BACKGROUND:

The Natural Energy Laboratory of Hawaii Authority (NELHA) manages an ocean science and technology park in Kailua-Kona on the island of Hawaii, operating under General Lease No. S-5619¹ (GL S-5619). NELHA is attached to the Department of Business and Economic Development and is the successor since 1990 to the Natural Energy Laboratory of Hawaii (NELH), a research and development (R&D) facility created by State legislation in 1974 on 322 acres of raw lava at Keahole Point. Its purpose was to take advantage of the abundant cold deep seawater and warm surface seawater lying just offshore to incubate alternate energy R&D. NELH installed seawater pipelines to bring the valuable natural resources ashore, built rudimentary research facilities, and engaged pioneering research tenants with visions of turning their ocean science ideas into business endeavors. One of these pioneers was Cyanotech Corporation, which still operates there today.

Four decades after the first pipeline was installed, NELHA is a successful, financially self-sustaining agency of state government that now includes over 800 acres of leased fastlands, together with an easement of over approximately 3,000 acres of submerged lands. Roughly 240 acres of fastlands have been subleased to tenants for natural energy and other uses, providing rental income for the State, and economic activity that contributes significantly to economic development in the County of Hawaii. Another 170 acres are used for roadways or reserved for setbacks and preserves. The balance of leasable lands remains in an unimproved state awaiting future tenants.

¹ Prior to the issuance of General Lease No. S-5619, NELHA/NELH operated on the premises pursuant to General Lease Nos. S-4717 and 5157, and Executive Order No. 3282.

DISCUSSION:

Upon approval of the NELHA Board on September 18, 2018, the Hawaii District Land Office received a request for consent to assignment of Sublease K-26 from Cellana LLC (Cellana), to Cyanotech Corporation (Cyanotech). Pursuant to Section 171-36(a)(5), Hawaii Revised Statutes, this request is being brought to the Board of Land and Natural Resources for its consent.

Cellana is the original sublessee of K-26 and developed the existing improvements on the subject parcel. It began as a research facility focused on development of technologies for the commercial production of biofuels from microalgae. The construction and operation of the facility was funded through multiple million-dollar level grants from US DOE, USDA and private investment.

Cellana started experiencing significant financial difficulties several years ago after existing grants ended and expected new grants did not materialize. Cellana ceased major operations and monthly payments in November 2017. The total amount due to NELHA was \$279,537.83. In May 2018, Cellana was given 90 days to cure the default or the sublease would be terminated. A termination letter was sent on August 31, 2018 requiring \$100,000 be paid by September 10, 2018 or the lease would be terminated. On September 5, 2018, NELHA received the \$100,000 payment which will allow continuation of the lease until the end of 2018.

On September 7, 2018, NELHA received a formal request for consent to assignment of the sublease to Cyanotech. Cyanotech is a world leader in microalgae technology and a solid sublessee of the NELHA facility. Cyanotech began operations at NELHA in 1986 and currently holds Sublease K-4 on the adjacent 90 acre parcel.

Cellana and Cyanotech have entered into an asset purchase agreement that allows Cyanotech to take over ownership of the research facility improvements at a cost of \$495,000. The agreement requires an immediate payment of \$100,000 to NELHA for delinquent rent (which was done on September 5th) with the remaining balance of \$179,537.83 to be paid to NELHA upon closing. The balance of the purchase price will be paid to Cellana in monthly installments over 12 months.

Both companies specialize in microalgae products. However, Cellana's focus has been on biofuels and as such, the base rent was in line with the energy use base rent of \$1800/acre/month. On the other hand, Cyanotech will be looking at potential marine microalgal products that are classified under NELHA's productive use rent structure. Cyanotech has requested an amendment to the sublease that changes the monthly rental rate from the energy use base rent to a more moderate production use base rent of \$500/acre/month. The NELHA Board has approved the amendment which results in a significant reduction in monthly income to NELHA, however, the proposed rate is fair given the expected use for the property. Additionally, NELHA will share in any

successes brought about by the development of new product lines and the Cellana facility will be in use and maintained so as to prevent a state of further disrepair.

Review of the lease file indicates that Lessee is in compliance with all terms and conditions of the lease. The outstanding rental reopening issues related to the K-26 Sublease by the assignor have been resolved by direct negotiation between NELHA and Cyanotech.

The proposed Assignee 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.

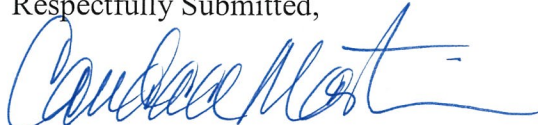
No agency or community comments were solicited as there will be no new disposition or change in land use in the assignment of the sublease.

RECOMMENDATION:

That the Board consent to the assignment of Sublease K-26 of General Lease No. S-5619 from CELLANA LLC, as Assignor, to CYANOTECH CORPORATION, as Assignee, subject to the following:

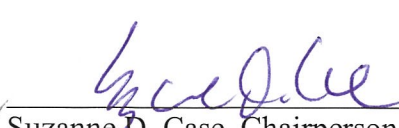
1. The standard terms and conditions of the most current consent to assignment form, as may be amended from time to time;
2. Review and approval by the Department of the Attorney General; and
3. Such other terms and conditions as may be prescribed by the Chairperson to best serve the interests of the State.

Respectfully Submitted,



Candace Martin
Land Agent

APPROVED FOR SUBMITTAL:



Suzanne D. Case, Chairperson

EXHIBIT A

NELHA at Keahole Point

