

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

August 14, 2020

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

Hawai'i

Consent to Amend Sublease under General Lease No. S-3742, JH Moku Ola, LLC, Lessee, to Maui Varieties Investments, Inc., Sublessee, Waiakea Industrial Lots, Waiakea, South Hilo, Hawai'i, Tax Map Key: (3) 2-2-058:014

APPLICANT:

JH Moku Ola, LLC, a Hawaii limited liability company, as Sublessor, to Maui Varieties Investment, Inc., a Hawaii corporation, as Sublessee.

LEGAL REFERENCE:

Section 171-36(a)(6), Hawaii Revised Statutes (HRS), as amended.

"Revision to Sublease Rent Participation Policy" adopted by the Board of Land and Natural Resources (Board) on May 26, 2000, agenda item D-24, as amended by "Resubmittal: Amendment to the Sublease Rent Participation Policy" approved by the Board on January 26, 2001, under agenda item D-8, and as further amended by "Modification of Staff Recommendation in Board Action of January 26, 2001, Item D-8, As Amended," on August 24, 2012, under agenda item D-14.

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

LEASE CHARACTER OF USE:

Allowed uses under the County of Hawaii zoning code, ML-20, Limited Industrial.

TERM OF LEASE:

Original term of 55 years, commencing on November 12, 1963 and expiring on November 11, 2018. Board approved extension of 10 years commencing on November 12, 2018 and expiring on November 11, 2028.

Board approved an additional extension of 30 years<sup>1</sup> pursuant to Act 149, Session Laws of Hawaii 2018, commencing on November 12, 2028 and expiring on November 11, 2058

TERM OF SUBLEASE:

Current approved sublease agreement, 9.5 years, commencing on May 12, 2019 and expiring on November 11, 2028.

Requesting extension of sublease agreement commencing November 12, 2028 and expiring November 11, 2058.

ANNUAL LEASE RENTAL:

Current rent is \$96,588.00, due in quarterly installments of \$24,147.00 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. The rent for the lease extension period is as follows:

November 12, 2028: \$104,750  
November 12, 2038: \$140,775  
November 12, 2048: \$189,190

ANNUAL SUBLEASE RENTAL:

\$300,000.

RECOMMENDED ADJUSTMENT TO LEASE RENTAL:

- November 12, 2028 - \$9,379.00 per year additional rent.
- November 12, 2038 - \$5,776.00 per year additional rent.
- November 12, 2048 - \$ 935.40 per year additional rent.

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<sup>1</sup> April 9, 2020, Agenda Item D-6

(Refer to attached Exhibit B for analysis of sublease rental income.)

DCCA VERIFICATION:

SUBLESSOR:

Place of business registration confirmed: YES X NO \_\_\_  
Registered business name confirmed: YES X NO \_\_\_  
Good standing confirmed: YES X NO \_\_\_

SUBLESSEE:

Place of business registration confirmed: YES X NO \_\_\_  
Registered business name confirmed: YES X NO \_\_\_  
Good standing confirmed: YES X NO \_\_\_

REMARKS:

At its meeting of June 28, 2019, under agenda item D-3, the Board of Land and Natural Resources (Board) authorized the Land Division to negotiate a development agreement as required in Act 149. The Board also consented to the sublease to Maui Varieties Investments, Inc., the business wanting to occupy a portion of the property. The Board deferred staffs' recommendation for increasing the rent based on the sublease rent to be paid to the lessee by the sublessee and asked staff to inquire with the Department of the Attorney General (AG) whether the lease, as amended, allows the Board to charge additional rent based on sublease rent collected and report back to the Board. Based on the AG's response, the Board has the right to increase the rent under the subject lease.

At its meeting of December 13, 2019, under agenda item D-4, the Board approved increasing the rent based on the rent paid to the lessee by the sublessee but deferred a decision on the amount of additional rent. Staff was asked to work with the lessee on an appropriate amount and report back to the Board along with a breakdown of the miscellaneous allowances as to the exact amount if improvement, insurance and maintenance allowances.

Staff met with the lessee and reached a tentative agreement on the amount for the additional rent. Then, at its meeting of April 9, 2020, under agenda item D-6, the Board approved an increase in the rent in the amount of \$11,328.00 per year through the remainder of the lease term.

The lessee is now requesting an amendment to the sublease agreement to extend the term from November 12, 2028 until November 11, 2058 with the same terms and conditions set forth in the sublease. The base rent paid under the sublease shall be adjusted with the rent increase as provided above.

Staff is recommending that the Board consent to the amendment to the sublease with the periodic adjustment in the lease rent as described above.

RECOMMENDATION:

That the Board:

1. Consent to the amendment to the sublease under General Lease No. S-3742 between JH Moku Ola, LLC, as Sublessor, and Maui Varieties Investments, Inc, as Sublessee, subject to any applicable conditions cited above which are by this reference incorporated herein and further subject to the following terms and conditions:
  - a. The Lessee shall submit construction plans of the Sublessee's improvements to the Land Division for the Chairperson's approval prior to constructing any improvements on the demised premises;
  - b. The standard terms and conditions of the most current consent to sublease form, as may be amended from time to time;
  - c. Approve the increase in lease rent for 30-year extension period as follows; November 12, 2028 – \$9,379.00 per year additional rent.  
November 12, 2038 – \$5,776.00 per year additional rent.  
November 12, 2048 – \$ 935.40 per year additional rent.
  - d. Review and approval by the Department of the Attorney General; and
  - e. Such other terms and conditions as may be prescribed by the Chairperson to best serve the interests of the State.

Respectfully Submitted,

*Gordon C. Heit*

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Gordon C. Heit  
District Land Agent

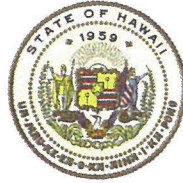
APPROVED FOR SUBMITTAL:

*Suzanne D. Case*

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*SD* Suzanne D. Case, Chairperson





## EXHIBIT B

**STATE OF HAWAII  
DEPARTMENT OF LAND AND NATURAL RESOURCES  
LAND DIVISION**

75 Aupuni Street, Room 204  
Hilo, Hawaii 96720  
PHONE: (808) 961-9590  
FAX: (808) 961-9599

July 20, 2020

### MEMORANDUM

TO: Suzanne D. Case, Chairperson

THROUGH: Russell Y. Tsuji, Land Division Administrator

FROM: Gordon C. Heit, Hawaii District Land Agent

SUBJECT: In-House Recommendation – Sublease Participation Calculation

GL No.: S-3742  
Lessee/Sublessor: JH Moku Ola, LLC  
Sublessee: Maui Varieties Investment, Inc.  
Location: Waiakea, South Hilo Hawaii  
Lease Area: 2.165 acres (94,307 square feet)  
(Total building area – 22,000 sq. ft.)  
Sublease Area: 74,000 square feet (includes 14,000 sq. ft. bldg.)  
Tax Map Key: (3) 2-2-058:014  
Char. of Use: Allowed uses under COH ML-20, Limited Industrial

We have been requested to provide an in-house evaluation of the sublease premium due to the State for the subleasing of a portion of GL S-3742 JH Moku Ola, LLC, Lessee/Sublessor to Maui Varieties Investment, Inc, Sublessee. The sublease documents and information provided by Lessee were analyzed and staff applied the formula approved by the Land Board on January 26, 2001, agenda item D-8, and modified by the Board at its meeting on August 24, 2012, agenda item D-14, comprising of the Sublease Rent Participation Policy.

The original term of this lease was for 55 years, commencing on November 12, 1963 and expiring on November 11, 2018. At its meeting of September 11, 2015, agenda item D-1, the Board approved an extension of the lease for 10 years to allow the Lessee to amortize self-financed improvements in the amount of \$37,000.00. These improvements were completed by September 30, 2016.

Further, at its meeting of April 9, 2020, under agenda item D-6, the Board extended the lease for an additional 30 years pursuant to Act 149, Session Laws of Hawaii 2018. This allowed the lessee to make significant improvements in the amount of \$800,000 to the property and structures.

In addition to the extension, the lease was also amended to provide that the Board shall have the right to review and approve the rent to be charged to the sublessee and shall have the right to revise the rent for the premises based on the rental rate charged to the sublessee.

The Lessee has submitted a proposal to sublease a portion of the lease area to Maui Varieties Investments, Inc. (doing business as Ace Hardware Hawaii). The subleased portion of the property includes 60,000 sq. ft. of open storage area as well as 14,000 sq. ft. of warehouse space. The Sublessee proposes to utilize the property as a distribution center for the company's retail outlets on the island of Hawaii. In addition, Sublessee will have a retail operation in the warehouse.

Staff was guided by the approved Rent Participation Policy item 1(c)(ii) for lessees paying fair market rent which states:

*“If the lessee subleases improvements not owned by the State, the Board shall not receive any portion of sublease rents from subleasing improved space unless: (i) that right and method of calculation are specifically stated in the lease, or (ii) participation in sublease rents is warranted considering the age of the improvements (including but not limited to the extent to which the improvements have been depreciated or amortized), lessee’s expenditures to maintain the same in relation to sublease revenues, and the extent to which the lessee actually occupies and uses the lease premises for its own business.”*

The Lessee made improvements to the lease in the amount of \$800,000 as a condition of the 30-year extension, pursuant to Act 149 SLH 2018 and therefore will need to amortize its cost over the remaining term of the lease. These improvements include the installation of a septic system, modifications to the warehouse to accommodate the sublessee's retail operation and resurfacing the parking lot.

The following calculations are for the three 10-year lease periods from 11/12/2028 through 11/11/58 and allows for amortization of the Lessee's financial improvements along with allowances for property insurance, maintenance costs, General Excise Tax, and Real Property Tax.<sup>1</sup>

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<sup>1</sup> 2019 Real Property Tax assessment

**CALCULATIONS: Rental Period 11/12/2028 – 11/11/2038**

Annual Sublease Ground Rent:	\$300,000.00
Less G. E. Tax	<u>- 12,750.00</u>
Net Annual Sublease Ground Rent:	\$287,250.00
<u>Allowances:<sup>2</sup></u>	
Investment Return (\$800,000 x 4.25%)	\$ 34,000.00
Real Property Taxes: (\$20,889 x 80%)	\$ 16,706.00
Maintenance	\$ 30,000.00
Insurance	<u>\$ 8,000.00</u>
Total Allowances:	\$ 88,706.00
Income to Land: (net annual sublease rent)	\$ 287,250.00
LESS: Annual Ground Rent	\$- 104,750.00
LESS: Total Allowances	<u>\$- 88,706.00</u>
Total	\$ 93,794.00
Annual Rent Increase (10%)	<u>\$ 9,379.40</u>

**Additional Annual Rent Due DLNR \$9,379.40**

Based on the analysis above, staff is recommending that the Board increase the annual lease rent by \$9,379.00 due to the excess income derived from the sublease for the lease period from 11/12/28 to 11/11/38.

**CALCULATIONS: Rental Period 11/12/2038 – 11/11/2048**

Annual Sublease Ground Rent:	\$300,000.00
Less G. E. Tax	<u>- 12,750.00</u>
Net Annual Sublease Ground Rent:	\$287,250.00
<u>Allowances:</u>	
Investment Return (\$800,000 x 4.25%)	\$ 34,000.00
Real Property Taxes: (\$20,889 x 80%)	\$ 16,706.00
Maintenance	\$ 30,000.00

<sup>2</sup> Allowances:

- Investment return – Lessee will be investing \$800,000.00 towards improvements to the property in order to qualify for a 30-year extension pursuant to §171-192. 4.25% rate of return = \$34,000.00
- Real property taxes – Current taxes paid in 2019 was \$20,889.00. Subleased area is 80% of subject property = \$16,706.00.
- Maintenance - Amount provided by Lessee - \$30,000.00.
- Insurance - Liability Insurance = \$6,124.00 Performance Bond = \$1,876.00 \$8,000.00 total for annual premium.



Insurance	<u>\$ 8,000.00</u>
Total Allowances:	\$ 88,706.00
Income to Land: (annual sublease rent)	\$ 287,250.00
LESS: Annual Ground Rent	\$- 140,775.00
LESS: Total Allowances	<u>\$- 88,706.00</u>
Total	\$ 57,769.00
Annual Rent Increase (10%)	<u>\$ 5,776.90</u>

**Additional Annual Rent Due DLNR                      \$5,776.90**

Based on the analysis above, staff is recommending that the Board increase the annual lease rent by \$5,776.90 due to the excess income derived from the sublease for the lease period from 11/12/38 to 11/11/48.

**CALCULATIONS: Rental Period 11/12/2048 – 11/11/2058**

Annual Sublease Ground Rent:	\$300,000.00
Less G. E. Tax	<u>- 12,750.00</u>
Net Annual Sublease Ground Rent:	\$287,250.00

Allowances:

Investment Return (\$800,000 x 4.25%)	\$ 34,000.00
Real Property Taxes: (\$20,889 x 80%)	\$ 16,706.00
Maintenance	\$ 30,000.00
Insurance	<u>\$ 8,000.00</u>
Total Allowances:	\$ 88,706.00

Income to Land: (annual sublease rent)	\$ 287,250.00
LESS: Annual Ground Rent	\$- 189,190.00
LESS: Total Allowances	<u>\$- 88,706.00</u>
Total	\$ 9,354.00
Annual Rent Increase (10%)	<u>\$ 935.40</u>

**Additional Annual Rent Due DLNR                      \$935.40**

Based on the analysis above, staff is recommending that the Board increase the annual lease rent by \$935.40 due to the excess income derived from the sublease for the lease period from 11/12/48 to 11/11/58.

Suzanne D, Case, ,Chairperson  
July 20, 2020  
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Approved/Disapproved:

*Suzanne D. Case*

Jul 21, 2020

*ET*

Suzanne D. Case, Chairperson

Date

cc: District Branch Files  
Central Files