

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

December 11, 2020

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

Hawai'i

Consent to Second Amendment to Sublease 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, and as amended by
"Resubmittal: Amendment to the Sublease Rent Participation Policy" approved by the
Board on January 26, 2001, under agenda item D-8.

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 (94,307 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

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 pursuant to Act 149, Session Laws of Hawaii (SLH) 2018, commencing on November 12, 2028 and expiring on November 11, 2058.

TERM OF SUBLEASE:

The Board initially approved the sublease agreement for 9.5 years, commencing on May 12, 2019 and expiring on November 11, 2028. The Board reviewed the sublease rental agreement and adjusted the annual lease rent from \$85,260.00 to \$96,588.00. The lessee subsequently requested an extension of sublease agreement commencing November 12, 2028 and expiring November 11, 2058. This request was approved by the Board at its meeting of August 14, 2020 under agenda item D-1.

The lessee is now requesting an increase of the sublease area by 18,282.5 square feet (sf) comprising of 6,600 sf of warehouse area and 11,682.5 sf of open area.

ANNUAL LEASE RENTAL:

Current rent is \$96,588.00, due in quarterly installments of \$24,147.00 on February 12th, May 12th, August 12th and November 12th of each year. The rent for the lease extension period is as follows:

November 12, 2028: \$114,129.00
November 12, 2038: \$146,551.00
November 12, 2048: \$190,125.40

ANNUAL SUBLEASE RENTAL:

Current sublease rent: \$300,000 effective July 13, 2019 – November 11, 2058
Additional sublease rent: \$150,000 effective January 1, 2021 - November 11, 2038.

On November 12, 2038 and November 12, 2048, the sublease rent will be renegotiated between the sublessor and sublessee. The revised sublease rent shall be reviewed by staff and approved by the Board of Land and Natural Resources.

RECOMMENDED ADJUSTMENT TO LEASE RENTAL:

- January 1, 2021 – November 11, 2028 - \$8,441.56 per year additional rent.
 - November 12, 2028 – November 11, 2038 - \$7,788.90 per year additional rent.
- (Refer to attached Exhibit B for rent adjustment worksheet of sublease rental income.)

DCCA VERIFICATION:

SUBLESSOR:

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

SUBLESSEE:

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

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 by Act 149 SLH 2018. 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 staff's 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, staff 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. The Land Board asked staff 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 of improvement, insurance and maintenance allowances.

Staff met with the lessee and a mutually agreed upon amount for the additional rent was achieved. 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 initial lease term. The Board also authorized the extension of the lease for an additional thirty (30) years commencing 11/12/2028.

Further, at its meeting of August 14, 2020, under agenda item D-1, the Board approved an amendment to the sublease. This amendment extended the sublease period to correspond with the recently extended lease term. The amendment to the sublease also allowed increases in the rent to correspond with the terms of the lease extension.

Additional Sublease Area:

The lessee had to make the difficult decision to contract its workspace out as its own business was downsized due to various factors. The primary consideration was the shutdown of non-essential businesses due to the COVID-19 pandemic. This, along with other personal matters resulted in the lessee's business effectively being shut down. The lessee has been struggling to revive the business with a much-reduced workforce. However, the business shutdown in March 2020 along with the personal issues have caused the lessee to reevaluate its business setup. One of the considerations was to significantly downsize the operation. Lessee does however, plan to retain an area in building A for its cabinet manufacturing business.

The lessee is now requesting a second amendment to the sublease agreement. This second amendment increases the square footage of the premises being subleased to MVI with an additional 6,600 square feet of warehouse space and 11,682.5 square feet of open storage and parking area (18,282.5sf). The lessee will receive an additional \$150,000 annually from MVI for the expanded sublease area. The sublessee, MVI will be making substantial renovations to the property in the amount of approximately \$1,000,000 and will be submitting plans for renovations and improvements prior to any work being performed.

Staff is recommending an increase in the lease rent based on the additional amount of sublease rent that will be paid to the lessee. In order to calculate this amount, the two sublease rent amounts were combined and using the calculation previously approved by the Board (Exhibit C), the total amount was then divided by three to determine the proportion of rent for the additional lease area. Using this method, staff was able to determine the current additional rent and the additional rent for the period beginning 11/12/2028. Adjustments were made to the real property tax for the increase in area.

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

RECOMMENDATION:

That the Board:

1. Consent to the second 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/sublessee 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 rent amount for the additional sublease area as follows; January 1, 2021 – November 11, 2028 - \$8,441.56 per year. November 12, 2028 – November 11, 2038 - \$7,788.90 per year. Sublease rent for the remainder of the lease term to be negotiated between the sublessor and sublessee and approved by the Board of Land and Natural Resources.
 - 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 Heit

Gordon C. Heit
District Land Agent

APPROVED FOR SUBMITTAL:

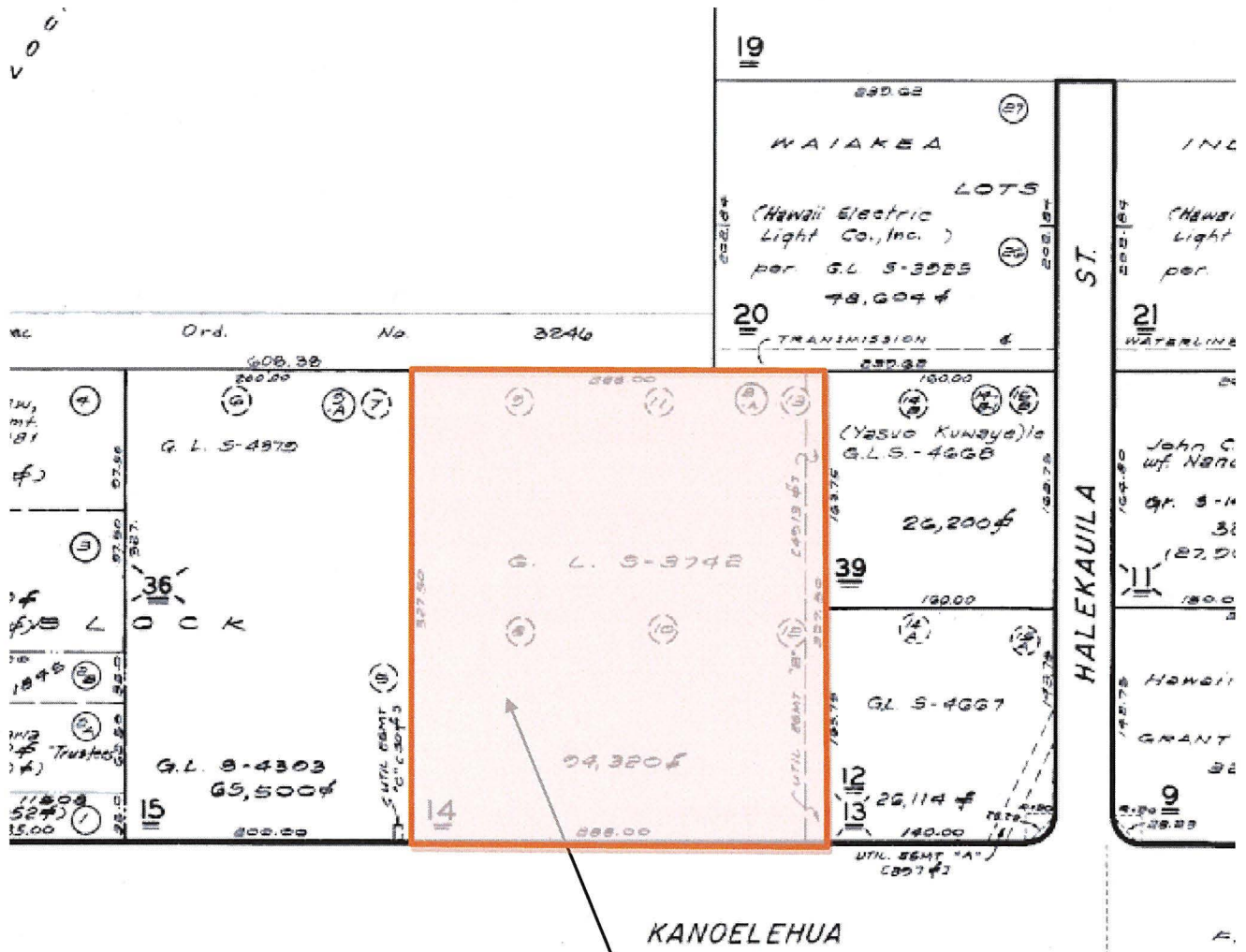
Suzanne D. Case

Suzanne D. Case, Chairperson

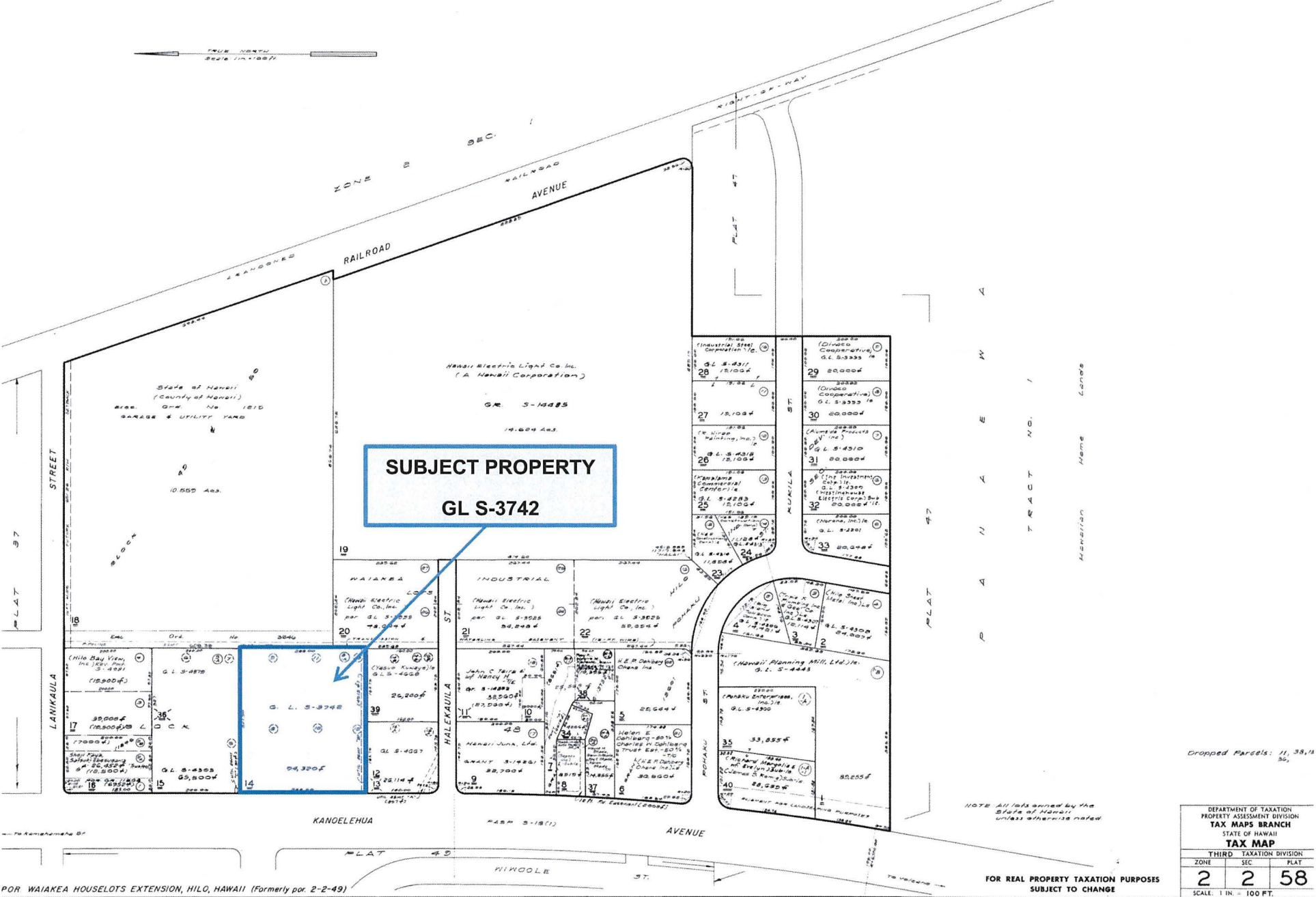
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EXHIBIT A

TMK: (3) 2-2-058:014




SUBJECT PROPERTY



GL S-3742

JH MOKU OLALLC

Legend

 GL S-3742

Google Earth

Data LDEO-Columbia, NSF NOAA

© 2020 Google

Image Landsat / Copernicus

Data SIO, NOAA, U.S. Navy, NGA, GEBCO

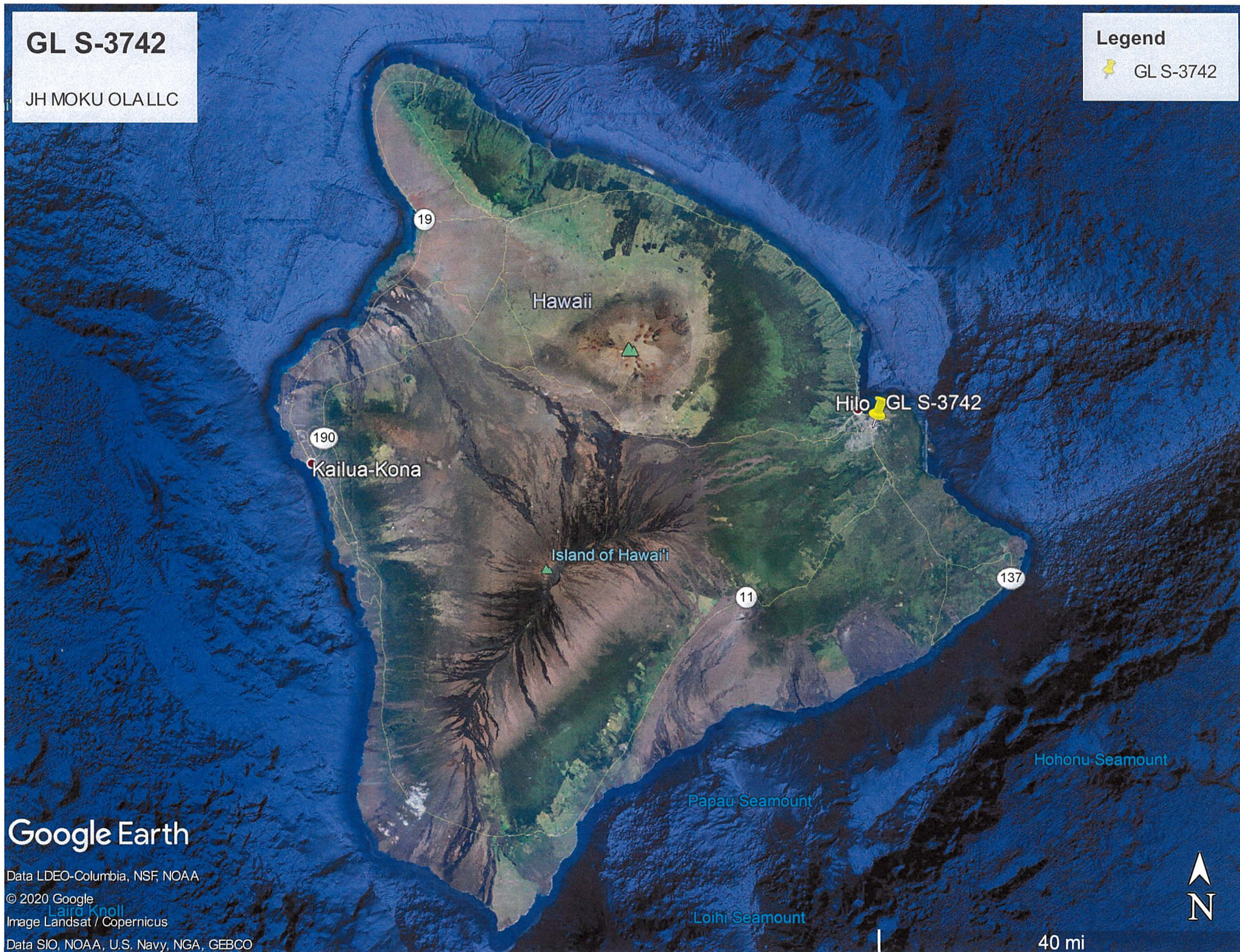
Hohonu Seamount

Papau Seamount

Loihi Seamount



40 mi



SUBLEASE RENT ADJUSTMENT WORKSHEET

General Lease No.: S-3742
Lessee: JH Moku Ola, LLC
Location: Waiakea, South Hilo, Hawaii
Tax Map Key: (3) 2-2-058:014
Land Area (sq ft): 94,307 sq. ft. (2.165 acres)
Annual Ground Rent: \$85,260.00

SUBLESSEE: Maui Varieties Investments, Inc.

CALCULATIONS:

Sublease Area 92,282.5 square feet
Annual Sublease Ground Rent: **\$450,000.00**
Less G. E. Tax - 18,765.00
Effective Annual Sublease Ground Rent: **\$431,235.00**

Allowances:

Investment Return (\$800,000 x 4.25%) \$ 34,000.00
Real Property Taxes: (\$21,243 x 98%) \$ 20,818.00
Maintenance \$ 30,000.00
Insurance \$ 8,000.00
Total Allowances: **\$ 92,818.00**

Income to Land: (annual sublease rent) \$ 431,235.00
LESS: Annual Ground Rent \$- 85,260.00
LESS: Total Allowances \$- 92,818.00
Total **\$ 253,247.00**
Annual Rent Increase (10%) \$ 25,324.70

Additional Annual Rent Due DLNR \$ 25,324.70

\$300,000 (original sublease amount)
\$150,000 (additional sublease amount) 1/3 \$ 8,441.56

EXHIBIT B

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 2020 was \$21,243.00. Subleased area is 98% of subject property = \$20,818.00.
- 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.

SUBLEASE RENT ADJUSTMENT WORKSHEET

General Lease No.:	S-3742
Lessee:	JH Moku Ola, LLC
Location:	Waiakea, South Hilo, Hawaii
Tax Map Key:	(3) 2-2-058:014
Land Area (sq ft):	94,307 sq. ft. (2.165 acres)
Annual Ground Rent:	\$104,750.00
 SUBLESSEE:	 Maui Varieties Investments, Inc.

CALCULATIONS:

Sublease Area	92,282.5 square feet
Annual Sublease Ground Rent:	\$450,000.00
Less G. E. Tax	<u>- 18,765.00</u>
Net Annual Sublease Ground Rent:	\$431,235.00

Allowances:

Investment Return (\$800,000 x 4.25%)	\$ 34,000.00
Real Property Taxes: (\$21,243 x 98%)	\$ 20,818.00
Maintenance	\$ 30,000.00
Insurance	<u>\$ 8,000.00</u>
Total Allowances:	\$ 92,818.00

Income to Land: (net annual sublease rent)	\$ 431,235.00
LESS: Annual Ground Rent	\$- 104,750.00
LESS: Total Allowances	<u>\$- 92,818.00</u>
Total	\$ 233,667.00
Annual Rent Increase (10%)	<u>\$ 23,366.70</u>

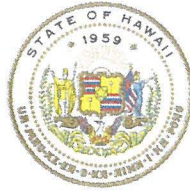
Additional Annual Rent Due DLNR	\$ 23,366.70
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\$300,000 (original sublease amount)	
\$150,000 (additional sublease amount)	1/3 \$ 7,788.90

EXHIBIT B

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 2020 was \$21,243.00. Subleased area is 98% of subject property = \$20,818.00.
- 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.



**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

March 10, 2020

MEMORANDUM

TO: Suzanne D. Case, Chairperson

THROUGH: Russell Y. Tsuji, Division Administrator

FROM: Gordon C. Heit, District Land Agent

SUBJECT: In-House Recommendation – Rent Adjustment 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 an additional 10 years to allow the Lessee to amortize self-financed improvements in the amount of \$37,000.00.¹ These improvements were completed by September 30, 2016.

¹ Improvements included replacement of existing roof, gutters and downspout, re-siding of exterior walls and electrical improvements.

EXHIBIT C

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 1I(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 \$37,000 as a condition of the 10-year extension and therefore will need to amortize its cost over the remaining term of the lease. Furthermore, the Lessee is requesting a 30-year extension of the lease pursuant to Act 149 SLH 2018 and will be making additional improvements to the property. 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.

Given the age of the improvements on the property, the lessee is anticipating an annual expense of approximately \$30,000 for maintenance for both warehouse structures, fencing and the open paved areas. The lessee has provided a summary of annual maintenance report for year ending in 2019 (Exhibit X).

The lessee is also requesting a 30-year extension to amortize improvements to the warehouse structures and property to accommodate the sublessee's business. The lessee will be seeking a loan for the improvements in the amount of \$800,000 at an initial rate of 4.25% for the first 10 years.

The following calculation allows for amortization of the Lessee's financial improvements (\$800,000 x 4.25% interest = \$34,000) along with allowances for property insurance (\$8,000), average annual maintenance costs (\$30,000), General Excise Tax, and Real Property Tax.

CALCULATION:

Annual Ground Rent	\$ 85,260.00
Annual Sublease Rent	\$300,000.00
Less G. E. Tax	\$ -12,750.00
Less Real Property Tax	\$ -16,706.00
Misc. Allowances	\$ -72,000.00
Total Allowances	<u>\$ -86,456.00</u>
Total Sublease Rent	\$113,284.00
Income to Land	\$ 300,000.00
Annual Ground rent	\$ -85,260.00
Total Allowances	<u>\$ -86,456.00</u>
Total Amount	\$ 113,284.00
DLNR Rent Participation	<u>10%</u>

Additional Annual Rent Due \$11,328.00

Based on the analysis above, staff is recommending that the Board increase the current annual lease rent by \$11,328.00 due to the excess income derived from the sublease.

cc: District Branch Files
Central Files