



**The Chamber of
Commerce of Hawaii**
Since 1850

TESTIMONY TO THE HOUSE COMMITTEE ECONOMIC DEVELOPMENT & BUSINESS
CONCERNS
TUESDAY, FEBRUARY 26, 2008 AT 10:00 A.M.
ROOM 325, STATE CAPITOL

RE: H.B. 1075 Relating to Real Property

Chair Yamashita, Vice Chair Wakai, Members of the Committee:

My name is Christine H. H. Camp, Chair of the Chamber of Commerce of Hawaii, Land Use and Transportation Committee. The Chamber of Commerce of Hawaii is strongly opposed to HB 1075.

The Chamber is the largest business organization in Hawaii, representing 1100 businesses. Approximately 80% of our members are small businesses with less than 20 employees. The organization works on behalf of members and the entire business community to improve the state's economic climate and to foster positive action on issues of common concern.

H.B. No. 1075 proposes to implement certain conditions governing long-term leases of commercial and industrial properties.

The legislature finds that certain elements of inequity exist in the relationship of fee simple owners of commercial and industrial properties and holders of long-term leasehold interest in those properties who undertake the leases for the purpose of developing, improving, operating, and subletting the properties. These inequities accrue to the detriment of Hawaii's business and economic development and harm Hawaii's working and retired taxpayers. Uncomplicated and fair legislative remedies exist that can obviate these inequities.

We do not believe it is appropriate for the legislature to interject itself into an existing contractual arrangement between to private parties.

The lease contract reflects a business decision that both parties made of their own free will. Amending or modifying the contract through legislation is inappropriate and may serve to discourage landowners for entertaining or entering into long-term leasehold arrangements in the future.

Thank you for this opportunity to express our views.



KAMEHAMEHA SCHOOLS

February 25, 2008

TESTIMONY TO THE HOUSE COMMITTEE ON ECONOMIC DEVELOPMENT & BUSINESS CONCERNS

By
Livingston S. Wong, Director
Legal/Endowment Legal Division
Kamehameha Schools

Hearing Date: Tuesday, February 26, 2008
10:00 a.m., Conference Room 325

To: Representative Kyle T. Yamashita, Chair
Representative Glenn Wakai, Vice Chair
Members of the Committee

RE: House Bill No. 1075 Relating to Real Property

Kamehameha Schools submits the following comments regarding H.B. No. 1075 (the "**Bill**"):

As a lessor of commercial and industrial real property, Kamehameha Schools **objects** to this Bill because, as written, it: (1) serves no legitimate public purpose; (2) would likely hurt both lessors and lessees; (3) could negatively impact our communities; and (4) appears to be legally deficient.

(1) The Bill serves no legitimate public purpose.

The Bill sets out to protect lessees, regardless of size, who lease from any lessor that "is the owner, directly or indirectly, of fifty thousand square feet or more of commercial or industrial leasehold property in the State." Such protection is on the basis that "inequities" exist in lessor-lessee relationships. However, the Bill offers no facts or data to support the suggestion that such inequities exist, or that the protections proposed are needed, or that such protections would provide a legitimate benefit to the public-at-large.

To the contrary, according to the study by the Legislative Reference Bureau – Report No. 5, 2003 "Real Property Leases" (the "**2003 Report**"), "there is no indication at this time of a broad based compelling need for the Legislature to pass legislation to mandate the alteration of existing lease agreements." 2003 Report at 24.

(2) The Bill would likely hurt both lessors and lessees.

- (a) The Bill would reduce a lessor's financial returns, as renegotiated rents would be unfairly limited to the financial feasibility of whatever business that the lessee elects to operate on the property.
- (b) The Bill would restrict a lessor's ability to enforce legitimate, mutually agreed-upon lease terms to repair, maintain and return leasehold properties in a superior condition (beyond what is minimally required to comply with existing laws).

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- (c) The Bill would reduce flexibility in leasing. Lessors subject to the Bill would lose the benefit of being able to freely negotiate leases in ways that best suit business requirements of both lessors and their lessees, especially lessees who are leasing smaller premises or starting new businesses. For example, lessors and lessees often agree to very low lease rents at the beginning of a long-term lease to permit new lessees to grow their business in exchange for a long-term commitment by the lessee to maintain and return the property in a superior condition, which allows lessors to realize fair returns at the end of the lease. These agreements help lessees, especially those starting new businesses, but they would no longer be feasible under the Bill.

(3) The Bill could negatively impact our communities.

- (a) If the Bill prohibits lessors from enforcing higher standards of repair, maintenance and surrender, properties would likely be poorly maintained and allowed to deteriorate over time. Neighborhoods and communities would suffer from these substandard properties.
- (b) The Bill would limit the ability of businesses to freely negotiate and rely on their lease contracts. This could impact the stability of business relationships, which depends, in part, on the right of parties to freely negotiate, rely on and enforce mutually agreed contract terms.

(4) The Bill appears to be legally deficient.

- (a) **The Bill appears to violate the Contracts Clause of the U.S. Constitution.** The Bill is unclear as to whether it applies to leases that are in effect prior to the effective date of the proposed act. While Section 3 of the Bill states that “[t]his Act does not affect rights and duties that matured, penalties that were incurred, and proceedings that were begun, before its effective date,” Section 1 states in part that “[t]he purpose of this Act is to implement certain conditions governing long-term leases of commercial and industrial properties.” Further, “commercial or industrial leasehold property” is defined, in part, to mean real property “[t]hat is subject to a lease with an unexpired term of twenty years or more.” This suggests that the act applies to leases in existence prior to the proposed enactment. The Hawai‘i Supreme Court recognized in Anthony v. Kualoa Ranch, Inc., 69 Haw. 112, 736 P.2d 55 (1987), that such a legislative attempt to change contractual obligations in existing leases is unconstitutional.

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- (b) **The Bill appears impermissibly vague.** Subsection (a)(4) of Section 2 of the Bill provides: “Where a lease provides for periodic step-ups in lease rent over the term of the lease, the increases in lease rent shall be determined, in part, on a determination of the financial feasibility of the rent increase in relation to the current use of the leasehold property.” Commercial leases that include increases in rent are typically structured with a specific, mathematical formula clearly stated in the lease instrument that is negotiated between the lessor and the lessee before the lease commences. If implemented, Subsection (a)(4) would cause that certainty to disappear in lieu of an unspecified derivative of “the financial feasibility of the rent increase in relation to the current use of the leasehold property.” The Bill does not define the phrase “financial feasibility.” Consequently, this broad, undefined phrase is subject to innumerable interpretations. Lacking such requisite specificity, it is doubtful the Bill could ever be enforced.
- (c) **The Bill likely constitutes an Unconstitutional Taking of Property without Just Compensation.** Even if Subsection (a)(4) was not void for vagueness, any limitation upon the rent that a lessor was permitted to receive from its lessee appears to constitute an impermissible rent cap that violates the Takings Clause of the Fifth Amendment of the U.S. Constitution. The United States District Court for the District of Hawai‘i and the Ninth Circuit have previously considered and rejected as unconstitutional a rent cap that the City and County of Honolulu attempted to impose upon leasehold residences. See Richardson v. City & County of Honolulu, 802 F. Supp. 326 (D. Haw. 1992) (“Richardson I”), aff’d, 124 F.3d 1150 (9th Cir. 1997), cert. denied, 525 U.S. 871 (1998). In that case, the rent cap did not provide lessors a just and reasonable rate of return on their investment. The same deficiency exists here, since the Bill would substantially interfere with a lessor’s investment-backed expectations, if lessor’s investment returns are limited to the “financial feasibility” of the lessee’s “current use of the leasehold property.”

Thank you for this opportunity to express our objection to this Bill.

JAMES W. Y. WONG

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Honorable Chair Kyle T. Yamashita
Honorable Vice Chair Glenn Wakai
Honorable Rep. Lyla B. Berg
Honorable Rep. Tom Brower
Honorable Rep. Jerry L. Chang
Honorable Rep. Corinne W. L. Ching
Honorable Rep. Faye P. Hanohano
Honorable Rep. Robert N. Herkes
Honorable Rep. Joey Manahan
Honorable Rep. Barbara C. Marumoto
Honorable Rep. Clift Tsuji
House Committee on Economic Development and Business Concerns

RE: Support of HB1075 – Relating to Real Property

Honorable Chair Yamashita and Members of the House Committee on Economic Development and Business Concerns:

I am pleased that your committee has scheduled hearing of HB1075. I am in full support of the adoption and passage of the bill with one exception. Section 2. (b) (3) of the bill should be amended to read: "That subject to a lease with an original ground lease of twenty years or more."

As a current and past lessee of several long term commercial ground leases (see list below), the proposed bill would go a long way towards correcting the numerous inequities imposed on holders of long term commercial and industrial leases. It is not uncommon for the ground leases to require the lessee to make substantial improvements to the building structure while there was less than 20 years remaining on the lease term, with little or no opportunity to recapture its investment over the remaining short term of the lease, while being required to pay high lease rents based on highest and best use of the property as compared to establishing the rent in relationship to the current use. There have been known cases where several ground lessees had to surrender their leasehold interest in the properties back to the fee simple owners because the income from the leasehold property could not support the high land values. Those same lessees were also mandated to make substantial improvements to the improvements on surrender, versus being able to return the property subject to reasonable wear and tear.

List of long term leasehold properties and fee simple landlords:

Hale Anue

Kamehameha Schools Bishop Estate

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Kapalama Shopping Center	Kamehameha Schools Bishop Estate
Kapalama Wong	Kamehameha Schools Bishop Estate
Kapolei Medical Park	Campbell Hawaii Investor
Wapko Investment Co.	Kamehameha Schools Bishop Estate
King University Plaza	Magoon Estate
Moilili Plaza	Kamehameha Schools Bishop Estate
University Plaza	Kamehameha Schools Bishop Estate
Paradise Park	Roman Catholic Church
Waiakamilo Shopping Center	Kamehameha Schools Bishop Estate
Waialae Plaza I	Fathers of the Sacred Hearts
Waialae Plaza II	Sisters of the Sacred Hearts
Windward Plaza	Kaneohe Ranch Co.
Windward Town & Country Plaza - Phase 1	Kaneohe Ranch Co.
Windward Town & Country Plaza - Phase 2	Kaneohe Ranch Co.
Windward Post Office	Kaneohe Ranch Co.

I urge your support of the passage of the proposed bill.

If you have any questions, please feel free to contact me directly at (808) 941-9030. Thank you.

JWYW:

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LETTER OF SUPPORT FOR HB1075

February 25, 2008

Honorable Chair Kyle T. Yamashita
Honorable Vice Chair Glenn Wakai
House Committee on Economic Development and Business Concerns

RE: Support of HB1075 – Relating to Real Property

Honorable Chair Yamashita and Members of the House Committee on Economic Development and Business Concerns:

We thank you for your willingness to hear and consider action on HB107t and we are in support of your favorable action on this bill.

We believe the proposed bill would go a long way towards correcting the numerous inequities imposed on holders of long term commercial and industrial leases. By making all things equal, the enormous pressures put on commercial and industrial lessees will be greatly improved and this, in turn, can only contribute to Hawaii's economy in a positive way.

We strongly urge your support of the passage of the proposed bill.

Name (sign and print)	Address	Phone
<i>Napualani Wong</i> Napualani Wong	1577 Nehoa St, Honolulu, HI 96822	944-4863
<i>Christie Miyasato</i> Christie Miyasato	94459 Hene St. Waipahu, HI 96797	852-0096
<i>Winnie Chang</i> Winnie Chang	520 Kapiolani St, Honolulu, HI 96815	
<i>Loi Lee</i> Loi Lee	3737 Honoa Road	943-3130