



**TESTIMONY TO THE SENATE COMMITTEE ON ECONOMIC DEVELOPMENT AND
TAXATION**

**THURSDAY, MARCH 13 2008 AT 1:40 P.M.
ROOM 224, STATE CAPITOL**

RE: H.B. 1075, HD1 Relating to Real Property

Chair Fukunaga, Vice Chair Espero, 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 HD1.

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 two private parties. Lessees who choose to invest in their improvements should make their respective decisions based on the remaining term of the lease. Should they require more time to amortize their investment, they should attempt to negotiate an extension of the lease prior to making their investment.

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.

**Testimony on HB1075 HD1
Relating to Real Property
Senate Committee on Economic Development and Taxation
Keali'i Lopez, President and CEO of 'Ōlelo Community Television
March 11, 2008**

Chair Fukunaga, Vice Chair Espero, members of the Senate Committee on Economic Development and Taxation. Aloha, I'm Keali'i Lopez, president and CEO of 'Ōlelo Community Television, and we support of HB1075 HD1.

We are a local non-profit organization located in Mapunapuna. The building that we own is located on a parcel of land that we lease from a mainland lessor. We have 27 years remaining on our lease and could soon see our lease rent increase by 120 percent when we renegotiate terms later this year.

A substantial increase in lease rent, coupled with major increases in our other operating expenses such as electricity, could place us in a very precarious financial position. In this respect, we are no different from a small business that operates on a very slim margin. However, we have no customers to pass these increases on to.

We understand that lessors have rights, to include the expectation of a reasonable return on their investments, but clearly there is a need for safeguards to ensure that lessees are not subject to unreasonable increases that drastically curtail services or force them out of business.

We are members of the Citizens for Fair Valuation, a non-profit organization committed to ensuring fair valuation of the commercial and industrial ground leases in the Sand Island, Mapunapuna and Kalihi Kai areas. We believe that fair interpretation of leases is crucial to the health of non-profit organizations and small businesses that all of us rely upon.

Because of this, we ask that you include a definition of "fair and reasonable" in Hawaii State law so that equity prevails as leases are renegotiated. In summary, I ask for your support of HB 1075, HD1. That concludes my testimony.

JAMES W. Y. WONG

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TO: Senator Carol Fukunaga, Chair, Economic Development and Taxation
Senator Will Espero, Vice Chair, Economic Development and Taxation
Senator Sam Slom, Member
Senator Kalani J. English, Member
Senator David Y. Ige, Member

FR: James W. Y. Wong

DT: March 12, 2008

RE: **HB1075 HD1 Relating to Real Estate**

My name is James W. Y. Wong, a Hawaii developer that strongly urges your favorable consideration of HB1075.

I cannot emphasize strongly enough that passage of this bill is urgently needed to help return Hawaii's rapidly failing economy to a healthy state. This bill will allow especially small industrial and commercial lease holders to remain viable in their ability to develop, improve, operate, or sublet their properties.

The very real dangers of continuing the status quo is becoming more and more evident every day. You are likely familiar with the Bowl-O-Drome property in Moiliili, which illustrates the effect of steep property costs resulting in excessive and burdensome commercial rentals. An analysis of the per square foot lease cost for the Bowl-O-Drome property shows that, assuming an 8% cap rate on the lease value, the land value would be \$180.00 per square foot. Based on a 6% cap, the amount rises to \$248.00 per square foot. At these rates, nobody will be able to afford rents like this and subsequently, our economy suffers.

Another case involves the economic peril our industrial lessees are facing in the Mapunapuna area and certainly in other areas as well. An analysis of this per square foot lease rental at \$9.25 per annum, assuming an 8% cap rate, shows the land value would be \$115.00 per square foot. Based on a 6% cap, the value of land would be \$154.00 per square foot. This situation is playing itself out in various forms throughout our State.

Please vote in favor of HB1075 and I thank you for all your efforts on behalf of the many business men and women of Hawaii.



SERVCO PACIFIC INC.

P.O. Box 2788 • Honolulu, Hawaii 96803-2788 • Telephone: (808) 564-1300 • Facsimile: (808) 528-3937 • www.servco.com

To: Senator Carol Fukunaga, Chair
Senator Will Espero, Vice Chair
Committee on Economic Development and Taxation
State Capitol, Conference Room 224
Honolulu, Honolulu 96813

From: Carol K. Lam
Senior Vice President
Servco Pacific Inc.
2850 Pukoloa Street, Suite 300
Honolulu, Hawaii 96819

Hearing Date: Thursday, March 13, 2008 (1:40 p.m.)

In Support of HB 1075 HD1, Relating To Real Property

On behalf of Servco Pacific Inc. ("*Servco*"), I am writing to ask that you support the adoption of HB 1075 HD1 (the "*Bill*") and we further ask for your support to extend the bill to incorporate the ground rent renegotiation process by adding a definition of "fair and reasonable rent." Commercial and industrial ground leases in the Sand Island, Mapunapuna and Kalihi Kai areas provide that the rent renegotiation process is to determine "fair and reasonable rent." This definition would provide that the ground rent that is determined must be fair and reasonable to both parties to the lease. The addition of this definition to the Bill will support an equitable interpretation of that term in the ground rent renegotiation process.

Servco Pacific Inc. is a member of the Citizens for Fair Valuation ("*CFV*"), a newly founded non-profit organization committed to ensuring fair valuation of the commercial and industrial ground leases in the Sand Island, Mapunapuna and Kalihi Kai areas. CFV represents businesses that employ thousands of Hawaii workers and represent millions of dollars of economic activity and tax revenue for the State of Hawaii. We believe that fair interpretation of the lease provisions is essential to the preservation of small businesses that constitute the backbone of our state's economy.

Thank you for your consideration and we again ask for your support of HB 1075 HD1 with the requested additions.

**HB 1075 HD1
RELATING TO REAL PROPERTY**

**PAUL T. OSHIRO
MANAGER – GOVERNMENT RELATIONS
ALEXANDER & BALDWIN, INC.**

MARCH 13, 2008

Chair Fukunaga and Members of the Senate Committee on Economic
Development & Taxation:

I am Paul Oshiro, testifying on behalf of Alexander & Baldwin, Inc. (A&B) on HB 1075 HD1, "A BILL FOR AN ACT RELATING TO REAL PROPERTY." We respectfully oppose this bill.

This bill establishes various conditions on long term leases for commercial and industrial properties. As leases for commercial and industrial properties reflect contractual business decisions between a lessor and a lessee, we have concerns with the impact that this bill may have upon the scope within which leases may be negotiated and executed. This bill will limit the ability to freely negotiate leases in a manner that best suits the business requirements of both the lessor and the lessee. Agreements to provide lower lease rents at the beginning of a long term lease to allow the lessee to grow their business in exchange for a long term commitment by the lessee to maintain and improve the property may no longer be feasible under the provisions of this bill. By prohibiting the enforcement of higher standards for the repair, maintenance, and surrender, the overall maintenance of properties may decline, impacting both subject property and the surrounding community.

As presently drafted, the bill appears to also apply to current leases that have an unexpired term of twenty years or more. We understand that changing contractual obligations in existing leases may be unconstitutional.

Based on the aforementioned, we respectfully request that this bill be held in Committee.

Thank you for the opportunity to testify.



KAMEHAMEHA SCHOOLS

March 12, 2008

TESTIMONY TO THE SENATE COMMITTEE ON ECONOMIC DEVELOPMENT & TAXATION

By

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

Hearing Date: Thursday, March 13, 2008
1:40 p.m., Conference Room 224

To: Senator Carol Fukunaga, Chair
Senator Will Espero, Vice Chair
Members of the Committee on Economic Development and Taxation

RE: **House Bill No. 1075, HD1 - Relating to Real Property**

Kamehameha Schools respectfully submits the following in opposition to H.B. No. 1075, HD1 (the "**Bill**"):

As a lessor of commercial and industrial real property, Kamehameha Schools **opposes** this Bill because, as written, it: (1) violates lessors' constitutional rights under the contract clause, (2) effects a taking under the 5th amendment, (3) violates lessors' due process rights, (3) denies lessors their equal protection rights, (5) is designed to benefit only a select group of lessees to the detriment of lessors, future lessees, sublessees, tenants, and consumers; and (6) negatively impacts our community.

I. The Bill Violates the Contract Clause because it serves No Legitimate Public Purpose.

A. A desire to achieve "equity" for a small group of individuals is **not** a legitimate public purpose. That is, merely trying to give selected lessees a benefit is **insufficient** to serve as a public purpose.

1. The Hawai'i Supreme Court recognized in Anthony v. Kualoa Ranch, Inc., 69 Haw. 112, 736 P.2d 55 (1987) ("**Anthony**") that an impairment of contractual rights in existing leases is unconstitutional. There, the Court rejected the application of amendments to Haw. Rev. Stat. § 516-70 to existing leases, stating:

"This statute, as applied to leases already in effect, purely and simply, is an attempt by the legislature to change contractual remedies and obligations, to the detriment of all lessors and to the benefit of all lessees . . . **simply for the purpose of doing equity, as the legislature saw it.** If there is any meaning at all to the contract clause [of the United States Constitution], it prohibits the application of HRS § 516-70 to leases existing at the time of the 1975 amendment. Accordingly, that section, as applied to leases existing at the time of the adoption of the 1975 amendment, is declared unconstitutional."

Id. at 123, 736 P.2d at 63.

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2. 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.
 3. 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.
- B. Opinions of the Department of the Attorney General dated April 20, 2000, March 22, 2001, April 11, 2002, and April 23, 2002, on proposed legislation changing the lease contract concluded that each violated the Contract Clause. The April 11, 2002 letter concluded that the proposed legislation “substantially impairs contractual relationships without promoting a significant and legitimate board societal interest.” In a June 19, 2000 communication from then Governor Cayetano, the Anthony case was cited by him to return a rent control bill unsigned to the Senate because he did not believe the “bill will pass constitutional muster.”

II. The Bill Violates the Takings Clause of the 5th Amendment.

- A. The government cannot take or damage private property without paying just compensation to the owner.
- B. 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).
- C. In the context of a rent control statute, the lessor is entitled to a just and reasonable rate of return on its investment.
- D. In Richardson I, Judge Ezra held that the rent control ordinance did not guarantee landlords a just and reasonable rate of return on its investment because, in part, **there was a lack of individualized consideration and an absence of any meaningful review process.** See Richardson I at 334-37.
- E. The Bill is unconstitutional because it also fails to ensure that lessors receive a just and reasonable rate of return.

III. The Bill Violates Lessors’ Due Process Rights.

- A. The fourteenth amendment of the United States Constitution provides that no state shall “deprive any person of life, liberty, or property, without due process of law.”

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- B. This clause is a guaranty against any legislation that arbitrarily deprives a lessor of its rights. It protects the lessor against the arbitrary, capricious, and unreasonable exercise of the legislature's power.
- C. Vague and ambiguous provisions of the Bill violate the due process rights of lessors because the provisions can be applied in an arbitrary, capricious, and unreasonable manner. For example, in R.S.T. Builders, Inc. v. Village of Bolingbrook, 141 Ill.App.3d 41, 44, 489 N.E.2d 1151, 1154 (1986), the court held that a city ordinance that failed to prescribe adequate standards to control the actions of a city land use committee in determining whether an application for a building permit would be approved was unconstitutionally vague and indefinite.
- D. By way example, 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.

IV. **The Bill Denies Lessors their Equal Protection Rights.**

- A. The United States Constitution, amend. XIV provides in pertinent part: "No State shall . . . deny to any person within its jurisdiction the equal protection of the laws."
- B. Legislation that burdens one class will not be upheld if the varying treatment does not bear a rational relation to a legitimate state interest.
- C. The Bill only applies "where the lessor is the owner, directly or indirectly, of fifty thousand square feet or more of commercial or industrial leasehold property in the state." Assuming that one can determine how this standard is applied, there is no rational relation between this class of landowners (versus other landowners) and any legitimate reason for the Bill.

V. **The Bill is Designed to Benefit Only a Select Group of Lessees.**

- A. The Bill benefits **only** the initial lessee and does not benefit subsequent lessees.
- B. The lessee is able to get a "premium" on a leasehold sale with below market rents and conditions – that is, the lessee can "monetize" the below market rents and conditions by selling the leasehold.

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1. There is no mechanism to limit the sales price of the leasehold interest.
 2. Thus, the initial lessee is allowed to sell the leasehold for any price and pocket the profits to the detriment of a purchasing lessee.
- C. The Bill benefits **only** the lessee and does not benefit sublessees, tenants, or consumers.
1. For a lessee merely subletting the premises, there is no mechanism to ensure that the lessee's cost savings are shared with its sublessees and tenants.
 2. For a lessee using the premises, there is no mechanism to ensure that the lessee's cost savings are shared with its customers.
 3. Thus, the lessee can keep all the profits from the below market rents and conditions with no requirement to pass on or even share the cost savings with sublessees, tenants, or consumers.
- D. The Bill impermissibly re-writes the contractual rights and obligations of lessors and lessees under unreasonable conditions.
1. The 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) is restricted.
 2. The lessee is allowed to keep the premises in disrepair even if that is a breach of the lease.
 3. The Bill may even encourage lessees to keep their premises in disrepair and reward them with below market rents.
 4. For a lessee merely subletting the premises, the Bill's effect is especially egregious because the sublessees and tenants suffer the consequences of such disrepair with no assurance of below market rents being passed along to them.

VI. The Bill has a Negative Impact on the Community.

- A. The Bill would reduce flexibility in leasing.
1. 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.
 2. 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

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help lessees, especially those starting new businesses, but they would no longer be feasible under the Bill.

- B. 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.
- C. 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.

In view of the numerous opinion letters cited above, we respectfully request that you hold the Bill or refer it to the Department of the Attorney General for review. Thank you for this opportunity to express our opposition to the Bill.

Support for HB1075 HD1 & HD2040

March ~~12~~¹³, 2008

Ben Villaflor
To: ~~Jason Watts~~ (Sergeant-at-Arms)
Fax No.: 808-586-6659

I wholeheartedly support HB1075 HD1 and HB 2040. In my opinion, these bills will help the Hawaii economy and all the people of Hawaii. HB 1075 HD1 will help keep the cost of living in Hawaii more manageable. Hopefully HB 2040 will identify new methods to keep the cost of living in Hawaii under control.

With what appears to be the early stages of a recession in Hawaii, these bills are, in my opinion, essential to cope with a Hawaii economy that could be headed to bad economic times.

I am a sandwich lessee in Hawaii, who hears from my tenants, even the very strongest, that they are worried about the recession which has begun to take effect in Hawaii. Because they have the ground rent pass through, they feel that if "fair and reasonable rent" which is part of their/my master lease is not "fair and reasonable rent to both of the parties to the lease" then their business will no longer be able survive.

Please pass both bills with this modification.

Please let me know if you have any questions regarding this matter.

Mahalo,

Stan Solomon

Stanley B. Solomon
Snyder Family Trust / STI Industries
E-mail: stansolo@aol.com
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HAWAII COUNCIL OF ASSOCIATIONS
OF APARTMENT OWNERS

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March 12, 2008

Senator Carol Fukunaga, Chair
Senator Will Espero, Vice-Chair
Senate Committee on Economic Development & Taxation
State Capitol
Honolulu, Hawaii 96813

RE: Testimony in Support of HB 1075 HD1, Re Real Property
Hearing: Thurs., March 13, 2008, 1:40 p.m. Conf. Rm. #224

Chair Fukunaga and Vice-Chair Espero and Members of the Committee:

I am Jane Sugimura, President of the Hawaii Council of Associations of Apartment Owners (HCAAO).

HCAAO supports this bill with the following revisions:

Insert between the existing paragraphs 4 and 5 of HB1075 HD1, a new paragraph 5 defining "fair and reasonable rent" as follows:

"(5) Where a lease provides for the renegotiation of rent during the term of the lease and such renegotiated rent is based, according to the terms of the lease, on fair and reasonable annual rent, or words of similar import, such rent must be fair and reasonable to both of the parties to the lease. A rental amount that is fair and reasonable to both parties shall provide a fair return on and of the investment of both parties to the lease.

Former paragraph 5, should be renumbered paragraph 6

Subsection (b) should be amended as follows:

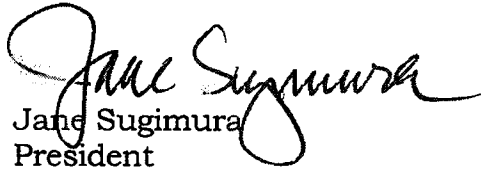
"b) For purposes of this section, "commercial or industrial leasehold property" means any real property **ground lease**:

- (1) Situated in the state;
- (2) Zoned by a county for commercial, industrial, or mixed use; and
- (3) That is subject to a lease with an **initial unexpired** term of **more than twenty-five years and an unexpired term of five years** or more".

According to a recent Advertiser new article, industrial lessees in the Mapunapuna/Kalihi area are being threatened with high lease rent that may drive many of them out of the area or make them close their businesses. This will affect apartment owners and other consumers in that area as well as in other parts of Oahu since they will have to pay higher prices for the goods and services currently being offered by those lessees.

We ask that the bill be amended as proposed and that the amended SD1 be passed out by this Committee.

Thank you for the opportunity to testify.


Jane Sugimura
President

BENDET, FIDELL, SAKAI & LEE

EDWARD R. BENDET
JAY M. FIDELL
WESLEY H. SAKAI, JR.
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March 12, 2008

Senator Carol Fukunaga, Chair
Senator Will Espero, Vice-Chair
Senate Committee on Economic Development & Taxation
State Capitol
Honolulu, Hawaii 96813

RE: Testimony in Support of HB 1075 HD1, Re Real Property
Hearing: Thurs., March 13, 2008, 1:40 p.m. Conf. Rm. #224

Chair Fukunaga and Vice-Chair Espero and Members of the Committee:

This firm is counsel to a non-profit entity known as Citizens for Fair Valuation ("CFV"), whose members include many of the ground lessees operating small businesses in Mapunapuna.

Those businesses are vital to Oahu's economy, provide hundreds of jobs and pay millions of dollars in state and local taxes. Those lessees are currently facing rent renegotiation of their ground leases and are concerned that the new rent increases will be so high that they may be forced to close their businesses or, if they are able to stay, the increased rent will be passed on to local consumers thereby contributing significantly to the already high cost of living in this state.

CFV supports this bill and requests that it be amended to include a definition of "fair and reasonable rent" so as to create a level playing field between lessees and lessors as follows:

Insert between the existing paragraphs 4 and 5 of HB1075 HD1, a new paragraph 5 defining "fair and reasonable rent" as follows:

"(5) Where a lease provides for the renegotiation of rent during the term of the lease and such renegotiated rent is based, according to the terms of

the lease, on fair and reasonable annual rent, or words of similar import, such rent must be fair and reasonable to both of the parties to the lease. A rental amount that is fair and reasonable to both parties shall provide a fair return on and of the investment of both parties to the lease.

Former paragraph 5, should be renumbered paragraph 6

Subsection (b) should be amended as follows:

"b) For purposes of this section, "commercial or industrial leasehold property" means any ~~real~~ property ground lease:

- (1) Situated in the state;
- (2) Zoned by a county for commercial, industrial, or mixed use; and
- (3) That is subject to a lease with an initial ~~unexpired~~ term of more than twenty-five years and an unexpired term of five years or more".

We ask that the bill as amended be passed out by this Committee.

Thank you for the opportunity to testify.

Very truly yours,



Jay M. Fidell

JMF/ss

testimony

From: Alohasstates1@aol.com
Sent: Thursday, March 13, 2008 1:37 AM
To: testimony
Cc: Alohasstates1@aol.com
Subject: Re: HB 1075 Senate committee on EDT to hear bill 3-13-2008 at 1:40pm in Room 224

March 13, 2008

RE: HB1075

The committee on EDT has scheduled a public hearing on 3-13-2008 at 1:40 pm
Room 224

Senator Carol Fukunaga, Chair, EDT Email: senfukunaga@capitol.hawaii.gov
Sen. Will Espero, Vice Chair senespero@capitol.hawaii.gov
Sen. David Y. Ige sendige@capitol.hawaii.gov
Sen. Sam Slom senslom@capitol.hawaii.gov
Sen. Kalani J. English senenglish@capitol.hawaii.gov

Dear Chairperson Sen. Fukunaga, Vice Chairperson Sen. Espero, and Committee Members,

Please pass HB 1075.

This bill will help correct several of the major issues that have evolved over the past decades, relating to commercial and industrial long term ground leases.

It is unfortunate that land issues have been and continue to be a major component to Hawaii's high cost of living, as well as Hawaii's high cost of doing business.

Please note that there appears to be an error in the wording of the bill at Section 2, subsection (b)(3). The bill currently states: "That subject to a lease with an unexpired term of twenty years or more". This wording should be: "That subject to a ground lease with an original term of twenty years or more".

Additionally, to be of any use to the people of this state, the bill should take affect immediately upon enactment.

By passing this bill, with the above referenced changes, the Hawaii legislators will be doing their part in helping address this important matter.

Please pass HB 1075, with the above referenced corrections.

Thank you.

3/13/2008

Rick Krystoff
Email: alohastates1@aol.com

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