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March 16, 2009

The Honorable Angus L.K. McKelvey, Chair
House Committee on Economic Revitalization,
Business & Military Affairs
State Capitol, Room 312
Honolulu, Hawaii 96813

RE: S.B. 764, S.D. 2 Relating to Real Property

HEARING DATE: Tuesday, March 17 at 7:30 a.m.

Aloha Chair McKelvey, Vice Chair Choy and Members of the Committee:

I am Myoung Oh, Government Affairs Director of the Hawai'i Association of REALTORS® ("HAR"), here to testify on behalf of HAR and our 9,600 members in Hawai'i. HAR opposes S.B. 764, S.D. 2, which mandates that rent renegotiation terms in commercial and industrial lease agreements must provide that rent be "fair and reasonable" to lessor and lessee.

HAR empathizes with the lease renegotiation issues that businesses are facing in Mapunapuna, Kalihi Kai and Sand Island. However, we are deeply concerned that this legislation will have serious consequences on all other long-term commercial and industrial leases in Hawai'i.

HAR is opposed to this bill because it unduly interferes with the rights of lessors and lessees to freely enter into lease agreements. In addition, to the extent that this bill affects all existing long-term commercial and ground leases, HAR feels that the problem one lessor faces does not warrant modifying previously negotiated lease agreements for all other long-term leases in Hawai'i.

HAR believes that it is problematic to specify through legislation that various factors must be taken into consideration during a rent renegotiation. For example, under Section 2, page 4, lines 12-15, a rent renegotiation term must state that it is taking into account the "uses and intensity of use approved by the lessor." If rent calculations must take this factor into account, it would be in a lessor's best interest to choose high-end businesses that maximize their properties usage. This could have a negative impact on non-profits and smaller businesses in Hawai'i. Instead of imposing these problematic terms, HAR believes that fair market and property valuation should be left in the hands of licensed appraisers.

Moreover as written, Section 2 of S.B. 764, S.D. 2 (at page4, lines 3-12) requires that, where "fair and reasonable" annual rent is provided for as a term of the lease, this term must include that the rent will be fair and reasonable to both the lessor and lessee. For future leases, this provision creates a problem, as it will be a disincentive for the lessor to provide for "fair and reasonable" annual rent at the outset of the lease.

Finally, HAR believes that, rather than require that leases include the ambiguous language

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provided in the bill, the parties to a lease agreement should be left to handle rent renegotiations as they typically always have - though the process of appraisals, mediation, arbitration and, as a last option, the court system. These are appropriate existing procedures through which parties can resolve lease disputes.

For the above reasons, we respectfully ask the Committee to hold this measure.

Mahalo for the opportunity to testify.

BIA-HAWAII
BUILDING INDUSTRY ASSOCIATION
March 17, 2009

Honorable Angus McKelvey, Chair
Committee on Economic Revitalization, Business
And Military Affairs
State Capitol, Room 312
Honolulu, Hawaii 96813

RE: SB764, SD2 "Relating to Real Property"

Dear Chair McKelvey and Members of the Committee on Economic Revitalization, Business and Military Affairs:

I am Karen Nakamura, Chief Executive Officer of the Building Industry Association of Hawaii (BIA-Hawaii). Chartered in 1955, the Building Industry Association of Hawaii is a professional trade organization affiliated with the National Association of Home Builders, representing the building industry and its associates. BIA-Hawaii takes a leadership role in unifying and promoting the interests of the industry to enhance the quality of life for the people of Hawaii.

BIA-Hawaii opposes SB764, SD2 "Relating to Real Property". While BIA-Hawaii sympathizes with the situation of lessees in the Mapunapuna, Kalihi Kai and Sand Island areas, some of whom are members of the Citizens for Fair Valuation, **we cannot support** SB764, SD2 which seeks to alter the original renegotiation clauses of existing lease contracts by adding new terms and conditions. We believe it is bad policy to pass a bill that is targeted to only one lessor and its lessees and to alter the conditions and terms of their leases. Once enacted, such as law will set a bad precedent and cause even more uncertainly in lease agreements..

The proponents of the bill believe that they can resolve their problems by enactment of this bill that uses the terms "fair and reasonable". We believe such terminology would be open to challenges. BIA-Hawaii believes that both parties to a lease should clarify their understanding of what the terms of the lease are and abide by the terms once agreement is reached. BIA-Hawaii believes that the terms of a contract between private parties should not be changed by state law. We also hope that the lessees can come to satisfactory agreements with the lessor.

Thank you for the opportunity to express our views.

Karen L. Nakamura

Chief Executive Officer
BIA-Hawaii

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March 14, 2009

Committee on Economic Revitalization, Business, & Military Affairs

Rep. Angus L.K. McKelvey, Chair
Rep. Isaac W. Choy, Vice-Chair

TESTIMONY IN SUPPORT OF SB 764

DATE: Tuesday, March 17, 2009
TIME: 7:30 AM
PLACE: Room 312

Dear Representatives McKelvey and Choy and Members of the Committee:

My name is Jay Fidell and I am general counsel of Citizens for Fair Valuation, Inc., a Hawaii non-profit corporation, which represents industrial and commercial ground lessees in Mapunapuna, Kalihi Kai and Sand Island.

The members of Citizens for Fair Valuation include various industrial and commercial ground lessees in these areas in which HRPT is the landlord. Many of these and other HRPT lessees in the area have gotten very high rent renegotiation proposals.

Although the HRPT lease form provides that the lease rent will be "fair and reasonable", the lease does not explain what "fair and reasonable" means. I do not believe that setting the rent at twice the rent or more is "fair and reasonable", particularly in view of the fact that these ground lessees are generally unable to afford to pay those increases and still operate their businesses and pay their employees.

If they cannot get a fair and reasonable rent from HRPT, they are at risk of losing their businesses and their improvements will revert to HRPT.

If they are charged higher rent, and in most cases it is double what they are paying now, they will have to raise their costs to their customers who buy their products and they in turn will have to increase their prices to the consumers that they serve. In this economy, people can't afford those higher prices and, so there will probably be less purchasing which will then affect their abilities to keep their workers employed.

This bill provides that the rent increase shall be "fair and reasonable" to both lessor and lessee and that the determination of the increase will depend on actual factors affecting to or relating to my property and not some imagined "highest and best use". Fair and reasonable rent will allow these lessees to continue to operate their business, pay their debts, service their customers and keep their employees working.

For these and other reasons, I urge you to pass this Bill. Thank you for allowing me to testify on this bill.

Very truly yours,

Jay M. Fidell
Of BENDET, FIDELL, SAKAI & LEE

JMF:dt

SERVCO PACIFIC INC.
2850 Pukoloa Street · Suite 300 · Honolulu, Hawaii 96819 · Telephone: (808) 564-1300 · Facsimile: (808) 523-3937 · www.servco.com

March 16, 2009

To: The Honorable Angus L. K. McKelvey, Chair
and Committee Members
Committee on Economic Revitalization, Business, & Military Affairs

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

Hearing Date: Tuesday, March 17, 2009, 7:30 a.m., Conference Room 312

In Support of SB764 SD2, Relating To Real Property

On behalf of Servco Pacific Inc. ("***Servco***"), I submit the following comments in support of the adoption of SB764 SD2 (the "***Bill***") as written.

As testified earlier, this bill affects businesses and lessees in the Mapunapuna, Sand Island, and Kalihi Kai areas who are trying to negotiate with landlowner, HRPT, a Boston-based real estate investment firm. Servco has long-term commercial and industrial ground leases with HRPT in Mapunapuna. Our ground leases specifically provide that "said rent shall be such fair and reasonable annual rent for the demised land". We and other similarly affected lessees are asking that you continue to support us by adopting this bill which calls for our ground lease rents to be negotiated on terms that are "fair and reasonable" to BOTH the landowner and lessees. HRPT is demanding rents that are double or triple what their lessees are now paying. They are also requiring a rent escalator of 3% to 4% that compounds annually. These rent offers are not "fair and reasonable" and our local companies simply cannot afford these rents.

This bill would only affect leases that use the "fair and reasonable" language and is not intended to amend or modify the terms of the lease. In addition, the bill will not limit the ability of landowners and lessees to freely negotiate lease rent but will encourage and facilitate an open and transparent negotiation process.

This bill will not cost the State anything. But without it, the State may lose additional revenues if companies are forced to shut down and more jobs are lost due to exorbitant ground lease rents that are not fair and reasonable given the difficult economy and challenges that we face today. With your support of this bill, you will be supporting our local companies, their workers, and the customers we serve throughout the State.

We again thank you for the opportunity to share our comments with you.

ACE Hardware
Ben Franklin Crafts

March 13, 2009

Rep. Angus L.K. McKelvey, Chair
Rep. Isaac W. Choy, Vice-Chair
Committee on Economic Revitalization, Business, & Military Affairs
State Capitol
Honolulu Hawaii 96813

RE: **Senate Bill 764 Relating to Real Property**
Hearing Date: March 17, 2009, 7:30 am., Room 312 State Capitol

Dear Representative McKelvey and Representative Choy and Members of Committee,

My name is Guy Kamitaki and I am one of the family members that own and operate the Ben Franklin Crafts Store at 2810 Paa St. in Mapunapuna. We employ over 50 people at this location.

We would like to urge you to pass Senate Bill 764 – Relating to Real Estate.
Our ground lease with our current landlord, LTMAC Properties, LLC a mainland based REIT came up for renewal on 1/1/09.

As our ground lease states, we would like our ground lease negotiations to be "fair and reasonable" to allow us to continue doing business in this location. We do not consider doubling or tripling our ground lease payments to be "fair and reasonable." We have been in this location for over 16 years and we have been operating stores in Hawaii for over 50 years.

We are currently having a difficult time leasing out some of the space in the building. Currently we are trying to lease out about 8,000 square feet of retail and office space.

We urge you to pass this legislation to better define the "fair and reasonable" clause in our lease and allow us to continue operating our store in the Mapunapuna area.
Thank you for your consideration.

Aloha,

Guy Kamitaki

BFS, Inc. dba Ben Franklin Crafts • Ace Hardware Hawaii, Inc. dba Ace Hardware
2810 Paa Street Bldg A • Honolulu, Hawaii 96819 • Phone: (808) 838-7773 • Fax: (808) 838-7776

AMERICAN ELECTRIC

Committee on Economic Revitalization, Business, & Military Affairs
Rep. Angus L.K. McKelvey, Chair
Rep. Isaac W. Choy, Vice-Chair

TESTIMONY IN SUPPORT OF SB 764

DATE: Tuesday, March 17, 2009
TIME: 7:30 AM
PLACE: Room 312

Dear Representatives McKelvey and Choy and Members of the Committee:

I support SB 764, as written, and urge you to act on this important bill to help local businesses survive this recession. My name is Robert Dewitz and I live in East Oahu. I own a business, American Electric Co., a Union Electrical Contractor (IBEW 1186) which is located in Sand Island area, and I employ roughly 200 people.

Many of my neighbors have family members who have lost their jobs, had their hours reduced, or have businesses which are barely surviving. Our business has seen a drop off in revenues last year, and we are trying to cut expenses before we have to cut benefits and lay off workers.

Rent is one of the largest expenses we face. Up to now, the rents charged by the Damon Estate were "fair and reasonable," which is what the lease specifically calls for. The new owners, mainland based HRPT, is demanding rents that are double or triple of the current amount plus, they want 4% per year escalations, at a time when the economy is in the worst recession since The Great Depression. In addition, HRPT demands that tenants sign a confidentially agreement before they will even start to negotiate. Such confidentiality agreements serve to eliminate the very "free market" principals that represent the foundation of America's economic vitality.

HRPT, by keeping transaction data out of the public domain, denies tenants the ability to negotiate a fair market rent. Access to transaction data is the single most stabilizing force in real estate. Open access to current market data levels the playing field and insures pricing that is based upon the free flow of information and not upon monopoly-like dominion over a given market. The Damon Estate made fair and reasonable rent escalations a central element of their business philosophy for more than 30 years. HRPT has made it clear that they intend to use their monopoly-like holdings to restrain the free trade of negotiation to their exclusive benefit, irrespective of the harm it does to many of Honolulu's small business owners.

Passage of this bill will require the mainland landowner to negotiate terms based on what is happening here in Hawaii, rather than trying to make up for losses on the mainland. We want rents that are fair and reasonable for both sides and reflect true market rents, not speculative land sales.

I want to stay in business and I want to keep my workers employed. However, I can't do that if the landlord makes demands that are not fair and not reasonable when times are so tough. I urge you to please pass SB 764 as it is written. Thank you.

Bob Dewitz

Robert Dewitz, Chairman
2308 Pahounui Drive
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Committee on Economic Revitalization, Business, & Military Affairs
Rep. Angus L.K. McKelvey, Chair
Rep. Isaac W. Choy, Vice-Chair

TESTIMONY IN SUPPORT OF SB 764

DATE: Tuesday, March 17, 2009
TIME: 7:30 AM
PLACE: Room 312

Dear Representatives McKelvey and Choy and Members of the Committee:

I support SB 764, as written, and urge you to act on this important bill to help local businesses survive this recession. My name is Glenn Kawamura and I live in Moiiliiili. I work at Polynesian Adventure Tours, which is located in the Mapunapuna area, and we employ roughly 350 people.

Many of my neighbors have family members who have lost their jobs, had their hours reduced, or have businesses which are barely surviving. Our business has seen a drop off in revenues last year, and we are trying to cut expenses before we have to cut benefits and lay off workers.

Rent is one of the largest expenses we face. Up to now, the rents charged by the Damon Estate were "fair and reasonable," which is what the lease specifically calls for. The new owners, mainland based HRPT, is demanding rents that are double or triple of the current amount plus, they want 4% per year escalations. In addition, they are demanding that I sign a confidentially agreement before they will even start to negotiate. Based on how Damon did it for over 30 years, this is not fair and reasonable.

Passage of this bill will require the mainland landowner to negotiate terms based on what is happening here in Hawaii, rather than trying to make up for losses on the mainland. We want rents that are fair and reasonable for both sides and reflect true market rents, not speculative land sales.

I want to stay in business and I want to keep my workers employed. However, I can't do that if the landlord makes demands that are not fair and not reasonable when times are so tough. I urge you to please SB 764 as it is written. Thank you.

Glenn Kawamura
Polynesian Adventure Tours, Inc.
1049 Kikowaena Place, Honolulu, HI 96819
Phone: 457-4302
Email: gkawamura@polyad.com

BACON UNIVERSAL COMPANY INC.

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March 16, 2009

Representative Angus L.K. McKelvey, Chair
Representative Isaac W. Choy, Vice-Chair
House Committee on Economic Revitalization, Business, & Military Affairs
State Capitol
Honolulu, HI 96813

Re: Testimony in Support of SB764
Hearing Date: Tuesday, March 17, 2009, Room #312

Dear Representatives McKelvey and Choy and Members of the Committee:

My name is Phillip John Silich, President& CEO and my company, Bacon Universal Company, Inc., is presently a lessee in Mapunapuna under an original lease with Damon Estate dating from 1967. Bacon has been in business in Hawaii for over sixty years.

Bacon owns and operates a retail heavy machinery and agriculture business which specializes in providing new, used and rental equipment as well as parts and service. Bacon is headquartered in Mapunapuna with branch operations in Kauai, Maui, Kona and Hilo. As of today, Bacon employs approximately 80 people: 45 of which are located in Mapunapuna with the balance in our other branches. Seven of my employees have been with the company in excess of 20 years and 5 for over 30 years.

Our customer base naturally comprises general contractors, builders, excavators, site work contractors, developers, and basically anyone involved in the earth moving and farming operations. We have a 35,000 sq. ft. warehouse, office and engineering workshop development on our 72,072 sq. ft. lot located on the corner of Ahua and Mokumoa Street. The buildings are worth approximately $3.5 to $4 million dollars assuming of course, that we are able to retain and afford our long-term ground lease. Bacon also has two additional lots on Mokumoa Street which we use to store our equipment and provide parking for our customers and staff. These two lots equal approximately one acre of land.

Although my lease covering the corner of Ahua and Mokumoa Street is not due for a renegotiation in the immediate future, my two lots in Mokumoa Street are scheduled for renegotiation in 18 month's time. These upcoming negotiations will not be with the Damon Trust, the original land owner, but with HRPT, a mainland-based real estate investment trust (REIT), who purchased the land roughly 5 years ago. Along with my fellow lessees in the Mapunapuna, Sand Island and Kalihi areas, we are very concerned

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because the current renegotiation rates being set by HRPT are simply beyond our ability to pay.

I believe the plight of our company and that of my colleagues is best illustrated by the under noted example:

a. The Mapunapuna area comprising about 200 acres of land and is a filled in former swamp. On high tide the ocean floods the intersection just off Nimitz Highway and Ahua Street to a depth of about 22 inches of water. Potential customers and workers are forced to either go away or negotiate their way around the various side streets to avoid damage from the brackish water to their vehicles. The entire area is subject to subsidence with the resultant cracking of walls, buildings and other problems associated with low lying lands. Meanwhile, HRPT is doubling the rents to between $8 and $10 per sq foot with a 4% annual escalating component. This compares with the current average rental rate of $3.70 to $4 per square foot for more than a 100% increase!!!

b. Now let us compare this rental rate to a prime location on Nimitz Highway (the former site occupied by the Jackson Auto Group) which is close to Mapunapuna but high and dry and not subject to flooding. This property faces Nimitz Highway with approximately 120,000 to 140,000 vehicles passing each way each day and has multiple entry and egress points. Loyalty Group, a long established Hawaiian family of property developers is offering this location at $6.24 per sq ft inclusive of the buildings and all development. My real estate colleagues tell me this translates in today's values at approximately $5 per sq. ft. land only for a premier location. This would then by deduction put the value of Mapunapuna in the range of $3.50 to $4.50 per sq. ft.

c. If one compares the HRPT extortionate rate of $9.25 with a comparable valuation of say $4.00 per sq. ft. per annum, you will clearly appreciate the lessees concerns.

d. The original Damon leases, which HRPT purchased, do not contain any provisions for an annual escalating factor but simply provide for a resetting of rates each 10 years with the further clause that the rate be "fair and reasonable." It is our contention that "fair and reasonable" be determined as a two way street whereby both Lessees and Lessors negotiate in good faith.

e. Another diabolical negotiating factor with HRPT, which was never ever used by the Damon Trust, is that to-date tenants entering into a renegotiation with HRPT are forced to sign a confidentiality agreement. Thus in all negotiations with the tenants HRPT has full knowledge of all rental rates, whereas the individual tenants are presently being extorted one by one. How can be it be a "fair and reasonable" rate when one powerful mainland based entity, holding all the cards, is extorting individual small and sole business owners into paying approximately 50% more than comparable market rates.

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On behalf of Bacon Universal and my fellow lessees I now appeal to you for passage of Senate Bill 764, House Bill 1593 Re Real Property. It is in no way intended to solely advance the Hawaiian lessees cause but to allow us to be given a fair opportunity of being able to negotiate a "fair and reasonable" rent as dictated by the lease agreement. Without the concept of "fair and reasonable" rents being applied to both sides, which is the purpose of this bill, then the tenants will be seriously disadvantaged and potentially forced out of business.

Again, please let me reiterate, this bill seeks to set parameters that "fair and reasonable" rents should be applicable to both parties of the lease. For the above reasons may I now petition you and your colleagues for your support and to ultimately pass this bill.

Yours Faithfully,

Phillip J. Silich
President & CEO

Phone: 839-7202
Fax: 839-9813
Email: psilich@baconuniversal.com

CITIZENS FOR FAIR VALUATION

841 Bishop Street, Suite 1500
Honolulu, HI 96813

ROBERT M. CREPS, PRESIDENT
CAROL LAM, VICE PRESIDENT
CONNIE SMALES, SECRETARY
PHILLIP J. SILICH, TREASURER

CULLY JUDD, DIRECTOR
KEALI'I LOPEZ, DIRECTOR
GUS COSSETTE, DIRECTOR
MICHAEL STEINER, EXEC. DIRECTOR

March 14, 2009

TESTIMONY TO THE HOUSE COMMITTEE ON ECONOMIC REVITALIZATION, BUSINESS, & MILITARY AFFAIRS

Tuesday March 17, 2009 at 7:30 A.M.
Room 312, Hawaii State Capitol

TESTIMONY IN SUPPORT OF SB 764
Leasehold; Commercial and Industrial Property

Aloha Chair McKelvey, Vice Chair Choy, and Members of the Committee:

My name is Michael Steiner and I am the Executive Director of Citizens for Fair Valuation ("CFV"), a non-profit coalition of businesses with long-term ground leases in the Mapunapuna, Kalihi Kai and Sand Island areas. A partial list of lessees is attached to this testimony. These are the old Damon Estate lands which were purchased in 2003 by HRPT; a mainland based Real Estate Investment Trust (REIT). These ground leases, which typically last for 50 years, call for the renegotiation of rents that are "fair and reasonable," every 10 years.

Need for Legislation to Protect Local Businesses

House Bill 1593 seeks to establish that "Fair and Reasonable" rents should be applicable to both the lessor and the lessee. Unlike other ground leases in Hawaii which call for rent to be calculated upon land value at a certain rate of return, the HRPT leases call for "fair and reasonable" rents. CFV supports this Bill as it seeks to set parameters that will encourage open and transparent negotiations resulting in ground lease rental rates that are "fair and reasonable" to both parties and would not simply favor HRPT, who is now the largest industrial and commercial landowner in the State.

To be "fair and reasonable," rents should take into account the original agreed upon use and stewardship of the land. It is not "fair and reasonable" to increase rents based upon a single fee simple sale of land in the middle of captive space. At a minimum, to be "fair and reasonable" HRPT needs to take into consideration the agreed upon use of the land under lease, other newly signed ground leases for similar properties, the rates currently in force for neighboring properties, the general condition of the neighborhood, and the overall condition of the economy.

A landlord and tenant need to work together to provide stability and ensure that both parties benefit from the relationship. However, when asked how Hawaii rents will impact HRPT's profit, Adam D. Portnoy, Managing Director of HRPT, said during HRPT's 2nd Quarter Earnings Call on August 5, 2008:

> "We are pushing rates very hard especially in places like Hawaii ... we've gotten a lot of flack in that market because we're pushing rates so hard ... So rest assured that we're doing everything we can, as much as we can and as fast as we can to try to increase the rates there to push cash flow to HRPT."

To accomplish this goal, HRPT is demanding base rents that are double or triple existing rates plus a 3.5% to 4.5% annual escalation. In addition, **HRPT is requiring its lessees to sign confidentiality agreements *before* negotiations will commence** – which is something the Damon Estate never required.

CFV is requesting that the State pass HB 1593 to provide the public a foundation upon which open and transparent negotiations will lead to rents that are "fair and reasonable" to both sides.

Not a Private Dispute

The situation with these leases is not a private dispute between a group of lessees and one lessor. HRPT is a monopolistic owner and, especially in light of the current recession in Hawaii where every day brings news of more lay-offs and downsizing, tenants need the assistance of the legislative body to set parameters in which ground lease rents are negotiated in an open and transparent manner to provide "fair and reasonable" rents.

The issue is the continued economic viability of the Mapunapuna/Kalihi Kai/Sand Island industrial properties, the businesses that are located there and the continued employment of the hundreds, if not, thousands, of employees who work there. Moreover, this bill addresses a state-wide concern as the lessees in the Mapunapuna area provide goods and services across the entire State of Hawaii. Among the lessees' businesses are Grace Pacific, Servco, Sony, Coca Cola, Ameron, Olelo Television, Bacon Universal and Inter-Island Solar Supply, all of which have multi-island responsibilities. In addition, there are numerous small and medium-sized companies that include electrical and plumbing supply houses that service contractors all over the state, general and sub-contractors who have jobs throughout the state and many others who provide goods and services to consumers and businesses on every island within the State.

Accordingly, significant increases in operating expenses will clearly impact the economy of the State of Hawaii. What happens to the Mapunapuna lessees is and should be a state-wide concern for legislators in this economy. This Bill recognizes that landlords and tenants, owners and lessees, need to come together to negotiate, in an open and transparent manner, to achieve rents that are "fair and reasonable" to all parties in order to preserve the businesses that provide for our way of life.

HRPT Violating Contract Language

Many contracts include definitions to assist the parties in performing their obligations under a contract; however, the former Damon Estate leases that contain the "fair and reasonable" provision do not.

The pending bills would establish parameters to ensure that rent adjustments under these particular leases be fair to both the lessor and the lessees. The bill does not add any new terms or delete existing terms from the lease or change any words in the lease. As such, the Hawaii Supreme Court case of Anthony v. Kualoa Ranch, Inc. 69 Haw. 112 (1987), is not applicable as HB 1593 does not seek to "operate as a substantial impairment of a contractual relationship." HB 1593 is written such that it supports the 2002 Attorney General's opinion that a Bill should "provide a reasonable and narrowly drawn means to accomplish a significant and legitimate public purpose."

The Damon leases call for a rent renegotiation every 10 years and that, "said rent shall be such fair and reasonable annual rent for the demised land (exclusive of buildings)" for that period. It is HRPT that is changing the contract language by insisting that renewals include annual escalations, confidentiality agreements, a right of first refusal and more... In this time of economic uncertainly, this is not in the public's best interest as these steep rental increases will result in higher consumer costs, more unemployment, possible business failures and ultimately, a lowering of revenue for the State of Hawaii.

HRPT Intimidation Conduct

Most ground leases in the Mapunapuna area have a term of 50 years. As mentioned, Damon would work with its tenants during tough times to ensure the viability of the businesses and protect its long-term relationship. Lessees have relied upon this conduct for the past 30 years.

With the sale of the property to the mainland-based HRPT, the old ways have been discarded. Instead of "fair and reasonable" negotiations, HRPT is demanding confidentiality agreements and mediation rather than simple open and transparent negotiation. No longer can neighbors meet to "talk story" without the fear of repercussion or law suit. Instead of setting a level rate for each new segment of the lease, HRPT is only offering rents with annual increases that range between 3.5% and 4.5%. In addition, HRPT is requiring the lessees to grant HRPT a right of first refusal to the lease in all re-openings.

As mentioned, HRPT is demanding that tenants sign a confidentially agreement before they will even start to negotiate. Such confidentiality agreements serve to eliminate the very "free market" principals that represent the foundation of America's economic vitality. HRPT, by keeping transaction data out of the public domain, denies tenants the ability to negotiate a fair market rent. Access to transaction data is the single most stabilizing force in real estate. Companies such as CoStar and others thrive by providing unfettered access to rent and other transaction data to any who subscribe, e.g. appraisers, real estate brokers, investors, landlords, property managers, and tenants alike.

Open access to current market data levels the playing field and insures pricing that is based upon the free flow of information and not upon monopoly-like dominion over a given market. The Damon Estate made fair and reasonable rent renegotiations a central element of their business philosophy for more than 30 years. HRPT has made it clear that they intend to use their monopolistic holdings to restrain the free trade of negotiation to their exclusive benefit, irrespective of the harm it does to many of Honolulu's small business owners.

These changes are not consistent with the "course of conduct" that was established over the years with Damon Estate. These changes are material and go beyond what would be considered "fair and reasonable" to both parties. They serve only to benefit the land owner and to reaffirm Portnoy's statement, "... you're going to see over the next 18-24 months [HRPT] continue to try to push rates as much as we can."

Negotiating under Duress

To state the obvious, ground leases are for just the ground. It is the lessees' responsibility to construct and maintain their buildings, which will revert to the land owner at the end of lease. In addition to the good-will built up over years of occupying the same location, the lessees' buildings represent a huge investment. Moving to another location is not an option as the lessee is bound to pay rent to the lessor whether they occupy the land or not. Without parameters to ensure that "fair and reasonable" rents will apply to both parties, the mainland owner can use its power to its advantage to create and demand rents that are not fairly negotiated. In essence, they are using their monopolistic power to economically evict tenants.

Arbitration Does Not Work

Should the owner and lessee fail to reach agreement, the lease requires the parties to enter arbitration. However, arbitration is not a viable method to determine the rent valuation.

Because the lessor has required the lessee to sign confidentiality agreements in advance of negotiations, and that agreement prohibits lessees from disclosing any terms offered or accepted, HRPT has made it

impossible for the lessees to obtain meaningful information regarding the results of any other lessees' negotiations – which could be argued to be the best comparable information. HRPT, on the other hand, is working with "inside information" as it has data for all current rents, pending negotiations, signed leases, and mediated or arbitrated outcomes.

HRPT holdings include more than 150 ground leases. With HRPT's announced course of "pushing rents" as high as possible, the number of arbitrations will increase. Unfortunately, Hawaii's pool of qualified appraisers is small and many may look to HRPT as a steady and lucrative source of business. The potential to sway the process to the land owner's benefit will increase and the individual lessee, who has no access to "fair and reasonable" data, be at a distinct disadvantage. HB 1593 will help set parameters to enable a fair and reasonable outcome to a negotiation, mediation and/or arbitration.

Arbitration is a lengthy and costly process that puts an extreme burden on the lessee. In these hard times, business owners are working frantically to maintain their existence and keep their employees employed. It is not within their budget projections to be forced to spend thousands of dollars to fight with the lessor – who truly should be a business associate and not an adversary.

Failure to Respond to Community Needs

HRPT is an extremely large Real Estate Investment Trust (REIT) that must return at least 90% of its profits to its Stakeholders in order to maintain its preferred tax status. Most of its holdings are commercial high-rise office buildings located on the mainland and not long-term ground leases. HRPT is not accustomed to doing business here and, in the opinion of the writer, cares little for the "Aloha" that comes with the responsibility of owning Hawaiian land.

HRPT has stated that it has spent $750,000 studying the tidal flooding its Mapunapuna land and has given the state a recommendation to cure the problem – it has not offered to tackle the problem or pay for it even though HRPT will ultimately receive the largest benefit. In contrast, back in 1999 Damon paid $6,000,000 to provide new sewers and cesspools to its lessees.

Citizens for Fair Valuation ("CFV"), a non-profit coalition of businesses that lease land from HRPT, has sent seven (7) separate invitations to HRPT offering to meet to discuss how we can mutually obtain "fair and reasonable" rents for everyone concerned; however and to-date, each offer was rejected by HRPT. HRPT has done everything possible to intimidate its lessees and has taken aggressive steps to "divide and conquer" its tenants by forcing them to operate under a veil of secrecy.

Conclusion: Help Us Save Our Jobs

As a final comment in support of this legislation, the lessees with HRPT leases are hard working business people who would rather conduct their business, which is getting harder to do each day, than campaign for new legislation. They do not object to paying rent that is fairly negotiated and determined by applicable economic and market factors including, but not limited to, applicable comparables, the current use of the property and the characteristics of neighborhood (i.e. daily flooding, poor streets, stream flooding, crime, construction, etc). They do, however, strongly object to a lessor who uses "take-it-or leave-it" tactics while insisting upon rents that range from $8.00 to $10.00 per sq. ft., with annual increases set between 3.5% and 4.5 %. As a comparison, the Jackson Auto dealership on Nimitz Highway, is listed at $6.24 per sq. ft. for the land *and* improvements (buildings) and does not have the infrastructure problems that the Mapunapuna lessees have to live with on a daily basis. Hawaiian Homelands has two parcels in Shafter Flats for lease at $5.36 but neither has attracted any takers other than the existing tenant.

In these hard times, small businesses need assistance. The state simply cannot afford to see more closures and the loss of employment. In particular, the businesses in the Mapunapuna, Kalihi Kai and Sand Island area represent a foundation upon which these islands were built. These are proud people who are not looking for a bail-out; they just want the comfort of knowing that both parties in these lease renegotiations will act in an open and transparent manner that will produce "fair and reasonable" rents for all concerned.

CFV appreciates your consideration and asks that you please pass SB 764, as written.

Thank you.

Michael Steiner

Michael Steiner
Executive Director
Citizens for Fair Valuation
Telephone: (808) 221-5955
Email: MSteiner@SteinerAssoc.com
Web Site: www.FairValuation.org
Video at: http://www.fairvaluation.org/video.aspx?video=cfv.wmv

Property Management & Leasing
Pacific Guardian Center - Makai Tower
733 Bishop Street, Suite 1820
Honolulu, HI 96813

tel: (808) 599-5800 fax: (808) 599-5806

Reit Management
& Research LLC
PROPERTY MANAGEMENT
DIVISION

[redacted] 200[redacted]

VIA EMAIL & CERTIFIED MAIL
RETURN RECEIPT REQUESTED

[redacted]
Honolulu, HI [redacted]
Email: [redacted]

RE: Lease dated [redacted] and between Masters Properties LLC [redacted]

Dear [redacted]

The purpose of this letter is to commence rent resetting negotiations as pursuant to your lease, it is not an offer to set lease rent. The following are the terms upon which Masters Properties LLC would consider setting the rent [redacted]

Landlord:	Masters Properties LLC, a wholly-owned subsidiary of HRPT Properties Trust.
Tenant:	[redacted]
Premises:	Land consisting of approximately [redacted]
Annual Rental Rate:	For the [redacted] square foot of land, NNN, increasing annually by 4%. Rent will be [redacted]
G.E.T.:	Tenant shall pay Hawaii General Excise Tax (currently 4.712%) on all amounts payable to Landlord.
Conditions:	Tenant will accept the Premises in its "as-is" condition.
Confidentiality:	Tenant acknowledges that the economic terms of this proposal, any lease or lease amendment prepared pursuant to acceptance of this proposal, which includes Rent, Tenant Improvement Allowances, and any other consideration provided herein by the Landlord, constitute information which is either non public, confidential or proprietary, or a combination thereof. Such information, in whole or in part, is hereinafter referred to as the "Information". Tenant agrees that the Information will be kept confidential and will not, without

Confidentiality (continued): Landlord's prior written consent, be disclosed by Tenant, in any manner whatsoever, in whole or in part. Tenant agrees to transmit the Information only to its attorneys and/or partners of the firm herein for the purpose of evaluating the proposed lease transaction. Tenant will be responsible for any breach of this confidentiality provision caused by its attorneys and/or partners. Upon breach of this confidentiality provision, Landlord reserves the right, at Landlord's sole discretion, to change or modify the terms and conditions of this proposal or to withdraw the proposal altogether.

Other Terms: As set forth in Tenant's existing Lease.

It is understood by both Landlord and Tenant that this proposal is non-binding and is subject to changes, modification and/or withdrawal at any time without notice. Accordingly, there shall not be a binding agreement between Landlord and Tenant unless and until a mutually acceptable, final lease document has been executed and delivered by both Landlord and Tenant. In any event, this proposal will expire [redacted]

Please indicate your agreement with the foregoing terms and conditions by signing below and returning this letter to our office. Should you have any further questions, I can be reached at (808) 599-5800.

Regards,

[redacted]

Bradford C. Leach
Vice President – Pacific Region

AGREED:

[redacted]

[redacted]
Name:
Its:
Date:

ESTATE OF SAMUEL MILLS DAMON

April 11, 1997

Dear Trustees:

Re: Options for Extension of Fixed Rental Period & Waiver of Deferred Rent
35,698 sq. ft., Mapunapuna Industrial Subdivision

In early 1993 the Trustees of the Damon Estate concluded rent negotiations with the lessees of Mapunapuna for the 10-year period commencing either 11/1/92 or 1/1/93. The rent was set at $3.45 per square foot per annum at that time, with the option for incremental step-ups of $2.45, $3.45 and $4.45 for 3, 3 and 4 year periods, respectively. In October of 1995, lessees were advised that the $1.00 increase scheduled for either 11/1/95 or 1/1/96 would be deferred for a one year period due to a number of circumstances, including the drastic decline in demand for warehouse space, the lack of construction work and depressed economic conditions in general. In September of 1996, lessees were advised that the rent increases that were fully deferred a year earlier would be partially deferred for the next 2-year period and rent was set at $2.95. As a result of the $1.00 deferred for 1996 and the $.50 deferred for 1997 and 1998, the total deferred obligation in the amount of $2.00 has resulted in a substantial financial liability to our tenants.

The Trustees' ongoing evaluation of Hawaii's economic climate has resulted in their belief that the business interest of all concerned would be best served by an extension of the fixed rental period along with a waiver of the $2.00 in deferred rent that you are currently obligated to pay. Doing so should reduce uncertainties with respect to your lease and make long range planning more meaningful. The value of your lease should also be enhanced by giving you the flexibility to more readily secure conventional mortgage financing for property improvements or other business requirements, as well as making your lease more marketable.

FIRST HAWAIIAN CENTER · 999 BISHOP STREET, SUITE 2900 · HONOLULU, HAWAII 96813 · (808) 536-3717

This offer is made available to certain Mapunapuna lessees who are not in default under the provisions of their lease at the present time. For those lessees who are currently in default, you will be given thirty (30) days to cure the default, or to submit a plan to cure the default that is acceptable to the Trustees.

The options being made available by the Trustees follow:

Option 1:

3 years @ $2.95 per sq. ft. per annum (1/1/97 - 12/31/99)
3 years @ $3.15 per sq. ft. per annum (1/1/00 - 12/31/02)
Waiver of $2.00 in deferred rent (1/1/96 - 12/31/98)

Option 2:

	mo	annual
3 years @ $2.95 per sq. ft. per annum (1/1/97 - 12/31/99)	$ 8,775	105,309
3 years @ $3.15 per sq. ft. per annum (1/1/00 - 12/31/02)	9,371	112,449
5 years @ $3.45 per sq. ft. per annum (1/1/03 - 12/31/07)	10,263	123,158
5 years @ $3.95 per sq. ft. per annum (1/1/08 - 12/31/12)	11,751	141,007
Waiver of $2.00 in deferred rent (1/1/96 - 12/31/98)		

Kindly indicate your acceptance in the space provided below, noting the option you have selected, and return one copy to this office for our files. If acceptance is not received by this office prior to the close of the Estate's office at 4:00 p.m., Hawaii time, on the 15th day of May, 1997, it is withdrawn.

Very truly yours,

ESTATE OF SAMUEL MILLS DAMON

James M. Whitman
Executive Secretary

Option No. 2, Accepted this

8 day of May 1997.

Lessee

ESTATE OF SAMUEL MILLS DAMON

MEMORANDUM

To: Lessees of the Mapunapuna Industrial Subdivision with Quarterly Rent Due November 1999

From: James M. Whitman
Chief Operating Officer

Date: October 19, 1999

Re: Increase in Rent of $0.20 Per Sq. Ft. Per Annum for the 3-year Period Commencing January 1, 2000

Your current rental agreement calls for an increase in your rent by $0.20 per square foot per annum for the 3-year period commencing January 1, 2000, which is incorporated into the enclosed quarterly rent billing for November 1999.

By way of background, in early 1993, the Trustees concluded rent negotiations with the Mapunapuna lessees for the 10-year period commencing January 1, 1993. The rent established as fair and reasonable was $3.45 per square foot per annum, with the option for incremental step-ups of $2.45, $3.45 and $4.45 for 3, 3 and 4 year periods, respectively. In October of 1995, the $1.00 increase scheduled for January 1, 1996 was deferred for a one year period due to a number of circumstances, including the drastic decline in demand for warehouse space, the lack of construction work and the depressed economic conditions in general. In September of 1996, the rent increase that was fully deferred a year earlier was partially deferred for the next 2-year period and rent was lowered from the scheduled $3.45 to $2.95 per square foot. The total deferred obligation in the amount of $2.00 per square foot was subsequently waived by the Trustees. The net result of this was to reduce the average rent for the seven year period from the $3.45 agreed to $2.66 per square foot.

Recently, the Estate completed the installation of the new low-pressure sanitary sewer system in Mapunapuna at a cost of some $6,000,000 to the Estate. The benefits accrued to you by the installation of the sewer system include:

- A cleaner and healthier environment.
- Elimination of the need to pump out cesspools.
- A reduction of the flooding potential by eliminating the saturation of the surrounding soils caused by cesspools.
- The option to upgrade your improvements, thereby increasing the value in your leasehold interest. Previously, the City would not issue permits to allow an increase in density on these properties due to the lack of a sewer system.

As you know, the Damon Estate will be absorbing the cost of maintaining your individual grinder pumps, as well as the service line from the pump to the main sewer line in the street.

Considering that the contracted rent agreed to was $3.45, the Trustees believe that the proposed rent increase of $0.20 per sq. ft. per annum is fair and reasonable. If you have any questions, please call 536-3717.

First Hawaiian Center, Suite 2800 • 999 Bishop Street • Honolulu, Hawaii, 96813 • Tel: (808) 536-3717 • Fax: (808) 536-3729

Addendum to Testimony from Michael Steiner
In Support of HB 1593 and SB 764
Hearing Date: February 26, 2009, 2:15 p.m., Room # 325
Partial List of Lessees in the Mapunapuna/Kalihi-Kai/Sand Island Area

	Company
1	179 Sand Island Warehouse, LLC
2	Affordable Casket Outlet
3	A S N Enterprises
4	A-1-A Electricians
5	Ahua Enterprises
6	Al Castillo
7	Albert Young
8	Allied Building Products Corp.
9	All Nations Fellowship
10	Allwaste of Hawaii LTD
11	Aloha Auto Auction
12	Aloha Products
13	American Electrical Co., LLC
14	American Savings Bank
15	American Tire (Hawaiian Island Tire)
16	Ameron Hawaii
17	Anches, Jerome
18	Associated Construction
19	AT&T Wireless
20	Bacon - Universal Company, Inc.
21	Bank of Hawaii
22	Ben Franklin
23	Beth Israel Jewish Ministries Int'l
24	Big Rock
25	Blackbern & Associates
26	BOC Group, Inc.
27	Boise Cascade Corp
28	Bond, Jan Tr
29	Boulware, Michael H
30	C & F Machinery Corp
31	Carmen, Wade & Paula
32	Chevron USA Inc
33	Coca-Cola
34	Concrete Coring Co of Hawaii
35	Cossette Investments
36	Deer,Donald G 1989 REV TR/ETAL
37	Dennis Sullivan
38	Dimauro, Pender, leona
39	Diversified Energy Services
40	First Hawaiian Bank
41	Foster Equipment Co., Ltd.
42	Gentre Properties
43	Grace Pacific Corporation
44	Grapac Properties
45	Gray, James, TRS
46	GSH&K Investment
47	H Q INC
48	Hart, Doris J TR
49	Hawaii Concrete Product, Inc
50	Hawaii Nut & Bolt,Inc

	Company
51	Hawaii Stage & Lighting
52	Hawaiian Bitumuls Paving
53	HIE Holdings Inc
54	Hirahara, Ronald Y TR
55	Honolulu Disposal Service
56	Honolulu Painting Co
57	Honolulu Warehouse Co Ltd
58	Horizon Waste Services
59	HSI Electric, Inc.
60	Hydro-Scape Irrigation Supply
61	I DOI Hauling Contr, Inc.
62	Intech, Inc.
63	Inter-Island Solar Supply
64	Island Lighting
65	Ito-En (USA) Inc.
66	Jack Endo Electric
67	John Wagner Assoc Inc
68	Kahai St Dev Partnership
69	Kaiser Foundations Helath Plan
70	Kaya, Darlynne
71	Ken Yee
72	Ken's Auto Fender Ltd
73	Kilgo, A TR
74	Killebrew, George III Fam Tr
75	Kimi, William J Jr.
76	Kobatake, Gilbert D. Tr
77	Komohana Corp
78	Langer Hawaii Corp
79	Leeward Auto Wreckers Inc
80	Luria, Mark T.
81	M.C. Auto Body& Paint
82	Marcus & Associates Inc.
83	McKillican American
84	MHI LLC
85	Mid Pac Petroleum, LLC
86	Moanalua Exchange Ltd
87	Moanalua Mortuary
88	Monier Inc
89	Moos Machine Works, Inc
90	Mr. Sandman Inc.
91	MW Group Ltd.
92	Nakasone, Lillian KG
93	Nordic Construction Ltd
94	Oahu Metal & Supply Inc.
95	Okuhara Foods Inc
96	Olelo Community Television
97	Pacific Allied Products Ltd
98	Pacific Jobbers Warehouse
99	Pacific Machinery
100	Pflueger Group LLC

	Company
101	Philip Services Hawaii Ltd
102	Pioneer Electric Inc
103	Plywood Hawaii, Inc.
104	Pohounui Partners LLC
105	Polynesian Adventure Tours
106	Prime Construction Inc.
107	R & H Machinery Inc.
108	R WO & Associates Inc.
109	Ralph S. Inouye Co., Ltd.
110	Rasko Supply
111	Refuse Inc
112	Renfro, Charles & Carol S
113	Royal Construction Co. Ltd
114	RSI Roofing & Building Supply
115	S I Center Partners
116	Sawdust
117	Sears Roebuck & Co
118	Servco Pacific, Inc.
119	SLSS Partners
120	Snyder, Family Tr
121	Sony Electronics, Inc.
122	Specialty Surfacing Co.
123	STI Industries
124	Stoneridge Recoveries LLC
125	Sugai, Rodney Y Trust
126	Sin Industries Inc.
127	Sylvia, Robert C. Tr
128	Tagupa, James Tr
129	Takane, Janlu M
130	Takiguchi, Raymond K Tr
131	Tesoro Hawaii Corporation
132	Time Warner Entertainment
133	Tokunaga Masonry
134	Tri-Palm Industries Inc.
135	Tropical Ethanol Prod Ltd
136	Twentieth Century Furn Inc.
137	United Truck Rentals
138	UTR Liquidation * Repos Inc
139	Value Service & Supply
140	W T Yoshimoto Corp
141	Walker-Moody Construction
142	Wallner, Family Trust
143	Warehouse Rentals Inc.
144	WASA Electrical Service
145	Webco Hawaii, Inc.
146	Weggeland, Francis M
147	WESCO Distribution Inc.
148	White Cap Construction Supplu
149	Won, Philip W.
150	World Carpets Inc

Hawaii State Legislature
House of Representatives
Committee on Economic Revitalization, Business, & Military Affairs
Rep. Angus L.K. McKelvey, Chair
Rep. Isaac W. Choy, Vice-Chair

Tuesday, March 17, 2009
7:30 AM
Room 312

Testimony on SB764 SD1 Relating to Real Property

Submitted by Jon M. Van Dyke
on behalf of
Citizens for Fair Evaluation

This testimony is provided to address the constitutional issues that have been raised regarding SB764 SD1. In my professional judgment this bill meets the standards that have been applied by state and federal courts regarding the Contracts Clause and, if challenged, would, without question, be upheld as constitutional.

It has been argued by opponents of this Bill that it violates the Contracts Clause of the U.S. Constitution, Article I, Section 10. This provision of the Constitution has been utilized very rarely to strike down statutes. When challenges are raised, courts use a three part test to evaluate the statute challenged:

(1) Does the statute significantly impair a private contractual relationship?

(2) If so, does the statute serve a significant and legitimate public purpose?

(3) Are the provisions of the statute reasonably related to achieving the statute=s goals?

A leading constitutional law specialist has explained that state statutes Aare upheld even if they interfere with contractual rights, so long as they meet a rational basis test. Not surprisingly, virtually all laws have been found to meet this deferential scrutiny.@ ERWIN CHEMERINSKY, CONSTITUTIONAL LAW: PRINCIPLES AND POLICIES 637 (3d ed. 2006).

The U.S. Supreme Court articulated this deferential level of scrutiny in *Home Building & Loan Assoc. v. Blaisdell*, 290 U.S. 398 (1934), where the Court upheld a Minnesota law designed provide relief for debtors by creating a moratorium on the foreclosure of mortgages during the Depression. Even though the original purpose of the Contract Clause was to limit this type of debtor relief legislation, the Court ruled that the Minnesota law did not violate the Contract Clause because it was an emergency measure designed Ato protect the vital interests of the community@ and Aa basic interest of society.@ *Id.* at 439 and 445.

In only one case since 1934 has the U.S. Supreme Court declared unconstitutional a state

law that was alleged to have interfered with private contracts. *Allied Structural Steel Co. v. Spannaus*, 438 U.S. 234 (1978) (striking down a Minnesota law regarding pension plans on the ground that it was not narrowly tailored emergency legislation and did not serve a broad societal interest).

Cases since 1934 that have rejected Contract Clause challenges include:

* *El Paso v. Simmons*, 379 U.S. 497, 513 (1965), upholding a Texas law that clearly changed the terms of a contract and limited the rights of landowners to reclaim land that had been forfeited, explaining that the law had a legitimate purpose Ato restore confidence in the stability and integrity of land titles@ and to end the Aimbroglio over land titles in Texas.@

* *Energy Reserve Group v. Kansas Power & Light*, 459 U.S. 400, 413 (1983), upholding a Kansas law that restricted a natural gas producer from charging higher prices, explaining that Ain reviewing economic and social regulation, courts properly defer to legislative judgments as to the necessity and reasonableness of a particular measure.@

* *Exxon Corp. v. Eagerton*, 462 U.S. 176 (1983), upholding a state law that prevented oil and gas producers from passing on the costs of a severance tax, even though their contracts permitted them to do so.

* *Keystone Bituminous Coal Assoc. v. DeBenedictis,* 480 U.S. 470 (1987), upholding a law limiting coal mining, even though it impaired existing contracts, because the law served a significant government interest.

* *General Motors v. Romein*, 503 U.S. 181 (1992), rejecting a challenge to a Michigan law that changed a workers= compensation program on the ground that it did not in fact interfere with existing contracts.

The *Allied Structural Steel* case thus appears to have been an anomaly, based on its unique facts, and the cases that have been decided by the U.S. Supreme Court since then have all distinguished this case and have refused to find a violation of the Contracts Clause.

Hawaii decisions have followed these U.S. Supreme Court decisions and Hawaii courts have been similarly reluctant to strike down statutes under the Contracts Clause. In *In re Herrick*, 82 Hawaii 329, 340, 922 P.2d 942, 953 (1996), the Hawaii Supreme Court followed federal decisions in explaining that three criteria governed Contract Clause claims: A(1) whether the state law operated as a substantial impairment of a contractual relationship; (2) whether the state law was designed to promote a significant and legitimate public purpose; and (3) whether the state law was a reasonable and narrowly-drawn means of promoting the significant and legitimate public purpose.@ With regard to the first criterion, the Court went on to explain that an impairment is not Asubstantial@ unless it interferes with the Alegitimate expectations of the contracting parties,@ and that in reaching such a determination courts must examine Athe severity of the impairment@ and Athe extent to which the subject matter has been regulated in the past.@ *Id.* at 341, 922 P.2d at 954.

The other recent Hawaii case involving the Contracts Clause, *Anthony v. Kualoa Ranch, Inc.*, 69 Hawaii 112, 736 P.2d 55 (1987), is clearly distinguishable from the issues raised by S.B. No. 764 CD1, because it involved a statute that required lessors to pay lessees for improvements

made on leased lands, a requirement that Avery substantially impairs@ the lessors= contractual rights. 69 Hawaii at 120, 922 P.2d at 60. Although the Court struck down that statute, it also noted that Athere are cases where, in the legitimate exercise of a state=s police power, statutes which impinge upon existing contractual rights can be validly enacted without contravening the constitutional provision [the Contracts Clause],@ and that statutes would not be struck down unless they imposed a Asubstantial@ impairment on contractual rights. *Id.*

Applying these principles to SB 764 CD1 leads to the conclusion that its enactment would not raise any serious Contract Clause issues. To begin with, its language does not operate as a Asubstantial impairment@ of any contractual rights. The Bill says only that leases that allow for adjustments in lease rents according to Afair and reasonable@ terms should have that term interpreted in a manner that is Afair and reasonable to both the lessor and the lessee to the lease@ and the Bill identifies factors that should be considered in deciding what is Afair and reasonable.@ The language in this Bill thus does not change the terms of any contract, but rather provides a logical interpretation of an existing term. Under no stretch of the imagination could this modest language be viewed as a Asubstantial@ impairment of any contractual right.

If, somehow, a court did decide that a substantial impairment was effected by this statute, the Contract Clause would nonetheless not be violated because of the second and third criteria that govern the invocation of this Clause. SB 764 CD certainly serves a significant and legitimate public purpose, and does so in a manner that is narrowly drawn. As Section 1 explains, this Bill is designed to clarify lease terms during Athis time of crisis@ when Anational and state economies are in free-fall.@ Section 1 explains that Ait is in the public interest that its citizens remain employed, that businesses continue to operate and pay wages and taxes, and that financial failures be reduced.@ These are certainly significant and legitimate public purposes, and they are directly promoted by the narrowly drawn provisions in Section 2. The Bill simply clarifies ambiguous lease terms for the purpose of ensuring that both parties to the relevant lease contracts are able to negotiate from a level playing field. Its provisions are carefully and narrowly aimed at allowing the contractual relationship between lessor and lessee to continue in a fair manner and thus to facilitate economic activity during the present difficult time.

As this analysis of federal and state cases makes clear, the requirements governing a challenge to a state statute under the Contracts Clause are high, courts are deferential toward state legislatures when evaluating such challenges, and the language in S.B. No. 764 S.D.1 is in no danger of being declared to be in violation of the Contracts Clause.

McKILLICAN

March 16, 2009

Committee on Economic Revitalization, Business, & Military Affairs
Rep. Angus L.K. McKelvey, Chair
Rep. Isaac W. Choy, Vice-Chair

TESTIMONY IN SUPPORT OF SB 764

DATE: Tuesday, March 17, 2009
TIME: 7:30 AM
PLACE: Room 312

Dear Representatives McKelvey and Choy and Members of the Committee:

I support SB 764, as written, and urge you to act on this important bill to help local businesses survive this recession. My name is Patrick K. Fujioka and I reside at 41 Prospect Street; Honolulu, Hawaii 96813. I work at 2858 Kaihikapu Street; Honolulu, Hawaii 96819, which is located in the Mapunapuna/Sand Island/Kalihi Kai area, and I employ roughly 11 people.

Many of my neighbors have family members who have lost their jobs, had their hours reduced, or have businesses which are barely surviving. Our business has seen a drop off in revenues last year, and we are trying to cut expenses before we have to cut benefits and lay off workers.

Rent is one of the largest expenses we face. Up to now, the rents charged by the Damon Estate were "fair and reasonable," which is what the lease specifically calls for. The new owners, mainland based HRPT, is demanding rents that are double or triple of the current amount plus, they want 4% per year escalations, at a time when the economy is in the worst recession since The Great Depression. In addition, HRPT demands that tenants sign a confidentially agreement before they will even start to negotiate. Such confidentiality agreements serve to eliminate the very "free market" principals that represent the foundation of America's economic vitality.

HRPT, by keeping transaction data out of the public domain, denies tenants the ability to negotiate a fair market rent. Access to transaction data is the single most stabilizing force in real estate. Companies such as CoStar and hundreds of others thrive on the mainland, by providing unfettered access to rent and other transaction data to any who subscribe, e.g. appraisers, real estate brokers, investors, landlords, property managers, and tenants alike.

Open access to current market data levels the playing field and insures pricing that is based upon the free flow of information and not upon monopoly-like dominion over a given market. The Damon Estate made fair and reasonable rent escalations a central element of their business philosophy for more than 30 years. HRPT has made it clear that they intend to use their monopoly-like holdings to

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restrain the free trade of negotiation to their exclusive benefit, irrespective of the harm it does to many of Honolulu's small business owners.

Passage of this bill will require the mainland landowner to negotiate terms based on what is happening here in Hawaii, rather than trying to make up for losses on the mainland. We want rents that are fair and reasonable for both sides and reflect true market rents, not speculative land sales.

I want to stay in business and I want to keep my workers employed. However, I can't do that if the landlord makes demands that are not fair and not reasonable when times are so tough. I urge you to please pass SB 764 as it is written. Thank you.

Patrick K. Fujioka
McKillican American, Inc.
2858 Kaihikapu Street
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Pfujioka@mckillican.com

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March 16, 2009

Committee on Economic Revitalization, Business & Military Affairs
Rep. Angus L.K. McKelvey, Chair
Rep. Isaac W. Choy, Vice Chair

Re: Testimony in Support of SB 764
Date: Tuesday, March 17, 2009
Time: 7:30 AM
Place: Room 312

Dear Representatives McKelvey and Choy and Members of the Committee:

My names is James Yamada, Jr., and I am a lessee in Mapunapuna under an original lease with Damon Estate dated 1971.

I own and operate the electrical contracting firm A-1 A-Lectrician, which my father James Yamada, Sr. built from the ground up in 1979. We have now grown to become one of the largest electrical contracting firms in the state, with nearly 150 office employees and electricians. I built and own my 5,000 square foot office space, and will be adding on a 2,000 square foot office extension, with building to commence in April 2009. Currently, we have a mortgage with First Hawaiian Bank with a balance due to date of $150,000.00.

My lease is scheduled for rent renegotiations in 2012 with HRPT. With the economy in such a dismal position, I am very concerned about the potential rent increases set to take place in 2012.

Last year, due to unforeseen economic circumstances, we were forced to lay off 60 to 70 of our employees, including one employee who has been with our company since 1990. Without a determination of what exactly "fair and reasonable" means, we could see our rent nearly double, which could effectively force us to again make cuts to our workforce and/or cuts to pay.

Due to the harsh economy, other electrical contracting firms have lowered their labor costs to remain competitive. If rent costs are raised, we would be forced to increase our labor costs, which would threaten our chances of being awarded job contracts, and thus we would again be forced to make cuts to our workforce.

This Bill provides that the rent increase shall be "fair and reasonable" to both lessor and lessee and that the determination of the increase will depend on actual factors affecting or relating to my property. Fair and reasonable rent will allow me to continue to operate my business, remain competitive in the industry and keep my employees working.

With utmost regard for the sake of our employees and their families, I ask that you pass this Bill as written.

Sincerely,

James Yamada, Jr.
CEO

TESTIMONY FOR THE HOUSE COMMITTEE ON ECONOMIC REVITALIZATION, BUSINESS & MILITARY AFFAIRS
TUESDAY, MARCH 17, 2009, AT 7:30 A.M.
ROOM 312, STATE CAPITOL

RE: S.B. 764, S.D. 2, Relating to Real Property

Chair McKelvey, Vice Chair Choy, and Members of the Committee:

My name is Chris Woodard, Senior Real Estate Officer, for Reit Management & Research LLC, the property manager for HRPT Properties Trust ("HRPT"). Through its affiliated companies, HRPT owns industrial zoned land in Mapunapuna, Sand Island, and Ewa, and leases many of its Hawaii properties pursuant to long-term leases.

HRPT respectfully, but strongly, opposes S.B. 764, S.D. 2 (the "Bill"). This Bill is unprecedented and unconstitutional. The Bill is targeted at a single landowner—HRPT—and would effectively change the agreed upon terms of previously negotiated long-term commercial and industrial lease contracts, for the sole benefit of a small group of lessees. The proponents of the Bill include some of the largest companies in Hawaii and wealthy sandwich lease investors, who have enjoyed substantially below-market lease rents for the last decade. These lessees generally have 50-year ground leases which require that the rent be re-set every ten years. In testimony before the State Senate on this Bill, the Bill's proponents candidly admitted that they are pushing the Bill to use as leverage in lease rent renegotiations with HRPT, to use it (in the words of a State Senator) as a "club" against HRPT. HRPT respectfully submits that is not an appropriate use of the legislative process, and reinforces the conclusion that this Bill violates the Contracts Clause of the United States Constitution. HRPT urges the Bill be held in committee, for the following reasons:

1. **There is no public need for this legislation**— Since HRPT acquired its Hawaii properties in 2003, it has negotiated mutually agreeable rental rates for the vast majority of leases with re-set dates prior to January 1, 2009. When the lessor and lessee cannot agree, the existing lease contracts and existing law in Hawaii establish a procedure whereby the land's fair market value and resulting lease rent are determined by neutral, qualified appraisers. This fair market value appraisal procedure for determining commercial and industrial lease rent rates has

been followed here in Hawaii for many decades on all such leases. Resetting the rent at fair market value means the rent can increase or decrease.

In those few cases where the tenant and HRPT have not reached an agreement on new lease rent, HRPT has never declined a tenant's request for mediation which avoids the time and expense of arbitration otherwise required by the lease. The proponents of this Bill have stated that HRPT has made "take it or leave it" offers. That is simply false. HRPT is now negotiating with several tenants on rent re-renegotiation and lease restructuring issues, where both parties have amicably exchanged offers. HRPT has even accommodated several tenants' requests to re-set rents earlier than contractually required. HRPT also has entered into dozens of new leases. Demand has remained strong for HRPT's properties, and HRPT has tried to balance that demand with the needs of its existing tenants.

HRPT is a long-term investor in Hawaii. HRPT's business plan is to work with existing tenants to offer extended lease terms and fixed-rent periods in return for rental adjustments to market rates. This approach enables more tenants to obtain bank financing to improve their buildings, because banks often will not make capital improvement loans to businesses when their lease terms are short. HRPT also is working with some tenants on plans to make more efficient use of their property, most likely by reducing the size of their rental lot and building taller or higher-ceiling warehouses. That way tenants can obtain a long-term lease where they pay less rent on a more functional warehouse, and at the same time free up additional industrial land for other companies who wish to move to the area.

Many of the proponents of the Bill are tenants whose lease rent was last re-set in the 1990s, when property values were far lower than they are today. Research data from a prominent local full-service real estate firm show that industrial warehouse rents on Oahu have doubled between 1998 and 2008. The data also show that estimated industrial land values in the Mapunapuna/Sand Island/Kalihi Kai area have doubled during the same period. Tenants who have had the benefit of a low, fixed rental rate for the last ten years will now have their rent re-set to reflect those increased values and current market rates. However, HRPT views each lease on its unique facts and circumstances, and has always carefully considered any reasonable tenant proposal.

2. **The Bill is unconstitutional**—While the Bill's proponents claim that this Bill merely "clarifies" HRPT's leases with its tenants, in fact the Bill seeks to re-define an

existing term in existing leases. By the admission of the Bill's own proponents, in their testimony before the State Senate, the Bill seeks to change the lease rent redetermination process in existing leases for the sole benefit of lessees, to attempt to reduce their lease rent.

The Hawaii Supreme Court has cited three criteria in analyzing whether a state statute violates the Contracts Clause of the U.S. Constitution: (1) whether the state law operates as a substantial impairment of a contractual relationship; (2) whether the state law was designed to promote a significant and legitimate public purpose; and (3) whether the state law was a reasonable and narrowly-drawn means of promoting the significant and legitimate public purpose. Application of Herrick, 82 Haw. 329, 340 (1996)

a. The Bill substantially impairs a contractual relationship

This Bill substantially impairs HRPT's contractual relationships with its lessees because, among other reasons:

-- The Bill materially affects the most essential term in a commercial and industrial lease: the lessee's obligation to pay rent.

-- The Bill regulates an area of commerce, commercial and industrial leasing, that was not previously regulated by the State. State and federal courts have repeatedly held that the lack of any prior regulation and government intervention is an important factor in determining whether a new law violates the Contracts Clause.

-- The Bill re-defines an existing term in an existing contract, and according to its proponents, would command appraisers, arbitrators, and courts to interpret the existing term under this new definition—contrary to how appraisers and arbitrators have interpreted that term for decades of the contract.

-- The preamble to the Bill and the abundant testimony of its proponents make clear that the intent of the Bill is to reduce the amount of rent lessees would be obligated to pay when their rents are re-set under the lease contract. In other words, the sole purpose of this Bill is to take an economic benefit from one contracting party, the lessor, and give that economic benefit to the other contracting party, the lessee.

In sum, there can be no dispute that a law which fundamentally changes the lease rent re-determination process, and which has the intent and effect of reducing lease rent paid under the lease contract, substantially impairs a contractual relationship.

b. The Bill does not promote a significant public purpose

In determining whether a state law promotes a significant and legitimate public purpose, the Hawaii Supreme Court has stated that the new law must "impose a generally applicable rule of conduct designed to advance broad societal interests." Anthony v. Kualoa Ranch, 69 Haw. 112, 123 (1987). In Anthony, the Court held that a state law that simply tries to "do equity as the legislature saw it", by changing contractual obligations for the benefit of lessees, is unconstitutional. Id.

This Bill does not "advance broad societal interests," and is therefore unconstitutional under Anthony. HRPT is the only landowner in the State who holds leases affected by this Bill. This Bill is targeted at one, and only one, landowner, and would benefit a small but vocal group of lessees. Many of these lessees are wealthy sandwich lease investors. Their subtenants, often small local businesses, will not benefit from the Bill because (1) the Bill allows sandwich investors to pass on any rent increases to their sub-tenants; and (2) the leases between tenants and sub-tenants can be written so that any savings received by the sandwich investors from this Bill would not have to be passed on to the sub-tenants. The Bill in fact will harm, not help, small local businesses.

This is simply a private dispute between one landowner and a few lessees who apparently have differing views as to the current value of industrial land in or around Mapunapuna. In such a situation, Anthony requires that this private dispute be resolved according to the existing terms of the contract—not by a new law that seeks to rearrange contractual rights and obligations.

Finally, while the Bill speaks generally about fears that "this economic crisis will lead to more unemployment and business closures and financial failures," there are no findings and no evidence whatsoever that reducing the rent for a small group of lessees of one landowner will resolve those problems. In fact, contrary to the claims of the Bill's proponents, there have been no mass evictions, lease terminations, or business failures in Mapunapuna. Mapunapuna has always been and will remain a dynamic center for Oahu's industrial and commercial businesses, both large and small.

c. **The Bill is not reasonably and narrowly drawn**

In 2002, the Legislature was considering a bill that, among other things, would have changed the way fair market value is calculated in commercial lease rent negotiations. The Senate Commerce & Consumer Protection Committee asked for an Attorney General's opinion on the bill's constitutionality. In an April 11, 2002 letter to the Senate, the Attorney General explained why the bill failed to provide a reasonably and narrowly drawn means to accomplish a significant and legitimate public purpose:

> [A]lthough the problem of the oligopoly and residential leases in Hawaii is unique and found nowhere else in the United States, this problem does not apply to commercial leases. Most businesses lease their property rather than purchase them in fee simple. Furthermore, the businesses that can construct major improvements involving significant capital investments are generally run by managers with the knowledge and skill to negotiate terms of leases that are favorable. Those businesses with less investment in their property are more likely to be able to relocate. Furthermore, agreeing to a fixed rent even though land values may fluctuate is a business risk that businesses seeking a profit should take into consideration when negotiating a lease in the first place. In addition, the lessees have options available to them. They may continue to lease at the higher than market rent, sell their leasehold and move elsewhere, [or] negotiate a more favorable lease with another lessor because the fair market value of the land at this time is lower . . .

See Attorney General's April 11, 2002 Opinion Letter, p. 3.

The Attorney General's comments from 2002 apply equally to this Bill, seven years later. This Bill is unconstitutional; bad policy; and bad for business throughout the State of Hawaii. The Bill sets a terrible precedent, sending a message to all businesses that they cannot necessarily rely on enforcing mutually agreed contract terms in this State. I ask that the Committee hold this Bill, and I thank the Committee for the opportunity to express our opposition.

Grant Merritt
Dba Sawdust
151-b Pu'uhale Road
Honolulu HI 96819

March 16, 2009

SB 764 - RELATING TO REAL PROPERTY

DATE: Tuesday, March 17, 2009
TIME: 7:30 AM
PLACE: Conference Room 312

TO: Committee on Economic Revitalization, Business, & Military Affairs
Rep. Angus L.K. McKelvey, Chair
Rep. Isaac W. Choy, Vice-Chair

Aloha Chair, Vice Chair, and Members of the Committee,

RE: Testimony in Support of SB 764

Dear Representatives McKelvey and Choy and members of the committee:

My name is Grant Merritt and I own and run a small woodworking business in Kalihi Kai. This property is within the old Damon Estate now owned by HRPT.

HRPT has stated that their goal in Hawaii is to raise rents as quickly as possible to make up for losses incurred on the mainland. While I am a sub-lessee, my landlord has said that he is in negotiation now with HRPT and the ground rent may rise to double or triple what it was last year. On a straight pass through, this could translate into a fifty percent or more hike in my rent.

I employ two people and have been in business for three decades. We have just gone through one of the slowest two months we have had in perhaps a decade. If my rent goes up 50% I will have a hard time justifying staying in business. My lease option is up in November so I have a way out, but that leaves my landlord, a personal friend since the 1970's, and my employees and customers holding the bag. Hardly fair and reasonable.

One of the basic tenets of fair real estate negotiations is the ability to access information on prior transactions. HRPT requires tenants to sign a non-disclosure agreement thereby making it impossible to determine fair market value. They are evidently using their monopolistic position as the largest landowner of industrial property on the island to force greedy and destructive rents on the business community and leaving the tenants with no recourse. As a tenant, I have no way to prove or disprove these charges, but I am left with no other way of looking at these carpetbaggers as anything but just that. More

Wall Street thieves ensuring their huge bonuses at my expense and the expense of my friends and neighbors.

Hawaii will always be subject to outside power taking what it will. Always has, always will. We need to have some recourse, even if it is so weak as this. We need full disclosure. Barring that possibility, this bill seems to be our best shot for now.

HB 1593 proposes parameters for "fair and reasonable," a term unique to this lease, and does not in any way change the lease itself. I respectfully request that you pass this bill.

Sincerely,
Grant W. Merritt
Owner, Sawdust

From: fujinoh001@hawaii.rr.com
Sent: Sunday, March 15, 2009 12:14 AM
To: EBMtestimony
Subject: PLEASE SUPPORT SB 764 AS WRITTEN

Committee on Economic Revitalization, Business, & Military Affairs Rep. Angus L.K. McKelvey, Chair Rep. Isaac W. Choy, Vice-Chair

TESTIMONY IN SUPPORT OF SB 764

DATE: Tuesday, March 17, 2009
TIME: 7:30 AM
PLACE: Room 312

Dear Representatives McKelvey and Choy and Members of the Committee:

My name is Hansel Fujino and I own a company in the Sand Island/Kalihi Kai industrial area. My business is scrap metal recycling and I am also a certified redemption center for the HI-5 beverage containers. I have been through many economic ups and downs over the years but I have never seen anything like what is happening now. Business has deteriorated to the extent that I can't turn a profit today even if my rent remained status quo.

I even suspect that the city's curbside recycling program is in danger due to the precipitous drop in the price of commodities, to which my business was also adversely affected . Our trade publication had an article about New Zealand bailing out its recycling industry because it was deemed essential. I am not advocating for the recycling industry per se but to impress that many businesses are already facing a catastrophe.

The rent charged by the Damon Estate was determined by negotiation, not arbitration, which was then offered to all of the tenants affected. Now, the new owner is threatening everyone individually with arbitration, unless we accept their offer no matter how unreasonable. I suspect some businesses will cease to exist because of this.

I hope to retain my employees and get through this recession. However, as more businesses fail and people lose their jobs, the chances of this recession turning into something even more sinister increases. As such, I support SB 764, as written, and urge you to pass this important legislation and help local businesses survive. Thank you.

Hansel Y. Fujino
Oahu Metal & Supply, Ltd.
204 Sand Island Access Road
Honolulu, HI 96819
Fujinoh001@hawaii.rr.com

From:	ManyaVogrg@aol.com
Sent:	Monday, March 16, 2009 11:30 AM
To:	EBMtestimony@Capitol.hawaii.gov?subject=testing; Rep. Angus McKelvey; Rep. Isaac W. Choy; Rep. Lyla B. Berg; Rep. Cindy Evans; Rep. Joey Manahan; Rep. James Tokioka; Rep. Clifton K. Tsuji; Rep. Glenn Wakai; Rep. Jessica Wooley; Rep. Gene Ward
Cc:	TPZerbe@aol.com
Subject:	7:30am hearing March 17th Rm. 312 OPPOSING SB764, SD2

COMMITTEE ON ECONOMIC REVITALIZATION, BUSINESS, & MILITARY AFFAIRS
Rep. Angus L.K. McKelvey, Chair
Rep. Isaac W. Choy, Vice Chair
Tuesday, March 17, 2009
TIME: 7:30 AM Conference Room 312

Re: SB 764, SD2 RELATING TO REAL PROPERTY.Clarifies provisions contained in long-term commercial and industrial ground leases. (SD2) EBM, JUD
Honorable Chairs and Members of the Committee:

Our names are Manya Vogrig and Phyllis Zerbe, and we are testifying on behalf of ourselves and the members of our organizations.

We STRONGLY OPPOSE this type of legislation that is the taking and breaking up of private property under the guise of a "public purpose".

We ourselves (as hundreds of small landowners who own land under a condo or a co-operative apartment building developments) ... go through regular negotiations of lease rent, not more than every 10 years. When property values increase, we get no help to get "fair" rents to help pay our living expenses. Our leases are fixed almost always in at least 10 year increments, usually to pay a set percentage of the land value. We have to live on the agreed upon amounts, no matter what happens. If you are going to give the long term lessees a break when their lease rents go higher, then you need to give the lessors huge increases when property values skyrocket. Also, you can imagine how the rental units are going to fluctuate without controls. Furthermore, banks will stop loaning on properties altogether.

You may say that this proposed legislation doesn't affect us but many of the buildings on our properties have mixed uses, some of which include commercial businesses.

We trust that you will hold this legislation in order to prevent the taking of private property rights under the guise of public purpose ... and to prevent the chaos among land rights in the State of Hawaii if you are to interfere with private contracts.

Thank you very much!

Manya Vogrig **T. Phyllis Zerbe**
2877 Kalakaua Ave. #1205 **1434 Punahou St.**
Honolulu, HI 96815 **Honolulu, HI 96822**
Phone: 922-6934 **Phone: 949-9998**

For: Small Landowners of Oahu &
Small Landowners Association of Hawaii
(Small Landowners who own land under Condominiums
and Co-operatives in the State of Hawaii)

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Nohea M. Santimer
2444 Huene Street
Honolulu, Hawaii 96817
Telephone: (808) 595-7214

March 17, 2009

House Committee on Economic Revitalization, Business & Military Affairs
Hearing Date: Tuesday, March 17, 2009, at 7:30 a.m. in CR 312

Testimony in Opposition to SB 764 SD2: Relating to Real Property
(Alteration of provisions in long-term
commercial and industrial ground leases)

Honorable Chair Angus L.K. McKelvey, Honorable Vice-Chair Isaac W. Choy and Members of the Economic Revitalization, Business & Military Affairs Committee:

My name is Nohea M. Santimer and I am a small private landowner. I am writing to state my opposition to SB 764 SD2: Relating to Real Property because it would have a huge detrimental impact on a piece of property our family has owned for generations.

I understand that lessees who are having trouble negotiating their leases with one lessor proposed this measure. While I remain hopeful that further negotiations, arbitration and mediation can resolve such differences and result in renegotiated leases which can be accepted by both parties, I respectfully **oppose SB 764, SD2,** which:

- Changes existing commercial and industrial ground leases by mandating new terms and conditions for the renegotiation of rent with the lessor, and
- changes existing commercial and industrial subleases by giving the master ground lessees the statutory right to automatically pass on any pro rata rent increases to sublessees, if not otherwise specified in the sublease, and denies the subtenants an opportunity to negotiate a fair and reasonable rent with the master lessee.

My objections to SB 764, SD2, can be summarized as follows:

- SB 764, SD2 is an unconstitutional violation of the Contracts clause of the United States Constitution. You cannot 'fix' an unconstitutional bill by trying to change the 'purpose and intent' section of the bill.
- **"It is not good public policy to pass a state-wide law because of a dispute between one lessor and a few lessees."** even in tough economic times. How many statewide lessees other than those being targeted by this proposed bill will be negatively affected? Does a dispute with one lessor warrant a new statewide law purporting to save Hawaii's economy?
- **"It is unfair and unconstitutional to change the terms of existing contracts to favor one party."** The Attorney General has issued prior opinions finding that such alterations in the terms of existing leases are unconstitutional.
- **"Changes via the proposed bill should cut both ways"** – Why does the proposed bill provide that negotiations between lessors and lessees must use a new definition of "fair and reasonable annual rent," but at the same time the bill

also denies subtenants the opportunity to negotiate a fair and reasonable rent, by mandating that "sublessees shall be charged their pro rata share of the renegotiated lease," of not otherwise specified in the sublease.

- **"No need to legislate, just arbitrate."** Instead of creating a new law that alters existing contracts, the disgruntled lessors should just use the rights and remedies in the contract – arbitration, or inexpensive mediation, which has been offered by the lessor.
- **Let's call a spade a spade"** Given the legal problems with this bill, I respectfully request that this Judiciary and Government Operations Committee **hold this bill**. The measure is intended to interfere with the ongoing lease negotiations for existing lease contracts with one lessor. The "amended" intent and purpose is a "pretext" (alleged reason, ploy, ruse, red herring, bogus), which states: "it is important to support local employers and small businesses in these difficult economic times.....there is a need to alleviate the economic consequences of allowing unfair and unreasonable rent increases for these properties until the local economy improves." As noted above, this bill is meant to affect the lease negotiations with one lessor. If that alleged purpose were true, shouldn't the legislature be trying to help all of the existing business leases in the state? If the alleged purpose is to help lessees "until the local economy improves," where is the sunset date or sunset provisions in the bill?

SB 764, SD2. The key provisions of SB 764, SD2, are described as follows:

- **Amendments by the Senate Committee on Commerce and Consumer Protection (CPN).** The CPN amended this measure to an SD1 version, by:
  (1) Amending section one to "accurately reflect the purpose and intent of this measure" – in truth, the CPN Committee is attempting to **"cover-over,"** by changing the original unconstitutional purpose and intent to another perpetual purpose and intent, which is also unconstitutional;
  (2) Removing the provision relating to the assignment, transfer, or encumbrance of leasehold property;
  (3) Removing the provision limiting the improvements to structures on leasehold property that may be required of lessees; and
  (4) Making technical, nonsubstantive changes for the purpose of clarity and accuracy in the language of this measure.

- **Key provisions of SD 764, SD2: Changes to contract terms of existing leases and existing subleases.** The proposed SB 764, SD2 applies to any commercial or industrial lease, and would mandate changes favorable to the lessee and detrimental to the lessor and sublessee, with respect to certain terms and conditions of the original lease and sublease agreement between parties, including, among other things:

  - Creates new terms and conditions in existing lease contract terms which provide for the calculations of renegotiation of "fair and reasonable annual rent" – - the new law would replace the existing contract terms with a new definitions and legal requirements for determination of lease rent. Requires that all leases existing or entered into on after July 1, 2009, that includes a renegotiation clause that renegotiates rent on a "fair and reasonable annual rent" be construed to mean that a fair and reasonable rent is a requirement and that such a determination take into account the uses, intensity,

subsurface and surface characteristics, and neighborhood of the leased site on the renegotiation date; and

- Creates new terms and conditions in existing sublease contract terms, by providing that, unless otherwise specified in the sublease, sublessees shall be charged their pro rata share of the renegotiated lease.

- **Amendments by the Senate Committee on Judiciary and Government Operations (JGO).** JGO amended this measure to the current SD2 version by changing the effective date to July 1, 2050, to encourage further discussions on this matter. SSCR 782

MY OBJECTIONS TO SB 764, SD2. I believe that the current version of SB 764 SD2 would result in the legislature changing the terms in existing leases and subleases for the clear benefit of lessees and to the detriment of lessors and sublessees. I am **opposed to SB 764 SD2,** based on the following:

- **"Putting lipstick on a pig."** Any judge or appellate court will review this legislation and ask – "Why did the bill start out with a 'geographic proximity' purpose and intent, then in a SD2, the purpose and intent changes radically to 'economic viability' – while the key lease renegotiation provisions remain identical?"

- **Senate Bill 764 SD2 violates the Contracts Clause (Article I, Section 10) of the United States Constitution ("U.S. Constitution").** The proposed bill would change the terms of existing leases, which have already been negotiated and agreed to by the lessor and lessee and would also change the terms and conditions of existing subleases. This bill is a brazen attempt to have the legislature change contractual remedies and obligations, to the detriment of all lessors and subtenants of commercial and industrial properties, and to the benefit of all lessees.

  The Hawaii State Department of the Attorney General (Attorney General) has opined that such legislation, which would change the terms and conditions of existing lease contract terms, is illegal. We believe that if challenged in court, the provisions of this measure, would fail to meet the legal test to determine whether a statute is constitutional under the Contracts Clause, as set forth in the Hawaii Supreme Court case of Applications of Herrick & Irish, 82 Haw. 329, 922 P.2d 942 (1996) and quoted by the Attorney General in its prior opinions relating to other bills which have attempted to alter existing lease terms to benefit lessees:

  > "In deciding whether a state law has violated the federal constitutional prohibition against impairments of contracts, U.S. Const., art I, § 10, cl.1, I must assay the following three criteria:
  >
  > 1) Whether the state law operated as a substantial impairment of a contractual relationship;
  > 2) Whether the state law was designed to promote a significant and legitimate public purpose; and
  > 3) Whether the state law was a reasonable and narrowly-drawn means of promoting the significant and legitimate public purpose."

This Bill **substantially impairs the contractual relationship** between the lessor and lessee, because it changes the original deal between the lessor and lessee by mandating a new definition for renegotiation of the lease, which is favorable to the lessee and objectionable to the lessor.

The proposed law is **not designed to promote a significant and legitimate public purpose.** First, there is **no significant statewide problem** to be addressed by this measure. The written testimony in support of this measure proves that it is based on **a dispute between one lessor and several lessees.**

Second, there is **no legitimate public purpose**. **The purpose stated in SD2, is a pretext, ploy, ruse and red herring.** It is very important to note that the key provisions in the original SB 764 and the SD2 are identical. However, the "purpose" changes radically - it appears that the CPN Committee attempted to "fix" the purpose and intent language in a SD2, by changing it completely.

- **Old purpose: "Geographic proximity."** The original public purpose of SB 764 SD2 was to change lease provisions which were "burdensome" and "so onerous as to force these businesses to relocate to rural areas away from the urban centers...Thus maintaining close geographic ties between small businesses and the communities they serve is a public purpose that requires legislative support."
- **Amended purpose in SB 764 SD2: "Economic viability."** Now, however, to justify the exact same changes in lease renegotiation definitions, the "amended purpose" in SD2 is that "it is in the public interest that its citizens remain employed, that businesses continue to operate and pay wages and taxes, and that financial failures be reduced."

The proposed law is **not a reasonable and narrowly drawn means of promoting a significant and legitimate public purpose**. The proposed bill is an attempt to resolve a dispute between one lessor and a few lessees in favor of the lessees, based on a state-wide law changing the renegotiation terms of existing leases and also changing and adding new terms of existing subleases, by providing that, unless not allowed under the lease, sublessees shall be automatically charged their pro rata share of the renegotiated lease.

- **Comparable legislation, which altered lease terms to the benefit of lessees and to the detriment of lessors, has been found to be unconstitutional by the Attorney General.** Over the past several years, legislation has been introduced with the recurring theme of legislatively altering the terms and conditions of existing leases to the benefit of lessees and to the detriment of lessors:

  - In 2008, HB 1075 proposed alterations of existing lease contracts to favor the lessee, however, the Senate Economic Development and Tourism Committee (EDT) held the bill. EDT later placed the contents of HB 1075 into HB 2040, SD2, however that bill was held in Conference Committee.
  - In 2007, SB 1252 and SB 1619, proposed alterations of existing lease contract to favor the lessee;

- In 2006, SB 2043, would have imposed a surcharge tax on the value of improvements to real property subject to reversion in a lease of commercial or industrial property;
- In 2000, SB 873 SD 1, .D 2 also attempted to alter existing lease contract terms to the detriment of lessors and to the benefit of lessees by proposing to alter existing lease terms to require a lessor to purchase a lessee's improvements at the expiration of the lease term. The Department of Attorney General opined that SB 873, SD 1, HD 2 violated the Contracts Clause (Article I, Section 10) of the U.S. Constitution as follows: "SB 873, as presently worded, will substantially impair existing leases without furthering any apparent public purpose... [It is] unlikely that SB 873 will be found to be a 'reasonable and narrowly-drawn means of promoting... [a] Significant and legitimate public purpose." Governor Cayetano relied on the Attorney General's opinion, and vetoed SB 873, SD 1, HD 1.
- In 2001, in response to HB 1131, HD 1, yet another bill, which proposed to alter existing lease, contracts to favor lessees, the Attorney General again reaffirmed its opinion that the proposed bill violated the Contracts Clause of the U.S. Constitution.
- In 1987, in the Hawaii Supreme Court case of Anthony v. Kualoa Ranch, 69 Haw. 112, 736 P.2d 55 (1987). The Court ruled that a statute requiring a lessor to purchase a lessee's improvements at the expiration of the lease term violated the Contracts Clause. The Court observed that: "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, without relation to the purposes of the leasehold conversion act; without the limitations as to leaseholds subject thereto contained in the conversion provisions; not in the exercise of the eminent domain power; but simply for the purpose of doing equity, as the legislature saw it. If there is any meaning at all to the contract clause, 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."

➢ **It is bad public policy to enact a statewide law to address a private dispute between one lessor and a group of lessees, and it is also bad policy to change the terms and conditions of existing contracts to favor one party to a contract.** The testimony submitted by proponents proves that SB 764 SD2 is based on complaints of a few lessees against **one lessor**. This situation should not warrant a new statewide law which changes the terms and conditions of existing leases and subleases of commercial and industrial properties. Prior to approving such legislation, this Committee should investigate the following issues:

- It is my understanding from the proponents of this bill, **that the proposed new State law is meant to address the problems of a few lessees with one lessor,** relating to the lease renegotiation clause in their leases;
- Prior to enacting statewide legislation, it is important to determine **just how many lessees are encountering the alleged problems, which have given rise to this statewide legislation?**

- Prior to enacting statewide legislation, it is also important to **determine whether the proponents of the bill are small businesses or "master lessees," who hold a master lease and sublease to other businesses?**
- The proposed bill is yet another brazen attempt to favor lessees - it infringes on a lessor's ability to enter into and renegotiate a lease and it creates a new law which would give master lessees the new legal right to automatically pass-on any increase in lease rent to subtenants, unless otherwise specified in the lease.

➢ **"No need to legislate – just Arbitrate." "It could just take one!"** Instead of pursuing a new statewide law to change existing lease contracts, the lessees should utilize the Arbitration alternative, which is available under their existing lease contracts, or through Mediation offered by the lessor. One major lessee, or a group of similarly situated lessees could share the costs on one arbitration or mediation. If the lessees' definition of "fair and reasonable" annual rent is legally justified and prevails in arbitration or mediation, it would avoid the need for statewide legislation.

Under the law, a lease is a contract between two parties entered into at their own free will; the terms and conditions of the lease are agreed to in their entirety when the lease is executed; the lessee and lessor may seek amendments or modifications to the lease terms and conditions as long as both parties agree. If there is a dispute regarding the lease terms, usually **either party may seek resolution through arbitration, mediation, or the courts**.

- The proponents of this bill have admitted that the existing leases include an arbitration clause regarding any disputes, which could be used to resolve the existing issue regarding what is a "fair and reasonable" annual rent.
- The lessor who is the purported target of this legislation confirmed that they have resolved other lease renegotiations with most of their lessees, and have offered mediation to other lessees who wish to renegotiate their annual rent;
- The proponents also stated that appraisal experts assisted in drafting the proposed new definition of "fair and reasonable" annual rent, and that their experts were confident that the lessees would prevail in arbitration;
- The proponents cited the costs of mediation or arbitration as a reason they are pursuing statewide legislation, however, **the lessees could all jointly contribute funding toward the first arbitration or mediations, which could set the standard and criteria for all future lease renegotiations.**
- Based on the confidence of the proponents and their experts - it would seem that if the lessees definition of "fair and reasonable" annual rent prevails in the first couple of cases which go to mediation or arbitration, those results would arguably set a precedent for all of the other lease renegotiations - - so no further mediations or arbitrations would be necessary!

CONCLUSION. The intent and application of SB 764 SD2 are unconstitutional, profoundly anti-business and bad public policy, and therefore I respectfully request that **SB 764, SD2 be held in this Committee**.

Thank you for the opportunity to express my **opposition to SB 764, SD2**.

Noelani Cobb-Adams
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March 17, 2009

House Committee on Economic Revitalization, Business & Military Affairs
Hearing Date: Tuesday, March 17, 2009, at 7:30 a.m. in CR 312

Testimony in Opposition to SB 764 SD2: Relating to Real Property
(Alteration of provisions in long-term commercial and industrial ground leases)

Honorable Chair Angus L.K. McKelvey, Honorable Vice-Chair Isaac W. Choy and Members of the Economic Revitalization, Business & Military Affairs Committee:

My name is Noelani Cobb-Adams. I am a small private landowner. I am writing to state my **opposition** to SB 764 SD2: Relating to Real Property because it would have a huge detrimental impact on a piece of property my family has owned for generations.

I understand that this measure was proposed by lessees who are having trouble negotiating their leases with one lessor. I remain optimistic that further negotiations, arbitration and mediation can resolve such differences and result in renegotiated leases which can be accepted by both parties. Nonetheless, I respectfully **opposes SB 764, SD2,** which:

- changes existing commercial and industrial ground leases by mandating new terms and conditions for the renegotiation of rent with the lessor, and
- changes existing commercial and industrial subleases by giving the master ground lessees the statutory right to automatically pass on any pro rata rent increases to sublessees, if not otherwise specified in the sublease, and denies the subtenants an opportunity to negotiate a fair and reasonable rent with the master lessee.

My objections to SB 764, SD2, can be summarized as follows:

- SB 764, SD2 is an unconstitutional violation of the Contracts clause of the United States Constitution. You cannot 'fix' an unconstitutional bill by trying to change the 'purpose and intent' section of the bill.
- Even in tough economic times, it is not good public policy to pass a state-wide law because of a dispute between one lessor and a few lessees.
- "It is unfair and unconstitutional to change the terms of existing contracts to favor one party." The Attorney General has issued prior opinions finding that such alterations in the terms of existing leases are unconstitutional.

- Why does the proposed bill provide that negotiations between lessors and lessees must use a new definition of "fair and reasonable annual rent," but at the same time the bill also denies subtenants the opportunity to negotiate a fair and reasonable rent, by mandating that "sublessees shall be charged their pro rata share of the renegotiated lease," of not otherwise specified in the sublease.
- Instead of creating a new law that alters existing contracts, the disgruntled lessors should just use the rights and remedies in the contract - arbitration, or inexpensive mediation, which has been offered by the lessor.
- Given the legal problems with this bill, we respectfully request that this Judiciary and Government Operations Committee **hold this bill.** The measure is intended to interfere with the ongoing lease negotiations for existing lease contracts with one lessor. The "amended" intent and purpose is a "pretext" (alleged reason, ploy, ruse, red herring, bogus), which states: ".....it is important to support local employers and small businesses in these difficult economic times.....there is a need to alleviate the economic consequences of allowing unfair and unreasonable rent increases for these properties until the local economy improves." As noted above, this bill is meant to affect the lease negotiations with one lessor. If that alleged purpose were true, shouldn't the legislature be trying to help all of the existing business leases in the state? If the alleged purpose is to help lessees "until the local economy improves," where is the sunset date or sunset provisions in the bill?

SB 764, SD2. The key provisions of SB 764, SD2, are described as follows:

- **Amendments by the Senate Committee on Commerce and Consumer Protection (CPN).** The CPN amended this measure to an SD1 version, by:
  (1) Amending section one to "accurately reflect the purpose and intent of this measure" - in truth, the CPN Committee **"tried to mask,"** by changing the original unconstitutional purpose and intent to another pretextual purpose and intent which is also unconstitutional;
  (2) Removing the provision relating to the assignment, transfer, or encumbrance of leasehold property;
  (3) Removing the provision limiting the improvements to structures on leasehold property that may be required of lessees; and
  (4) Making technical, nonsubstantive changes for the purpose of clarity and accuracy in the language of this measure.

- **Key provisions of SH 764, SD2: Changes to contract terms of existing leases and existing subleases.** The proposed SB 764, SD2 applies to any commercial or industrial lease, and would mandate changes favorable to the lessee and detrimental to the lessor and sublessee, with respect to certain terms and conditions of the original lease and sublease agreement between parties, including, among other things:

- Creates new terms and conditions in existing lease contract terms which provide for the calculations of renegotiation of "fair and reasonable annual rent" - - the new law would replace the existing contract terms with a new definitions and legal requirements for determination of lease rent. Requires that all leases existing or entered into on after July 1, 2009, that includes a renegotiation clause that renegotiates rent on a "fair and reasonable annual rent" be construed to mean that a fair and reasonable rent is a requirement and that such a determination take into account the uses, intensity, subsurface and surface characteristics, and neighborhood of the leased site on the renegotiation date; and

- Creates new terms and conditions in existing sublease contract terms, by providing that, unless otherwise specified in the sublease, sublessees shall be charged their pro rata share of the renegotiated lease.

- **Amendments by the Senate Committee on Judiciary and Government Operations (JGO).** JGO amended this measure to the current SD2 version by changing the effective date to July 1, 2050, to encourage further discussions on this matter. SSCR 782

MY OBJECTIONS TO SB 764, SD2 . We believe that the current version of SB 764 SD2 would result in the legislature changing the terms in existing leases and subleases for the clear benefit of lessees and to the detriment of lessors and sublessees. LURF is **opposed to SB 764 SD2,** based on the following:

- **"Putting lipstick on a pig."** Any judge or appellate court will review this legislation and ask - "Why did the bill start out with a 'geographic proximity' purpose and intent, then in a SD2, the purpose and intent changes radically to 'economic viability' - while the key lease renegotiation provisions remain identical?"

- **Senate Bill 764 SD2 violates the Contracts Clause (Article I, Section 10) of the United States Constitution ("U.S. Constitution").** The proposed bill would change the terms of existing leases, which have already been negotiated and agreed to by the lessor and lessee and would also change the terms and conditions of existing subleases. This bill is a brazen attempt to have the legislature change contractual remedies and obligations, to the detriment of all lessors and subtenants of commercial and industrial properties, and to the benefit of all lessees.

  The Hawaii State Department of the Attorney General (Attorney General) has opined that such legislation, which would change the terms and conditions of existing lease contract terms, is illegal. We believe that if challenged in court, the provisions of this measure, would fail to meet the legal test to determine whether a statute is constitutional under the Contracts Clause, as set forth in the Hawaii Supreme Court case of Applications of Herrick & Irish, 82 Haw. 329, 922 P.2d 942 (1996) and quoted by the Attorney General in its

prior opinions relating to other bills which have attempted to alter existing lease terms to benefit lessees:

> "In deciding whether a state law has violated the federal constitutional prohibition against impairments of contracts, U.S. Const., art I, § 10, cl.1, we must assay the following three criteria:
>
> 1) whether the state law operated as a substantial impairment of a contractual relationship;
> 2) whether the state law was designed to promote a significant and legitimate public purpose; and
> 3) whether the state law was a reasonable and narrowly-drawn means of promoting the significant and legitimate public purpose."

This Bill **substantially impairs the contractual relationship** between the lessor and lessee, because it changes the original deal between the lessor and lessee by mandating a new definition for renegotiation of the lease, which is favorable to the lessee and objectionable to the lessor.

The proposed law is **not designed to promote a significant and legitimate public purpose.** First, there is **no significant statewide problem** to be addressed by this measure. The written testimony in support of this measure proves that it is based on **a dispute between one lessor and several lessees.**

Second, there is **no legitimate public purpose**. **The purpose stated in SD2, is a pretext, ploy, ruse and red herring.** It is very important to note that the key provisions in the original SB 764 and the SD2 are identical. However, the "purpose" changes radically - it appears that the CPN Committee attempted to "fix" the purpose and intent language in a SD2, by changing it completely.

- **Old purpose: "Geographic proximity."** The original public purpose of SB 764 SD2 was to change lease provisions which were "burdensome" and "so onerous as to force these businesses to relocate to rural areas away from the urban centers...Thus maintaining close geographic ties between small businesses and the communities they serve is a public purpose that requires legislative support."
- **Amended purpose in SB 764 SD2: "Economic viability."** Now, however, to justify the exact same changes in lease renegotiation definitions, the "amended purpose" in SD2 is that "it is in the public interest that its citizens remain employed, that businesses continue to operate and pay wages and taxes, and that financial failures be reduced."

The proposed law is **not a reasonable and narrowly-drawn means of promoting a significant and legitimate public purpose**. The proposed bill is an attempt to resolve a dispute between one lessor and a few lessees in favor of the lessees, based on a state-wide law changing the

renegotiation terms of existing leases and also changing and adding new terms of existing subleases, by providing that, unless not allowed under the lease, sublessees shall be automatically charged their pro rata share of the renegotiated lease.

- **Comparable legislation which altered lease terms to the benefit of lessees and to the detriment of lessors has been found to be unconstitutional by the Attorney General.** Over the past several years, legislation has been introduced with the recurring theme of legislatively altering the terms and conditions of existing leases to the benefit of lessees and to the detriment of lessors.
-
- **It is bad public policy to enact a state-wide law to address a private dispute between <u>one lessor</u> and a group of lessees, and it is also bad policy to change the terms and conditions of existing contracts to favor one party to a contract.** The testimony submitted by proponents proves that SB 764 SD2 is based on complaints of a few lessees against **<u>one lessor</u>**. This situation should not warrant a new state-wide law which changes the terms and conditions of existing leases <u>and</u> subleases of commercial and industrial properties. Prior to approving such legislation, this Committee should investigate the following issues:
  - It is my understanding from the proponents of this bill, that **the proposed new State law is meant to address the problems of a <u>few lessees</u> with <u>one lessor</u>,** relating to the lease renegotiation clause in their leases;
  - Prior to enacting state-wide legislation, it is important to determine **just how many lessees are encountering the alleged problems which have given rise to this state-wide legislation?**
  - Prior to enacting state-wide legislation, it is also important to **determine whether the proponents of the bill are small businesses or "master lessees," who hold a master lease and sublease to other businesses?**
  - The proposed bill is yet another brazen attempt to <u>favor lessees</u> - it infringes on a lessor's ability to enter into and renegotiate a lease <u>and</u> it creates a new law which would give master lessees the new legal right to automatically pass-on any increase in lease rent to subtenants, unless otherwise specified in the lease.

- **"No need to Legislate – just Arbitrate." "It could just take one!"** Instead of pursuing a new state-wide law to change existing lease contracts, the lessees should utilize the Arbitration alternative which is available under their existing lease contracts, or through Mediation offered by the lessor. One major lessee, or a group of similarly situated lessees could share the costs on one arbitration or mediation. If the lessees' definition of "fair and reasonable" annual rent is legally justified and prevails in arbitration or mediation, it would <u>avoid the need</u> for <u>statewide legislation</u>.

  Under the law, a lease is a contract between two parties entered into at their own free will; the terms and conditions of the lease are agreed to in their entirety when the lease is executed; the lessee and lessor may seek

amendments or modifications to the lease terms and conditions as long as both parties agree. If there is a dispute regarding the lease terms, usually **either party may seek resolution through arbitration, mediation, or the courts.**

- The proponents of this bill have admitted that the existing leases include an arbitration clause regarding any disputes, which could be used to resolve the existing issue regarding what is a "fair and reasonable" annual rent.
- The lessor who is the purported target of this legislation confirmed that they have resolved other lease renegotiations with most of their lessees, and have offered mediation to other lessees who wish to renegotiate their annual rent;
- The proponents also stated that appraisal experts assisted in drafting the proposed new definition of "fair and reasonable" annual rent, and that their experts were confident that the lessees would prevail in arbitration;
- The proponents cited the costs of mediation or arbitration as a reason they are pursuing statewide legislation, however, **the lessees could all jointly contribute funding toward the first arbitration or mediations, which could set the standard and criteria for all future lease renegotiations.**
- Based on the confidence of the proponents and their experts - it would seem that if the lessees definition of "fair and reasonable" annual rent prevails in the first couple of cases which go to mediation or arbitration, those results would arguably set a precedent for all of the other lease renegotiations - - so no further mediations or arbitrations would be necessary!

CONCLUSION. The intent and application of SB 764 SD2 are unconstitutional, profoundly anti-business and bad public policy, and therefore I respectfully request that **SB 764, SD2 be held in this Committee.**

Thank you for the opportunity to express our **opposition to SB 764, SD2.**

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March 17, 2009

House Committee on Economic Revitalization, Business & Military Affairs
Hearing Date: Tuesday, March 17, 2009, at 7:30 a.m. in CR 312

Testimony in Opposition to SB 764 SD2: Relating to Real Property
(Alteration of provisions in long-term
commercial and industrial ground leases)

Honorable Chair Angus L.K. McKelvey, Honorable Vice-Chair Isaac W. Choy and Members of the Economic Revitalization, Business & Military Affairs Committee:

My name is Liesel Santimer, and I am a small private landowner. I am writing to state my opposition to SB 764 SD2: Relating to Real Property because it would have a huge detrimental impact on a piece of property our family has owned for generations.

I understand that this measure was proposed by lessees who are having trouble negotiating their leases with one lessor. While I remain hopeful that further negotiations, arbitration and mediation can resolve such differences and result in renegotiated leases which can be accepted by both parties, I respectfully **oppose SB 764, SD2,** which:

- changes existing commercial and industrial ground leases by mandating new terms and conditions for the renegotiation of rent with the lessor, and
- changes existing commercial and industrial subleases by giving the master ground lessees the statutory right to automatically pass on any pro rata rent increases to sublessees, if not otherwise specified in the sublease, and denies the subtenants an opportunity to negotiate a fair and reasonable rent with the master lessee.

My objections to SB 764, SD2, can be summarized as follows:

- SB 764, SD2 is an unconstitutional violation of the Contracts clause of the United States Constitution. You cannot 'fix' an unconstitutional bill by trying to change the 'purpose and intent' section of the bill.
- **"It is not good public policy to pass a state-wide law because of a dispute between one lessor and a few lessees.",** even in tough economic times. How many state-wide lessees other than those being targeted by this proposed bill will be negatively affected? Does a dispute with one lessor warrant a new state-wide law purporting to safe Hawaii's economy?
- **"It is unfair and unconstitutional to change the terms of existing contracts to favor one party**." The Attorney General has issued prior opinions finding that such alterations in the terms of existing leases are unconstitutional.
- **"Changes via the proposed bill should cut both ways"** - Why does that proposed bill provide that negotiations between lessors and lessees must use a new definition of "fair and reasonable annual rent," but at the same time the bill also denies subtenants the opportunity to negotiate a fair and reasonable rent, by mandating that "sublessees shall

be charged their pro rata share of the renegotiated lease," of not otherwise specified in the sublease.

- **"No need to legislate, just arbitrate."** Instead of creating a new law that alters existing contracts, the disgruntled lessors should just use the rights and remedies in the contract – arbitration, or inexpensive mediation, which has been offered by the lessor.
- **"Let's call a spade a spade."** Given the legal problems with bill, I respectfully request that this Judiciary and Government Operations Committee hold this bill. The measure is intended to interfere with the ongoing lease negotiations for existing lease contracts with one lessor. The "amended" intent and purpose is a "pretext" (alleged reason, ploy, ruse, red herring, bogus), which states: "...it is important to support local employers and small businesses in these difficult economic times... there is a need to alleviate the economic consequences of allowing unfair and unreasonable rent increases for these properties until the local economic improves." As noted above, this bill is meant to affect the lease negotiations with one lessor. If that alleged purpose were true, shouldn't the legislature be trying to help all of the existing businesses leases in the state? If the alleged purpose is to help lessees "until the local economy improves," where is the sunset date or sunset provisions in the bill?

SB 764, SD2. The key provisions of SB 764, SD2, are described as follows:

- **Amendments by the Senate Committee on Commerce and Consumer Protection (CPN).** The CPN amended this measure to an SD1 version, by:
  (1) Amending section one to "accurately reflect the purpose and intent of this measure" – in truth, the CPN Committee is attempting to **"cover-over,"** by changing the original unconstitutional purpose and intent to another pretextual purpose and intent which is also unconstitutional;
  (2) Removing the provision relating to the assignment, transfer, or encumbrance of leasehold property;
  (3) Removing the provision limiting the improvements to structures on leasehold property that may be required of lessees; and
  (4) Making technical, nonsubstantive changes for the purpose of clarity and accuracy in the language of this measure.

- **Key provisions of SH 764, SD2: Changes to contract terms of existing leases and existing subleases.** The proposed SB 764, SD2 applies to any commercial or industrial lease, and would mandate changes favorable to the lessee and detrimental to the lessor and sublessee, with respect to certain terms and conditions of the original lease and sublease agreement between parties, including, among other things:

  - Creates new terms and conditions in existing lease contract terms which provide for the calculations of renegotiation of "fair and reasonable annual rent" – - the new law would replace the existing contract terms with a new definitions and legal requirements for determination of lease rent. Requires that all leases existing or entered into on after July 1, 2009, that includes a renegotiation clause that renegotiates rent on a "fair and reasonable annual rent" be construed to mean that a fair and reasonable rent is a requirement and that such a determination take into account the uses, intensity, subsurface and surface characteristics, and neighborhood of the leased site on the renegotiation date; and

  - Creates new terms and conditions in existing sublease contract terms, by providing that, unless otherwise specified in the sublease, sublessees shall be charged their pro rata share of the renegotiated lease.

- **Amendments by the Senate Committee on Judiciary and Government Operations (JGO).** JGO amended this measure to the current SD2 version by changing the effective date to July 1, 2050, to encourage further discussions on this matter. SSCR 782

MY OBJECTIONS TO SB 764, SD2. I believe that the current version of SB 764 SD2 would result in the legislature changing the terms in existing leases and subleases for the clear benefit of lessees and to the detriment of lessors and sublessees. I am **opposed to SB 764 SD2,** based on the following:

- **"Putting lipstick on a pig."** Any judge or appellate court will review this legislation and ask – "Why did the bill start out with a 'geographic proximity' purpose and intent, then in a SD2, the purpose and intent changes radically to 'economic viability' – while the key lease renegotiation provisions remain identical?"

- **Senate Bill 764 SD2 violates the Contracts Clause (Article I, Section 10) of the United States Constitution ("U.S. Constitution").** The proposed bill would change the terms of existing leases, which have already been negotiated and agreed to by the lessor and lessee and would also change the terms and conditions of existing subleases. This bill is a brazen attempt to have the legislature change contractual remedies and obligations, to the detriment of all lessors and subtenants of commercial and industrial properties, and to the benefit of all lessees.

  The Hawaii State Department of the Attorney General (Attorney General) has opined that such legislation, which would change the terms and conditions of existing lease contract terms, is illegal. I believe that if challenged in court, the provisions of this measure, would fail to meet the legal test to determine whether a statute is constitutional under the Contracts Clause, as set forth in the Hawaii Supreme Court case of Applications of Herrick & Irish, 82 Haw. 329, 922 P.2d 942 (1996) and quoted by the Attorney General in its prior opinions relating to other bills which have attempted to alter existing lease terms to benefit lessees:

  > "In deciding whether a state law has violated the federal constitutional prohibition against impairments of contracts, U.S. Const., art I, § 10, cl.1, I must assay the following three criteria:
  >
  > 1) whether the state law operated as a substantial impairment of a contractual relationship;
  > 2) whether the state law was designed to promote a significant and legitimate public purpose; and
  > 3) whether the state law was a reasonable and narrowly-drawn means of promoting the significant and legitimate public purpose."

  This Bill **substantially impairs the contractual relationship** between the lessor and lessee, because it changes the original deal between the lessor and lessee by mandating a new definition for renegotiation of the lease, which is favorable to the lessee and objectionable to the lessor.

  The proposed law is **not designed to promote a significant and legitimate public purpose.** First, there is **no significant statewide problem** to be addressed by this measure. The written testimony in support of this measure proves that it is based on **a dispute between one lessor and several lessees.**

Second, there is **no legitimate public purpose**. **The purpose stated in SD2, is a pretext, ploy, ruse and red herring.** It is very important to note that the key provisions in the original SB 764 and the SD2 are identical. However, the "purpose" changes radically - it appears that the CPN Committee attempted to "fix" the purpose and intent language in a SD2, by changing it completely.

- **Old purpose: "Geographic proximity."** The original public purpose of SB 764 SD2 was to change lease provisions which were "burdensome" and "so onerous as to force these businesses to relocate to rural areas away from the urban centers…Thus maintaining close geographic ties between small businesses and the communities they serve is a public purpose that requires legislative support."
- **Amended purpose in SB 764 SD2: "Economic viability."** Now, however, to justify the exact same changes in lease renegotiation definitions, the "amended purpose" in SD2 is that "it is in the public interest that its citizens remain employed, that businesses continue to operate and pay wages and taxes, and that financial failures be reduced."

The proposed law is **not a reasonable and narrowly-drawn means of promoting a significant and legitimate public purpose**. The proposed bill is an attempt to resolve a dispute between one lessor and a few lessees in favor of the lessees, based on a state-wide law changing the renegotiation terms of existing leases and also changing and adding new terms of existing subleases, by providing that, unless not allowed under the lease, sublessees shall be automatically charged their pro rata share of the renegotiated lease.

- **It is bad public policy to enact a state-wide law to address a private dispute between one lessor and a group of lessees, and it is also bad policy to change the terms and conditions of existing contracts to favor one party to a contract.** The testimony submitted by proponents proves that SB 764 SD2 is based on complaints of a few lessees against **one lessor**. This situation should not warrant a new state-wide law which changes the terms and conditions of existing leases and subleases of commercial and industrial properties. Prior to approving such legislation, this Committee should investigate the following issues:
  - We have been informed by the proponents of this bill, that **the proposed new State law is meant to address the problems of a few lessees with one lessor,** relating to the lease renegotiation clause in their leases;
  - Prior to enacting state-wide legislation, it is important to determine **just how many lessees are encountering the alleged problems which have given rise to this state-wide legislation?**
  - Prior to enacting state-wide legislation, it is also important to **determine whether the proponents of the bill are small businesses or "master lessees," who hold a master lease and sublease to other businesses?**
  - The proposed bill is yet another brazen attempt to favor lessees - it infringes on a lessor's ability to enter into and renegotiate a lease and it creates a new law which would give master lessees the new legal right to automatically pass-on any increase in lease rent to subtenants, unless otherwise specified in the lease.

- **"No need to Legislate – just Arbitrate." "It could just take one!"** Instead of pursuing a new state-wide law to change existing lease contracts, the lessees should utilize the Arbitration alternative which is available under their existing lease contracts, or through Mediation offered by the lessor. One major lessee, or a group of similarly situated lessees could share the costs on one arbitration or mediation. If the lessees' definition of "fair and

reasonable" annual rent is legally justified and prevails in arbitration or mediation, it would avoid the need for statewide legislation.

Under the law, a lease is a contract between two parties entered into at their own free will; the terms and conditions of the lease are agreed to in their entirety when the lease is executed; the lessee and lessor may seek amendments or modifications to the lease terms and conditions as long as both parties agree. If there is a dispute regarding the lease terms, usually **either party may seek resolution through arbitration, mediation, or the courts**.

- The proponents of this bill have admitted that the existing leases include an arbitration clause regarding any disputes, which could be used to resolve the existing issue regarding what is a "fair and reasonable" annual rent.
- The lessor who is the purported target of this legislation confirmed that they have resolved other lease renegotiations with most of their lessees, and have offered mediation to other lessees who wish to renegotiate their annual rent;
- The proponents also stated that appraisal experts assisted in drafting the proposed new definition of "fair and reasonable" annual rent, and that their experts were confident that the lessees would prevail in arbitration;
- The proponents cited the costs of mediation or arbitration as a reason they are pursuing statewide legislation, however, **the lessees could all jointly contribute funding toward the first arbitration or mediations, which could set the standard and criteria for all future lease renegotiations**.
- Based on the confidence of the proponents and their experts - it would seem that if the lessees definition of "fair and reasonable" annual rent prevails in the first couple of cases which go to mediation or arbitration, those results would arguably set a precedent for all of the other lease renegotiations - - so no further mediations or arbitrations would be necessary!

CONCLUSION. The intent and application of SB 764 SD2 are unconstitutional, profoundly anti-business and bad public policy, and therefore I respectfully request that **SB 764, SD2 be held in this Committee**.

Mahalo,

Liesel Santimer
Private Land Owner

MOANI M. ZABLAN
3330 Keanu Street
Honolulu, Hawaii 96816

March 15, 2009

House Committee on Economic Revitalization, Business & Military Affairs
Hearing Date: Tuesday, March 17, 2009, at 7:30 a.m. in CR 312

Testimony in Opposition to SB 764 SD2: Relating to Real Property
(Alteration of provisions in long-term
commercial and industrial ground leases)

Honorable Chair Angus L. K. McKelvey, Honorable Vice-Chair Isaac W. Choy and Members of the Economic Revitalization, Business & Military Affairs Committee:

My name is Moani M. Zablan and I am a small private landowner. I also represent my two children's interests in that same piece of property which has been in our family for generations. **I am writing to state my opposition to SB 764 SD2: Relating to Real Property.** This particular piece of legislation, if enacted as "law", would have a huge negative impact on our jointly held property.

We recently went through 'Rent renegotiation' and the "Arbitration" process, re: our property. We started the rent renegotiation process before the term was to expire, but we, the 'landowners', and the 'lessees' did not agree on the "fair market value". We then invoked "arbitration", a provision in our lease designed to settle differences in setting the "fair market value" for rent for a specific term. After a year and a half of negotiations & arbitration, the "fair market value" was finally established, and a year and a half later, we are finally collecting our rent. Although the whole process was lengthy and expensive, it was what we, as "landowners", and they, the "lessees", agreed to upon execution of the contract, the Lease. The Lease was agreed to by both parties and I do not believe any other party should be able to enter into this agreement without mutual consent of both parties, and change the intent or terms of the agreement.

It is my understanding that, this portion of the Bill was proposed to help specific lessees who are having trouble negotiating their leases with one lessor. I hope the two parties can come to some sort of resolution, but I find it difficult to understand why these lessees may be given the "relief" of not abiding by a contract that they entered into by way of this Bill. I believe this portion of the Bill is unconstitutional because it is contrary to a mutual agreement set forth by willing parties and changes the intent and content of that agreement. Again, both parties willingly entered into a contract that they should both abide by. I did what I agreed to do in the contract/lease re: renegotiation, and the same should hold true for others in the same situation.

After going through our 'rent renegotiation'/'arbitration', I am aware of how large the spectrum of "fair market value" is and wonder how much more complicated establishing the "fair market value' will be should this bill become law. Who will actually set the "fair market value" and by what valuation method? How will this Bill be integrated into my lease? Does this mean that I will have to incorporate new language into my existing lease and who will pay for this legal expense? Our lease calls for amendments to the document to be agreed upon by "both" parties. The State of Hawaii is not a party to the lease. If passed, will the State then become a party to the lease and who or which department will be added as an additional party and in what capacity? What would their responsibilities be and how would they be made accountable to **all** lessors and lessees? When there is a 'fair market value' established, what will be the role of the State, will there be a State Agency that will only do appraisals of all leases within the State of Hawaii for purposes of 'rent renegotiation'? Would there be any recourse for differences of opinions? Am I, as a taxpayer of the State of Hawaii, going to have to pay for this, in addition to the expenses of my ongoing lease?

Our State has a multitude of problems. We have a huge deficit to overcome, we need help with our social services & our education system. There is widespread unemployment, homelessness, crime due to drugs, theft and other criminal activities. In the face of our current situation, I do not believe we should be enacting legislation that is intended to help a small segment of our population when a-lot of others things that serve more or all the population in our State need our undivided attention.

As I stated in the beginning, **I AM OPPOSED TO SB 764 SD2** and respectfully request that **SB 764 SD2 be held in this Committee.**

Thank you for the opportunity to express my **opposition to SB 764 SD2.**

Respectfully,

Moani M. Zablan