

JAN 23 2009

A BILL FOR AN ACT

RELATING TO REAL PROPERTY.

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF HAWAII:

1 SECTION 1. The legislature finds that certain elements of
2 inequity exist in the relationship of fee simple owners of
3 commercial and industrial properties and holders of long-term
4 leasehold interest in those properties who undertake the leases
5 for the purpose of developing, improving, operating, and
6 subletting the properties. These inequities accrue to the
7 detriment of Hawaii's business and economic development and harm
8 Hawaii's working and retired taxpayers. Uncomplicated and fair
9 legislative remedies exist that can obviate these inequities.

10 The purpose of this Act is to implement certain conditions
11 governing long-term leases of commercial and industrial
12 properties.

13 SECTION 2. Chapter 519, Hawaii Revised Statutes, is
14 amended by adding a new section to be appropriately designated
15 and to read as follows:

16 "§519- Leases of commercial and industrial property.

17 (a) Anything to the contrary notwithstanding, any lease of
18 commercial or industrial leasehold property where the lessor is



1 the owner, directly or indirectly, of fifty thousand square feet
2 or more of commercial or industrial leasehold property in the
3 State shall be subject to the following terms and conditions:

4 (1) Whenever a lease condition requires that a lessee
5 obtain the approval of the lessor for the assignment,
6 transfer, or encumbrance of the leasehold property,
7 the approval of the lessor may not be unreasonably
8 withheld;

9 (2) Where a lessee is required by a lease with less than
10 thirty years remaining on its term to make major and
11 substantial improvements to any structures on the
12 leasehold property or to any infrastructure supporting
13 the leasehold property, the requirement to the lessee
14 shall be limited to making reasonable maintenance and
15 repair work to satisfy federal, state, and county
16 laws, ordinances, and code requirements to ensure the
17 public's health, safety, and welfare, and the lessee
18 shall not be required to make substantial new
19 improvements to infrastructure or structures;

20 (3) Where a lease provides for the reversion of any
21 improvements on the leasehold property at the
22 termination of the lease, the improvements shall be



1 returned subject to reasonable wear and tear that may
2 have resulted from the use of the improvements over
3 the full term of the lease;

4 (4) Where a lease provides for periodic step-ups in lease
5 rent over the term of the lease, the increases in
6 lease rent shall be determined, in part, on a
7 determination of the financial feasibility of the rent
8 increase in relation to the current use of the
9 leasehold property; and

10 (5) In the event that a lessor determines to sell the
11 leasehold interest and all improvements on the
12 leasehold property to the lessee, the lessor shall be
13 entitled to exclude from gross income subject to the
14 tax imposed by chapter 235, in the year of the sale,
15 any gain the lessor realizes from the sale.

16 (b) For purposes of this section, "commercial or
17 industrial leasehold property" means any real property:

18 (1) Situated in the State;

19 (2) Zoned by a county for commercial, industrial, or mixed
20 use; and

21 (3) That is subject to a lease with an unexpired term of
22 twenty years or more."



1 SECTION 3. Section 235-7, Hawaii Revised Statutes, is
2 amended by amending subsection (a) to read as follows:

3 "(a) There shall be excluded from gross income, adjusted
4 gross income, and taxable income:

5 (1) Income not subject to taxation by the State under the
6 Constitution and laws of the United States;

7 (2) Rights, benefits, and other income exempted from
8 taxation by section 88-91, having to do with the state
9 retirement system, and the rights, benefits, and other
10 income, comparable to the rights, benefits, and other
11 income exempted by section 88-91, under any other
12 public retirement system;

13 (3) Any compensation received in the form of a pension for
14 past services;

15 (4) Compensation paid to a patient affected with Hansen's
16 disease employed by the State or the United States in
17 any hospital, settlement, or place for the treatment
18 of Hansen's disease;

19 (5) Except as otherwise expressly provided, payments made
20 by the United States or this State, under an act of
21 Congress or a law of this State, which by express
22 provision or administrative regulation or



1 interpretation are exempt from both the normal and
2 surtaxes of the United States, even though not so
3 exempted by the Internal Revenue Code itself;

4 (6) Any income expressly exempted or excluded from the
5 measure of the tax imposed by this chapter by any
6 other law of the State, it being the intent of this
7 chapter not to repeal or supersede any express
8 exemption or exclusion;

9 (7) Income received by each member of the reserve
10 components of the Army, Navy, Air Force, Marine Corps,
11 or Coast Guard of the United States of America, and
12 the Hawaii national guard as compensation for
13 performance of duty, equivalent to pay received for
14 forty-eight drills (equivalent of twelve weekends) and
15 fifteen days of annual duty, at an:

16 (A) E-1 pay grade after eight years of service;
17 provided that this subparagraph shall apply to
18 taxable years beginning after December 31, 2004;

19 (B) E-2 pay grade after eight years of service;
20 provided that this subparagraph shall apply to
21 taxable years beginning after December 31, 2005;



- 1 (C) E-3 pay grade after eight years of service;
- 2 provided that this subparagraph shall apply to
- 3 taxable years beginning after December 31, 2006;
- 4 (D) E-4 pay grade after eight years of service;
- 5 provided that this subparagraph shall apply to
- 6 taxable years beginning after December 31, 2007;
- 7 and
- 8 (E) E-5 pay grade after eight years of service;
- 9 provided that this subparagraph shall apply to
- 10 taxable years beginning after December 31, 2008;
- 11 (8) Income derived from the operation of ships or aircraft
- 12 if the income is exempt under the Internal Revenue
- 13 Code pursuant to the provisions of an income tax
- 14 treaty or agreement entered into by and between the
- 15 United States and a foreign country; provided that the
- 16 tax laws of the local governments of that country
- 17 reciprocally exempt from the application of all of
- 18 their net income taxes, the income derived from the
- 19 operation of ships or aircraft that are documented or
- 20 registered under the laws of the United States;



- 1 (9) The value of legal services provided by a prepaid
2 legal service plan to a taxpayer, the taxpayer's
3 spouse, and the taxpayer's dependents;
- 4 (10) Amounts paid, directly or indirectly, by a prepaid
5 legal service plan to a taxpayer as payment or
6 reimbursement for the provision of legal services to
7 the taxpayer, the taxpayer's spouse, and the
8 taxpayer's dependents;
- 9 (11) Contributions by an employer to a prepaid legal
10 service plan for compensation (through insurance or
11 otherwise) to the employer's employees for the costs
12 of legal services incurred by the employer's
13 employees, their spouses, and their dependents;
- 14 (12) Amounts received in the form of a monthly surcharge by
15 a utility acting on behalf of an affected utility
16 under section 269-16.3 shall not be gross income,
17 adjusted gross income, or taxable income for the
18 acting utility under this chapter. Any amounts
19 retained by the acting utility for collection or other
20 costs shall not be included in this exemption; [and]
- 21 (13) One hundred per cent of the gain realized by a fee
22 simple owner from the sale of a leased fee interest in



1 units within a condominium project, cooperative
 2 project, or planned unit development to the
 3 association of owners under chapter 514A or 514B, or
 4 the residential cooperative corporation of the
 5 leasehold units.

6 For purposes of this paragraph:

7 "Fee simple owner" shall have the same meaning as
 8 provided under section 516-1; provided that it shall
 9 include legal and equitable owners;

10 "Legal and equitable owner", and "leased fee
 11 interest" shall have the same meanings as provided
 12 under section 516-1; and

13 "Condominium project" and "cooperative project"
 14 shall have the same meanings as provided under section
 15 514C-1; [and]

16 (14) One hundred per cent of the gain realized by a lessor
 17 where the lessor is the owner, directly or indirectly,
 18 of fifty thousand square feet or more of commercial or
 19 industrial leasehold property in the State, upon the
 20 sale of the leasehold interest and all improvements on
 21 the leasehold property to the lessee in the year of
 22 sale.



1 For purposes of this paragraph:
2 "Commercial or industrial leasehold property"
3 shall have the same meaning as provided in section
4 519- ; and
5 "Lessor" and "lessee" shall have the same
6 meanings as provided under section 516-1."

7 SECTION 4. This Act does not affect rights and duties that
8 matured, penalties that were incurred, and proceedings that were
9 begun, before its effective date.

10 SECTION 5. New statutory material is underscored.

11 SECTION 6. This Act shall take effect on July 1, 2009;
12 provided that section 3 shall apply to taxable years beginning
13 after December 31, 2009.

14

INTRODUCED BY: Enzarne Chun Alalano
Norman Sakamp

Report Title:

Real Property; Leasehold

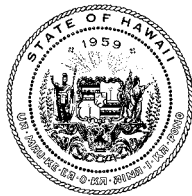
Description:

Mandates certain conditions applicable to certain commercial and industrial leases. Exempts certain sales of fee interest to lessee from state income tax.



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**SENATE COMMITTEE ON COMMERCE & CONSUMER PROTECTION
TESTIMONY REGARDING SB 770
RELATING TO REAL PROPERTY**

TESTIFIER: KURT KAWAFUCHI, DIRECTOR OF TAXATION (OR DESIGNEE)

DATE: FEBRUARY 17, 2009

TIME: 8:30AM

ROOM: 229

This bill proposes to exempt the gain realized on the sale by the lessor of commercial or industrial property to the lessee, including improvements, from the income tax.

The Department of Taxation **opposes the tax provision contained in this bill.** The Department takes no position on the remaining provisions of this legislation.

SUBJECT TO ABUSE—The Department is concerned that the bill as written has the potential for abuse. The bill does not provide how long the lease must exist before the sale to qualify for this provision or provide any restrictions on sales to related parties. The Department is concerned that as written, the bill would allow a lessor to lease property to a related party for a month and then sell the property to the related party without having to pay any tax on the appreciation in the property.

IMPROVEMENTS ARE DEPRECIABLE—Also, the Committee must be cognizant of the fact that the lessee's improvements to leased land are subject to the allowance of depreciation and that the taxpayer/lessee will not be without tax benefit for improving commercial real property. And, in most commercial leases, the lessee is entitled to return of any improved property, subject to negotiation.

The revenue impact with respect to this bill is estimated to be approximately \$16.2 million per year beginning in FY 2011.

**SB 770
RELATING TO REAL PROPERTY**

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

FEBRUARY 17, 2009

Chair Baker and Members of the Senate Committee on Commerce & Consumer Protection:

I am Paul Oshiro, testifying on behalf of Alexander & Baldwin, Inc. (A&B) on SB 770, "A BILL FOR AN ACT RELATING TO REAL PROPERTY." We respectfully oppose this bill.

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

As presently drafted, the bill appears to also apply to current leases in effect prior to the effective date of this bill. We understand that changing contractual obligations in existing leases may give rise to questions of constitutionality.

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

Thank you for the opportunity to testify.