

STAND. COM. REP. NO.

864

Honolulu, Hawaii

March 6, 2009

RE: H.B. No. 1604

Honorable Calvin K.Y. Say  
Speaker, House of Representatives  
Twenty-Fifth State Legislature  
Regular Session of 2009  
State of Hawaii

Sir:

Your Committee on Finance, to which was referred H.B. No. 1604 entitled:

"A BILL FOR AN ACT RELATING TO REAL PROPERTY,"

begs leave to report as follows:

The purpose of this bill is to establish a tax on the value of improvements, surrendered to a lessor by a lessee without compensation to the lessee, at the expiration of a long-term lease on non-residential real property.

Alexander & Baldwin, Inc., testified in opposition to this bill. The Tax Foundation of Hawaii, Kamehameha Schools, and Hawaii Association of REALTORS® provided comments.

As affirmed by the record of votes of the members of your Committee on Finance that is attached to this report, your Committee is in accord with the intent and purpose of H.B. No. 1604 and recommends that it pass Third Reading.

Respectfully submitted on  
behalf of the members of the  
Committee on Finance,

  
MARCUS R. OSHIRO, Chair

HB1604 HSCR FIN HMS 2009-2699







1 "Lessee" means any person to whom land is leased or  
2 subleased under a long-term lease and the lessee's heirs,  
3 successors, legal representatives, and assigns.

4 "Lessor" means any person who leases or subleases land to  
5 another under a long-term lease and the lessor's heirs,  
6 successors, legal representatives, and assigns.

7 "Long-term lease" means a conveyance of land or an interest  
8 in land by a fee simple owner, as lessor, or by a lessee or  
9 sublessee, as sublessor, to any person in consideration of a  
10 return of rent or other compensation or remuneration for a term,  
11 measured from the initial date of the conveyance, of twenty  
12 years or more, including any periods for which the lease may be  
13 extended or renewed at the option of the lessee.

14 "Non-residential real property parcel" means a parcel of  
15 real property that is not used for apartment or residential  
16 purposes, provided that:

17 (1) "Apartment or residential purposes" shall not include  
18 hotel, resort, transient accommodation, or time share  
19 use; and

20 (2) If the parcel is a mixed use parcel, only that portion  
21 of the parcel not used for apartment or residential



1           purposes, as determined by the relevant county, shall  
2           be subject to the tax of this chapter.

3           § -3 Tax on improvements surrendered to a lessor without  
4 compensation to the lessee. (a) There is established a tax on  
5 the value of improvements on a non-residential real property  
6 parcel that are surrendered by the lessee to the lessor at the  
7 expiration of a long-term lease if:

8           (1) The lessee, without financial or capital assistance  
9           from the lessor, constructed or installed the  
10           improvements during the period the lessee held the  
11           long-term lease to the non-residential real property  
12           parcel; and

13           (2) The lessee did not receive compensation equaling the  
14           value of the surrendered improvements at the time of  
15           surrender.

16           (b) Except as provided under subsection (c), the tax shall  
17 be levied at a rate of           per cent of the value of the  
18 improvements surrendered to the lessor. The value of the  
19 improvements shall be the same as established by the county for  
20 real property tax purposes for the taxable year in which the  
21 lease expires.

1 (c) If the lessor has paid compensation to the lessee for  
2 surrendered improvements, but in an amount less than the value  
3 of the improvements, then the tax shall be levied on the  
4 difference between the total value of the improvements and the  
5 compensation paid.

6 § -4 Administration. (a) Each county shall administer  
7 the tax imposed by this chapter. The county shall establish the  
8 deadline for the payment of the tax, which shall not be later  
9 than ninety days after expiration of the relevant long-term  
10 lease.

11 (b) To establish the value of improvements on a  
12 non-residential parcel, a county may use the gross value of the  
13 improvements as assessed by mass appraisal for real property tax  
14 purposes and without reduction for exemptions or appeals. The  
15 county shall not be required to prepare an individual appraisal  
16 for each non-residential parcel with improvements taxable under  
17 this chapter.

18 § -5 Enforcement. Each county shall enforce the  
19 collection of the tax imposed by this chapter. The county may  
20 attach a lien on the land, surrendered improvements, or both, of  
21 the real property that was the subject of the long-term



1 non-residential lease. The county may bring an action in the  
2 circuit court to collect any delinquent tax.

3       **§ -6 Appeal.** Each county shall establish a process for  
4 the administrative appeal by a lessor of the tax imposed by this  
5 chapter. The administrative appeal process shall not need to be  
6 in conformance with chapter 91.

7       Each county, upon exhaustion of the administrative appeal  
8 process, shall provide for judicial appeal by either the county  
9 or lessor to the circuit court.

10       **§ -7 Ordinance or rule.** Each county shall establish the  
11 administration, enforcement, and appeal provisions by ordinance  
12 or rule.

13       **§ -8 Revenue distribution.** Revenues collected from the  
14 tax imposed by this chapter shall be distributed as follows:

- 15       (1) The county that collected the revenues shall retain an  
16 amount equaling the cost of collection; and
- 17       (2) Of the remainder, the county shall retain fifty per  
18 cent and transmit to the State the other fifty per  
19 cent, which shall be deposited into the state general  
20 fund."

21       SECTION 3. The tax established under chapter           , Hawaii  
22 Revised Statutes, shall be imposed on a lessor who receives



1 surrendered improvements upon the expiration of a long-term  
2 non-residential lease from the effective date of this Act, even  
3 if the term of the subject long-term lease commenced before that  
4 date.

5 SECTION 4. This Act shall take effect on January 1, 2010.

6

INTRODUCED BY:

Calvin M. Day

JAN 28 2009



**Report Title:**

Taxation; Leasehold Improvements

**Description:**

Imposes a tax upon the value of improvements surrendered to a lessor by a lessee, without compensation to the lessee, upon the expiration of a long-term non-residential lease.



March 18, 2009

**The Honorable Rosalyn H. Baker, Chair**  
Senate Committee on Commerce  
and Consumer Protection  
State Capitol, Room 229  
Honolulu, Hawaii 96813

**RE: H.B. 1604, Relating to Real Property**

**HEARING DATE: Thursday, March 19, 2009 at 9:00 a.m.**

Aloha Chair Baker and Members of the Committee:

I am Craig Hirai, a member of the Subcommittee on Taxation and Finance of the Government Affairs Committee of the Hawai'i Association of REALTORS® (“HAR”), here to testify on behalf of the HAR and its 9,600 members in Hawai'i. HAR **opposes** H.B. 1604, Relating to Real Property, which imposes a tax upon the value of improvements surrendered to a lessor by a lessee, without compensation to the lessee, upon the expiration of a long-term non-residential lease.

HAR would note that a lessor could possibly avoid the tax (and the cost of demolition) by having the lessee demolish or remove the improvements prior to the termination of a lease to non-residential real property. If the lessor elects to keep the improvements, the lessor would presumably have made a decision that the improvements (less the possible cost of future demolition) were worth more than the tax.

A possible consequence of this bill could be the **premature demolition or removal of improvements with a remaining useful life** on non-residential properties awaiting redevelopment which may be delayed and/or planned for a number of years in the future.

HAR looks forward to working with our state lawmakers in building better communities by supporting quality growth, seeking sustainable economies and housing opportunities, embracing the cultural and environmental qualities we cherish, and protecting the rights of property owners.

Mahalo for the opportunity to testify.



## KAMEHAMEHA SCHOOLS

Written Testimony to the Senate Committee  
on Commerce and Consumer Protection

By Paul A. Quintiliani  
Vice President of Endowment, Kamehameha Schools

Hearing Date: Thursday, March 19, 2009  
9:00 a.m., Conference Room 229

March 19, 2009

To: Senator Rosalyn Baker, Chair  
Senator David Ige, Vice Chair  
Members of the Committee on Commerce & Consumer Protection

**RE: House Bill No. 1604 Relating to Real Property**

Kamehameha Schools submits the following comments regarding H.B. No. 1604 (the "Bill"). The Bill sets out to tax the value of improvements surrendered to a lessor by a lessee without compensation to the lessee, upon the expiration of a long-term non-residential lease.

As a lessor of residential, commercial and industrial real property, Kamehameha Schools objects to this Bill because, as written, it would likely hurt both lessors and lessees and could negatively impact our communities.

1. When surrendered, many properties that revert to lessors are in disrepair and require major capital improvements to bring into code compliance. This bill does not recognize the severe burdens and risks placed on lessors when such properties are surrendered, including the need to make expenditures on repairs, demolition and environmental remediation, which may be difficult to impossible to collect from lessees. A tax on the value of the improvements without a corresponding deduction or credit to lessor for its "losses" on these reversionary events would be unfair.

567 South King Street • Honolulu, Hawai'i 96813-3036 • Phone 808-523-6200

*Founded and Endowed by the Legacy of Princess Bernice Pauahi Bishop*

2. This bill amends the contractual relationships between parties to a lease by statutorily changing the expected allocation of benefits and costs established in the original contract. For example, a lessor may agree to lower near term rent in exchange for the expectation of receiving a well maintained property at the lease's termination. If the lessor is now required to pay additional compensation to the lessee for such improvements constructed, the lessee will enjoy an unintended windfall profit.
3. Passage of this bill will have the unintended consequence of altering future contractual arrangements whereby a) lessors may be disinclined to provide early periods of low rent and/or b) may cause lessors to re-evaluate future transactions and ultimately pass tax consequences on to lessees.
4. The determination of value is equated to the tax assessed value. This is not always a fair representation of the value of the improvements and does not take into account the cost to the landowner to clear or remove these improvements if the property is deemed unusable.
5. The administrative procedures established in this bill are cumbersome.
6. According to the study by the Legislative Reference Bureau – Report No. 5, 2003 “Real Property Leases” (the “2003 Report”), “there is no indication at this time of a broad based compelling need for the Legislature to pass legislation to mandate the alteration of existing lease agreements.” 2003 Report at 24.

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

**HB 1604  
RELATING TO REAL PROPERTY**

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

**MARCH 19, 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 HB 1604, "A BILL FOR AN ACT RELATING TO REAL PROPERTY." We respectfully oppose this bill.

This bill establishes a tax on the value of improvements on non-residential real property that are constructed or installed by a lessee and surrendered to a lessor without compensation to the lessee at the expiration of a long term lease. 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 are negotiated and executed. It is envisioned that the imposition of a new tax on the value of the improvements made by a lessee at the end of the lease term may result in the exclusion of certain lease conditions that may be mutually agreeable and meet 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 commitment by the lessee to construct or install improvements on the property and/or to maintain and improve the property may no longer be feasible under the provisions of this bill.

Based on the aforementioned, we respectfully request that this bill be held in Committee. Thank you for the opportunity to testify.



Testimony to the Senate Committee on Commerce and Consumer Protection

Cameron W. Nekota  
Development Project Manager  
Kapolei Property Development LLC

March 19, 2009

House Bill 1604 Relating to Real Property

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

My name is Cameron Nekota, testifying on behalf of Kapolei Property Development LLC (“KPD”), an affiliate of the James Campbell Company LLC (formerly the Estate of James Campbell) on HB 1604 Relating to Real Property. We respectfully oppose this bill.

The purpose of HB 1604 is to establish a tax on the value of improvements, surrendered by a lessee to a lessor, without compensation to the lessee, at the expiration of a long-term lease of non-residential real property. KPD has serious concerns regarding the impact of HB 1604 on existing contracts between lessors and lessees. A lease is defined as an “agreement under which owner gives up possession and use of his property for valuable consideration for definite term.” As the definition of lease provides, its terms and conditions represent an agreement or meeting of the minds between the parties and are not unilaterally imposed. As with many terms and conditions in leases, the final disposition of tenant improvements are negotiated by the lessor and lessee at the time the contract is signed. In many instances, lessees are provided lower lease rents in early years to account for the cost of tenant improvements. Therefore, we believe the current proposal unconstitutionally impacts existing contractual relationships and respectfully request the Committee on Commerce and Consumer Protection hold HB 1604.

# TAXBILLSERVICE

126 Queen Street, Suite 304

TAX FOUNDATION OF HAWAII

Honolulu, Hawaii 96813 Tel. 536-4587

SUBJECT: MISCELLANEOUS, Tax on surrendered leasehold improvements

BILL NUMBER: SB 766; HB 1604 (Identical)

INTRODUCED BY: SB by Chun Oakland, Sakamoto and 2 Democrats; HB by Say

BRIEF SUMMARY: Adds a new chapter to the HRS to establish a new tax on the value of improvements on nonresidential real property that are constructed or installed by a lessee and surrendered to a lessor, without compensation to the lessee when the long-term lease expires if: (1) the lessee, without financial or capital assistance from the lessor, constructed or installed the improvements; and (2) the lessee did not receive compensation equaling the value of the surrendered improvements at the time of surrender.

The tax shall be \_\_\_\_% of the value of improvements surrendered to the lessor. The value of the improvements shall be the same as established by the county for real property tax purposes for the tax year in which the lease expires. If the lessor has paid any compensation to the lessee for surrendered improvements, but in an amount less than the value of the improvements, then the tax shall be levied on the difference between the total value of the improvements and the compensation paid.

Each county shall administer the tax, establish the deadline for the payment of the tax within 90 days of the expiration of the lease, and enforce the collection of the tax. Requires each county to establish a process for appeals by the lessor. The revenues collected from the tax shall be distributed to: (1) the county that collected the revenues to retain an amount equaling the cost of collection; and (2) of the remainder, the county shall retain 50% and transmit the other 50% to the state for deposit into the general fund.

The tax shall be imposed on a lessor who receives the surrendered improvements upon the expiration of a long-term non-residential lease from the effective date of this act, even if the term of the long-term lease commenced before that date.

EFFECTIVE DATE: January 1, 2010

STAFF COMMENTS: This measure proposes to levy a tax on the owner of leasehold property equal to \_\_\_\_% of the value of the improvements on the leasehold property at the termination of the lease under the conditions delineated and provides that the revenues generated from this surcharge shall be used for public education and affordable housing in the state.

Obviously, there is some lessee who is not happy that such improvements have to be surrendered upon the termination of the lease without any compensation. However, it should be noted that the lessee knew full well that someday the lease would come to an end and that there was no promise of compensation for improvements. Further, it should be acknowledged that leasing, as opposed to outright purchasing, gives the lessee an economic and financial gain in not having to sink as much capital into acquiring the site, capital that can then be used for equipment, the improvements, and payroll. Thus, the lessee had a choice

between leasing the real property or attempting to find a site which was available in fee.

It should be noted that the 1978 Constitutional Convention, with the ratification of the electorate, turned all powers governing the real property tax over to the counties. Therefore, the enactment of this measure will have no effect on the taxation of real property in the state. It is also questionable whether or not the state can change the terms and conditions of an existing contract by imposing a tax where one was never a consideration in the lease of the property.

It should be noted that this proposal may bring a halt to the leasing of real property depending on how confiscatory the tax would be. Why would a fee owner of real property want to make his property available for use when there is the possible exposure to tax at the termination of the lease for which there is no compensation? If that is the result, it will become even more expensive to establish a new business or build multi-family housing in Hawaii as there is the prospect that the fee owner will have to pay this tax. As noted above, the lessee knew and understood the terms of the lease when it was entered into including the prospect that the improvements may have to be forsaken at the end of the lease with no compensation.

Digested 2/6/09

**From:** ManyaVogrg@aol.com  
**Sent:** Tuesday, March 17, 2009 9:05 AM  
**To:** CPN Testimony  
**Subject:** In Opposition to HB 1598 HD1 & HB 1604

**COMMITTEE ON COMMERCE AND CONSUMER PROTECTION**  
**Senator Rosalyn H. Baker, Chair**

**Senator David Y. Ige, Vice Chair**

**DATE:** Thursday, Mar. 19th, 2009  
**TIME:** 9 a.m.  
**PLACE:** Conference Room 229

**Honorable Chairs and Members of the Committees:**

**Re: [HB 1598](#) HD 1  
RELATING TO TAXATION.**

**Taxes a lessor of real property for capital improvements made by a lessee upon the termination of a lease. FIN**

**&**

**Re: [HB 1604](#) ([HSCR864](#))  
RELATING TO REAL PROPERTY.**

**Imposes a tax upon the value of improvements surrendered to a lessor by a lessee, without compensation to the lessee, upon the expiration of a long-term non-residential lease. CPN, WAM**

~~~~~  
**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 our private property under the guise of tax revenues. The "improvements", when they revert back to the landowners, may be a detriment, as the landowner may not wish the same use on their property. Furthermore our leases are all different and most, if not all, of our families were not compensated for our homes and "improvements" on our properties ... which were demolished in order for the lessee to build their "improvements." It is an integral part of our lease, as to whether the "improvements" are to be removed by the lessee or surrendered at the end of the term. You would be interfering with our contracts by altering these terms.**

**We trust that you will hold this legislation in order to prevent the taking of private property under the guise of public purpose.**

**Thank you very much!**

**Manya Vogrig**

**T. Phyllis Zerbe**

2877 Kalakaua Ave. #1205  
Honolulu, HI 96815  
Phone: 922-6934

1434 Punahou St.  
Honolulu, HI 96822  
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)**

\*\*\*\*\*

A Good Credit Score is 700 or Above. See yours in just 2 easy steps!

([http://pr.atwola.com/promoclk/100126575x1219850974x1201371016/aol?redir=http:%2F%2Fwww.fr  
eecreditreport.com%2Fpm%2Fdefault.aspx%3Fsc%3D668072%26hmpglD%3D62%26bcd%3DMarc  
hfooterNO62](http://pr.atwola.com/promoclk/100126575x1219850974x1201371016/aol?redir=http:%2F%2Fwww.fr<br/>eecreditreport.com%2Fpm%2Fdefault.aspx%3Fsc%3D668072%26hmpglD%3D62%26bcd%3DMarc<br/>hfooterNO62))