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March 31, 2009

Committee on Economic Revitalization, Business, & Military Affairs

Rep. Jon Riki Karamatsu, Chair
Rep. Ken Ito, Vice-Chair

TESTIMONY IN SUPPORT OF SB 764, SB 2, HB 1

DATE: Tuesday, March 31, 2009
TIME: 3:30 PM
PLACE: Room 312

Dear Representatives Karamatsu and Ito 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

Testimony on S.B. 764, SD2, HD1
Relating to Real Property
House Committee on Judiciary
Keali`i Lopez, President and CEO of ʻŌlelo Community Television
Tuesday, March 31, 2009

Chair Karamatsu, Vice-Chair Ito and members of the House Judiciary Committee. Thank you for the opportunity to provide written comments on S.B. 764 S.D.2., H.D.1. ʻŌlelo supports this Bill. We are a local non-profit organization located in Mapunapuna. The building that we own is located on a parcel of land that we lease. We have 26 years remaining on our lease and could soon see our lease rent increase substantially when we renegotiate terms later this month.

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

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

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

Because of this, we ask that you support that the term of "fair and reasonable" in commercial ground leases that are renegotiated have these equity provisions. In summary, I ask for your support of SB764. Mahalo.

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Via Capitol Website

March 30, 2009

House Committee on Judiciary
Hearing Date: Tuesday, March 31, 2009, at 4:00 p.m. in CR 309

Testimony in Opposition to SB 764 SD2, HD1: Relating to Real Property (Alteration of provisions in long-term commercial and industrial ground leases)

Honorable Chair Jon Riki Karamatsu, Vice Chair Ken Ito and House Committee on Judiciary Members:

My name is Dave Arakawa, and I am the Executive Director of the Land Use Research Foundation of Hawaii (LURF), a private, non-profit research and trade association whose members include major Hawaii landowners, developers and a utility company. One of LURF's missions is to advocate for reasonable, rational and equitable land use planning, legislation and regulations that encourage well-planned economic growth and development, while safeguarding Hawaii's significant natural and cultural resources and public health and safety.

LURF understands that this measure was proposed by lessees who claim they are having trouble negotiating their leases with one lessor - HRPT. We and hope that further negotiations, arbitration and mediation can resolve such differences and result in renegotiated leases which can be accepted by both parties. Nonetheless, LURF respectfully **opposes SB 764, SD2 HD1,** which:

- Is "special legislation," which is targeted against a single landowner – HRPT;
- changes the previously negotiated and agreed-upon terms of existing commercial and industrial ground leases by mandating new terms and conditions for the renegotiation of rent with the lessor, which are for the sole benefit of a small group of lessees; and
- changes existing commercial and industrial subleases by giving the master ground lessees of properties owned by HRPT 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 lessees of HRPT's properties.

LURF's objections to SB 764, SD2, HD1 can be summarized as follows:

- **"Stabilizing Hawaii's economy by maintaining close geographic ties between small businesses and the communities they serve" is not a justifiable valid public purpose which would justify altering the terms of existing lease contracts.** SB 764, SD2, HD1 is an unconstitutional violation of the Contracts clause of the United States Constitution. In an effort to try to save the bill from being held unconstitutional, the purpose and intent section of the bill justifies the bill based on "stabilizing Hawaii's economy by assuring geographic proximity between small businesses and their customers." There is no credible evidence that changing the terms of contracts will assure that small businesses stay close to their customers, or that small businesses will fail if they move to another location – this unconstitutional law **c**annot be "fixed" by merely stating an illogical "purpose and intent" for the bill, without credible facts supporting it.

- **"SB 764, SD2, HD1 is a "special law," which violates Article XI, section 5 of the Hawaii Constitution.** SB 764 is **"special legislation,"** which is prohibited by the Hawaii constitution, because it applies to one particular lease renegotiation provision in the leases of just one particular lessor - HRPT, discriminates against one particular lessor - HRPT, and operates in favor of certain lessees, by granting them a special or exclusive privilege. The proponents of this bill have admitted that this legislation is aimed at only one lessor – HRPT; we also understand that the proponents have reportedly testified that the bill is being used as "leverage" in their lease negotiations with HRPT; and there is no testimony or evidence regarding any other lessors in the state who utilize the lease renegotiation language which is the subject of this bill.

- **"It is also not good public policy to pass a state-wide 'special law' because of a dispute between one lessor and a few lessees."** How many state-wide lessees are affected? Does a dispute with one lessor warrant a new state-wide 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.

- **"What is good for the goose, should be good for the gander" "You can't have it 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," if not otherwise specified in the sublease.

- **"There is no need for this legislation – current lessees are going through the renegotiation process as provided in the existing contracts."** The written testimony shows that HRPT has successfully renegotiated a mutually acceptable rent rate in dozens of leases which have been up for renegotiation.

- **"Don't 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. The written testimony confirms that HRPT has always accepted lessees' requests for mediation.

- **"Cut the Shibai." "The buck stops here."** Given the legal problems with this bill, we respectfully request that this Committee **hold this bill**.
  - The measure is a **"special law"** which is intended to provide "leverage" in current contract negotiations with <u>one lessor</u>;
  - The proposed law <u>changes the terms of existing leases</u> and interferes with the ongoing lease negotiations for existing lease contracts with <u>one lessor</u>.
  - The purported intent and purpose, which is to "stabilize the State's economy," "during the recessionary period," by "preserving the proximity of small businesses to urban communities" **is a "pretext"** (alleged reason, ploy, ruse, red herring, bogus).
    - How many leases will this law effect? The law will only affect the leases with <u>one lessor – HRPT</u>. How will affecting only HRPT leases assure the proximity of small businesses to the urban communities they serve and stabilize the entire State's economy?
    - If that alleged purpose of supporting small businesses were really true, why does the law only apply to leases with <u>one lessor, HRPT</u>?
    - If the bill is trying to stabilize the economy by changing the terms of lease negotiations - shouldn't the law apply to the terms of <u>all</u> of the existing business leases in the state? Instead, this bill is meant to affect the lease negotiations with <u>only one lessor, HRPT</u>.
  - If the alleged purpose is to truly help lessees, "<u>especially during the recessionary period</u>"- - **Where are the <u>sunset dates</u> or <u>sunset provisions</u> in the bill?**

<u>SB 764, SD2, HD1</u>. This bill alters major terms of existing long-term commercial and industrial ground leases by mandating new standards for interpreting the terms "fair and reasonable rent" in contract renegotiations; alters major terms in existing subleases which provide for lessee's recovery of ground lease rent by mandating that subtenants be automatically charged their pro-rata share of the renegotiated rent without the opportunity for renegotiation with the master lessee The key provisions of SB 764, SD2, HD1 are described as follows:

- **Key provisions of SB 764, SD2, HD1: Changes to contract terms of existing leases and existing subleases.** The proposed SB 764, SD2, HD1 applies to any commercial or industrial lease, and would mandate <u>changes favorable to the lessee</u> 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 <u>existing lease contract terms</u> 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 SD2 version by changing the effective date to July 1, 2050, to encourage further discussions on this matter. SSCR 782.

- **Amendments by the House Committee on Water, Land and Ocean Resources (WLO).** WLO amended this measure by replacing its substance with that of H.B. No. 1593, which was reported out of the WLO Committee earlier this session. House Standing Committee Report 1225 note that "given the complex nature of real property lease negotiations and their concomitant impact on Hawaii's economy, your Committee respectfully requests the Committee on Judiciary, to which this bill is referred, take a fresh look at the standards for "fair and reasonable" as used in this bill, as well as examine the constitutional contract clause issues that it raises." As amended, this bill differs from the Senate Draft 2, in that the bill:
  1. Does not specify that the lessor of the real property to which this bill applies must hold an "aggregate" of 50,000 square feet or more of industrial and commercial property; and
  2. Takes effect upon its approval.

LURF's OBJECTIONS to Section 2 of SB 764 SD2, HD1 and. We believe that the Section 2 of the current version of SB 764 SD2, HD1 will 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, HD1** based on the following:

- **No justifiable public purpose**. There are no logical facts stated to justify this bill, and the stated purpose - "stabilizing Hawaii's economy by maintaining close geographic ties between small businesses and the communities they serve" is not a justifiable valid public purpose which would justify altering the terms of existing lease contracts.

- **Senate Bill 764 SD2, HD1 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.** The bill changes the original negotiated agreement 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 bill impairs the contractual relationship by, among other things:
  - Altering the process for determining the amount of rent to be paid by a lessee, which is an essential terms of the lease contract;
  - Seeking solely to reduce the amount of rent which lessees would be obligated to pay based on the renegotiation provisions in the existing contracts;
  - Mandating a new process and definitions for renegotiation of rent, which is contrary to the methods and interpretations previously followed by appraisers in prior rental renegotiations under the existing contracts;
  - Regulating an area of commerce – commercial and industrial leasing – that was not previously regulated by the state;

- 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, the bill **does not "advance broad societal interests,"** as it operates to the benefit of a few lessees and to the detriment of one lessor – HRPT;
  - Third, as stated above, there is **no legitimate public purpose**. **The purpose stated in SD2, HD1 – "to stabilize Hawaii's economy by maintaining geographic proximity between small businesses and their clients" - is a pretext, ploy, ruse and red herring.** There is no evidence that changing lease provisions relating to one lessor,

will stabilize Hawaii's economy; there is no evidence that changing the lease terms will result in small businesses staying in the same location; and if the legislature really wanted to help the economy – why doesn't the bill include retail or agricultural leases?

- Finally, there are **no facts or proof that the new law will succeed in achieving the stated purpose of the bill, or that it will avoid the problems described in the section 1 of the bill.** According to HRPT, close to fifty businesses have renegotiated their lease rent pursuant to the existing contractual terms, and there is not evidence that any of those business have suffered the problems which are listed in the bill (home foreclosures, bankruptcy filings, financial failures, more unemployment, and business closures), as a result of the new lease rent.

- 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, however, it is unreasonably broad – as it is a state-wide law, which changes the rent renegotiation terms of existing leases and also broadly changes all existing subleases, by adding new terms, 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 virtually identical 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 virtually identical 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 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, HD1 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, HD1 are unconstitutional, profoundly anti-business and bad public policy, and therefore we respectfully request that **SB 764, SD2, HD1 be held in this Committee**.

Thank you for the opportunity to express our **opposition to SB 764, SD2, HD1**.

TESTIMONY OF THE STATE ATTORNEY GENERAL
TWENTY-FIFTH LEGISLATURE, 2009

ON THE FOLLOWING MEASURE:
S.B. NO. 764, S.D. 2, H.D. 1, RELATING TO REAL PROPERTY.

BEFORE THE:
HOUSE COMMITTEE ON JUDICIARY

DATE: Tuesday, March 31, 2009 **TIME:** 4:00 PM

LOCATION: State Capitol, Room 309

TESTIFIER(S): Mark J. Bennett, Attorney General
or Shari Wong, Deputy Attorney General

Chair Karamatsu and Members of the Committee:

The Department of the Attorney General has concerns about this bill.

This bill appears to change the process for renegotiating the amount of rent during the term of an existing commercial or industrial lease, unless expressly stated otherwise in the lease. In addition, this bill proposes a new requirement, providing for how subtenants shall be charged, unless expressly stated otherwise in the lease. Legal concerns regarding state impairment of contracts are raised by the proposed language affecting existing leases.[1]

It is well established that a retroactive law in a constitutional sense is one that takes away or impairs vested rights acquired under existing laws or attaches a new obligation, imposes a new duty, or attaches a new disability with respect to transactions or considerations already concluded. Employees Retirement Sys. v. Chang, 42 Haw. 532, 535 (1958). Generally, retrospective laws are not favored and all laws will be construed as prospective unless retrospective application is clearly intended and expressly declared, or is

[1] The United States Constitution states, in part, that "[n]o state shall . . . pass any . . . Law impairing the Obligation of Contracts . . . ." U.S. Const., Art I, § 10, cl. 1. ("Contracts Clause")

necessarily implied from the language used. Clark v. Cassidy, 64 Haw. 74 (1981). This principle is particularly applicable where the statute or amendment involves substantive, as opposed to procedural, rights. Clark, 64 Haw. at 77; Dash v. Wayne, 700 F. Supp. 1056 (D. Haw. 1988).

With respect to the constitutional proscription against impairment of contracts, it is a fundamental principle that obligations of a contract cannot be impaired by subsequent passage of any law. Taylor v. Taylor, 537 P.2d 483, 486 (Mont. 1975); Pulos v. James, 302 N.E.2d 768, 775 (Ind. 1973). The obligation of a contract is impaired by a law that alters the contract's terms by creating new rights or imposing new conditions or different liabilities. Northern Pacific Railway v. Duluth, 208 U.S. 583, 590 (1908). "Any law which changes the . . . legal effect of the original parties, giving to one greater or the other a less interest or benefit in the contract, impairs its obligation." Kentucky Utilities Co. v. Carlisle Ice Co., 131 S.W.2d 499, 504 (1939). See also Anthony v. Kualoa Ranch, Inc., 69 Haw. 112, 119-24 (1987) (law, enacted after lease executed, that required lessors to pay, at the sole option of the lessees, for improvements built upon the leased premises in order to get the leased premises back, substantially impaired the contractual rights of the parties and was unconstitutional).

> The importance of protecting the obligation of contracts from all legislative action tending to its impairment has been emphasized by the Supreme Court of the United States. That high tribunal has stated that the inviolability for contracts and the duty to perform them, as made, are at the foundation of all well-ordered society that, to prevent the removal or disturbance of these foundations was one of the great objects for which the Constitution was framed, and that it is one of the highest duties of that court to take care that the prohibition should neither be evaded nor frittered away.

16A Am. Jur. 2d Constitutional Law § 694 (1979) (emphases added).

However, because states are vested with authority to safeguard the vital interests of their residents, the impairment clause is liberally construed and prohibits only unreasonable impairment. Id.; Energy

Reserves v. Kansas Power & Light, 459 U.S. 400, 409 (1983). Reasonableness is determined by whether the law addresses a legitimate end and whether the measures taken to reach that end are reasonable and appropriate. It is important to recognize that the power of a state to modify or affect the obligation of a contract under the state's protective powers is not without limit. "Yet the contract clause limits otherwise legitimate exercises of state legislative authority, and the existence of an important public interest is not always sufficient to overcome that limitation." United States Trust Co. v. New Jersey, 431 U.S. 1, 21 (1977). See also El Paso v. Simmons, 379 U.S. 497, 506-9 (1965).

As noted above, this bill appears to intrude upon renegotiations of lease rent by interjecting, unless otherwise stated in the lease, its construction of "fair and reasonable annual rent" in commercial or industrial leases to mean that "rent shall be fair and reasonable to both the lessor and the lessee to the lease." S.B. No. 764, S.D. 2, H.D. 1, page 4, lines 3-5. Unless otherwise stated in the lease, this bill also imposes a new requirement in such lease rent renegotiations that they include consideration of the "uses and intensity of use approved by the lessor, and the surface and subsurface characteristics of the site and the neighborhood on the renegotiation date." S.B. No. 764, S.D. 2, H.D. 1, page 4, lines 6-9. In addition, this bill proposes a new requirement, unless expressly stated otherwise in the commercial or industrial lease, providing for how subtenants shall be charged.

Despite the customary deference accorded to social and economic legislation, laws altering the rights and obligations of contracting parties must be reasonable and necessary for the public purpose for which they were enacted. Allied Structural Steel Co. Spannaus, 438 U.S. 234, 244 (1977), Applications of Herrick & Irish, 82 Haw. 329, 922 P.2d 942 (1996). While section 1 of this bill describes the need to strengthen and diversify Hawaii's economy, there is no evidence that this bill will achieve the stated purpose to stabilize the economy by addressing some of the burdensome provisions of existing commercial and

industrial leases. S.B. No. 764, S.D. 2, H.D. 1, page 3, lines 3-5. For example, this bill provides four factors in defining "commercial or industrial leasehold property." S.B. No. 764, S.D. 2, H.D. 1, page 4, lines 18-21, and page 5, lines 1-5. However, these four factors do not necessarily identify how they are linked to a benefit for the business tenants in Oahu's urban center, as opposed to those in the Ewa region or central Oahu, as stated in section 1 of the bill. S.B. No. 764, S.D. 2, H.D. 1, page 2, lines 1-21. A lessor in Kapolei could meet those four factors, thus owning property that falls within the definition "commercial or industrial leasehold property", and be subject to the requirements of this bill.

On the other hand, a lessor in Mapunapuna with fewer than fifty thousand square feet would not meet the fourth factor and not own property that falls within the definition of "commercial or industrial leasehold property", and thus not be subject to the requirements of this bill.

In addition, the third factor, regarding a lease with a term of ten years or more and an unexpired term of five years or more, could apply to various recent leases in the Ewa region or central Oahu, whereas section 1 of the bill appears to focus on urban communities which historically have housed small commercial or industrial businesses. S.B. No. 764, S.D. 2, H.D. 1, page 2, lines 15-17 ("In practical terms, consumers will find that the auto service center or the small retailer in Mapunapuna is no longer in business where the consumer lives or works.")

In summary, it is unclear how focusing the definition of "commercial or industrial leasehold property" on the nature of the lessor is sufficiently tailored to the bill's stated purpose of easing burdensome lease provisions on lessees. S.B. No. 764, S.D. 2, H.D. 1, page 3, lines 3-5.

Thus, we recommend that, before this bill is passed, the Legislature make appropriate findings to sufficiently demonstrate the nexus between the bill's purpose and its proposals. At this time, it is

unclear from the record how pervasive the alleged problem is, or the actual number of commercial and industrial leases affected by this bill, or how the bill's proposals actually benefit urban businesses. The government must use the least intrusive means to achieve its goals. It is not free to impose a drastic impairment when an evident and more moderate course would serve its purposes equally well. United States Trust Co. v. New Jersey, 431 U.S. at 31.

Legislation impairing commercial or industrial leases would be more defensible if based on articulated findings of need, demonstrated evidence that the proposed legislation will achieve the stated purpose, and explanation that no lesser remedy (such as arbitration, mediation, or litigation) is available. The bill's proposed definition of "commercial or industrial leasehold property" seems focused upon lessors and does not appear to be "a reasonable and narrowly-drawn means of promoting the significant and legitimate public purpose." Applications of Herrick & Irish, 82 Haw. 329, 340, 922 P.2d 942, 953. Consequently, it appears this bill may violate the Contracts Clause and be found unconstitutional.