



NATURAL ENERGY LABORATORY OF HAWAII AUTHORITY

An Authority of the State of Hawaii attached to the Department of Business, Economic Development & Tourism



**NATURAL ENERGY LABORATORY OF HAWAII AUTHORITY (NELHA)
BOARD OF DIRECTORS
MEETING MINUTES
Monday August 26, 2019
10:15 a.m.**

**NELHA Oceanview Conference Room
Hale Iako Building
73-970 Makako Bay Drive
Kailua-Kona Hawaii 96740**

Members

Linda Rosehill (Gov. Appointee - Chair)
William Mielcke (Gov Appointee – Vice-Chair)
Cyd Miyashiro (Gov. Appointee)
Alan Hilton (RAC-Chair)
Philip Bossert (RAC-Secretary)
Mike McCartney (DBEDT)
Robert Masuda (DLNR)
Diane Ley (County of Hawaii)
Dr. Gerry Cysewski (Tenant Representative)
Neil Sims (Tenant Representative)
Dr. Vassilis Syrmos (UH)

Staff

Gregory Barbour (NELHA)
Daniel Jacobs (Deputy AG)
Laurence Sombardier (NELHA)
Stacey Burge (NELHA)

Guests

Randy Tanaka (DBEDT)
Hirokazu Ishikawa, Big Island Abalone
Taishi Kurihara, Big Island Abalone
Jacob Conroy, Kanaloa Octopus Farm

1. Call to Order.

The meeting was called to order at 10:18am by Chair Rosehill.

2. New Business

- a. **Discussion and Decision-Making regarding waiver agreement to permit TriplePoint Capital LLC to hold a security interest in Forever Ocean Corporation's personal property.**

This agenda item was deferred.

3. Old Business

- a. **Discussion and Decision-Making regarding 15.5-acre expansion project final approval for Kowa Premium Foods Hawaii Corporation and amendment of the existing Sublease K6*.**

Ms. Sombardier presented updates and changes from the initial presentation given at the July 16, 2019 BOD meeting.

KOWA proposes to expand to two lots on either side of their current property, a 10-acre lot on the mauka side and a 5.5-acre lot on the makai side. Construction of new facilities would be completed in three phases over five years. The expansion will allow KOWA to develop new abalone products as well as improve and expand on current operations. The second and third phases may include construction of a water bottling facility.

Kowa submitted revisions to the business plan presented at the July 16, 2019 Board meeting. These changes do not impact the overall concept and are detailed in Attachment 3. Phase I will cover less area than originally anticipated primarily because the initial cannery operation will be smaller at first (capacity is reduced to 250,000 cans versus 1.5 million cans per year) before expanding to full size by the last phase. Also, the bottling facility construction will not be started until Phase II. This means that the ratio of extractive/retail land to productive land for Phase I is smaller than previously expected although that ratio will increase by the end of the construction phases.

Kowa has also revised its profit and loss and cash flow plans. The changes are reasonable and provide for larger sales which staff still believes are conservative given previous sales performance on the existing 10 acres.

A Supplemental No. 2 sublease document (Attachment 4) has been reviewed by both Kowa's legal department and NELHA's AG. The supplemental addresses the fresh water, ingress and egress concerns that were brought up during the approval in concept discussions. It also addresses a process and timeline to establish the mixed-use acreage. Initially, acreage will correspond to the acreage as shown on drawings and plans that are approved by the county for construction. It is estimated that the extractive/retail acreage will be on the order of 3 acres yielding a total monthly rental fee of \$11,326.28.

In addition, on January 1, 2023, the mixed land use ratio will be re-evaluated and re-established according to final construction and land use. It is expected that extractive/retail land acreage will increase to approximately 12 acres by the time Phase III construction is complete.

The supplemental lease is in line with the leasing policy including mixed use base rent as discussed above and percentage rent (5% for retail products including tours, restaurant sales, canned abalone products and bottled mineral water). Dilmore curve has been applied to rent rates and annual CPI adjustments are in effect. The initial annual rent will be \$136K per year (base rent) and will increase to \$270K per year over the next 4-5 years.

Kowa does not intend to produce brine or salt products or additives and will need to obtain Board approval if they decide to do so later.

Staff recommends that the NELHA Board grant final approval to the proposed KOWA expansion of 15.5 acres and instruct NELHA Executive Director to finalize and execute Supplemental No. 2 to Sublease No. K-6.

Chair Rosehill entertained a motion to accept the NELHA staff recommendation. Director Masuda made the motion, which was seconded by Director Cysewski. A vote was taken, and the motion passed unanimously, 11-0.

Chair Rosehill asked for any questions of a non-confidential/non-proprietary nature. There were none.

Chair Rosehill entertained a motion to enter Executive Session. Director Masuda made the motion, which was seconded by Director Hilton. A vote was taken, and the motion passed unanimously, 11-0.

(Executive Session)

Chair Rosehill entertained a motion to exit Executive Session. Director Masuda made the motion which was seconded by Director Mielcke. A vote was taken, and the motion passed unanimously, 11-0.

Chair Rosehill asked for vote to accept the NELHA staff recommendation that the NELHA Board grant final approval to the proposed KOWA expansion of 15.5 acres and instruct NELHA Executive Director to finalize and execute Supplemental No. 2 to Sublease No. K-6. A vote was taken, and the motion passed 9-0. As Tenant Representatives, Director Sims and Director Cysewski recused themselves from this vote.

b. Discussion and Decision-Making regarding 4.5-acre project final approval for Fat Fish Farms LLC, dba Kanaloa Octopus Farm.

Ms. Sombardier presented updates and changes from the initial presentation given at the BOD meeting on July 16, 2019.

Kanaloa Octopus Farm currently operates a small successful pilot octopus farm on 4,085 sq. ft of space in the NELHA research campus. Kanaloa is seeking final approval for an expansion of their project to the 4.5 acres facility previously occupied by Hawaii Deep Marine Inc.

On July 16, 2019, Kanaloa sought and obtained approval in concept from the NELHA Board to expand to a 4.5 acres facility to establish a commercial facility with the aim to produce and sell cephalopods and related products such as squid ink. Products will be sold to the bioresearch, food and aquarium markets. The facility plans to provide ecotours to educate the public about cephalopods and generate the bulk of their revenue. Revenue from the sale of products and tours will allow to continue technical research to breed various cephalopod species.

Background information on Kanaloa's project in the research campus and discussions at the approval in concept stage of the proposed project are available in Attachment 1 (For Action Summary for Approval in Concept).

A final business plan addressing items of concern from NELHA staff and Research Advisory Committee (RAC) reviews was submitted and is included as Attachment 3. The final business plan now includes and addresses the impact of economic downturn and dependency on ecotourism income, biosecurity concerns regarding tours to other NELHA facilities, the ability to provide enough feed should sales of cephalopods increase rapidly, as well as the request for additional information regarding the marketing, industry overview and competitor areas of the business plan. Staff has discussed bioethical considerations which are becoming increasingly important in cephalopod aquaculture, acknowledging that these considerations may add some challenges to the project but should not impede the project significantly.

NELHA staff and Kanaloa have reached final agreement on the sublease terms. The draft sublease K-37 has been reviewed by and agreed to by Kanaloa. It has also been reviewed by NELHA's AG and is provided under Attachment 4.

As indicated in July, Kanaloa lease terms are in line with NELHA's leasing policy. Since most of the anticipated revenue will be from tours including gift shop sales, Kanaloa's percent rent is established at 5% of gross revenue. That revenue includes any revenue derived by affiliated non-profit organizations. Retail activities and tours are expected to be conducted on approximately 2 of the 4.5 acres and therefore, the mixed base rent will include base rent at the extractive/retail rate for 2 acres and at the productive rate for the remaining 2.5 acres. The Dilmore curve is applied. Annual CPI adjustments are included.

Although Kanaloa is interested in purchasing the building, they will not have the financial ability to do so immediately. Therefore, Kanaloa will be initially leasing the building. NELHA will retain full ownership of the building and its fixtures while the building is being leased. Lease rate will be in line with the leasing policy and Hale Iako building lease rates at the research campus at \$2.25/sq. ft/month for air-conditioned office space. Approximately, half of the building will be air-conditioned office space. The other half of the building will be non-air-conditioned warehouse space.

The leasing policy does not list non-air-conditioned warehouse space. However, it does list tented covered space at \$0.75/sq. ft/month and air-conditioned stand-alone building space in the campus at \$1.75/sq. ft/month. Therefore, an appropriate and fair rate for the non-air-

conditioned warehouse space is \$1/sq. ft/month. NELHA staff plans to update the leasing policy to include warehouse space in the future.

Kanaloa has agreed to cover maintenance and repairs of the building (up to \$5,000 per occurrence). Any larger maintenance or repairs shall be covered by NELHA.

To assist with the initial financial burden of leasing building space, approximately 25% of the building space (approximately 2000 sq. ft of non-air-conditioned warehouse space) shall continue to be leased by NELHA to the current tenant, UH Infrasond Laboratory through a rental agreement with RCUH, until Kanaloa needs the entire space or NELHA is able to offer an alternative space to ISLA. Minor modifications will be completed by NELHA staff to accommodate separate building ingress/egress for the two tenants. These include a small chain link fence and construction of an access door on an inside wall.

Kanaloa plans to start public tours at the 4.5-acre site in January 2020. For October through December 2019, they will be leasing both space in the research campus and the 4.5-acre facility. The campus rental agreement includes a percent rent clause, therefore, the percent rent clause in sublease K-37 would start applying January 2020.

In order to ensure a successful project and because Kanaloa will be initially leasing two separate spaces at NELHA, it is proposed to provide base rent discounts to allow the project to get on its feet. The discounts diminish over 4 years (60% the first 3 months, 55% in 2020, 25% in 2021 and 5% in 2022) and still provide significant revenue to NELHA (see draft Sublease in Attachment 4). NELHA staff feels that this is a reasonable approach which will help ensure project success. In the past, other projects have experienced trouble with startup costs and have left before starting operations. Should the startup period go smoother than expected, percent rent will make up the difference and cover in part or in full the base rent discount.

Kanaloa has agreed to purchase the reverse osmosis (RO) system for \$10,000. Kanaloa intends to refurbish the system and produce freshwater for its operations as well as incorporate the RO machine in the ecotours to provide addition interest. The RO system was appraised at \$63,000 in early 2018. However, efforts to sell the system have been unsuccessful. Efforts to sell the RO system have included advertisements, reaching out to RO system resellers and directly contacting parties that might be interested over 1.5 years.

Kanaloa does not wish to purchase the salt racks. It is not cost effective to remove the racks and resell as scrap metal. Therefore, NELHA proposes to leave the salt racks in place at no cost and Kanaloa has accepted. Kanaloa may choose to incorporate some salt production as part of their ecotours in the future. It is important to note that the boiler plate sublease language includes a requirement for royalty to be paid on salt or eater products that are sold. This may provide additional revenue to NELHA in the future.

NELHA staff conducted tests to evaluate the capacity of the water discharge wells. Staff was able to confirm that the existing system can accommodate up to 230gpm flow over 24 hours continuous flow. This is well above Kanaloa's estimated flow rates for return water.

The building is in good condition. However, one area of concern is the AC system. In order to reduce electrical costs, Kanaloa plans to cool only the half of the building that corresponds to

the offices and retail area. The warehouse area (including the space leased by ISLA) will not have any AC. This will be possible by not operating the warehouse chiller and closing a few smaller vents on the mezzanine.

The AC system consists of three chillers servicing separate areas in the 7,500 sq. ft building. Two of the AC chillers are needed for the office area. One of these units works and can chill although minor repairs are needed. A specialist has been hired to evaluate and repair the other chiller. The office rate of \$2.25/sq. ft/month includes AC to be provided by NELHA. Once the AC units are fully functional, NELHA will estimate the cost of operating the AC system and provide a credit on monthly invoices for the electrical costs incurred. Language may be added to the sublease to reflect this arrangement.

In the final proposal to NELHA (Attachment 4), Kanaloa clarified that they would operate a small café as part of the retail gift store. Kanaloa understands that the public needs to have exited the park by the established closing time of NELHA's main gate.

Ms. Sombardier pointed out that typos were uncovered in the attached draft sublease subsequent to distribution of the Board packet to Board members. The final corrected sublease will have a slightly different base rent.

Staff recommends that the NELHA Board grant final approval for the project as described above and instruct the NELHA Executive Director to finalize and execute the sublease.

Director Masuda asked who the previous tenant in the building was. Ms. Sombardier stated the previous tenant was Hawaii Deep Marine. It was a Japanese company and one of the first water bottling company selling desalinated deep seawater. Hawaii Deep Marine left approximately 2 years ago.

Director Hilton provided the board the Research Advisory Committee's feedback. The RAC had received the revised Kanaloa proposal and, as a committee, support the NELHA staff recommendation to proceed with this project.

Chair Rosehill asked if there were any additional questions. There was not. Chair Rosehill entertained a motion to accept the staff recommendation that the NELHA Board grant final approval for the project as described and instruct the NELHA Executive Director to finalize and execute the attached sublease. Director Masuda made the motion which was seconded by Director McCartney. A vote was taken, and the motion passed 9-0. As Tenant Representatives, Director Sims and Director Cysewski recused themselves from this vote.

- c. **Report from the Special Investigative Committee regarding the annual performance evaluation of the NELHA Executive Director.**

Chair Rosehill entertained a motion to enter Executive Session. Director Mielke made the motion, which was seconded by Director Masuda. A vote was taken, and the motion passed unanimously, 11-0.

The board entered Executive Session. All NELHA staff were excused from Executive Session.

The board exited Executive Session at approximately 12:10pm.

4. Announcements.

None.

5. Adjournment.

There being no further business, Chair Rosehill entertained a motion to adjourn the meeting. Director Masuda made the motion which was seconded by Director McCartney. The motion passed unanimously, 11-0, and the meeting was adjourned at 12:20pm.