

STATE OF HAWAII
DEPARTMENT OF LAND AND NATURAL RESOURCES
Division of Forestry and Wildlife
Honolulu, Hawaii 96813

October 23, 2009

Chairperson and Members
Board of Land and Natural Resources
State of Hawaii
Honolulu, Hawaii

Land Board Members:

**SUBJECT: RE-SUBMITTAL FOR AMENDMENT NO. 2 OF TIMBER LAND
LICENSE NO. 2007-H-01 HELD BY HAWAII ISLAND HARDWOODS,
LLC.**

Background: At its June 22, 2007 meeting under item C-2, the Board approved issuance of a Timber Land License to Hawaii Island Hardwoods, LLC (HIH) for timber resources within the Waiakea Timber Management Area (WTMA) on Hawaii island, in support of HIH establishing a state-of-the-art, medium sized sawmill facility. Timber Land License No. 2007-H-01 (“License”), was fully executed on September 10, 2007.

License terms included details for four (4) phases of development (see copy of License Table 2 below), a condition that harvesting within the licensed WTMA timber stands be initiated within 28 calendar days of License execution, specifications for mill size/capacity and others. HIH initiated harvesting within the designated time frame during the period of October to December 2007, but has not conducted harvest operations in the License area since that time.

Table 2. Licensee sawmill development schedule. [Note: Start date was 9/10/07]

Item	Phase	Time Period
Traveling carriage head saw	II	6-12 months
Band or circle head saw	II	6-12 months
Dry kiln capacity to accommodate 1,000,000 BF/yr	II	6-12 months
Sorting line	III	9-18 months
Stacking machine	III	9-18 months
Planer	III	9-18 months
Two-saw, dual laser board edger	IV	12-48 months
Dry kiln capacity to accommodate 5,000,000 BF/yr	IV	12-48 months

The Department considered and approved this License for many objectives, some of which included: Promotion of local forest industry processing to provide products for the Hawaii Market; providing a steady revenue stream to the Department; and fostering the establishment of a state-of-the-art sawmill with considerably larger processing capacity than any other existing operation in the State. Upon request from HIH and approval of the Board, the License was

amended on December 10, 2008, by extending all of the deadlines in Table 2, as depicted above, for Phases II and III to 24 months.

In two additional letters dated July 23, 2009, and September 15, 2009, HIH provided DOFAW with additional information regarding their business progress to date, and requested further amendments to the License. Staff brought that request before the Board at its September 25, 2009 meeting, under agenda item C-3.

Because HIH indicated that it needed additional time to develop its sawmill than the deadlines contemplated in their written request and as reflected in item C-3, the Board deferred C-3 and instructed Staff to work with HIH to revise its License amendment request as follows: Re-state the License sawmill development deadlines to reflect realistic time frames; and scale the HIH-requested reduction in the License Bond requirement according to the size of HIH's field harvesting operations.

HIH subsequently submitted an updated request for License amendments on October 14, 2009 (Exhibit A) requesting two principal amendments to the License. The first would amend License Table 2 by re-stating the time frames and phases within which each mill component will be brought on line, as well as adding new mill equipment components. The second amendment would scale HIH's bond obligation between \$50,000 and \$250,000 depending on the extent of their active field harvesting activities at any one given time.

Discussion: Results to date have been mixed. Though harvesting was initiated immediately after License execution in September 2007, there has not been a subsequent stream of harvesting and associated revenue generation for the Department since approximately February 2008. HIH indicates a plan to re-initiate harvesting in the License area during 2009. HIH has incrementally increased their mill equipment inventory and mill capacity, secured a prospective site for new mill construction, but has not met extended deadlines for Phase II, Phase III or overall milling capacity. None the less and as detailed in their latest letter, HIH is operational, has recorded growth in gross receipts, marketing and sales efforts, and is supplying product to the Hawaii market while providing local employment opportunities – this all during the current economic recession. Based on continuing discussions with HIH, Staff suggests continued partnership between the Department and HIH through License amendments by:

1. Re-stating License Table 2 as follows:

Table 2. Licensee sawmill development schedule. [Note: Start date was 9/10/07]

Item	Phase	Time Period
Band or circle head saw	II	24 months
Planer	II	36 months
Straight line rip saw	II	36 months
End trimming chop saw	II	36 months
Four-sided planer	II	36 months
Dry kiln capacity to accommodate 1,000,000 BF/yr	III	48 months
Sorting line	III	48 months
Stacking machine	III	48 months
Five-head moulder	III	48 months
Two-saw, dual laser board edger	IV	60+ months*
Dry kiln capacity to accommodate 5,000,000 BF/yr	IV	60+ months*
Traveling carriage head saw	IV	60+ months*

*Phase IV items may come on-line within 60 months or thereafter subject to potential extension of the License term.

2. Amending License Section 10.17 whereby the deadline within which HIH would be obligated to have a mill with a 1,000,000 annual board foot processing capacity would be extended to 48 months.

3. Amending License Section 4.4 whereby the Bond requirement for HIH be scaled according to the size of HIH's active harvesting operations within the WTMA as follows:

- a. For 0-20 acres - \$50,000
- b. For 21-40 acres - \$100,000
- c. For 41-60 acres - \$150,000
- d. For 61-80 acres - \$200,000
- e. For 81 acres or more - \$250,000

In addition, a clause requiring a harvest area closeout audit by DOFAW prior to HIH proceeding to new or additional harvest areas should be added.

4. Staff notes that relating to road maintenance, License Section 5.3 specifies that DOFAW was to be responsible for maintaining/upgrading one (1) road within the License area by this time. The Division has not met this responsibility nor initiated this work due to the dormant state of HIH's field operations in the License area. Staff recommends amending Section 5.3 whereby DOFAW's maintenance and upgrade activities for this road be tied to a 180 day written notice requirement from HIH regarding their intent to harvest in the affected and adjacent timber stands. If DOFAW decides, in its sole and absolute discretion, that it is unwilling or unable to perform the maintenance and upgrading of that one (1) road mentioned above, then; (a) HIH will be notified of the same in writing within thirty (30) days of the Department receiving HIH's

intent to harvest notification; (b) HIH shall become responsible for maintenance and upgrade work for the aforementioned road segment; and (c) as compensation, the stumpage pricing basis paid by HIH to the Department for timber harvested from the three (3) adjacent timber stands accessed by this road shall be reduced by 33%.

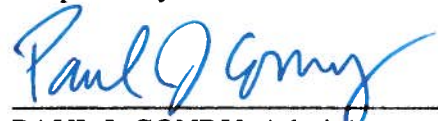
RECOMMENDATIONS:

1. That the Board of Land and Natural Resources amend Timber Land License No. 2007-H-01 held by Hawaii Island Hardwoods, LLC by:
 - a. Amending and re-stating License Table 2 as detailed in Discussion Section No. 1 above;
 - b. Extending the deadline in section 10.17 for HIH to establish a mill with a 1,000,000 annual board foot capacity to 48 months;
 - c. Amending License Section 4.4 whereby the Bond requirement for HIH be scaled according to the size of their active harvesting operations within the WTMA as detailed in Discussion Section No. 3 above; and
 - d. Revising License Section 5.3 regarding road maintenance or upgrade responsibilities as detailed in Discussion Section No. 4 above.

2. That the amendment of the License be subject to:
 - a. Review and approval by the Department of the Attorney General; and

- b. Such other terms and conditions as may be prescribed by the Chairperson to best serve the interests of the State.

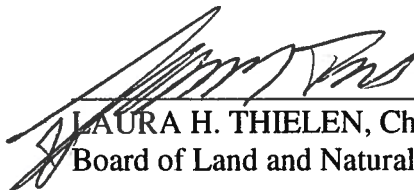
Respectfully submitted,



PAUL J. CONRY, Administrator
Division of Forestry and Wildlife

Exhibit A – Letter from Hawaii Island Hardwoods requesting License amendments.

APPROVED FOR SUBMITTAL:



LAURA H. THIELEN, Chairperson
Board of Land and Natural Resources

EXHIBIT A



Hawaii Island Hardwoods Inc

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October 14, 2009

Laura H. Thielan, Chairperson
 Board of Land and Natural Resources
 P.O. Box 621
 Honolulu, HI 96809

Dear Ms Thielan:

This letter is to supplement our recent letters and presentations to the Board of Land and Natural Resources (BLNR) regarding our request for extension of Timber Land License No. 2007-H-01. At the BLNR meeting on September 25th the Board asked that we return with a more detailed outline for our best estimates for the future. The 2008 amendment and extension contained the following schedule:

Table 2 (from 2008 Amendment)

Item	Phase	Time Period
Traveling carriage head saw	II	6-24 months
Band or circle head saw	II	6-24 months
Dry kiln capacity to accommodate 1,000,000 BF/yr	II	6-24 months
Sorting line	III	9-24 months
Stacking machine	III	9-24 months
Planer	III	9-24 months
Two-saw, dual laser board edger	IV	12-48 months
Dry kiln capacity to accommodate 5,000,000 BF/yr	IV	12-48 months"

We have shifted our near term strategy to more finishing and value adding activities and we have installed a planer, a rip saw, and a chop saw at a temporary site and we have a sorting line ready for installation when we can establish three phase power at our permanent Kea'au mill site. We are proposing a revised schedule as follows:

Item	Phase	Time Period
Band or circle head saw	II	24 months
Planer	II	36 months
Straight line rip saw	II	36 months
End trimming chop saw	III	36 months
Four-sided planer	III	36 months
Dry kiln capacity to accommodate 1,000,000 BF/yr	III	48 months
Sorting line	III	48 months
Stacking machine	III	48 months
Five-head molder	III	48 months
Two-saw, dual laser board edger	IV	60+ months*
Dry kiln capacity to accommodate 5,000,000 BF/yr	IV	60+ months*
Traveling carriage head saw	IV	60+ months*

*Phase IV items may come on-line within 60 months or thereafter subject to potential extension of the License term.

An extensive review by our owner group and staff leads us to believe that the return of a robust economy and the development of markets for the species that are in the WTMA are going to require something in the range of five (5) years. Our hope is to be able to meet the following timelines for harvesting over the next two years as we continue to develop market acceptance of the products of the WTMA:

<u>Species</u>	<u>Year</u>	<u>Quantity</u>	<u>Year</u>	<u>Quantity</u>
		bf		bf
• Toona Ciliata	<i>2010</i>	2,000	<i>2011</i>	10,000
• Nepal Alder	<i>2010</i>	3,000	<i>2011</i>	5,000
• E. Saligna/Grandis	<i>2010</i>	3,000	<i>2011</i>	5,000
• Eucalyptus Robusta	<i>2010</i>		<i>2011</i>	10,000
• Queensland Maple	<i>2010</i>	2,000	<i>2011</i>	<u>5,000</u>
Estimated totals:		10,000		35,000

We further anticipate that we should be able to have the following additional facilities added to our site during the next two years:

- (1) Finishing plant with the following facilities:
 - (a) Relocated planer/surface, rip saw and chop saw.
 - (b) Acquire a five or six head moulder for flooring and other tongue and groove product development.
- (2) Additional dry kiln (approximately 30,000 board foot capacity).
- (3) Interim higher capacity stationery band saw.
- (4) Three phase power connections

We have further requested a reduction in the bond requirements. We are amenable toward to a staged or graduating schedule based upon the numbers of acres harvested.

Respectfully submitted:

James E. Quinn,

Member Manager, Hawaii Island Hardwoods LLC