

CITY AND COUNTY OF SAN FRANCISCO
BOARD OF SUPERVISORS
BUDGET AND LEGISLATIVE ANALYST

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May 2, 2014


TO: Budget and Finance Sub-Committee
FROM: Budget and Legislative Analyst 
SUBJECT: May 7, 2014 Budget and Finance Sub-Committee Meeting

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<p>Item 3 File 14-0225 <i>(Continued from April 16, 2014)</i></p>	<p>Department: San Francisco Municipal Transportation Authority (SFMTA)</p>
<p>EXECUTIVE SUMMARY</p>	
<p>Legislative Objectives</p>	
<ul style="list-style-type: none"> • The proposed resolution would authorize the SFMTA to enter into an agreement with Titan Outdoor LLC (Titan) to provide advertising on SFMTA vehicles and other property for a term of five years. SFMTA would also have two five-year options to extend the contract. 	
<p>Key Points</p>	
<ul style="list-style-type: none"> • In 2009, the City entered into an agreement with Titan to provide advertising on SFMTA vehicles and other property for a five-year term, which expires on June 30, 2014. SFMTA issued an RFP on October 16, 2013 to solicit a new advertising contract, and SFMTA received three proposals, two of which met the minimum qualifications. After undergoing review, Titan’s proposal received a score of 383, and CBS Outdoor’s proposal received a score of 334.1, out of 400; and SFMTA awarded the advertising agreement to Titan. • The proposed agreement differs from the previous agreement in that it would allow full window wraps on 15-30 buses, whereas only 15 window wraps on buses are currently permitted. • The proposed agreement also allows for advertising to be negotiated in the Central Subway upon its completion. Any modification to the agreement that includes an increase in the Minimum Annual Guarantee (MAG) is subject to Board of Supervisors approval in accordance with Charter Section 9.118(a). 	
<p>Fiscal Impact</p>	
<ul style="list-style-type: none"> • Under the proposed agreement, Titan will pay SFMTA the greater of (a) 65% of its gross advertising revenues; or (b) a MAG of \$5,400,000 in the first year of the agreement, increasing annually by \$150,000 per year. Titan will also pay the SFMTA an annual administrative fee of \$150,000 and annual marketing support of \$150,000, payments which will escalate annually according to the Consumer Price Index of the Bay Area. resulting in minimum first year revenue of \$5,700,000. • The minimum revenue to the SFMTA over the initial five-year term of the agreement is \$30,000,000, including the MAG, and administrative and marketing fees. 	
<p>Recommendation</p>	
<ul style="list-style-type: none"> • Approve the proposed resolution. 	

MANDATE STATEMENT / BACKGROUND

Mandate Statement

City Charter Section 9.118(a) states that agreements entered into by a department, board or commission that will generate revenue in excess of \$1 million, or any modification of that agreement, is subject to Board of Supervisors approval.

Background

In 2009, based on a competitive Request for Proposals (RFP), the Board of Supervisors approved an agreement between the San Francisco Municipal Transportation Agency (SFMTA) and Titan Outdoor LLC (Titan) for advertising on SFMTA vehicles and other SFMTA property for a term of five years from July 1, 2009 through June 30, 2014 (File 09-0633). On October 16, 2013, the SFMTA Board of Directors authorized the issuance of a competitive RFP for a new agreement for these services that would commence on July 1, 2014, following the termination of the existing agreement on June 30, 2014.

The SFMTA received three proposals, two of which were responsive to the minimum qualifications set forth in the RFP. The qualifications included a minimum of three years of advertising experience in the transit advertising business, a corporate net worth of \$25,000,000 for the last three years, and a demonstration of financial stability. Other criteria pertained to experience, quality of the proposals and amount to be paid to the SFMTA. The SFMTA conducted an evaluation of Titan and CBS Outdoor, the proposers that submitted the responsive proposals. Titan received the highest score, as shown in Table 1 below.

Table 1: Name of Advertising Business and Total Score Received

Name of Advertising Business	Score (Out of 400)
Titan Outdoor LLC (Titan)	383
CBS Outdoor	334.1

DETAILS OF PROPOSED LEGISLATION

The proposed resolution would authorize SFMTA to execute a new transit advertising agreement with Titan for an initial five-year term, from July 1, 2014, through June 30, 2019. Titan would be required to pay SFMTA a Minimum Annual Guarantee (MAG) of \$5,400,000 for the first year. The MAG would increase by the Consumer Price Index (CPI) in each subsequent year. The agreement includes two five-year options to extend, for a total term up to 15 years. Table 2 below shows a comparison of the provisions under the proposed and current agreements with Titan.

Table 2: Summary of Differences between Current Agreement and Proposed Agreement

Requirement	Current Agreement	Proposed Agreement
Initial Contract Term	Five years July 1, 2009 through June 30, 2014	Five years July 1, 2014 through June 30, 2019
Options to Extend	None	Two 5-year options through June 30, 2029, for a total contract term of up to 15 years
Minimum Annual Guarantee (MAG)	\$4,000,000 for first year	\$5,400,000 for first year
Annual Increase in MAG	5% per year	\$150,000 per year (2.8% in the first year)
Administrative Fee	None	\$150,000 per year, adjusted annually by the Consumer Price Index (CPI)
Marketing Fee	None	\$150,000 per year, adjusted annually by the CPI
Revenue (Percentage of gross advertising revenue if greater than the MAG)	65% of gross advertising revenues	65% of gross advertising revenues
Window Wraps	15 at any one time	15-30 at discretion of the Director of Transportation
Central Subway advertising program	None	To be negotiated, including the revenues payable to the SFMTA, before the opening of Central Subway as an amendment to the agreement, subject to approval by the Board of Supervisors
Corporate Sponsorships/ Naming Rights	If exercised, would be a contract amendment	None
Letter of Credit	100% of MAG	75% of MAG
Security Fund	\$250,000	\$150,000
Hire Trainees	None	Minimum of two trainees

Advertising Provisions in the Proposed Agreement between SFMTA and Titan

The proposed agreement differs in several ways from the current agreement. Key activities, requirements and changes are highlighted below.

Window Wraps and Non-Window Coverings

Under the current agreement, SFMTA allows full wraps of vehicles with windows covered (“window wraps”) on not more than 15 vehicles at any one time. The proposed agreement allows window wraps on at least 15 vehicles to not more than 30. The number of window wraps for the first fiscal year of the proposed agreement will be 30. The calculated MAG assumes the continuation of a minimum of 15 window wraps. If the Board of Supervisors does not approve a program of at least 15 window wraps, then the MAG will be decreased by \$325,000 for each fiscal year of the agreement.

The SFMTA also intends to continue a program of non-window coverings, which cover the body of the vehicles but not windows. The total number of window wraps and non-window coverings together will not exceed 20% of the SFMTA’s transit vehicles at any one time. Cable cars and historic vehicles will not receive any window wraps or non-window coverings. The number of window wraps and the approval of the window wraps program do not affect the number of advertisements on transit vehicles that can partially cover windows, which are not limited.

The SFMTA reports that the quality of the material for window wraps has improved throughout the term of the existing contract and that visibility has improved. The SFMTA has provided a video which illustrates this point.¹ In addition, Titan is responsible for maintaining all of the advertisements, including cleaning off all graffiti and/or replacing the defaced advertisements and addressing all vandalism. In the case of the window wraps, this means that Titan is responsible for the maintenance of the entire outside of the wrapped vehicle.

Central Subway

The proposed agreement includes a provision that enables the SFMTA to include an advertising program in the new Central Subway stations and tunnel after their completion. If exercised, the SFMTA and Titan will negotiate the increased amounts to the MAG payable by Titan to the SFMTA over the remaining term of the agreement. Any modification to the proposed agreement regarding the Central Subway would be subject to Board of Supervisors approval in accordance with Charter Section 9.118(a).

¹ The video can be found here: <http://www.youtube.com/watch?v=y5YAVI2HyE8>

SFMTA Property; Other Property; Limitations on Advertising Displays

The following SFMTA property is available for advertising under the agreement: transit vehicles, parking garages (including those under the jurisdiction of the Recreation and Park Department), transit stations, other SFMTA facilities, and fare and parking media. Only interior advertisements are allowed on historic streetcars, and all advertisements on cable cars and historic vehicles must be in conformity with the character, style, and design of such vehicles. Titan may place digital advertising on up to 20 percent of the SFMTA's transit vehicles at any one time, excluding cable cars and historic streetcars. The SFMTA will be able to override digital advertising with emergency signage.

Performance Requirements and Security Deposits

Titan will provide a letter of credit for 75% of the MAG each fiscal year for the duration of the agreement. The SFMTA may draw on the letter of credit in the event that a) Titan fails to pay the SFMTA the annual required revenues due to the SFMTA under the proposed agreement, b) there is a failure to replenish the Security Fund, or c) termination of the agreement due to a default by Titan. Titan will also provide a Security Fund in the amount of \$150,000 to guarantee the performance of obligations not covered under the letter of credit. Titan has provided the SFMTA with a bid security check for \$1,000,000 to secure its proposal. If Titan fails to execute the agreement and furnish the required letter of credit and insurance certificates, then the SFMTA will keep the \$1,000,000 as compensation for damages sustained by the SFMTA. The SFMTA would return the bid security check to Titan upon final approval of the agreement.

Termination

The SFMTA may terminate the agreement for default or convenience. The SFMTA may also partially terminate advertising rights with respect to any category of advertising space, other than transit vehicles, that Titan does not sell over a period of 60 days unless Titan demonstrates to the SFMTA that it intends to sell advertising on that space even though it has been unable to previously do so.

FISCAL IMPACT

Under the proposed agreement, Titan is required to pay the SFMTA the greater of (a) 65% of its gross advertising revenues or (b) the MAG. The MAG for the first year of the agreement is \$5,400,000, which is \$537,975, or 11 percent, more than the MAG for the final year of the existing agreement, \$4,862,025. The MAG is subject to annual CPI adjustments over the remaining term of the agreement. Titan is also required to pay the SFMTA an annual administrative fee of \$150,000 and an annual marketing fee of \$150,000, payments which will escalate annually according to the CPI of the Bay Area.

As shown in Table 3 below, the total MAG payable by Titan to SFMTA over the initial five-year term of the agreement is \$28,500,000, and the total minimum revenues payable to SFMTA by Titan over the entire five-year period is \$30,000,000.

**Table 3: Minimum Annual Guarantee and Fees
Payable by Titan to SFMTA during Initial 5-Year Term**

Fiscal Year	MAG	Administrative Fee¹	Marketing Fee¹	Total
2014-15	\$5,400,000	\$150,000	\$150,000	\$5,700,000
2015-16	5,550,000	150,000	150,000	5,850,000
2016-17	5,700,000	150,000	150,000	6,000,000
2017-18	5,850,000	150,000	150,000	6,150,000
2019-20	6,000,000	150,000	150,000	6,300,000
TOTAL	\$28,500,000	\$750,000	\$750,000	\$30,000,000

¹ Does not include annual CPI adjustments.

According to Ms. Gail Stein, SFMTA Finance Manager, the SFMTA will receive a \$150,000 increase annually in the MAG under the proposed agreement which differs from the existing agreement in which SFMTA received 5% annual increases in the MAG. The SFMTA accepted this change for two reasons: (1) As previously noted, the initial MAG of \$5,400,000 in the new agreement is \$537,975 more, or 11 percent, than the final year, 2013-2014 MAG in the existing agreement; and (2) the proposed new agreement includes an additional \$300,000 per year in fees escalated by Bay Area CPI to cover SFMTA administrative costs (\$150,000) and marketing costs (\$150,000) which were not received under the existing contract. Therefore, the SFMTA believes that the provisions under the proposed new agreement structure will result in more certainty and additional revenues to the SFMTA than the existing agreement.

Under the existing 5-year agreement between SFMTA and Titan, the revenues paid by Titan to the SFMTA exceeded the MAG in every year as shown in Table 4 below.

**Table 4: Payments by Titan to SFMTA
FY 2009-10 through FY 2013-14**

Fiscal Year	MAG	65% of Gross Revenues
2009-2010	\$4,000,000	\$4,219,066
2010-2011	\$4,200,000	\$5,112,527
2011-2012	\$4,410,000	\$4,758,319
2012-2013	\$4,630,500	\$5,799,660
2013-2014 (through February 2014)*	\$4,862,025	\$3,806,298

*The SFMTA estimates that the percentage of gross revenues payable by Titan to the SFMTA will exceed the MAG for Fiscal Year 2013-2014 by at least \$500,000.

RECOMMENDATION

Approve the proposed resolution.

Item 4 File 14-0410	Department: Municipal Transportation Agency
EXECUTIVE SUMMARY	
<p style="text-align: center;">Legislative Objective</p> <ul style="list-style-type: none"> • The proposed resolution would approve a new agreement negotiated between the City, on behalf of the SFMTA, and BART to continue the Fast Pass program allowing MUNI Fast Pass patrons to take an unlimited number of monthly rides on BART within San Francisco city limits. SFMTA would reimburse BART at a fixed reimbursement rate for each trip by an Adult Fast Pass rider, for a six-year term from July 1, 2014 through June 30, 2020. <p style="text-align: center;">Key Points</p> <ul style="list-style-type: none"> • The amount reimbursed by SFMTA to BART for each trip in San Francisco by an Adult A Fast Pass rider would increase by 5 percent from the current rate of \$1.21 per trip to the proposed rate of \$1.27 per trip, effective July 1, 2014. • The SFMTA reimbursement rate to BART for each trip would increase once every two years in accordance with BART's productivity-adjusted Consumer Price Index (CPI) formula which is also used to increase BART fares every two years. Under the proposed agreement, SFMTA's reimbursement rate to BART would increase in 2016, 2018 and 2020, concurrent with BART fare increases. • The annual cap on SFMTA's reimbursement to BART would increase by 5 percent from the current cap of \$10.5 million in FY 2013-14 to the proposed cap of \$11 million in FY 2014-15. The cap would increase annually by 5 percent on July 1 of each subsequent year. • BART will reimburse the SFMTA for Clipper Card transaction costs related to the use of the Fast Pass on BART. <p style="text-align: center;">Fiscal Impact</p> <ul style="list-style-type: none"> • Estimated reimbursements by SFMTA to BART over the six-year term of the proposed agreement range from \$52,800,00 to \$63,048,926 based on an estimated 5 percent increase to the reimbursement rate every two years and growth up to 5 percent to annual ridership per year. The total amount of the cap over the six-year term is \$74,821,040. <p style="text-align: center;">Recommendations</p> <ul style="list-style-type: none"> • Amend the proposed resolution to provide for a total not-to-exceed amount of \$74,821,040 under the proposed new Fast Pass agreement between the SFMTA and BART. • Approval of the proposed resolution, as amended, is a policy decision for the Board of Supervisors. 	

MANDATE STATEMENT

In accordance with Charter Section 9.118(b), City agreements having a term of more than ten years with anticipated expenditures of \$10,000,000 or more, or amendments to such City agreements with expenditures of more than \$500,000 are subject to Board of Supervisors approval.

BACKGROUND

The Fast Pass Agreement between the San Francisco Municipal Transportation Agency (SFMTA) and Bay Area Rapid Transit (BART) allows Municipal Railway (MUNI) Adult Fast Pass¹ riders who purchase the Fast Pass with the BART option (Adult A Fast Pass) to take unlimited monthly rides on BART within San Francisco city limits at no additional cost to the rider. SFMTA reimburses BART at a fixed reimbursement rate for each BART trip taken by an Adult Fast Pass rider. The most recent Fast Pass Agreement between SFMTA and BART was approved by the Board of Supervisors in 2012 and expires on June 30, 2014 (Resolution 12-1187).

DETAILS OF PROPOSED LEGISLATION

The proposed resolution would approve a new agreement negotiated between the SFMTA and BART to continue the Fast Pass program allowing MUNI Fast Pass patrons to take an unlimited number of monthly rides on BART within San Francisco city limits. The proposed agreement would be for a six-year term from July 1, 2014 through June 30, 2020. Under the new agreement:

- a) The amount reimbursed by SFMTA to BART for each BART trip in San Francisco taken by an Adult A Fast Pass rider would increase by approximately 5 percent or \$0.06 per trip from the current rate of \$1.21 per trip to the proposed rate of \$1.27 per trip, effective July 1, 2014.
- b) The SFMTA reimbursement rate to BART for each BART trip would increase once every two years in accordance with BART's productivity-adjusted Consumer Price Index (CPI) formula which is also used to increase BART fares every two years.² Under the proposed agreement, SFMTA's reimbursement rate to BART would increase in 2016, 2018 and 2020, concurrent with BART fare increases.

¹ The Fast Pass is a prepaid monthly pass that allows the rider unlimited rides on the Municipal Railway (MUNI).

² Under the productivity-adjusted CPI, the two-year reimbursement rate is adjusted by the average change in the National and Bay Area CPI over two years, less ½ percentage point "productivity factor". For example, if the average change in the National and Bay Area CPI over two years was 4 percent and ½ percentage point was subtracted, the fare increase would be 3.5 percent.

- c) The annual cap on SFMTA’s reimbursement to BART in FY 2014-15 will be \$11 million, with an annual increase to the cap of 5 percent on July 1 of each subsequent year.
- d) BART will reimburse the SFMTA for Clipper Card³ transaction costs related to the use of the Fast Pass on BART.

The proposed new agreement requires that the SFMTA and BART to begin negotiations for a new Fast Pass Agreement by January 1, 2020. If both parties cannot agree on the terms of a new agreement effective July 1, 2020, then the agreement shall continue on a month-to-month basis with a reimbursement rate adjustment based on BART’s CPI formula effective on the date of a BART fare increase on or after July 1, 2020.

Decrease in Muni Riders Using the Fast Pass with the BART Option

As shown in Table 1 below, MUNI Adult Fast Pass ridership on BART has decreased by 48 percent and SFMTA reimbursements to BART have decreased by 39 percent from FY 2008-09 through FY 2013-14.

**Table 1: Change in MUNI Fast Pass Ridership on BART and SFMTA Reimbursements to BART
FY 2008-09 to FY 2013-14**

Fiscal Year	Number of MUNI Fast Pass Riders on BART	Payment to BART
FY 2008-09	12,732,283	\$12,986,214
FY 2009-10	10,295,484	10,575,817
FY 2010-11	8,074,923	9,572,380
FY 2011-12	7,725,533	9,137,810
FY 2012-13	7,609,677	9,089,591
FY 2013-14 (projected)	6,600,000	7,986,000
Decrease FY 2008-09 to FY 2013-14	(6,132,283)	(\$5,000,214)
Percent Decrease	-48%	-39%

Source: SFMTA

FY 2013-14 Costs of the Fast Pass Agreement between SFMTA and BART

In FY 2013-14, the monthly price of a MUNI Adult A Fast Pass, which allows the rider unlimited rides on BART within San Francisco city limits, is \$76. In contrast, the monthly price for the Adult M Fast Pass is \$66 but only provides unlimited use of MUNI lines. Thus, the incremental revenue which the SFMTA receives from the sale of the MUNI Adult A Fast Pass with the BART option is \$10. According to Mr. Steven Lee, SFMTA Financial Services and Contracts Manager, approximately 347,000 of Adult A Fast Passes with the BART option are sold annually, resulting

³ The Clipper Card is a reloadable card that is administered by the Metropolitan Transportation Commission and can be used on various regional transit systems, including MUNI and BART.

in total estimated incremental revenues to SFMTA in FY 2013-14 of \$3,470,000. Table 2 below displays the FY 2013-14 net cost of \$4,516,000 to the SFMTA for the MUNI Fast Pass program with the BART option.

Table 2: Estimated Cost to SFMTA for providing MUNI Adult A Fast Pass riders with the BART Option in FY 2013-14

Source	Total
Total SFMTA Incremental Revenue	\$3,470,000
Total SFMTA Reimbursement to BART	(7,986,000)
Net Cost to the SFMTA	(\$4,516,000)

Source: SFMTA

Reimbursement by BART to SFMTA for Clipper Card Transaction Costs

SFMTA requires Fast Pass patrons to purchase a Clipper Card. Under the existing Fast Pass Agreement between SFMTA and BART, SFMTA is reimbursed by BART for the transaction costs of the Clipper card. Table 3 below shows the annual reimbursements by BART to SFMTA for Clipper Card transaction fees in FY 2011-12 and FY 2012-13.

Table 3: BART Clipper Card Transaction Reimbursement Payments to SFMTA FY 2011-12 and FY 2012-13

Fiscal Year	Total Number of Clipper Transactions	BART Reimbursement to SFMTA
FY 2011-12	181,157,770	\$118,910
FY 2012-13	212,373,721	118,118

Source: SFMTA

FISCAL IMPACT

The total estimated reimbursements by SFMTA to BART over the six-year term of the proposed agreement to continue to provide MUNI Fast Pass riders with the BART option, thereby allowing such riders to take an unlimited number of monthly rides on BART within San Francisco city limits, ranges from \$52,800,00 to \$63,048,926 based on an estimated 5 percent increase to the reimbursement rate every two years and based on ridership growth of up to 5 percent per year, as shown in Table 4 below.

The Fast Pass Agreement also provides an annual cap on SFMTA’s reimbursement fees to BART of \$11 million, which will increase at a rate of 5 percent per year. The \$11 million cap under the proposed new agreement is approximately 5 percent more than the FY 2013-14 cap of \$10.5 million under the current Fast Pass Agreement.

Table 4: Projected SFMTA Reimbursement Payments to Bart from FY 2014-15 to FY 2019-20 for MUNI Riders to have the BART Option

Fiscal Year	Reimbursement Rate (Assuming a 5% CPI-adjusted increase)	Reimbursement Expenses (Assuming 6,600,000 Riders and No Ridership Growth)	Reimbursement Expenses (Assuming 5% Annual Ridership Growth)	Proposed Annual Reimbursement Cap Payable by the SFMTA to BART
FY 2014-15	\$1.27	\$8,382,000	\$8,801,100	\$11,000,000
FY 2015-16	\$1.27	8,382,000	9,241,155	11,550,000
FY 2016-17	\$1.33	8,778,000	10,161,632	12,127,500
FY 2017-18	\$1.33	8,778,000	10,669,714	12,733,875
FY 2018-19	\$1.40	9,240,000	11,792,842	13,370,568
FY 2019-20	\$1.40	9,240,000	12,382,484	14,039,097
Total		\$52,800,000	\$63,048,926	\$74,821,040

Additionally, BART will reimburse SFMTA for Clipper Card transaction fees, based on a formula in the proposed agreement and shown in the table below. For fiscal year 2014-15, the projected reimbursement for Clipper Card transaction fees is \$102,366, which is less than the reimbursement to the SFMTA for Clipper Card transaction fees of \$118,118 in FY 2012-13 (see Table 3 above), reflecting the reduced number of MUNI Fast Pass riders using the BART system within San Francisco city limits in FY 2014-15.

Table 5: Estimated Reimbursements by BART to SFMTA for Clipper Card Transactions

Fiscal Year	Estimated Reimbursements for Clipper Transactions (Assuming no growth in ridership)	Estimated Reimbursements for Clipper Transactions (Assuming 5% growth in ridership)
FY 2014-15	\$102,366	\$102,366
FY 2015-16	102,366	106,590
FY 2016-17	102,366	111,026
FY 2017-18	102,366	115,683
FY 2018-19	102,366	120,572
FY 2019-20	102,366	125,707
FY 2014-15	102,366	131,098
Total	\$716,562	\$813,042

POLICY CONSIDERATION

The Budget and Legislative Analyst previously recommended that any Fast Past Agreement between SFMTA and BART should include (1) a not-to-exceed amount, and (2) reimbursement rate increases tied to the rate of inflation (File 11-0201). As noted above, under the proposed agreement, increases in SFMTA's reimbursement rate to BART are based on BART's fare increases every two years and are adjusted by the average of the National and Bay Area CPI, and therefore conform to the Budget and Legislative Analyst's prior recommendation. The proposed agreement does not include a not-to-exceed amount that the SFMTA will reimburse BART for the six-year term of the agreement, and therefore, the proposed resolution should be amended to specify a not-to-exceed amount of \$74,821,040, as shown in Table 4 above.

Because the SFMTA's Adult A Fast Pass program results in an estimated net cost to SFMTA in FY 2013-14 of \$4,516,000, as shown in Table 2 above, and will continue to result in estimated net costs to the SFMTA over the entire six-year agreement, the Budget and Legislative Analyst considers approval of the proposed resolution to be a policy matter for the Board of Supervisors.

RECOMMENDATIONS

1. Amend the proposed resolution to provide for a total not-to-exceed reimbursable amount of \$74,821,040 (see Table 4 above) payable by the SFMTA to BART under the proposed new Fast Pass agreement between the SFMTA and BART.
2. Approval of the proposed resolution, as amended, is a policy decision for the Board of Supervisors.

Item 5 File 14-0093	Department: San Francisco Municipal Transportation Agency (SFMTA)
EXECUTIVE SUMMARY	
<p style="text-align: center;">Legislative Objectives</p> <ul style="list-style-type: none"> • The proposed resolution would approve the (a) First Amendment to the Restated and Amended Towing Agreement and (b) Property Use License for towing, storage and disposal of abandoned and illegally parked vehicles between SFMTA and TEGSCO, LLC, dba San Francisco AutoReturn (AutoReturn). <p style="text-align: center;">Key Points</p> <ul style="list-style-type: none"> • In July of 2005, based on a competitive process, the Board of Supervisors approved an agreement and property use license between SFMTA and AutoReturn to provide towing, storage, and disposal or auction of abandoned and illegally parked vehicles for an initial five-year period from July 31, 2005 through July 31, 2010, with an option to extend for an unspecified term. This agreement was subsequently amended to specify other procedures, increase rates and extend the term through July 31, 2015. • Under the agreement, AutoReturn is responsible for managing a long-term vehicle storage facility and auction area for the towed vehicles. Originally, AutoReturn provided such services on Pier 70, which was leased by the Port to the SFMTA. Because of the Port's plans to develop Pier 70, on October 23, 2012, the Board of Supervisors approved a 20-year lease, with two five-year options to extend, between Prologis and SFMTA for a 556,055 square foot property at 2650 Bayshore Boulevard in Daly City for AutoReturn's towed vehicle operations and SFMTA's signal shop and training facilities <p style="text-align: center;">Fiscal Impact</p> <ul style="list-style-type: none"> • Under the Bayshore lease, SFMTA pays Prologis \$204,137 per month or \$2,449,642 the first year, plus increases of 3% annually and another 4% every five years. AutoReturn currently pays \$150,379 per month in rent to the SFMTA for the Bayshore lease, or \$1,804,548 annually, the same rent AutoReturn previously paid the Port for Pier 70. SFMTA's net cost for the Bayshore lease is \$645,094 (\$2,449,642 less \$1,804,548). • Under the proposed new license agreement, total rent credits of \$168,115, or approximately \$6,226 per month over the 27-month lease term would be deducted by AutoReturn from the monthly rent paid to SFMTA for the Bayshore lease to offset AutoReturn's (a) unanticipated costs to relocate from Pier 70 (\$4,081) and (b) net increased operating expenses at 2650 Bayshore Boulevard (\$2,145). AutoReturn will pay SFMTA a total of \$3,926,870 over the 27-month term of the license agreement. <p style="text-align: center;">Recommendations</p> <ul style="list-style-type: none"> • Amend the proposed resolution to reflect that the subject new License Use Agreement at 2650 Bayshore Boulevard in Daly City would be retroactive from May 1, 2013 through July 31, 2015. • Approve the proposed resolution as amended. 	

MANDATE STATEMENT / BACKGROUND

Mandate Statement

City Charter Section 9.118 requires that contracts, or amendments to contracts with anticipated revenues to the City of \$1,000,000 or more, be subject to Board of Supervisors approval.

Existing San Francisco AutoReturn Agreement with SFMTA

In July of 2005, based on a competitive process, the Board of Supervisors approved an agreement and property use license¹ between the San Francisco Municipal Transportation Agency (SFMTA) and San Francisco AutoReturn (AutoReturn) for AutoReturn to provide towing, storage, and disposal or auction of abandoned and illegally parked vehicles for an initial five-year period from August 1, 2005 through July 31, 2010, with one option to extend for an unspecified term (File 05-1196; Resolution 556-05). On June 12, 2007, the Board of Supervisors approved a First Amendment to this agreement to increase the rates for towing, storage and administrative fees (File 07-0585; Resolution 318-07). On July 20, 2010, the Board of Supervisors approved an amended and restated service agreement and property use license² between SFMTA and AutoReturn to (a) extend the agreement for five years, or from August 1, 2010 through July 31, 2015, (b) establish a new Contract Monitor Fund and Audit Fund, and (c) modify service and reporting procedures (File 10-0796; Resolution 232-10).

Currently, the major tow fees are as follows:

<u>Current Major Tow Fees</u>	<u>FY2014</u>
SFMTA Administrative Tow Fee	\$ 254.00
AutoReturn Tow Fee	218.00 ³
AutoReturn Storage Fee-1st Day	56.25
AutoReturn Storage Fee-2nd Day	65.75

Under the existing agreement with AutoReturn, SFMTA receives administrative fees, referral fees and a fee equaling one percent of AutoReturns' gross revenues. Table 1 below identifies the various fee revenues totaling \$58,982,284 SFMTA has received under the existing AutoReturn agreement during the eight-year period from FY 2005-06 through FY 2012-13.

¹ The property use license was an appendix to the agreement, which was a separate revocable contract between SFMTA and AutoReturn for AutoReturn's use of Seawall Lot 349 on Pier 70 as a long-term vehicle storage lot, office space and auction site.

² As reported by the City Attorney's Office in 2010, because a majority of the proposed modifications to the agreement were to codify practices and procedures that became operational after the first amendment to the agreement, the parties negotiated an amended and restated agreement which incorporated into one document the previously approved original agreement, the previously approved first amendment to the agreement and the proposed modifications, rather than proposing a second amendment to the agreement.

³ Includes a \$24.50 referral fee paid to SFMTA for each vehicle towed.

Table 1: SFMTA Fee Revenues Received Under Existing AutoReturn Agreement

<i>Fiscal Years</i>	<i>SFMTA Administrative Fee</i>	<i>Referral Fee</i>	<i>1% Gross Revenue Fee</i>	<i>Total Revenue</i>
<i>FY 2005-2006</i>	\$3,230,140	\$1,261,905	\$153,739	\$4,645,784
<i>FY 2006-2007</i>	3,309,830	1,332,164	166,903	4,808,897
<i>FY 2007-2008</i>	4,108,025	1,373,579	208,090	5,689,694
<i>FY 2008-2009</i>	4,135,314	1,409,100	216,911	5,761,325
<i>FY 2009-2010</i>	7,229,706	1,227,336	187,087	8,644,129
<i>FY 2010-2011</i>	8,485,983	1,146,828	186,268	9,819,079
<i>FY 2011-2012</i>	8,117,300	1,123,498	186,491	9,427,289
<i>FY 2012-2013</i>	9,042,696	979,811	163,580	10,186,087
<i>Total</i>	\$47,658,994	\$9,854,221	\$1,469,069	\$58,982,284

Ms. Lorraine Fuqua, Contract Administrator for SFMTA advises that the number of vehicles towed each year has steadily declined over the past nine years. As shown in Table 2 below, between FY 2005 and FY 2013, the number of vehicles towed in San Francisco declined from 73,067 to 47,289, a reduction of 25,778 or 35%.

Table 2: Number of Vehicles Towed Annually in San Francisco

FY 2005	FY 2006	FY 2007	FY 2008	FY2009	FY 2010	FY 2011	FY 2012	FY 2013
73,067	69,336	69,139	68,136	67,211	58,622	53,793	51,249	47,289

Under the existing agreement, AutoReturn is also responsible for management of a long-term vehicle storage facility and vehicle auction area for the towed vehicles. Originally, AutoReturn provided such services on a portion of Pier 70, which was leased by the Port to the SFMTA. However, in 2011, the Port selected Forest City Development California, Inc. as part of an overall development project of the Pier 70 Waterfront Site, which necessitated the SFMTA finding another location for long-term vehicle storage and area to auction towed vehicles.

Existing Lease for Storing Towed Vehicles

Because of the Port's plans to develop Pier 70, on October 23, 2012, the Board of Supervisors approved a 20-year lease, with two five-year options to extend, with Prologis, on behalf of the SFMTA, for a 556,055 square foot (12.72 acre) property at 2650 Bayshore Boulevard in Daly City for the SFMTA's towed vehicle operations and other SFMTA uses, including SFMTA's signal shop and employee training facilities (File 12-0904; Resolution 365-12).

According to Mr. Steven Lee, Manager of Financial Services for SFMTA, between October 2012, when the Board of Supervisors approved the Bayshore Boulevard lease and April of 2013, Prologis completed the necessary SFMTA tenant improvements on the Bayshore site. In May 2013, the SFMTA exercised its right to move the long-term vehicle storage facilities from Pier 70 to the 2650 Bayshore Boulevard location. Under the Bayshore lease, the SFMTA pays Prologis \$204,137 per month or \$2,449,642 for the first year, plus 3% annual increases, plus an additional 4% increase every five years.

AutoReturn is currently paying \$150,379 per month in rent to the SFMTA for their leased space on the Bayshore site, or \$1,804,548 annually, which reflects the same monthly rent that AutoReturn previously paid to the Port for leasing the Pier 70 facilities. SFMTA's net annual rent cost for the Bayshore lease is \$645,094 (\$2,449,642 total rent less \$1,804,548 paid by AutoReturn). AutoReturn's monthly rent payments to SFMTA are in addition to the SFMTA revenues shown in Table 1 above.

DETAILS OF PROPOSED LEGISLATION

The proposed resolution would approve the First Amendment to the Amended and Restated Towing Agreement and a new Property Use License Agreement (Appendix H) for towing, storage and disposal of abandoned and illegally parked vehicles between the City, on behalf of the SFMTA and San Francisco AutoReturn (AutoReturn).

The term of the First Amendment to the agreement between SFMTA and AutoReturn would remain the same as the existing agreement, from August 1, 2010 through July 31, 2015. According to Mr. Lee, the SFMTA will be issuing a Request for Proposal (RFP) by the end of September 2014 for a new towing, storage and disposal of abandoned and illegally parked vehicle agreement, to commence August 1, 2015. The term of the new Property Use License Agreement (Appendix H) for the leased premises at 2650 Bayshore Boulevard would be retroactive to May 1, 2013, when SFMTA and AutoReturn moved into the Bayshore space, through July 31, 2015.

The proposed resolution should therefore be amended to reflect that the provisions in the subject new Property Use License Agreement would be retroactive back to May 1, 2013. Mr. Lee advises that the proposed resolution was delayed because although AutoReturn moved into the Bayshore Boulevard leased space in May 2013, SFMTA's signal shop did not fully move into the Bayshore Boulevard space until December 2013. As a result, SFMTA could not determine the exact square footage of space to be leased under the proposed license agreement to AutoReturn until January of 2014, after SFMTA had fully moved into the Bayshore Boulevard space.

The proposed First Amendment would approve the following major changes:

- Amend the language in the existing agreement to reflect the new leased facility at 2650 Bayshore Boulevard instead of the previous Pier 70 leased location for the towing, storage and auction of vehicles;

- Delete Appendix C, which is a Memorandum of Understanding between the Port and SFMTA, which addressed the previous lease provisions for Pier 70;
- Delete Appendix D, which is the license agreement between the City and AutoReturn regarding the previous Pier 70 lease;
- Modify the financial assurance requirements from the current \$1,000,000 Letter of Credit and \$1,000,000 Performance Bond to a single \$2,000,000 Performance Bond, as requested by AutoReturn; and
- Add Appendix H, which is a new license agreement between the City and AutoReturn for the 2650 Bayshore Boulevard leased location shown in the map attached to this report. A summary of the new major license agreement provisions are summarized in Table 3 below.

Table 3: SFMTA and AutoReturn's New License Agreement Major Provisions

Location	2650 Bayshore Boulevard, Daly City
Square Feet (sf)	330,771 sf or 59% of 556,055 sf total
Permitted Uses	Parking for storage of vehicles, auction and office space
Term	May 1, 2013 through July 31, 2015 (27 months)
Monthly Base Rent Payable by AutoReturn to SFMTA	\$150,379
Rate per sf/month	\$0.45
Annual Adjustment to Base Rent	On August 1, 2014, increase of 2.549% or \$154,212
Rent Credits	\$6,226 x 27 months (\$168,115)
Utilities and Security	Paid by AutoReturn

On April 1, 2014 the SFMTA Board of Directors approved the proposed First Amendment to the Amended and Restated Towing Agreement and the new Property Use License between SFMTA and AutoReturn (SFMTA Resolution 14-050).

FISCAL IMPACTS

Under the proposed new license agreement, which is Appendix H to the Agreement, total rent credits of \$168,115, or approximately \$6,226 per month over the 27-month lease term from May 1, 2013 through July 31, 2015 would be deducted by AutoReturn from the base monthly rent payments paid to SFMTA for the 2650 Bayshore Boulevard leased premises to

compensate AutoReturn for (a) unanticipated costs to relocate from Pier 70 (\$4,081⁴) and (b) net increased operating expenses at 2650 Bayshore Boulevard (\$2,145⁵).

As summarized in Table 4 below, SFMTA is projected to receive a total of \$3,926,870 in rent payments from AutoReturn, net of the \$168,115 in rent credits, over the 27-month term of the proposed license agreement between SFMTA and AutoReturn.

⁴ AutoReturn's unanticipated one-time costs to relocate from Pier 70 to the Bayshore Boulevard site totaled \$110,191, including (a) \$28,937 to tow over 1,200 vehicles, (b) \$24,819 to provide additional security at Pier 70 through June 30, 2013, (c) \$10,111 to reimburse AutoReturn employees for overtime to complete the move and setup the new facility, and (d) \$46,323 to install a surveillance and access gate control system for SFMTA. The total one-time cost of \$110,191 divided by 27 months equals \$4,081.

⁵ AutoReturns net increased monthly operating expenses of \$2,145 are primarily due to (a) additional \$5,000 costs for the time and mileage to tow vehicles and cab fares to the more distant Bayshore Boulevard site, additional forklift requirements by Daly City, and janitorial expenses, (b) offset by decreased \$2,855 expenses for mobile office rents at Pier 70, reduced insurance and elimination of valet services on auction days.

Table 4: 27-Month Revenue Projections of Rent to be Paid by AutoReturn to SFMTA Under the Proposed License Agreement

	Current Monthly Rent	Rent Credit	Net New Monthly Rent
May 2013	\$146,631	\$6,226	\$140,405
June 2013	\$146,631	\$6,226	\$140,405
July 2013	\$146,631	\$6,226	\$140,405
August 2013	\$150,379	\$6,226	\$144,153
September 2013	\$150,379	\$6,226	\$144,153
October 2013	\$150,379	\$6,226	\$144,153
November 2013	\$150,379	\$6,226	\$144,153
December 2013	\$150,379	\$6,226	\$144,153
January 2014	\$150,379	\$6,226	\$144,153
February 2014	\$150,379	\$6,226	\$144,153
March 2014	\$150,379	\$6,226	\$144,153
April 2014	\$150,379	\$6,226	\$144,153
May 2014	\$150,379	\$6,226	\$144,153
June 2014	\$150,379	\$6,226	\$144,153
July 2014	\$150,379	\$6,226	\$144,153
August 2014	\$154,212	\$6,226	\$147,986
September 2014	\$154,212	\$6,226	\$147,986
October 2014	\$154,212	\$6,226	\$147,986
November 2014	\$154,212	\$6,226	\$147,986
December 2014	\$154,212	\$6,226	\$147,986
January 2015	\$154,212	\$6,226	\$147,986
February 2015	\$154,212	\$6,226	\$147,986
March 2015	\$154,212	\$6,226	\$147,986
April 2015	\$154,212	\$6,226	\$147,986
May 2015	\$154,212	\$6,226	\$147,986
June 2015	\$154,212	\$6,226	\$147,986
July 2015	\$154,212	\$6,226	\$147,986
Total	\$4,094,985	\$168,115*	\$3,926,870

*Due to rounding.
Source: SFMTA

The proposed new license agreement with AutoReturn reflects the same monthly rent paid by AutoReturn to the Port under the Pier 70 lease. Mr. Lee advises that although the square feet was reduced from 519,328 square feet at Pier 70 to 330,771 square feet at the Bayshore facility, a reduction of 188,557 square feet or 36%, the rate per square foot increased from \$0.29 per month to \$0.45 per month, an increase of \$0.16 or 55%. The significantly higher per square foot monthly rate at the Bayshore Boulevard site reflects the significantly improved

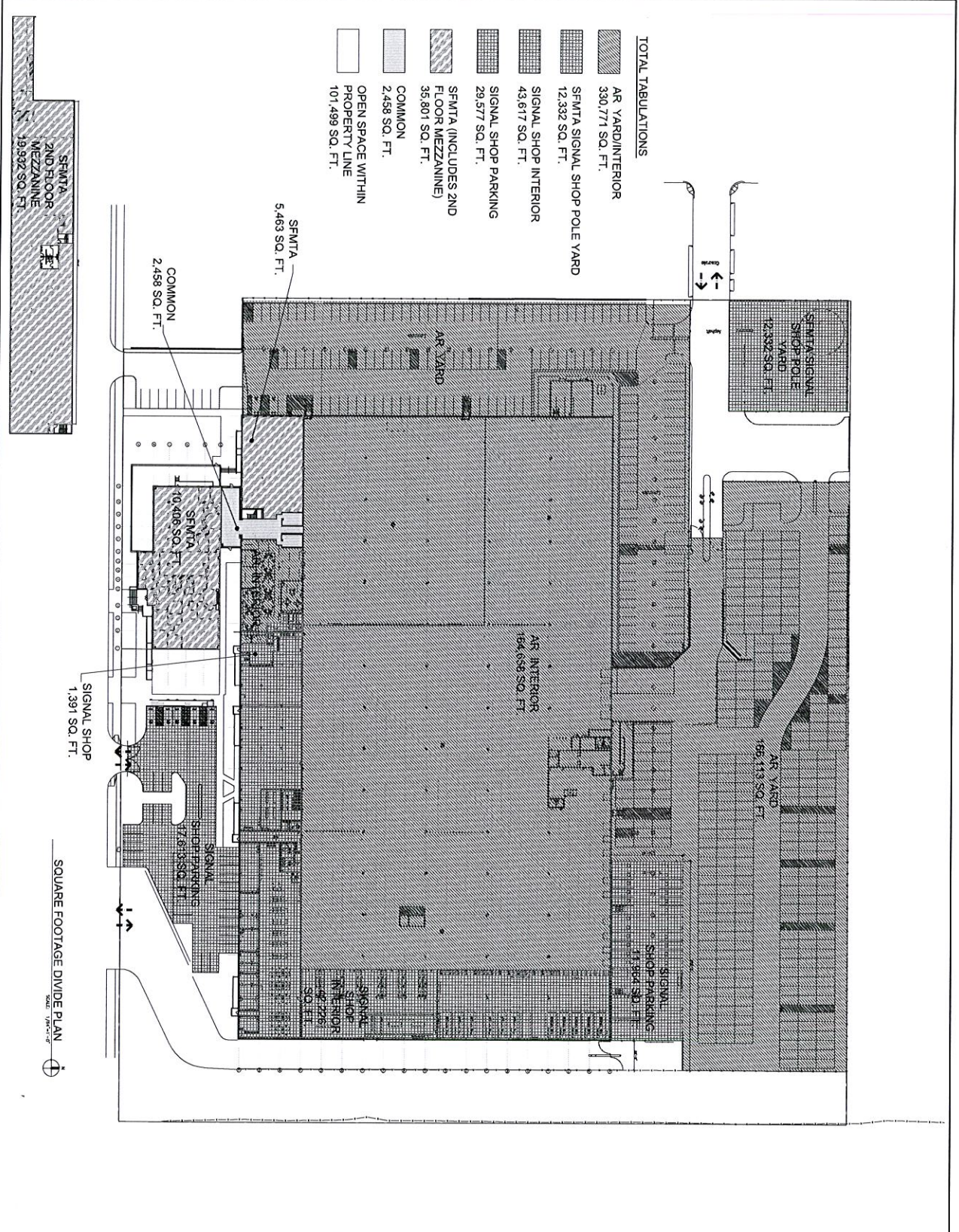
facilities, including new permanent office space and available public auction space for AutoReturn.

As noted above, the proposed amendments also include modifications to the financial assurance requirements from the current \$1,000,000 Letter of Credit and \$1,000,000 Performance Bond to a single \$2,000,000 Performance Bond, as requested by AutoReturn. According to Mr. Lee, the existing \$1,000,000 Letter of Credit was required by the Port due to the (a) proximity of Pier 70 to the Bay, (b) potential for a major environmental incident, and (c) an abundance of caution. Mr. Lee notes that Prologis, the landlord at the new 2650 Bayshore Boulevard lease location does not require a Letter of Credit and the higher \$2,000,000 Performance Bond matches the SFMTA's lease insurance requirements. Furthermore, Mr. Lee notes that the proposed increased \$2,000,000 Performance Bond provides better risk mitigation for the City because the AutoReturn contract is a performance-based service agreement.

RECOMMENDATIONS

1. Amend the proposed resolution to reflect that the subject new License Use Agreement at 2650 Bayshore Boulevard in Daly City would be retroactive from May 1, 2013 through July 31, 2015.
2. Approve the proposed resolution as amended.

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<p>SP-01</p> <p>DATE: 10/11/2011</p> <p>BY: [Signature]</p> <p>CHECKED: [Signature]</p> <p>SCALE: 1/8" = 1'-0"</p>	<p>TITLE SHEET</p> <table border="1" style="width: 100%; border-collapse: collapse;"> <thead> <tr> <th>DATE</th> <th>REVISION</th> <th>DATE</th> <th>REVISION</th> </tr> </thead> <tbody> <tr><td> </td><td> </td><td> </td><td> </td></tr> <tr><td> </td><td> </td><td> </td><td> </td></tr> <tr><td> </td><td> </td><td> </td><td> </td></tr> <tr><td> </td><td> </td><td> </td><td> </td></tr> <tr><td> </td><td> </td><td> </td><td> </td></tr> <tr><td> </td><td> </td><td> </td><td> </td></tr> <tr><td> </td><td> </td><td> </td><td> </td></tr> <tr><td> </td><td> </td><td> </td><td> </td></tr> <tr><td> </td><td> </td><td> </td><td> </td></tr> <tr><td> </td><td> </td><td> </td><td> </td></tr> </tbody> </table>	DATE	REVISION	DATE	REVISION																																									<p>Architect: [Signature]</p> <p>Structural: [Signature]</p> <p>Mechanical: [Signature]</p> <p>Electrical: [Signature]</p> <p>Plumbing: [Signature]</p> <p>Fire Protection: [Signature]</p> <p>Site: [Signature]</p> <p>Interior: [Signature]</p> <p>Exterior: [Signature]</p> <p>General Contractor: [Signature]</p> <p>Subcontractors: [List]</p> <p>Scale: 1/8" = 1'-0"</p> <p>Project: [Project Name]</p> <p>Sheet: [Sheet Number]</p>	<p>WARE MALCOMB</p> <p>Leading Design for Commercial Real Estate</p>
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<p>Item 8 File 14-0448</p>	<p>Department: Mayor’s Office of Housing and Community Development</p>
<p>EXECUTIVE SUMMARY</p>	
<p style="text-align: center;">Legislative Objectives</p> <ul style="list-style-type: none"> • The proposed resolution would (1) authorize the execution of a Transfer Agreement between the City and 1500 Page Street, LLC, the legal entity formed by Pacific Institute/AgeSong (AgeSong), for the transfer to the City from AgeSong of land at 1500 Page Street for the development of 16 studios for developmentally disabled adults and a one-bedroom manager’s unit; (2) authorize the execution and performance of an option to ground lease and a ground lease between the City and Mercy Housing California 57 (Mercy Housing), a California limited partnership; (3) adopt findings under the California Environmental Quality Act (CEQA); and (4) adopt findings that the acquisition of the property by the City and the associated ground lease is consistent with the City’s General Plan and Eight Priority Policies of City Planning Code Section 101.1. <p style="text-align: center;">Key Points</p> <ul style="list-style-type: none"> • 1500 Page Street is a 38-bed Single Resident Occupancy (SRO) building. In 2006, the Mayor’s Office of Housing and Community Development (MOHCD) awarded a loan to AgeSong to purchase the property and pay predevelopment costs to rehabilitate the building into supportive housing for chronically homeless individuals. Because AgeSong was unable to secure additional financing for the rehabilitation of the building, in 2011, the Citywide Affordable Housing Loan Committee approved use of the site for affordable housing for developmentally disabled adults with Mercy Housing California Special Needs (Mercy Housing), a non-profit public benefit corporation, as the project sponsor. • The City would enter into a Transfer Agreement for transfer of the property at 1500 Page Street from AgeSong to the City. In exchange, the City would forgive outstanding loans to AgeSong and pay the balance of a private loan obtained by AgeSong. • The City would enter into an option to ground lease with Mercy Housing, in which Mercy Housing would be required to rehabilitate the existing building at 1500 Page Street to create 16 housing units for developmentally disabled adults and one manager’s unit. <p style="text-align: center;">Fiscal Impact</p> <ul style="list-style-type: none"> • Under the proposed Transfer Agreement, the City would forgive the outstanding balances of loans previously issued by the City to AgeSong (\$3,721,563) and pay the balance of the private loan obtained by AgeSong (\$836,706), totaling \$4,558,269. In exchange, AgeSong would transfer the property at 1500 Page Street to the City, with a value of \$1,500,000, resulting in a net loss to the City of \$3,058,269. This loss is \$1,594,821 or 34% less than the loss of \$4,653,090 that the City would incur by not entering into the Transfer Agreement for 1500 Page Street, as shown in Table 7 below. Therefore, the Budget and Legislative Analyst recommends approval of the proposed resolution. 	

- Mercy Housing's project costs for rehabilitating the existing facility at 1500 Page Street to create 16 units for developmentally disabled adults and one managers unit (totaling 17 units) are \$10,324,880, or \$607,346 per unit, which is 49% higher than MOHCD's average cost of \$408,984 per unit. According to discussions with MOHCD staff, the costs of \$607,346 per unit are higher than MOHCD's average costs because the project is rehabilitating an existing facility rather than building a new facility, and the design of the housing units must fit within the existing building envelope, resulting in less efficient use of space. Because of the high per unit project costs, the Budget and Legislative Analyst recommends requesting MOHCD to report to the Board of Supervisors on (1) the reliability of financing sources for the project; alternative financing that would be available if the project is not awarded low income housing tax credits or other major sources of financing; and the impact of the 1500 Page Street and other pipeline projects on the City's access to future low income housing tax credits; and (2) MOHCD's procedures to manage project costs once the project receives financing.

Policy Considerations

- The City will incur a net loss of \$3.0 million because the original supportive housing project to be developed by AgeSong was not financially feasible. Because the initial AgeSong project was not considered a typical affordable housing project, it was not eligible to obtain standard MOHCD development financing. Instead, AgeSong had to rely on unreliable, outside private financing which never materialized, leading to the project's dissolution. MOHCD staff has acknowledged that the AgeSong project should have been more thoroughly vetted through a more rigorous loan approval process and that a back-up financing plan should have also been in place due to the project's inability to retain standard MOHCD funding sources.
- Additionally, the original 2006 appraisal overvalued the property at \$2,900,000 because it did not account for the SRO replacement obligation. Based on this appraisal, AgeSong paid \$2,850,000 for the property. A subsequent appraisal in February 2014 valued the property at \$1,500,000, or \$1,350,000 less than the \$2,850,000 purchase price.

Recommendations

- Amend the resolution to request MOHCD to report back to the Board of Supervisors during the June 2014 budget review on (a) the reliability of financing sources for the 1500 Page Street project; alternative financing that would be available if the project is not awarded low income housing tax credits or other major sources of financing; and the impact of the 1500 Page Street and other pipeline projects on the City's access to future low income housing tax credits; and MOHCD's procedures to manage project costs once the project receives financing; and (b) procedures to vet the accuracy of appraisals prior to purchasing property, and further mitigate the risks to MOHCD as the gap lender for affordable housing, such as requiring a feasible back-up financing plan.
- Approve the proposed resolution as amended.

MANDATE STATEMENT/ BACKGROUND

Administrative Code Section 23.1 requires Board of Supervisors' approval of all resolutions and ordinances approving real property transactions. Administrative Code Section 23.4 requires Board of Supervisors' approval of the granting of real property before the Director of Real Estate can accept the deed to the property.

Charter Section 9.118 requires Board of Supervisors' approval for any lease of real property for a period of ten years or more.

BACKGROUND

1500 Page Street is a three-story, residential building with 38 bedrooms that was previously leased by the Department of Public Health (DPH) as a placement site for mental health patients. The building has been vacant since 2007 when DPH relocated its patients in order to rehabilitate the building. In 2006, the Mayor's Office of Housing and Community Development (MOHCD) issued a Notice of Funding Availability (NOFA) to provide acquisition and predevelopment funds to purchase 1500 Page Street and develop supportive housing for chronically homeless individuals. Pacific Institute/AgeSong (AgeSong) was selected and established a separate entity, 1500 Page Street, LLC, under which to acquire the property and develop the project. In 2010, after acquiring 1500 Page Street and preparing for the property's rehabilitation, AgeSong was unable to secure outside, private financing to develop the project rendering the project infeasible.

In 2011, the Citywide Affordable Housing Loan Committee approved reprogramming the site for affordable housing for developmentally disabled adults with Mercy Housing California Special Needs (Mercy Housing), a non-profit public benefit corporation, as the project sponsor and The Arc of San Francisco as the service provider. According to MOHCD staff, MOHCD selected Mercy Housing as the project sponsor without issuing a NOFA because Mercy Housing was in the process of applying to U.S. Housing and Urban Development (HUD) for capital and operating funding to develop housing for developmentally disabled adults, and needed a development site.

DETAILS OF PROPOSED LEGISLATION

The proposed resolution would (1) authorize the execution of a Transfer Agreement between the City and 1500 Page Street, LLC (the legal entity formed by AgeSong) for the transfer from AgeSong to the City of land at 1500 Page Street for the development of 16 studios for developmentally disabled adults and a one-bedroom manager's unit; (2) authorize the execution and performance of an option to ground lease and enter into a ground lease between the City and Mercy Housing California 57 (Mercy Housing), a California limited partnership formed by Mercy Housing California Special Needs; (3) adopt findings under the California Environmental Quality Act (CEQA); and (4) adopt findings that the acquisition of the property by the City and the associated ground lease is consistent with the City's General Plan and Eight Priority Policies of City Planning Code Section 101.1.

Terms of the Transfer Agreement

According to the February 13, 2014 appraisal by MacLane and Company, Inc., commissioned by Mercy Housing and reviewed by the City's Director of Real Estate, 1500 Page Street has an appraised value of \$1,500,000 which is \$1,350,000 or 47% less than the \$2,850,000 that AgeSong paid to acquire the property in 2007.¹

Under the proposed Transfer Agreement between the City and AgeSong, AgeSong would transfer approximately 5,400 square feet of land at 1500 Page Street to the City and all improvements and fixtures including the 15,782 square foot, three-story building and two-parking spaces located on the land.

AgeSong will transfer the property at 1500 Page Street to the City in exchange for (1) the City paying the outstanding balance of AgeSong's senior acquisition loan from East West Investment Inc., (East West) at \$836,706; and (2) forgiving the principal and interest of an acquisition and predevelopment loan of \$2,080,950, of which \$230,950 was used for predevelopment and \$1,850,000 for acquisition, and a predevelopment loan of \$1,057,400 previously made by the City to AgeSong totaling \$4,558,269 as shown in Table 1 below.

Table 1: Balance of Loans Made by City and East West to AgeSong from 2007 to 2009

Date of Loan	Funding Source		Principal Balance	Interest Accrued as of May 1 st 2014	Total Loan Forgiveness/Senior Loan Repayment in Exchange for Land Transfer
<u>Citywide Affordable Housing Loan Committee:</u>					
March 2007	Federal	HOME Loan	\$2,080,950	\$448,366	\$2,529,316
March 2009	Local	Hotel Tax Set Aside	<u>1,057,400</u>	<u>134,847</u>	<u>1,192,247</u>
		Subtotal	3,138,350	583,213	3,721,563
<u>Private Loan:</u>					
March 2007	Private	East West Loan	836,706	0	836,706
Total			\$3,975,056	\$583,213	\$4,558,269

Under the terms of the Transfer Agreement, the City will pay the cost of the title, escrow and recording fees, and transfer taxes which are estimated to be \$18,091. According to Ms. Ruby Harris, MOHCD Project Manager, an U.S. Department of Housing and Urban Development (HUD) HOME Investment Partnerships Program (HOME) grant will be used to pay the aforementioned closing costs. AgeSong will be responsible for any other escrow costs and real estate taxes up to the closing date, June 30, 2014.

¹ The September 14, 2006 appraisal report valued the property at \$2,900,000. The subsequent appraisal report in February 2014 notes that the decrease in the value of the property is due to: (1) the cost to renovate the building exceeds the value of the building leaving value only in the land; and (2) the building is registered as 38 Single Room Occupancy Units (SRO) which typically provide affordable rental housing for solo occupancy and is generally rented to lower income individuals. Chapter 41 of the San Francisco Administrative Code requires a one-to-one replacement if any SRO units are lost or converted which reduces the fair market value of the site. The Board of Supervisors approved a Special Use District for the property on February 11, 2014 allowing the 38 SRO units to be replaced by less than the required one-to-one replacement as long as it remains affordable housing.

**Terms of the Option to Ground Lease Agreement and
Ground Lease Agreement**

Mercy Housing California has formed a limited partnership, Mercy Housing California 57, LP (Mercy Housing), which will enter into an option for a ground lease agreement with the City at 1500 Page Street. The initial term of the option to ground lease agreement will commence on the date the agreement is signed and will end on June 30, 2015, with an option to extend for one additional six-month period. During the option to ground lease agreement term, Mercy Housing and City staff agree to negotiate a ground lease agreement for 1500 Page Street. If a ground lease agreement is executed prior to June 30, 2015, the option to ground lease agreement term will be terminated early and replaced with the ground lease.

According to Ms. Harris, Mercy Housing must have entered into a ground lease or execute an option to ground lease for 1500 Page Street in order to apply for a low income tax credit allocation by the July 1, 2014 application deadline. Because the City and Mercy Housing could not draft and obtain the Board of Supervisor’s approval of a ground lease agreement by the deadline, an option to ground lease agreement that included the forthcoming ground lease agreement terms has been proposed instead. Mercy Housing is proposing to apply for \$6,617,344 in low income housing tax credits which would finance approximately 64% of the total construction costs of 1500 Page Street project.

Approval of the proposed option to ground lease agreement by the Board of Supervisors would also authorize the Director of Real Estate and the Director of MOHCD to execute the subsequent ground lease agreement without returning to the Board of Supervisor’s for approval.² The terms of the proposed ground lease are shown in Table 2 below.

Table 2: Proposed Ground Lease Terms between the City and Mercy Housing

Initial Lease Term	75 years
Option to Extend the Lease	24 years
Total Possible Term	99 years
Annual Rent Payable by Mercy Housing to the City	\$1
Rent Adjustments	Adjusted every 15 years to 10% of appraised land value or consistent with HUD Section 811 program regulations
Construction, Operations, Maintenance, Insurance, Taxes and Licenses, Utilities and Other Operating Costs	Paid by Mercy Housing California 57, LP
Ownership	The City will own the land and Mercy Housing California 57, LP will own all improvements which will be transferred to the City at the end of the term. Mercy Housing is permitted to secure loans against the property pending MOHCD approval.

² The ground lease agreement would return to the Board of Supervisor’s for approval only if there are any material changes to the terms that would negatively impact the City as determined by the Director of the MOHCD.

Base Rent

Under the proposed ground lease terms, Mercy Housing will pay the City annual rent of 10% of the appraised land value consisting of \$1 in base rent; the balance will consist of residual rent derived from the project's residual income at the end of the year after all operating expenses and required reserves have been paid. For as long as the project receives a HUD Section 811 Project Rental Assistant Contract (PRAC) program subsidy, the project will not be required to pay residual rent to be consistent with the program requirements. One requirement of the HUD Section 811 PRAC subsidy is that the subsidy can only be used to pay for the necessary and reasonable operating costs of the units not met from tenant incomes and cannot be used for debt service of any financing or cash flow distributions to owners or other lenders; therefore there would be no residual income to pay any residual rent.

Under MOHCD's Residual Receipts Policy, affordable housing developers and operators are only required to pay residual rent and principal and interest on outstanding loans if the affordable housing development generates sufficient surplus cash to make these payments.³ Because Mercy Housing's project cannot generate a cash flow pursuant to HUD regulations, residual rent will not be required.

The Mercy Housing project will receive approximately \$135,709 a year from the HUD Section 811 PRAC program to subsidize 15 units for a 20-year term with options to extend.⁴ In the event that the HUD Section 811 PRAC program is not extended, Mercy Housing's annual rent will revert back to the original ground lease terms.

Required Property Uses

Pursuant to the proposed ground lease terms, the property can only be used for affordable housing with maximum income levels for tenants set at no greater than 50% of area median income which is approximately \$34,000 in annual income for an individual. Mercy Housing plans to rehabilitate the three-story building at 1500 Page Street into 16 studio units of affordable housing for developmentally disabled adults and one, one-bedroom manager's unit, totaling 17 units. Mercy Housing has partnered with The Arc of San Francisco who will provide on-site services to future 1500 Page Street tenants.

Renovation of the Building

Although the proposed option to ground lease agreement does not include a timeline for the renovation of the affordable housing project, MOHCD and Mercy Housing developed the project schedule shown in Table 3 below for their report to the Citywide Affordable Housing

³ According to the Residual Receipts Policy, MOHCD requires repayment of loans to the extent that such repayment is feasible and does not jeopardize the long-term affordability or maintenance of safe and secure housing for its residents.

⁴ Mercy Housing originally applied for the HUD Section 811 affordable housing subsidy for 15 units; however, the project changed to 16 units after receiving the award. Therefore, 15 units will be subsidized and the 16th unit will be restricted to 50% AMI rent levels, or approximately \$870 per month. The manager's unit will be unrestricted.

Loan Committee dated April 4, 2014. The building at 1500 Page Street is expected to be completed and 95% occupied by February 2016.

Table 3: Timeline for Renovation and Occupancy of 1500 Page Street

Performance Milestone	Estimated or Actual Date
Selection of development team by Mercy Housing	November 2011 through May 2013
CEQA review and General Plan referral	December 2013
Other planning, design, permitting, and preconstruction	October 2013 through August 2014
Site acquisition by the City	June 1, 2014
Construction commencement	December 2014
Substantial completion of construction	December 2015
Certificate of Occupancy	December 2015
95% occupancy of units	February 2016

FISCAL IMPACT

Loans Issued by the City and East West Investment, Inc. to AgeSong

The City and East West Investment, Inc. (East West) previously issued loans to AgeSong for the acquisition and predevelopment of 1500 Page Street to develop supportive housing, with outstanding principal and interest of \$4,558,269 as of May 1, 2014, as shown in Table 1 above.

In the April 4, 2014 meeting of the Citywide Affordable Housing Loan Committee, the Committee approved forgiving \$3,721,563 of principal and interest on loans to AgeSong as payment for the land at 1500 Page Street and approved paying off the remaining \$836,706 balance from East West for a total loan forgiveness and East West repayment of \$4,558,269 for AgeSong and a remaining loan balance of \$0. According to Ms. Harris, funds received by the City from HUD's HOME Investment Partnerships Program (HOME) will be used to pay off the East West loan.

According to Ms. Harris, the City is paying off the East West loan because if AgeSong defaults on its loan payment, East West will likely foreclose on the property. MOHCD is currently negotiating a reduction of the East West loan balance; however, MOHCD believes that this reduction is unlikely due to East West's senior loan status and the fact that East West could fully recoup the outstanding loan balance through foreclosure.

Loans to Mercy Housing

The Citywide Affordable Housing Loan Committee has also issued predevelopment loans to Mercy Housing for the development of housing at 1500 Page Street for developmentally disabled adults, as shown in Table 4 below.

Table 4: Predevelopment Loans Issued to Mercy Housing for 1500 Page Street

	Principal Loan Balance	Interest	To be Forgiven by the City	Remaining
Loans issued to Mercy Housing in 2013	\$ 911,867	\$19,660	(\$175,589)	\$755,938
Loans issued to Mercy Housing in 2014	916,375	0	0	916,375
Total	\$1,828,242	\$19,660	(\$175,589)	\$1,672,313

The following are the remaining loan balances owed by Mercy Housing to the City for predevelopment and development activities for 1500 Page Street:

- **\$755,938** HUD HOME program loan issued by the City to Mercy Housing in April 2013 to pay for the project's predevelopment costs, which has a 48-month term and bears 3% interest. The original loan amount was \$911,867, of which \$175,589 was used by Mercy Housing to pay AgeSong's outstanding mortgage, insurance and other property costs, and will be forgiven by the City.

On April 4, 2014, the Citywide Affordable Housing Loan Committee approved up to \$450,000 of Mercy Housing's remaining \$755,938 predevelopment loan be converted to a permanent loan and remain in the project with MOHCD's standard loan terms, a 55-year term bearing 3% interest, in order to finance the project's development.

- **\$916,375** HUD HOME program loan issued by the City consisting of a \$320,000 bridge loan for project development and an additional \$596,375 predevelopment loan. The \$320,000 bridge loan was issued in anticipation of the project being awarded private Affordable Housing Program (AHP)⁵ funds next year, and has a 24-month term and bears 3% interest. The \$596,375 predevelopment loan has a 55-year term and bears 3% interest and will remain in the project as a permanent loan to help finance the development of the project, which was also approved by the Citywide Affordable Housing Loan Committee on April 4, 2014. These loans will not be provided to Mercy Housing until the ground lease is executed, as the loans will be recorded against the property; therefore no interest has accrued.

Sources and Uses of Funds to Rehabilitate 1500 Page Street

Estimated project costs to rehabilitate 1500 Page Street are \$10,324,880. Mercy Housing's available funding sources total \$10,341,519 which is \$16,639 more than the estimated project costs. Table 5 below shows these various funding sources and uses for Mercy Housing's 1500 Page Street project.

⁵ Affordable Housing Program (AHP) funds are private funds administered by the Federal Home Loan Bank.

Table 5: Sources and Uses of Funds

Sources	
<u>City Loans to Mercy Housing</u>	
2013 Predevelopment Loan	\$450,000
2014 Predevelopment Loan	596,375
Subtotal	1,508,242
<u>Non-City Sources to Mercy Housing</u>	
Tax Credit Equity	6,617,344
HUD 811 Capital Award	2,347,800
General Partner Equity	10,000
AHP Loan	320,000
Subtotal	9,295,144
Total Sources	\$10,341,519
Uses	
<u>Initial Costs</u>	
Closing and other costs	\$ 211,620
Subtotal, Initial Costs	673,487
<u>Planning, Permitting, Design, and Related Project Costs</u>	
Architecture and Engineering	662,505
Financing Costs	320,234
Legal Costs	50,000
Other Planning, Permitting, and Related Costs	488,882
Contingency (10.6% of planning, permitting, design and related project costs)	162,254
Subtotal	1,683,875
<u>Construction Costs</u>	
Construction Costs	5,760,820
Contingency (15% of planning, permitting, design and related project costs) ^a	863,948
Subtotal	6,624,768
<u>Reserves and Other Costs</u>	
Reserves	478,065
Developer Costs	1,326,552
Subtotal	1,804,617
Total Uses	\$10,324,880

^a Construction contingency is 15% consistent with MOHCD's loan underwriting guidelines; however, Mercy Housing has requested to reduce its construction contingency to 10% at the start of construction for the purpose of keeping costs low for its other financing requirements. There is no bid contingency as Mercy Housing anticipates a bid price that will not exceed the construction contingency. MOHCD will not approve the reduction of the construction contingency until the project has been bid out and construction commences.

The average cost per unit for constructing the 1500 Page Street affordable housing project for developmentally disabled adults is \$607,346⁶, which is 49% higher than MOHCD's average of \$408,984 per unit. According to discussions with MOHCD staff, the costs of \$607,346 per unit are higher than MOHCD's average costs because the project is rehabilitating an existing facility rather than building a new facility, and the design of the housing units must fit within the

⁶ Total estimated project costs are \$10,324,880 for 17 studio units, or \$607,346 per studio unit.

existing building envelope, resulting in less efficient use of space. According to Ms. Harris, while the cost per unit is high on a per unit basis, on a per square foot basis the project cost is \$739 per square foot, which is reasonable compared to project costs of comparable facilities of \$731 per square foot. Because of the high per unit project costs, the Budget and Legislative Analyst recommends requesting MOHCD to report to the Board of Supervisors on (1) the reliability of financing sources for the project; alternative financing that would be available if the project is not awarded low income housing tax credits or other major sources of financing; and the impact of the 1500 Page Street and other pipeline projects on the City's access to future low income housing tax credits; and (2) MOHCD's procedures to manage project costs once the project receives financing.

Annual Operating Costs

Based on MOHCD's projected annual operating income and expenses for 1500 Page Street, as shown in Table 6 below, there will be a \$0 cash flow at the end of each program year consistent with HUD's Section 811 PRAC program affordable housing subsidy requirements.

Table 6: Projected Annual Operating Income and Expenses

Income	
Tenant Rents	\$57,600
Tenant Assistance Payments	135,709
Laundry and Vending	1,000
5% Vacancy	(2,880)
Total	\$191,429
Operating Expenses	
Management Fee	\$12,480
Staff Salaries and Benefits	16,150
Administration	16,516
Utilities, Taxes , Licenses, Insurance	68,333
Maintenance and Repair	31,300
Supportive Services	13,650
Total	\$158,429
Net Operating Income	\$33,000
Uses of Net Operating Income	
Replacement Reserve ^a	33,000
Total Cash Flow	\$0

^a Pursuant to HUD guidelines, replacement reserve funds are set aside into a separate interest accruing account and will be used for the buildings' periodic and more expensive maintenance needs.

POLICY CONSIDERATIONS**The City will incur a net loss of \$3.0 million because the original supportive housing project to be developed by AgeSong was not financially feasible**

According to MOHCD staff, MOHCD is typically able to convert a project that has been determined infeasible into another project and not incur the substantial losses that are projected with AgeSong. MOHCD staff note, however, that the AgeSong project was unique in that: (1) it was a facility with beds as opposed to legal dwelling units making the building ineligible for MOHCD's standard funding resources; and (2) the building has a Single Room Occupancy (SRO) replacement housing obligation. SROs typically provide affordable rental housing for single occupancy and are generally rented to lower income individuals. Chapter 41 of the San Francisco Administrative Code requires a one-to-one replacement if any SRO units are lost or converted which reduces the fair market value of the site.

Because the initial AgeSong project was not considered a typical affordable housing project, it was not eligible to obtain standard MOHCD development financing. Instead, AgeSong had to rely on unreliable, outside private financing which never materialized, leading to the project's dissolution. MOHCD staff has acknowledged that the AgeSong project should have been more thoroughly vetted through a more rigorous loan approval process and that a back-up financing plan should have also been in place due to the project's inability to retain standard MOHCD funding sources.

Additionally, the original 2006 appraisal overvalued the property at \$2,900,000 because it did not account for the SRO replacement obligation. Based on this appraisal, AgeSong paid \$2,850,000 for the property. A subsequent appraisal in February 2014 valued the property at \$1,500,000, or \$1,350,000 less than the \$2,850,000 purchase price.

According to Ms. Harris, MOHCD by design is the gap lender for affordable housing developments and bears the most risk in order to provide affordable housing in the City which otherwise would not be built due to the high cost of real estate. In order to mitigate this risk, MOHCD has recently established a structure where the affordable housing property is purchased by the City and ground leased to a non-profit corporation, similar to the proposed resolution with the City and Mercy Housing. The ground lease structure ensures that the project will stay in the City's control and remain affordable housing despite market fluctuations.

The Budget and Legislative Analyst recommends that the Board of Supervisors request a report from MOHCD on procedures to (1) vet the accuracy of appraisals prior to purchasing property; and (2) further mitigate the risks to MOHCD as the gap lender for affordable housing such as requiring a feasible back-up financing plan.

Transferring 1500 Page Street to the City and forgiving prior loans by MOHCD is the more cost effective option

If the City purchases 1500 Page Street, pays the balance of the private loan by East West Bank to AgeSong, and forgives the City's outstanding loans to AgeSong, the net loss to the City is \$3,058,269. This loss is \$1,594,821 or 34% less than the loss of \$4,653,090 that the City would

incur by not purchasing 1500 Page Street, as shown in Table 7 below. Therefore, the Budget and Legislative Analyst recommends approval of the proposed resolution.

Table 7: Costs to City for Approval or Disapproval of Proposed Resolution

Loans	Cost if Resolution is Approved	Cost if Resolution is Not Approved	Difference
East West Bank	\$836,706	\$0	(\$836,706)
AgeSong Loans	3,721,563	3,721,563	0
Mercy Housing Loan in 2013 ⁷	0	931,527	931,527
1500 Page St. Appraised Value	(1,500,000)	0	1,500,000
Total	\$3,058,269	\$4,653,090	\$1,594,821

RECOMMENDATIONS

1. Amend the resolution to request MOHCD to report back to the Board of Supervisors during the June 2014 budget review on (a) the reliability of financing sources for the 1500 Page Street project; alternative financing that would be available if the project is not awarded low income housing tax credits or other major sources of financing; and the impact of the 1500 Page Street and other pipeline projects on the City's access to future low income housing tax credits; and MOHCD's procedures to manage project costs once the project receives financing; and (b) procedures to vet the accuracy of appraisals prior to purchasing property, and further mitigate the risks to MOHCD as the gap lender for affordable housing, such as requiring a feasible back-up financing plan.
2. Approve the proposed resolution as amended.

⁷ \$911,867 in principal and \$19,660 in interest, as shown in Table 4 above. Because the loan of \$911,867 to Mercy Housing paid for predevelopment costs of the new proposed project, if the project were not to proceed, this amount would be a loss to the City.

Item 10 File 14-0374	Department: San Francisco International Airport (Airport)
EXECUTIVE SUMMARY	
<p>Legislative Objectives</p> <ul style="list-style-type: none"> • The proposed resolution would approve a new lease between Federal Express, Inc. (Federal Express) and the Airport (1) for a term of five years with option to extend the term by five years at the sole discretion of Federal Express, (2) for a 58,676 square feet of office and warehouse space as well as 0.151 acres of ramp space, and (3) at a base rental rate of \$1,363,591. <p>Key Points</p> <ul style="list-style-type: none"> • Federal Express currently leases 133,846 square feet of office and warehouse space at the Airport under an existing three-year lease that expires on May 31, 2014. • Rather than exercise its option to extend the term of the existing lease, Federal Express requests to enter into a new lease with the Airport under different term and provisions. • The new lease is for 58,676 square feet of office and warehouse space and for 0.151 acres of ramp space. According to Mr. Dan Ravina, Airport Senior Property Manager, Federal Express no longer requires 133,846 square feet of space because consumer behaviors have changed and Federal Express no longer needs large amounts of space for storing overnight deliveries. <p>Fiscal Impact</p> <ul style="list-style-type: none"> • Under the subject new lease of the proposed resolution, Federal Express will pay base rent in the first year of \$1,363,591 comprised of (1) \$23 per square foot for 58,676 of office and warehouse space and (2) \$93,000 per acre for 0.151 acres of ramp space. Excluding annual rental increases, the minimum rent over the five-year term of the proposed lease is \$6,817,955. • The rental rate per square foot of office and warehouse space will be adjusted annually in accordance with the Airport's Schedule of Rates and Charges that are approved annually by the Airport Commission. • The rental rate per acre of ramp space will increase annually to reflect inflation as calculated by the Consumer Price Index. <p>Recommendation</p> <ul style="list-style-type: none"> • Approve the proposed resolution. 	

MANDATE STATEMENT / BACKGROUND**Mandate Statement**

City Administrative Code Section 2A.173 authorizes the Airport to negotiate and execute leases of Airport land and space in Airport buildings without undergoing a competitive bid process for leases where the original term does not exceed 50 years.

City Charter Section 9.118(a) states that contracts entered into by a department, board or commission that will generate revenue in excess of \$1 million or any modification of that contract is subject to Board of Supervisors approval.

Background

The Federal Express Corporation (Federal Express) currently leases 133,846 square feet of warehouse and office space at the San Francisco International Airport (Airport) under an existing three-year lease that the Board of Supervisors approved (File 10-0176) in March 2010.

At the time the Board of Supervisors approved the existing lease, the Airport anticipated that the lease would commence on April 1, 2010 and terminate on March 31, 2013. However, according to Mr. Dan Ravina, Airport Senior Property Manager, at the time the Board of Supervisors approved the existing lease, Federal Express had not received confirmation from the Human Rights Commission that it was compliant with the Equal Benefits Ordinance requirements of City Administrative Code Sections 12B.1-12B.6. Federal Express received notification of its compliance in May 2011, which allowed the Airport to commence the lease effective June 1, 2011 through May 31, 2014.

The existing lease between Federal Express and the Airport includes one three-year option to extend the term of the lease at the discretion of Federal Express. According to Mr. Ravina, Federal Express is not exercising that option in order to secure a new lease for less warehouse and office space as well as new ramp space, not included in the existing lease, and under new terms and provisions.

DETAILS OF PROPOSED LEGISLATION

The proposed resolution would approve a new five-year lease with one five-year option between Federal Express and the Airport. The provisions of the proposed lease, which would provide Federal Express with a total of 58,676 square feet of office and warehouse space and 0.151 acres of ramp space, are shown in Table 1 below.

Table 1: Provisions of the Proposed Lease Between Federal Express and the Airport

Term	Five Years From approximately July 1, 2014 through June 30, 2019
Premises	<ul style="list-style-type: none"> • 44,152 square feet of warehouse space <li style="padding-left: 20px;"><u>14,524 square feet of office space</u> 58,676 total square feet • 0.151 acres of ramp space
Options	One five-year option to extend the term at discretion of Federal Express through approximately June 30, 2024
Base Rent	<ul style="list-style-type: none"> • \$1,349,548 annually (\$23.00 per square foot) for office and warehouse space • \$14,043 annually (\$93,000 per acre) for ramp space
Rental Increases	<ul style="list-style-type: none"> • Annual increase for warehouse and office space in accordance with Airport rates and schedules • Annual inflationary increases for ramp space as calculated by the Consumer Price Index (CPI)

Under the proposed resolution, the new lease is for a total of 58,676 square feet in office and warehouse space and for 0.151 acres of ramp space, which is less than the 133,846 square feet of office and warehouse space that Federal Express leases currently. According to Mr. Ravina, Federal Express requested to lease a smaller space because of changing consumer behavior. Federal Express entered into the existing lease with the Airport at a time when consumer demand for overnight shipping was higher, which required Federal Express to use more space for storage and distribution. However, according to Mr. Ravina, consumers are increasingly using standard shipping, which is less-expensive for the consumer and which requires relatively less space for storage and distribution.

FISCAL IMPACT

The proposed resolution would require that, for fiscal year 2014-15 from July 1, 2014 through June 30, 2015, Federal Express must pay annual base rent to the Airport in the amount of \$1,363,591 including \$1,349,548 for the warehouse space and \$14,043 for ramp space as shown in Table 2 below. Such rent would be subject to annual rental increases over the remaining term of the lease, as shown in Table 1 above.

Table 2: Proposed FY 2014-15 Rent

	Proposed Lease
Warehouse and Office	\$58,676
Rental Rate Per Square Foot	\$23
Total Warehouse and Office	\$1,349,548
Ramp (In Acres)	0.151
Rental Rate (Per Acre)	\$93,000
Total Ramp	\$14,043
Total Base Rent	\$1,363,591

Excluding annual rental increases, the minimum rent over the five-year term of the proposed lease is \$6,817,955.

Under the current lease, Federal Express pays \$27.19 per square foot for warehouse and office space, which is \$4.19 more per square foot than the rental rate of \$23.00 per square foot under the proposed new lease. According to Mr. Ravina, the rental rate in the proposed lease is consistent with the current rental rate charged to other airlines under the Airport's FY 2013-14 Schedule of Rates and Charges, which is approved annually by the Airport Commission and which varies year-to-year based on a number of factors including: (1) the projected number of enplaned passengers, (2) the projected amount of aircraft landed weight, and (3) the projected amount of non-airline revenues.

Airport Break Even Policy

As a result of the Airport's "residual rate-setting methodology," a break even policy used by the Airport to determine rental rates, landing fees, and related fees for all Airlines, the proposed resolution approving a new lease between Federal Express and the Airport, in which the rent per square foot is less than under the current lease, will not result in any budgetary shortfall for the Airport. The residual rate-setting methodology is a formula that sets the schedule of all rental rates, landing fees and related fees to a level that ensures that Airport revenues received from all of the airlines at the Airport, plus the non-airline revenues received by the Airport, is equal to the Airport's total costs, including debt service and operating expenditures.

RECOMMENDATION

Approve the proposed resolution.