**CITY AND COUNTY OF SAN FRANCISCO**

**BOARD OF SUPERVISORS**

**BUDGET AND LEGISLATIVE ANALYST**

1390 Market Street, Suite 1150, San Francisco, CA 94102 (415) 552-9292
FAX (415) 252-0461

April 2, 2021

**TO:** Budget and Finance Committee

**FROM:** Budget and Legislative Analyst

**SUBJECT:** April 7, 2021 Budget and Finance Committee Meeting

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## EXECUTIVE SUMMARY

### Legislative Objectives

- The proposed ordinance would allow the Director of Property to (1) amend three leases to forgive rent due between April 2020 through December 2020, totaling $258,215, without adding Administrative and Environmental Code provisions enacted since these leases were last executed, and (2) amend the leases specified as well as other Real Estate Division managed leases meeting certain conditions to allow Real Estate to provide rent forgiveness for rent due between January 2021 and June 2021, without Board of Supervisors approval.

### Key Points

- In response to the pandemic, the City Administrator has waived late charges, fees, and penalties related to unpaid rent for all commercial tenants between April 2020 and December 2020 but required resumption of rent in January 2021. The City Administrator now believes that rent forgiveness, not just rent deferral, is needed for three City tenant businesses and non-profits: (1) New Asia Restaurant, (2) New Conservatory Theater Center, and (3) Stephen M. Paoli.

### Fiscal Impact

- The proposed legislation would result in a known reduction in revenues of $258,215, of which $33,215 are non-dedicated General Fund reductions and $225,000 are dedicated General Fund reductions.

### Policy Consideration

- The proposed ordinance is not intended to apply to the 33 leases under Real Estate's jurisdiction but that are managed by other General Fund departments, including rent collection.
- Unlike similar legislation for rent forgiveness for Port and Recreation and Park tenants, the proposed legislation does not require a determination that the tenant was unable to pay rent due to COVID-19 related impacts.
- Real Estate continues to negotiate repayment of outstanding rent for seven other tenants (estimated at approximately $161,295) or amendments to leases to collect same. According to Real Estate, the remaining tenants who have unpaid rent declined rent forgiveness.

### Recommendations

1. Amend the proposed ordinance to add the following language (a) to Section 4, page 7, line 23, after "City Administrator," "for which the Real Estate Division collects rent," and (b) at page 8, line 10, after "at the discretion of the City Administrator" ", on the condition that a tenant's inability to pay rent is due to negative financial impacts from the COVID-19 pandemic."
2. Approval of the proposed ordinance as amended is a policy matter for the Board of Supervisors.

## MANDATE STATEMENT

City Charter Section 9.118(c) states that (1) any lease of real property for ten or more years, including options to renew, or anticipated to have revenues to the City of $1,000,000 or more, or (2) the modification, amendment, or termination of any such leases, is subject to Board of Supervisors approval.

City Administrative Code Section 23.30 states that the Board of Supervisors can authorize the Director of Property to lease any City-owned property that is not required for the purposes of the Department. The Director of Property is also required to lease City Property for no less than market rent unless authorized by the Board of Supervisors for a “proper public purpose.” This authority excludes month-to-month and year-to-year leases with a fair market rental value of $15,000 or less per month which the Director of Property can enter into without Board approval, per Section 23.31.

## BACKGROUND

On March 27, 2020,[1] the City Administrator issued a memo to all City Departments regarding the enforcement of tenant lease obligations for private and non-profit tenants of City-owned property in response to the COVID-19 pandemic and related public health orders. This memo set out a City policy which provided the following relief for commercial City tenants: (1) waived all late charges, interest and other penalties related to late payment of rent from March 17 to December 31, 2020 due to the impact of COVID-19, (2) required the resumption of timely rent payment on January 1, 2021, and (3) specified that any delinquent rent not repaid by June 30, 2021 would be subject to applicable interest and penalties thereafter. The policy authorized City Departments to provide further relief to tenants if warranted. This policy only applied to General Fund Departments and not enterprise Departments.

The policy was intended to provide COVID-19-affected City tenants the ability to retain their leasehold while using financial reserves for other operational needs, including payroll, to remain in business.

The City Administrator now believes that rent forgiveness, not just rent deferral, is needed to facilitate the reopening and preservation of three City tenant businesses and non-profits. Specifically, the City’s Real Estate Division (“Real Estate”) has identified that rent forgiveness is needed for three City tenants with past due rent between April 2020 and December 2020, totaling $258,214.78[2] and may be needed in the future for rent due by these same three and other tenants between January 2021 and June 2021.

[1] The memo was subsequently updated on June 1, 2020 to extend protections to December 31, 2020.

[2] The total rent forgiveness amount differs from the total in the legislation ($257,723.92) by $490.86 as the amount used in the legislation does not include an annual rent increase for the National Conservatory Theater Center that went into effect in October 2020.

According to data provided by Real Estate, there are nine other City tenants who have missed rent payments due between April 2020 and December 2020, totaling approximately $189,942.[3] Real Estate has already reached a rent repayment agreement for five of these,[4] discussions are ongoing with two tenants, and two tenants left. The tenants include private retail or food service firms, a small professional services business, and a non-profit business.

**Status of Other City Properties Leased to Private or Non-Profit Tenants**

According to Chapter 23 of Administrative Code, the Director of Property (head of the City Administrator's Real Estate Division) is generally responsible for determining the market rent, entering into leases, and collecting rents for City-owned property. This does not apply to the Recreation and Parks Commission, Public Utilities Commission, Airport Commission, Port Commission, and Airport Commission, who are authorized to manage and lease property under their jurisdiction directly. The Municipal Transportation Agency is also authorized to enter into and manage leases for its property directly.

According to the Real Estate Division, there are approximately 98 properties where the City is the landlord. Of these, around 90 are agreements with non-profit or commercial tenants, with the remaining eight being agreements between City departments or between a City department and Real Estate.[5] The Real Estate Division collects rent for around 57 of these properties and City Departments collect rent for the remaining 33 properties.

## DETAILS OF PROPOSED LEGISLATION

The proposed ordinance authorizes the Director of Property to (1) amend three specified leases to forgive rent due between April 2020 through December 2020, totaling $258,214.78, without adding Administrative and Environmental Code provisions enacted since these leases were last executed, and (2) amend the leases specified as well as other Real Estate Division managed leases meeting certain conditions to allow Real Estate to provide rent forgiveness for rent due between January 2021 and June 2021, without Board of Supervisors approval.

[3] In addition to the tenants noted above, according to Real Estate, the current tenant for the Bill Graham Civic Auditorium has not paid rent since April 2020 (approximately $236,391 in base rent), however, Real Estate has facilitated agreements with other City Departments to use this space In lieu of paying rent. The Bill Graham Civic Auditorium tenant did not charge the City use fees for the COVID-19 response use and the Elections use during 2020, which Real Estate states was of equal value to the unpaid rent. In particular, the Auditorium was used by the Department of Public Health for COVID-19 response functions and by the Elections Department for the November 2020 General Elections. In addition, the current tenant of the Old U.S. Mint, NPU, Inc., has $198,000 in unpaid rent for the period from April 2020 to December 2020. Real Estate is still negotiating possible rent deferral or a rent waiver with NPU, Inc.

[4] Of the three tenants with agreements, one had a rent deferral/ repayment agreement, one tenant was transferred to the Municipal Transportation Agency's jurisdiction, and the third lease was terminated with agreement from the tenant.

[5] Approximately 70 of these agreements are standard real estate leases while 20 are permits for use or other miscellaneous agreements rather than full property leases (i.e. access to property for temporary uses, cell towers, etc.).

**Waiver of Administrative and Environmental Code Provisions**

Administrative and Environmental Code provisions enacted after City leases were executed or amended must be included in any subsequent amendments. According to the proposed legislation, these requirements are being waived because requiring existing tenants to comply with these new requirements could impose additional costs on tenants and impede the intended purpose of providing financial relief.

The Administrative Code requirements being waived may include:

- Section 4.1-3 (All-Gender Toilet Facilities);
- Section 4.9-1(c) (Vending Machines; Nutritional Standards and Calorie Labeling Requirements; Offerings);
- Section 4.20 (Tobacco Product And Alcoholic Beverage Advertising Prohibition);
- Chapters 12B and 12C (Nondiscrimination in Contracts and Property Contracts);
- Section 12F (MacBride Principles—Northern Ireland);
- Chapter 12K (Salary History);
- Chapter 12Q (Health Care Accountability);
- Chapter 12T (Criminal History in Hiring and Employment Decisions);
- Chapter 21C (Miscellaneous Prevailing Wage Requirements);
- Sections 23.50-23.56 (Labor Representation Procedures In Hotel And Restaurant Developments);
- Section 23.61 (Prevailing Wage and Apprenticeship Requirements and Local Hire Requirements); and
- Sections 83.1 et seq. (First Source Hiring Program).

The Environment Code provisions being waived may include:

- Chapter 3 (Restrictions on Use of Pesticides);
- Sections 802(b) and 803(b) (Tropical Hardwood and Virgin Redwood Ban);
- Chapter 13 (Preservative-Treated Wood Containing Arsenic); and
- Chapter 16 (Food Service and Packaging Waste Reduction Ordinance).

**Impact on City Tenants (Real Estate Division Managed Leases)**

According to City Administrative Code Section 23.30, any lease of City-owned property for a term greater than a year, must be at market rent, unless approved by the Board of Supervisors for a public purpose. As rent forgiveness would lower the rent required by the lease below market rent, the proposed legislation approves forgiveness of all rent due between April and December 2020 for three specified leases, and waives Board approval for future forgiveness of rent due between January and June 2021 for leases that meet certain conditions detailed in the ordinance and discussed below.

***City Tenants to Receive Rent Forgiveness Immediately***

The proposed legislation would approve lease amendments to forgive rent for three City tenants, totaling $258,214.78 as set out in Exhibit 1.

**Exhibit 1: City Tenants to Receive Rent Forgiveness Immediately and Outstanding Rent Amounts, April to December 2020**

| Tenant (Property Address) | Outstanding Rent (Apr - Dec 2020) | Monthly Rent (as of Jan 2021) | Months of Rent Outstanding |
|---|---|---|---|
| New Asia Restaurant (772 Pacific Ave.) | $202,500.00 | $22,500.00 | 9 |
| New Conservatory Theater Center (25 Van Ness Ave.) | $33,214.78 | $8,344.60 | 4 |
| Stephen M. Paoli (11th St. & Natoma St.) | $22,500.00 | $2,500.00 | 9 |
| **Total**** | **$257,723.92** | **$33,344.60** | - |

*Source: Real Estate Division*
** Total Outstanding Rent for New Conservatory Theater Center is slightly less than 4 months of rent at $8.344.60 x4 because the rent for that tenant increased from $8,181 to $8,345 in October 2020.*
*** The total rent forgiveness amount differs from the total in the legislation ($455,723.92) by $490.86 as the amount used in the legislation does not include an annual rent increase for the National Conservatory Theater Center that went into effect in October 2020.*

Two of the three properties are interim uses pending final development into affordable housing (772 Pacific Avenue), and a public park (11th Street and Natoma Street).

A short summary of the status of each of these properties is provided below.

*<u>New Asia Restaurant (772 Pacific Avenue)</u>*

The Mayor's Office of Housing and Community Development acquired 772 Pacific Avenue on June 28, 2017 for the development of new affordable housing. A Request for Proposals (RFP) for development of the site is currently open for proposals and predevelopment is expected to continue through FY 2021-22 with expected opening in FY 2024-25. The site is expected to provide around 70 affordable housing units for seniors.

As part of the acquisition, the City was assigned a lease with the existing restaurant tenant, New Asia Restaurant. The Restaurant has been closed to indoor dining since March 2020 under local health orders and is unable to provide outdoor seating. Real Estate was unable to confirm whether the restaurant had applied for or received any government funding to cover negative financial impacts from COVID-19. The current lease is due to expire on December 31, 2021.

*<u>New Conservatory Theater Center (25 Van Ness)</u>*

The City leases the lower level of 25 Van Ness Avenue to the New Conservancy Theater Center, an arrangement in place since 1984. The current lease expires on September 30, 2023. The Theater has been closed since March 2020 due to local health orders but secured federal CARES

Act funding to pay rent through August 2020. The Theater entered into a rent deferral agreement with the City in September 2020 for rent due through December 2020, per the City Administrator's initial policy. The Theater currently owes $33,214.78 in outstanding rent for September to December 2020 and is not expected to open for the foreseeable future.

*Stephen M Paoli (11th Street & Natoma Street)*

The Recreation and Parks Department acquired a building at 11th Street and Natoma Street on May 4, 2018 for development of a public park. According to the Recreation and Parks Department, planning for the project is expected to start this spring/ summer with an anticipated construction start in FY 2023-24 and completion in FY 2024-25.

As part of the acquisition, the City was assigned several leases on the site, including one with Stephen M Paoli for a "pop-up" restaurant space. According to the Real Estate Division, the restaurant has been closed since March 2020 and Mr. Paoli applied for, but did not receive, federal government assistance to pay for operating costs. There is currently $22,500 in outstanding rent due for April 2020 to December 2020. The current lease is due to expire on September 30, 2021.

***Criteria for Additional City Tenants to be Eligible for Rent Forgiveness***

The proposed legislation allows the City Administrator, at her discretion, to provide rent forgiveness to the three tenants that are the subject of the proposed legislation as well as other Real Estate-managed City tenants for rent due between January 1, 2021 and June 30, 2021 if they meet the following conditions:

1) Tenant has a lease previously approved by the Board of Supervisors under Chapter 23 of the Administrative Code, if required,
2) Tenant is in compliance with all other lease provisions,
3) Tenant must disclose information regarding any funds received from any government-funded financial aid, grant, or loan program intended for rent and these funds will be deducted from rent forgiveness provided,
4) Tenant must comply with all other lease provisions, comply with "back to work" requirements and other work-force related ordinances and applicable COVID-19 laws relating to workplace safety and employment rights.

The proposed ordinance is not intended to apply to the 33 leases under Real Estate's jurisdiction that are managed by other General Fund departments, including rent collection. We therefore recommend amending the legislation to clarify that the authority to amend leases only applies to leases for which Real Estate collects rent.

## FISCAL IMPACT

In total, the proposed legislation is estimated to result in a known reduction in revenues of $258,214.78, of which $33,214.78 are non-dedicated General Fund reductions and $225,000 are dedicated General Fund reductions, as shown in Exhibit 2.

However, the legislation also provides authority for the City Administrator, at her discretion, subject to the conditions outlined in the ordinance, to provide rent forgiveness for rent due between January 2021 and June 2021 for the three specified tenants and other Real Estate-managed lease tenants. Based on data from Real Estate, this could cost an additional $72,209 per month, or up to $433,254 over the six-month period for the three specified tenants and an additional five tenants currently behind on rent.[6] While it is unlikely this full amount will be necessary given new federal funding now available and the reopening of some outdoor dining, additional rent forgiveness may still be needed as several of the tenants specified were not approved for Paycheck Protection Program loans in the first round of the program and cannot provide outdoor dining.

**Exhibit 2: Estimated Rent Forgiveness Costs and Funds Impacted, April to December 2020**

| Tenant (Property Address) | Outstanding Rent (Apr 2020 - Dec 2020) | Fund Impacted |
|---|---:|---|
| New Asia Restaurant (772 Pacific Ave.) | $202,500.00 | Project Fund (AH Project Costs) |
| New Conservatory Theater Center (25 Van Ness Ave.) | $33,214.78 | General Fund |
| Stephen M. Paoli (11th St. & Natoma St.) | $22,500.00 | Project Fund (Park Development Costs) |
| **Total** | **$258,214.78** | |
| Total General Fund Impact | $33,214.78 | |
| Total Project Fund Impact | $225,000.00 | |

*Source: Real Estate Division*

According to the Mayor's Office of Housing and Community Development, any rental income from the New Asia Restaurant lease at 772 Pacific Avenue is dedicated to covering costs associated with the site, including current operating costs and future predevelopment and development costs. For example, funds were recently used to cover past-due water bills and to resolve a water leak on the property.

According to the Recreation and Parks Department, the rental income from Stephen M. Paoli is deposited in a General Fund Continuing Authority account dedicated to future development of the 11th and Natoma Street site as a public park.

[6] Estimated based on data from the Real Estate Division which shows $55,344.60 per month due in rent among the four specified tenants as of January 2021 and an additional $16,864.77 per month due in rent among five additional Real Estate-managed tenants behind on rent for the period April to December 2020. The latter also includes rent for a non-profit City tenant that has been behind on rent since before the pandemic.

## POLICY CONSIDERATION

**Program Design Considerations**

*Selective and Limited Access to Rent Forgiveness for City Tenants in Need*

The proposed legislation provides rent forgiveness for the April 2020 to December 2020 period for the three tenants mentioned above. Rent forgiveness for other tenants would only be available for rent due between January 2021 and June 2021. While several other City tenants missed rent between April 2020 and December 2020, Real Estate continues to negotiate repayment of this outstanding rent (estimated at approximately $161,295) or amendments to leases to collect same. According to Real Estate, the remaining tenants who have unpaid rent declined rent forgiveness.

Authorization to amend leases to provide for pandemic-related rent forgiveness approved by the Board of Supervisors for Port and Airport commercial tenants made rent forgiveness available for rent due since the start of the pandemic and was generally available to all tenants of those two departments.[7] While these departments have much larger property portfolios, similar principles apply. As noted above, Real Estate intends to provide rent forgiveness to tenants that it has determined are unable to repay unpaid rent.

*Rent Forgiveness Not Explicitly Tied to Negative Impacts related to the COVID-19 Pandemic*

Unlike the legislation authorizing amendments to Port leases related to its rent forgiveness program, the proposed legislation does not require a determination or evidence that the tenant was unable to pay rent due to COVID-19 related impacts.[8] Pending legislation to authorize amendments to Recreation & Parks Department leases (File 21-0029) also requires demonstrated negative impact related to the COVID-19 pandemic to be eligible. We therefore recommend amending the proposed ordinance to add a requirement in Section 4 that future rent forgiveness be conditioned on a tenant's inability to pay rent due to negative financial impacts from the COVID-19 pandemic.

**Waiver of Board Lease Amendment Review and Municipal Code Requirements**

The proposed ordinance will approve the amendment of three leases and waive the Board of Supervisors' approval of lease amendments for an unspecified number of leases managed by Real Estate. It will also waive compliance requirements under the Administrative Code and Environmental Code enacted after the most recent modification of each lease for leases that are amended pursuant to the proposed legislation. Because the proposed ordinance waives Administrative and Environmental Code provisions and Board of Supervisors' approval of lease

[7] See File 20-1278 (Authorizing Amendments to Airport Leases for COVID-19 Rent Relief) and File 20-1163 (Authorizing Amendments to Port Leases for COVID-19 Rent Relief).

[8] The Board also approved legislation authorizing amendments to leases with Airport tenants to allow for rent forgiveness which did not require a demonstration of COVID-19 impact to be eligible. However, given the direct link between the COVID-19 pandemic and air passenger traffic, the risk of funds not targeting affected businesses was relatively small.

amendments under Administrative Code Section 23.30 and Charter Section 9.118(c), we consider approval of the proposed ordinance to be a policy matter for the Board of Supervisors.

## RECOMMENDATIONS

3. Amend the proposed ordinance to add the following language (a) to Section 4, page 7, line 23, after "City Administrator," "for which the Real Estate Division collects rent," and (b) at page 8, line 10, after "at the discretion of the City Administrator" ", on the condition that a tenant's inability to pay rent is due to negative financial impacts from the COVID-19 pandemic."
4. Approval of the proposed ordinance as amended is a policy matter for the Board of Supervisors.

| **Item 2**<br>**File 21-0159** | **Department:**<br>Public Utilities Commission (PUC) |
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**EXECUTIVE SUMMARY**

**Legislative Objectives**

- The proposed ordinance would approve a Transmission Facilities Agreement (TFA) between San Francisco Public Utilities Commission (SFPUC) and Pacific Gas and Electric Company (PG&E) to interconnect City-owned transmission facilities to the electric grid for a term of four years and three months from April 2021 through June 2025, for an amount to be paid by SFPUC not to exceed $21,165,000, and waive certain provisions of the Administrative and Environment Codes.

**Key Points**

- SFPUC's Power Enterprise Bay Corridor Transmission and Distribution Project (BCTD) is a $166.6 million project consisting of a high voltage transmission line, transmission substation (Davidson Substation), distribution lines, and related electric facilities in the southeast area of the City. The project will deliver Hetch Hetchy power to City facilities and other SFPUC customers between Pier 50 and south of Islais Creek, bypassing PG&E distribution services. The Davidson Substation would need to be connected to PG&E's Potrero Switchyard to power the BCTD, which requires PG&E to upgrade the Potrero Switchyard to connect to the BCTD.

**Fiscal Impact**

- Under the proposed TFA, the not-to-exceed cost for SFPUC would be $21,165,000. This amount is comprised of (i) $15,000,000 for Substation work, (ii) $3,600,000 to compensate PG&E for income taxes it must pay (Income Tax Component of Contribution, or ITCC), and (iii) $2,565,000 for 45 months of Cost of Ownership Charges, at an amount of $57,000 per month.
- The $18,600,000 amount for the Substation work and ITCC would be funded by the SFPUC Hetch Hetchy Power Enterprise capital budget, and the $2,565,000 in Cost of Ownership Charges would be funded by the Hetch Hetchy Power Enterprise operating budget.
- The SFPUC has already made related payments to PG&E of $4,750,000 under a separate agreement. Costs included a feasibility study, engineering design work, and purchase the necessary equipment that has a long-lead time. These costs are also included in the proposed TFA.

**Recommendation**

- Approve the proposed ordinance.

## MANDATE STATEMENT

City Charter Section 9.118(b) states that any contract entered into by a department, board or commission that (1) has a term of more than ten years, (2) requires expenditures of $10 million or more, or (3) requires a modification of more than $500,000 is subject to Board of Supervisors approval.

## BACKGROUND

The San Francisco Public Utilities Commission (SFPUC) Power Enterprise Bay Corridor Transmission and Distribution Project (BCTD) is a $166.6 million project consisting of a high voltage transmission line, transmission substation (Davidson Substation), distribution lines, and related electric facilities in the southeast area of the City. The project will deliver Hetch Hetchy power to City facilities and other SFPUC customers between Pier 50 and south of Islais Creek, bypassing Pacific Gas and Electric Company's (PG&E) distribution services.

The Davidson Substation, to be constructed at 1535 Davidson Avenue, would need to be connected to PG&E's Potrero Switchyard, located at 1201 Illinois Street, to power the BCTD. Connecting the Davidson Substation to the Potrero Switchyard requires PG&E to design, furnish equipment and materials, and expand its existing switchgear at the Potrero Switchyard to connect to the BCTD. In January 2021, the SFPUC Commission approved a Transmission Facilities Agreement (TFA) with PG&E to furnish and construct a new 230 kV interconnection from the Potrero Switchyard to the Davidson Substation.

## DETAILS OF PROPOSED LEGISLATION

The proposed resolution would approve a TFA between SFPUC and PG&E to interconnect City-owned transmission facilities to the PG&E electric grid for a term of four years and three months from April 2021 through June 2025, for an amount not to exceed $21,165,000, and waive certain provisions of the Administrative and Environment Codes.

According to Mr. Ramon Abueg, SFPUC Deputy Assistant General Manager, the BCTD system would allow SFPUC to serve customers directly. Otherwise, to provide Hetch Hetchy power to these customers, including City facilities, SFPUC would have to apply for a Wholesale Distribution Tariff (WDT) with PG&E.[1] According to Mr. Abueg, each service connection through the WDT requires costly upgrades to the PG&E system and installation of primary equipment; the cost invested in WDT services to upgrade the PG&E system benefits only PG&E. Additionally, according to Mr. Abueg, installation of primary equipment is duplicative in that PG&E installs the same equipment as installed by SFPUC to establish a utility to utility connection. This requires that the customers provide property that could otherwise be available for other uses to install

[1] According to the California Public Utilities Commission, the Wholesale Distribution Tariff is a tariff that describes the interconnection, operating and metering requirements for generation facilities to be connected to a utility's distribution system. The tariff provides customers wishing to install generating or storage facilities on their premises with access to the electric grid while protecting the safety and reliability of the distribution and transmission systems at the local and system levels.

the equipment. The BCTD project is intended to reduce costs to SFPUC and customers over the long-term, maintain control of the power distribution system, and eliminate the need for giving up space to accommodate the installation of duplicative equipment.

According to Mr. Abueg, the decision to supply Hetch Hetchy Power directly to the area between Pier 50 and south of Islais Creek is due to the number of City-owned facilities in the area, particularly the SFPUC's Southeast Treatment Plant, which is undergoing major upgrades through the Sewer System Improvement Project (SSIP). Other customers served by BCTD would include Seawall Lot 337, Pier 48, Pier 50, Mission Rock, Mission Bay Ferry Landing, Mariposa Pump Station, Pier 70, Booster Pump Station, Central Bayside Station, Bruce Flynn Station, Southeast Community Center, and University of California, San Francisco (UCSF).

The proposed TFA would expire June 30, 2025. According to Mr. Abueg, SFPUC would seek to renew the TFA once it expires. If renewed, SFPUC would continue paying PG&E the Cost of Ownership Charge of $57,000 per month, an amount that would be fixed in perpetuity for the duration of the agreement.

The TFA is a form agreement that needs to be approved by the Federal Energy Regulatory Commission (FERC).[2] Because the TFA is a form agreement, it does not include the terms and conditions required for City contracts under the Administrative and Environment Codes.[3] Therefore, the proposed ordinance would waive these provisions.

## FISCAL IMPACT

Under the proposed TFA, the not-to-exceed cost for SFPUC would be $21,165,000. This amount is comprised of (i) $15,000,000 for Substation work, (ii) $3,600,000 to compensate PG&E for income taxes it must pay (Income Tax Component of Contribution, or ITCC), and (iii) $2,565,000 for 45 months of Cost of Ownership Charges, at an amount of $57,000 per month. The cost breakdown for the TFA is shown in Table 1 below.

[2] A form agreement is a standard, or boilerplate, contract where the terms and conditions are set by one party and typically cannot be negotiated by the other party. Because the TFA must comply with FERC requirements, it is not possible to include the City's Administrative and Environment Code requirements.

[3] Administrative and Environmental Code provisions waived by the proposed ordinance include non-discrimination in contracts (Admin Code Sec. 12B); minimum compensation (Admin Code Sec. 12P); health care accountability (Admin Code Sec. 12Q); consideration of criminal history in hiring (Admin Code Sec. 12T); small and micro local business participation (Admin Code Sec. 14B); competitive bidding (Admin Code Sec. 21.1); tropical hardwood and virgin redwood ban (Env. Code Chapter 8); preservative treated wood products (Env. Code Chapter 13); use of City funds for political activities (Admin Code Chapter 12B); and guaranteed maximum costs (Admin Code Sec. 21.19).

**Table 1: TFA Cost Breakdown**

| Item | Amount |
|---|---|
| Substation Work | |
| Engineering | $2,000,000 |
| Project Management | 1,500,000 |
| Property Improvements | 750,000 |
| Station Equipment and Labor | 3,500,000 |
| Removal | 50,000 |
| Telecommunications | 150,000 |
| Testing | 1,300,000 |
| Maintenance & Operations | 500,000 |
| Land & Environmental | 250,000 |
| *Subtotal Project Costs* | *$10,000,000* |
| Contract & Group Support | 5,000,000 |
| **Substation Work Subtotal** | **$15,000,000** |
| Income Tax Component of Contribution | 3,600,000 |
| Cost of Ownership Charges | 2,565,000 |
| **Total Not to Exceed Amount** | **$21,165,000** |

Previously Paid Costs

Under a separate 2018 agreement with PG&E, the SFPUC made related payments of $4,750,000 to perform a feasibility study for the interconnection, engineering design, and to purchase the necessary equipment that has a long-lead time. According to Mr. Abueg, FERC required that the costs also be included under the proposed TFA amount of $21,165,000.

Contract and Group Support

The $5,000,000 Contract & Group Support amount shown in Table 1 accounts for contingencies including environmental mitigation, coverage for loss of transmission clearance window due to system conditions, unforeseen or unknown items as a result of insufficient engineering, increase in overhead costs due to schedule delays, increase in labor due to level of effort being insufficient, and increased contract costs due to unexpected change orders. The Contract & Group Support amount of $5,000,000 is one-third of total project costs estimated by PG&E to be $15,000,000.

In accordance with the proposed TFA, SFPUC paid an initial charge of $4,750,000 to PG&E for feasibility study, engineering work and purchase of the equipment. The TFA provides for PG&E to invoice SFPUC periodically for PG&E's project costs, and to provide a final accounting of project costs at project completion. According to Mr. Abueg, the most recent scope and cost estimate provided by PG&E for the project is approximately $11,000,000, or approximately $1,000,000 more than the $10,000,000 in direct project costs shown in Table 1 above, which would be paid from the $5,000,000 Contract & Group Support contingency. The total Contract & Group Support contingency amount of $5,000,000 is intended to provide sufficient spending authority to prevent project delays that could disrupt the planned timing of connecting the new substation to the distribution system.[4]

Income Tax Component of Contribution

According to the proposed TFA, the Income Tax Component of Contribution is calculated based on PG&E's gross income realized for income tax purposes multiplied by the percentage set forth in PG&E's electric tariffs approved by the California Public Utilities Commission.

Cost of Ownership

The estimated Cost of Ownership is calculated based on PG&E's estimate of the cost of substation work of $15,000,000 times the current FERC transmission customer-financed monthly Cost of Ownership rate, which is fixed at the time that the substation is placed into service. If the actual cost of substation work is less than $15,000,000, the Cost of Ownership charge would be less.

The $18,600,000 amount for the Substation work and ITCC would be funded by the SFPUC Hetch Hetchy Power Enterprise capital budget, and the $2,565,000 in Cost of Ownership Charges would be funded by the Hetch Hetchy Power Enterprise operating budget.

## RECOMMENDATION

Approve the proposed ordinance.

[4] According to Mr. Abueg, the window for connecting the new substation to PG&E's electric grid is narrow because PG&E must shut down high voltage electricity for the interconnection work.

| Item 4<br>File 21-0068 | Department:<br>San Francisco International Airport (Airport) |
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**EXECUTIVE SUMMARY**

**Legislative Objectives**

- The proposed resolution would approve Amendment No. 2 to the Terminal 3 lounge lease between San Francisco International Airport (Airport) as landlord and American Express Travel Related Services Company, Inc. (American Express) as tenant, (a) expanding the leased premises to 15,287 square feet; (b) establishing a new Minimum Annual Guaranteed (MAG) rent of $3,226,546, (e) increasing the promotional charge to $15,287, and (f) extending the term by seven years through November 5, 2031.

**Key Points**

- American Express has operated the 8,199 square foot Centurion Lounge in Terminal 3 since November 2014. According to Airport staff, prior to the COVID-19 pandemic, the lounge was very popular with travelers and often reached maximum capacity. Airport staff has explored expanding the space to accommodate demand and increase revenue.
- Airport staff has identified 7,088 square feet of pre-security space adjacent to the lounge suitable for expansion. The space is occupied by offices and vacant corridor space and is not marketable as stand-alone concession space. The Airport and American Express have agreed to amend the lease to include the expansion space. The amendment extends the lease seven years through November 5, 2031 to amortize the expansion construction costs.

**Fiscal Impact**

- Under the proposed Amendment, American Express would pay MAG rent of $3,226,546, subject to annual adjustment. Over the approximately nine-year and four-month term of the new rent structure, the Airport would receive at least $30,114,429 in total MAG rent.

**Policy Consideration**

- The negotiated rental rate of $160 per square foot for the expansion premises is less than the annual rental rate of $255.21 per square foot for Category II terminal space set in the FY 2020-21 Airport Rates and Charges. The negotiated rate of $160 per square foot for the expansion space is based on American Express' costs to construct tenant improvements. Although the lease states that the minimum tenant investment per square foot is $350, according to Airport staff, tenant investment costs are estimated to be approximately $1,200 per square foot. Therefore, the proposed resolution should be amended to state that the Airport estimates that American Express' cost to construct tenant improvements in the expansion space is at least $1,200 per square foot.

**Recommendations**

- Amend the proposed resolution to state that the Airport estimates that American Express' cost to construct tenant improvements in the expansion space is at least $1,200 per square foot.
- Approval of the proposed resolution as amended is a policy matter for the Board of Supervisors because (1) the negotiated rent is less than the scheduled rent set in the Airport Rates and Charges, and (2) the proposed lease term exceeds the original 10-year term advertised in the RFP.

## MANDATE STATEMENT

City Charter Section 9.118(c) states that (1) any lease of real property for ten or more years, including options to renew, (2) have anticipated revenues to the City of $1,000,000, or (3) the modification, amendment or termination of these leases is subject to Board of Supervisors approval.

## BACKGROUND

In 2012, the San Francisco International Airport (Airport) conducted a Request for Proposals (RFP) for an airport lounge lease in Terminal 3. American Express Travel Related Services Company, Inc. (American Express) submitted the only proposal and was determined to be a responsive and responsible proposer and was awarded a lease. In October 2013, the Board of Supervisors approved a lease with American Express, with initial annual rent of $1,515,475 and a term of 10 years, from November 6, 2014 through November 5, 2024 (File 13-0779).

Under the lease, American Express occupies approximately 8,199 square feet, branded as Centurion Lounge. According to Airport staff, prior to the COVID-19 pandemic, the lounge was very popular with travelers and often reached maximum capacity and had to turn away members and guests. Airport staff has explored expanding the space to accommodate demand and increase revenue. The lounge was closed from March 20, 2020 through October 11, 2020 but has now reopened and American Express expects demand to return. Furthermore, the Airport and American Express expect there to be an increased sensitivity to crowding due to the pandemic.

Airport staff has identified approximately 7,088 square feet of pre-security space adjacent to the lounge suitable for expansion. The space is occupied by offices, an employee break room and smaller concession operators under storage permits that can be terminated with 30 days' notice, as well as vacant corridor space. Due to the location of the space on a pre-security mezzanine level, the space is not marketable as stand-alone concession space. In November 2020, the Airport Commission approved Amendment No. 2[1] to the American Express lease to include the expanded space.

## DETAILS OF PROPOSED LEGISLATION

The proposed resolution would approve Amendment No. 2 to the Terminal 3 lounge lease between the Airport as landlord and American Express as tenant, expanding the leased premises to approximately 15,287 feet, establishing a new Minimum Annual Guaranteed (MAG) rent of $3,226,546, and extending the term seven years through November 5, 2031.

Under the existing lease, American Express pays $2,092,467 in annual rent. The rent is determined by the FY 2020-21 Airport Rates and Charges, which sets the annual rental rate for Category II terminal space, including VIP clubs and lounges, at $255.21 per square foot. Under the proposed Amendment No. 2, American Express would pay a negotiated Minimum Annual

[1] In October 2020, the Airport Commission approved Amendment No. 1 to the lease to memorialize the Airport's COVID-19 Emergency Rent Relief Program, which waived certain rents and fees to encourage business recovery, employee rehiring, and continued concession operations at the Airport (File 20-1278).

Guaranteed (MAG) rent of $3,226,546. The MAG amount is based on the current annual rental rate of $255.21 per square foot for the existing premises and a negotiated annual rental rate of $160 per square foot for the expansion premises, as shown in Table 1 below.

**Table 1: Initial MAG Rent Calculation**

| Premises | Square Footage | Rental Rate per Square Foot | Total Rent |
|---|---|---|---|
| Existing | 8,199 | $255.21 | $2,092,467 |
| Expansion | 7,088 | 160.00 | 1,134,080 |
| **Total** | **15,287** | | **$3,226,546** |

*Source: Airport. Totals may not add due to rounding.*

According to Airport Management, the lower rental rate of $160 per square foot was negotiated based on the location of the expansion premises, the significant demolition and construction costs to be incurred by the tenant in reconfiguring and incorporating the expansion premises from a pre-security mezzanine level space into a natural extension of the post-security existing premises, and the requisite buildout of lounge features and improvements for the expansion premises.[2] The total MAG rent of $3,226,546 would be adjusted annually based on the Consumer Price Index (CPI), rather than through annual adjustments to the Airport Rates and Charges.

The proposed Amendment No. 2 would also extend the term of the lease seven years, through November 5, 2031, for a total term of 17 years. The 17-year term exceeds the 10-year lease term advertised in the 2012 RFP. According to Airport Management, the seven-year term extension allows the tenant to amortize the capital investment for the expansion and buildout costs. The Airport may also require the facility to close due to the future T3 West project. If closure is required, the lease may be extended by the amount of time the facility is closed.

The key terms of the proposed Amendment No. 2 are shown in Table 2 below.

**Table 2: Key Provisions of Lease Amendment**

| | |
|---|---|
| **Premises** | 15,287 square feet (increase of 7,088 square feet) |
| **Term Extension** | 7 years, through November 5, 2031 |
| **Options to Extend** | None |
| **MAG Rent** | $3,226,546 |
| **MAG Adjustment** | Annually based on CPI |
| **Minimum Investment Amount** | $350 per square foot of expansion space ($2,480,800) |
| **Promotional Charge** | $1 per square foot per year ($15,287) |
| **T3 West Project Closure** | Airport may require closure due to T3 West project with 90 days' notice. MAG rent is abated during closure period. Lease may be extended by number of days facility is closed. |

*Source: Proposed Lease Amendment No. 2*

As noted above, the negotiated rate of $160 per square foot for the expansion space is based on American Express' costs to construct tenant improvements. Although the lease states that the minimum tenant investment per square foot is $350, according to Ms. Cheryl Nashir, Airport

[2] According to Airport staff, American Express invested $10.3 million in its facility in 2014 and is expected to invest an additional $9 million on this expansion.

Director of Revenue Development and Management, tenant investment costs are estimated to be approximately $1,200 per square foot. Therefore, the proposed resolution should be amended to state that the Airport estimates that American Express' cost to construct tenant improvements in the expansion space is at least $1,200 per square foot.

According to Ms. Nashir, the anticipated rent commencement date for the expansion premises is July 1, 2022. Until the expansion premises is opened, American Express will continue paying the Category II rental rate for the existing premises, which is currently $255.21 per square foot annually.

## FISCAL IMPACT

Under the proposed Amendment No. 2, American Express would pay $3,226,546 in initial MAG rent, starting on the expected date of July 1, 2022, subject to annual adjustment. Over the approximately nine-year and four-month term of the new rent structure, the Airport would receive at least $30,114,429 in total MAG rent.

The expansion premises are currently occupied by United Airlines and Covenant Security Services, which pay $502,508 in combined annual rent. According to Ms. Nashir, both tenants will be relocated into other vacant space at the Airport, so rent will not be lost when the space is converted into a lounge.

## POLICY CONSIDERATION

The proposed negotiated annual rental rate of $160 per square foot is less than the annual rental rate of $255.21 per square foot for Category II terminal space set in the FY 2020-21 Airport Rates and Charges. Over the approximately nine-year and three-month term of the negotiated rate structure, American Express will pay approximately $6,298,586 less than it would have to under the Category II rental rate. The negotiated rental rate may signal to other prospective Airport tenants that the posted rates and charges are negotiable.

According to Ms. Nashir, the negotiated rental rate is unique for this lease and is unlikely to be replicated for future leases. The proposed Amendment No. 2 is a mid-term modification of an existing lease, not a new lease. American Express will incur significant costs to convert existing office and corridor space into an airport lounge. According to Ms. Nashir, American Express spent approximately $1,200 per square foot to construct the existing lounge in 2014 and will likely spend more for the expansion due to cost escalation and COVID-19 safety requirements. The tenant also provides free access to its lounge for American Express premium cardholders and does not receive sales revenue from the facility, unlike other concession tenants. Additionally, it differs from an airline lounge frequented by passengers who have made a purchase in the form of an airline ticket. According to Ms. Nashir, the premises cannot be marketed as stand-alone concession space as it on a mezzanine level not within the passenger flow and currently has no post-security access, so utilizing the space for the lounge expansion provides the Airport the best opportunity to generate revenue.

The Budget and Legislative Analyst considers approval of the proposed resolution to be a policy matter for the Board of Supervisors because (1) the negotiated rent is less than the scheduled rent set by the Airport Commission in the Rates and Charges, and (2) the proposed lease term is extended by seven years beyond the original 10-year term advertised in the RFP.

## RECOMMENDATIONS

1. Amend the proposed resolution to state that the Airport estimates that American Express' cost to construct tenant improvements in the expansion space is at least $1,200 per square foot.
2. Approval the proposed resolution as amended is a policy matter for the Board of Supervisors.

| **Item 5**<br>**File 21-0069** | **Department:**<br>San Francisco International Airport (Airport) |
|---|---|

**EXECUTIVE SUMMARY**

**Legislative Objectives**

- The proposed resolution would approve Amendment No. 2 to the lease between the San Francisco International Airport (Airport) as landlord and American Travel Agency, Inc. (ATA) as tenant, extending the term by two years and six months from January 2021 through June 2023**.** The lease has been in holdover status since expiration in December 2020 under the same MAG rent and terms as the original lease.

**Key Points**

- In 2013, the Board of Supervisors approved an Airport Amenities and Business Services lease with ATA. Under the lease, ATA provides a full-service travel agency, baggage storage, shower facilities, business center services, and luggage wrapping.
- ATA's lease expired December 31, 2020 and has been in holdover status. Due to the COVID-19 pandemic and severe downturn in enplanements and concession sales, Airport Management has determined that it would not be prudent to initiate a Request for Proposals (RFP) process to select a new tenant at this time. The proposed Amendment No. 2 would extend ATA's lease by two years and six months from January 2021 through June 2023, with no change to the MAG rent. The lease can be terminated at the Airport Director's sole discretion by providing six months' written notice.

**Fiscal Impact**

- Under the lease, the Airport receives the greater of MAG rent, which is currently $221,042, or 15 percent of gross revenues. Over the two-year and six-month term of the lease extension, the value of the MAG rent is at least $552,605.
- The lease contains a provision that suspends the MAG rent if enplanements drop below 80 percent of 2012 levels for three consecutive months, consistent with Airport policy. The MAG is than reinstated if enplanements increase back to at least 80 percent of 2012 levels for two consecutive months. When the MAG is suspended, ATA still pays percentage rent, which may be lower than the MAG. MAG rents are currently suspended due to the impact of COVID-19 on air travel.

**Recommendations**

- Amend the proposed resolution to state that the Amendment No. 2 is retroactive to January 1, 2021.
- Approve the proposed resolution.

## MANDATE STATEMENT

City Charter Section 9.118(c) states that (1) any lease of real property for ten or more years, including options to renew, (2) any leases that have anticipated revenues to the City of $1,000,000, or (3) the modification, amendment or termination of these leases is subject to Board of Supervisors approval.

## BACKGROUND

In 2013, the San Francisco International Airport (Airport) conducted a Request for Proposals (RFP) for an Amenities and Business Services lease. Airport Travel Agency, Inc. (ATA), which had provided similar services at the Airport since 1996, submitted the only proposal and was determined to be a responsive and responsible proposer and was awarded a lease. In December 2013, the Board of Supervisors approved a lease with ATA, with initial Minimum Annual Guaranteed (MAG) rent of $180,000 and a term of seven years, from January 2014 through December 2020 (File 13-1098).

The lease expired December 31, 2020 and has been in holdover status. Due to the COVID-19 pandemic and severe downturn in enplanements and concession sales, Airport Management has determined that it would not be prudent to initiate an RFP process to select a new tenant at this time. In December 2020, the Airport Commission approved Amendment No. 1 to the ATA lease, extending the term by two years and six months through June 2023.

## DETAILS OF PROPOSED LEGISLATION

The proposed resolution would approve Amendment No. 2 to the lease between the Airport as landlord and ATA as tenant, extending the term by two years and six months from January 2021 through June 2023.[1] As noted above, the lease has been in holdover status since expiration in December 2020 under the same terms as the original lease. Under the proposed Amendment No. 1, the MAG rent and other lease terms would not change. The lease can be terminated at the Airport Director's sole discretion by providing six months' written notice.

According to Mr. Sam ElGord, Airport Principal Property Manager, ATA has not suspended operations due to COVID-19. ATA currently occupies approximately 2,434 square feet of space in the International Terminal. ATA provides a full-service travel agency, baggage storage, shower facilities, business center services, and luggage wrapping. ATA has participated in the COVID-19 Emergency Rent Relief Program, which waived certain rents and fees to encourage business recovery, employee rehiring, and continued concession operations at the Airport (File 20-1278).

The proposed Amendment No. 2 adds new sections to Article 19 of the lease, including (a) nutritional standards and calorie labeling requirements for vending machines; (b) Administrative Code Chapter 12K restrictions on considering current and past salary history of job applicants; (c) local hire requirements for site alterations; (d) compliance with the City's resource-efficient

[1] The Airport Commission approved Amendment No. 1 in October 2020 to incorporate the COVID-19 Emergency Rent Relief Program for Airport Concession Tenants.

building requirements; (e) compliance with all-gender toilet facilities requirements; and (f) compliance with Federal Labor Standards Act (FLSA) and Occupational Health and Safety Act (OSHA) requirements.

## FISCAL IMPACT

Under the lease, the Airport receives the greater of MAG rent, which is currently $221,042, or 15 percent of gross revenues. Over the two-year and six-month term of the lease extension, the value of the MAG rent is at least $552,605.

The current MAG rent of $221,042 is based on the original MAG rent of $180,000 from 2014, adjusted annually by the Consumer Price Index (CPI). In calendar year 2019, the last full year before the COVID-19 pandemic, ATA paid $355,839 in percentage rent.

**MAG Suspension**

The lease contains a provision that suspends the MAG rent if enplanements drop below 80 percent of 2012 levels for three consecutive months, consistent with Airport policy. The MAG is than reinstated if enplanements increase back to at least 80 percent of 2012 levels for two consecutive months. When the MAG is suspended, ATA still pays percentage rent, which may be lower than the MAG. MAG rents are currently suspended due to the impact of COVID-19 on air travel.

## RECOMMENDATIONS

1. Amend the proposed resolution to state that the Amendment No. 2 is retroactive to January 1, 2021.
2. Approve the proposed resolution as amended.

| **Item 6**<br>**File 21-0190** | **Department:** Department of Real Estate |
|---|---|

## EXECUTIVE SUMMARY

### Legislative Objectives

- The proposed resolution would approve the first amendment to the restated lease at 35 Onondaga Avenue with Clinic by the Bay, increasing the City share of tenant improvement costs by $250,000, from $1,410,000 to $1,660,000.

### Key Points

- The City owns two properties at 35 Onondaga Avenue and 45 Onondaga Avenue which are currently rented to Clinic by the Bay and ArtSpan, community-based non-profits that provide free medical services and community art and cultural space, respectively.
- The City initially agreed to reimburse the tenants for $1,410,000 of needed site remediation, which exceeded the value of the below market rate rent. The tenants have exhausted the initial $1,410,000 City reimbursement for tenant improvements.
- Estimates of the cost of needed repairs have increased from the initial estimate of $1,598,099 to $2,399,428. This increase reflects work change orders due to conditions uncovered once work began, and more recently, discovery of additional water and mold damage.
- Due to the increase in repair and remediation costs, the Department of Real Estate has agreed to an increase of $250,000 in the total City reimbursement.

### Fiscal Impact

- The total cost to the City if the amendment is approved would be $1,660,000, or the initial $1,410,000 already paid plus the proposed $250,000 for additional reimbursement. The additional $250,000 in City costs would be funded by the Real Estate Division's FY 2020-21 General Fund budget.
- The remaining additional $610,428 in tenant improvement costs would be funded by the tenants.

### Policy Consideration

- As part of the initial agreement, the tenants agreed to assume responsibility for covering the balance of needed repair work, which parties agreed would be paid for through fundraising activities. Clinic by the Bay and Art Span have not identified funding sources for their share of the remaining additional $610,428 tenant improvement costs.
- The City has not conducted an independent verification as to whether the additional costs reflect the true amount of the required improvements.

### Recommendation

Because the City's contribution for tenant improvements exceeds estimated rent from the properties, approval of the proposed resolution is a policy matter for the Board of Supervisors.

## MANDATE STATEMENT

City Charter Section 9.118(c) states that any lease, modification, amendment or termination of a lease that had an initial term of ten years or more, including options to extend, or that had anticipated revenues of $1 million or more is subject to Board of Supervisors approval.

## BACKGROUND

**Existing Lease**

In July 2019, the Board of Supervisors approved a resolution authorizing an amended and restated lease between the City and Volunteers in Medicine, DBA Clinic by the Bay, for use of 35 Onondaga Avenue, a City-owned property (File 19-0739). In 2018, the Board of Supervisors approved a lease with Art Span, a non-profit, for use of 45 Onondaga Avenue, an adjacent City-owned property (File 18-1094). Both leases are below market rate rent.

The amended and restated lease for 35 Onondaga that was approved by the Board of Supervisors increased the City's share of tenant improvement costs for 35 Onondaga and 45 Onondaga, from $410,000 to $1,410,000, with the remaining $129,000 in estimated tenant improvement costs to be funded by the tenants. Under the existing leases, base rent paid to the City over the initial ten-year term (including estimated annual CPI increases of 3 percent) by Clinic by the Bay is $544,764, and by Art Span is $583,832, totaling $1,128,596. These rents are offset by (a) the tenant improvement allowance of up to $1,410,000, and (b) potential annual rent abatements for repair and maintenance of the HVAC system up to an estimated $188,099. In November 2019, the City also provided a six-month waiver of base rent in the amount of $49,224 to tenants to offset repair and improvement costs (File 19-0855). As a result, the City's contribution for tenant improvements and rent abatement for HVAC system maintenance of $1,598,099 exceeds estimated rent of $1,128,596 to be paid by Clinic by the Bay and Art Span. According to Real Estate, the tenants have not yet occupied the properties so no rent has been paid to date.

**Clinic by the Bay**

Clinic by the Bay is the San Francisco affiliate of Volunteers in Medicine, a national network of free primary care medical clinics. To qualify to receive services through Clinic by the Bay, patients must be uninsured, over 18 years of age, a San Francisco or San Mateo County resident, and must meet the low-income designation, which is set at 500 percent of the Federal Poverty Level. According to Clinic by the Bay Executive Director Sarah Gordon, many of the patients seen in the clinic are undocumented immigrants. Clinic by the Bay does not accept any form of medical insurance, including public options such as Medi-Cal.

Uninsured San Francisco residents meeting this qualification are eligible to receive on-site primary care. Patients with more intensive medical needs that may require consultation with specialists, additional diagnostic testing, and access to longer-term specialty treatments are provided access to such services through partnership agreements with various local medical institutions, including California Pacific Medical Center, University of California San Francisco, and Sutter Health.

Clinic by the Bay is not a member of the Community Clinic Consortium or San Francisco Health Network. According to Executive Director Sarah Gordon, patients seen at the Clinic are not advised or referred to apply for Medi-Cal or coverage through Healthy San Francisco. Ms. Gordon stated that even minimal co-payments would impose undue burden of many of the patients seen at the Clinic; for undocumented persons, there could be additional concerns due to immigration and residency status.

## DETAILS OF PROPOSED LEGISLATION

The proposed resolution would approve the first amendment to the restated lease with Clinic by the Bay, increasing the City share of tenant improvement costs for 35 Onondaga by $250,000, from $1,410,000 to $1,660,000.

**Increase in Tenant Improvement Costs**

Since approval of the existing lease, the estimated cost of all needed repairs has increased from $1,539,000 to $2,399,428. According to the Real Estate Division, in the course of conducting the repair and improvement work anticipated by the 2019 amended and restated lease, the contractor discovered additional water and mold damage. According to Mr. Andrico Penick, Director of the Real Estate, discovery of the additional damage led to a round of discussions between City officials that resulted in a new agreement in which the City would contribute an additional $250,000 to offset a portion of the additional repair and mold abatement costs.

According Director Penick, Clinic by the Bay has exhausted the initial $1,410,000 made available by the City to pay for site improvements. According to figures provided by Mr. Penick, without any further adjustment in the City funding commitments, the Clinic by the Bay and Art Span would need to fund the balance of $989,428 of improvement costs to carry out the necessary repair work.

## FISCAL IMPACT

If the proposed resolution is approved, the total City contribution to site repair and improvement will be $1,660,000 ($1,410,000 original contribution + $250,000 in additional contributions), as shown below in Exhibit 1.

**Exhibit 1: Change in City Share of Tenant Improvements**

| | Current | Proposed | Change |
|---|---:|---:|---:|
| Total | $1,539,000 | $2,399,428 | $860,428 |
| City Share | 1,410,000 | 1,660,000 | 250,000 |
| Tenant Share | 129,000 | 739,428 | 610,428 |

Source: Current and Proposed Lease

As shown above, the tenant share of the facility improvement costs would increase by $610,428. Mr. Penick reports that, at the present time, the Clinic by the Bay and Art Span will need to do additional fundraising to fund their portion of the repair work.

The additional $250,000 in City costs would be funded by the Real Estate Division's FY 2020-21 General Fund budget. As noted above, rent from both leases over the initial ten-year terms is less than the City share of the tenant improvement costs.

## POLICY CONSIDERATION

According to Director Penick, the City has not conducted an independent site review to determine if the contractor's additional cost estimates are valid. Mr. Penick provided our office with an itemized statement of a portion of the additional costs provided by Clinic by the Bay and stated that the costs appear to be reasonable.

As noted above, Clinic by the Bay and Art Span have not identified funding sources for their share of the $610,428 tenant improvement costs. Additional City funding may be necessary to fully fund the identified improvements if the tenant fundraising is not successful.

Because the City has not conducted any independent verification of the tenant improvement costs, we consider approval of the proposed resolution to be a policy matter for the Board of Supervisors.

## RECOMMENDATION

Because the City's contribution for tenant improvements exceeds estimated rent, approval of the proposed resolution is a policy matter for the Board of Supervisors.

| **Item 8**<br>**File 21-0175** | **Department:**<br>Municipal Transportation Agency (MTA) |
|---|---|

**EXECUTIVE SUMMARY**

**Legislative Objectives**

- The proposed resolution would approve the third amendment to the contract between San Francisco Municipal Transportation Agency (SFMTA) and TEGSCO, LLC, dba San Francisco AutoReturn (AutoReturn) for services related to towing, storage, and disposal of abandoned and illegally parked vehicles, increasing the not-to-exceed amount of the contract by $23,200,000, for a total not to exceed $88,600,000.

**Key Points**

- In 2016, the Board of Supervisors approved an agreement with AutoReturn to provide towing services, for a term of five years and an amount not to exceed $65,400,000, with an option to extend an additional five years. In February 2021, the SFMTA Board approved the third amendment to the agreement, exercising the option to extend and increasing the not-to-exceed amount to $88,600,000. SFMTA has requested two years of spending authority to allow time for SFMTA to assess how COVID-19 impacts pre-pandemic towing program costs and to reevaluate the program's policies and funding needs as the City emerges from sustained shelter-in-place conditions under the pandemic.
- Under the contract, AutoReturn collects fees from the owners of towed vehicles and remits those fees to SFMTA. SFMTA then pays AutoReturn a fixed management fee and reimburses AutoReturn for towing and related services, including a per tow charge paid to tow truck subcontractors. SFMTA rents a short-term facility for AutoReturn at 450 7th Street and a storage, office, and auction facility at 2650 Bayshore Boulevard in Daly City.

**Fiscal Impact**

- Actual and projected AutoReturn contract expenditures through March 2023 total approximately $88,154,960. In addition to the contract costs, the tow program costs include rent for the two facilities and SFMTA administrative costs. Over the initial five-year term and the first two years of the extension term, total actual and projected tow program costs are approximately $165,785,442 and revenues are approximately $123,879,825, for total net program costs to SFMTA of approximately $41,905,617.

**Recommendations**

- Amend the proposed resolution to (i) reduce the not-to-exceed amount of the contract by $400,000, for a total not to exceed $88,200,000, and (ii) request that SFMTA provides a comprehensive report on the tow program and cost containment strategies by March 31, 2023.
- Approve the resolution as amended.

## MANDATE STATEMENT

City Charter Section 9.118(b) states that any contract entered into by a department, board or commission that (1) has a term of more than ten years, (2) requires expenditures of $10 million or more, or (3) requires a modification of more than $500,000 is subject to Board of Supervisors approval.

## BACKGROUND

In June 2015, the San Francisco Municipal Transportation Agency (SFMTA) issued a Request for Proposals (RFP) to select a towing service provider. TEGSCO, LLC, dba San Francisco AutoReturn (AutoReturn), which had provided the service since 2004, was deemed the highest scoring responsive and responsible proposer and was awarded a contract. In March 2016, the Board of Supervisors approved a five-year contract with AutoReturn, from April 2016 through March 2021, for an amount not to exceed $65,400,000, and an option to extend an additional five years through March 2026 (File 16-0134). Under the contract, AutoReturn provides customer service for towed vehicles, tow truck dispatching, vehicle storage, and lien processing and vehicle auctions.

The AutoReturn contract has been amended twice. The first amendment, approved by the SFMTA Board in September 2016, allowed AutoReturn to use the short-term storage facility at 450 7th Street. The second amendment, approved by the Director of Transportation in July 2019, documented service requirement adjustments to customer service and tow request response times and provided clarification on the process to calculate annual Consumer Price Index (CPI) increases for management and variable fees paid to AutoReturn.

While the existing contract allows for SFMTA to extend the term five years through March 2026, the not-to-exceed amount of $65,400,000 does not provide sufficient funding for the contract extension term. In February 2021, the SFMTA approved the third amendment to the contract, exercising the five-year option to extend the term through March 2026 and increasing the not-to-exceed amount by $23,200,000, for a total not to exceed $88,600,000.

## DETAILS OF PROPOSED LEGISLATION

The proposed resolution would approve the third amendment to SFMTA's contract with AutoReturn, increasing the not-to-exceed amount by $23,200,000, for a total not to exceed $88,600,000.[1]

The proposed contract increase of $23,200,000 is intended to provide sufficient spending authority for the first two years of the extension term, through March 2023. SFMTA has requested two years of spending authority to allow time for SFMTA to assess how COVID-19 impacts pre-pandemic towing program costs and to reevaluate the program's policies and funding needs as the City emerges from sustained shelter-in-place conditions under the

[1] The resolution in File 16-0134 authorized SFMTA to exercise the five-year option to extend the contract, however Board of Supervisors approval is required to increase the not-to-exceed amount of the contract to fund the extended term.

pandemic. SFMTA intends to request spending authority for the remaining three years of the contract by March 2023.

Under the contract, AutoReturn collects fees from the owners of towed vehicles and remits those fees to SFMTA. SFMTA then pays AutoReturn a fixed management fee and reimburses AutoReturn for towing and related services, including a per tow charge paid to tow truck subcontractors. AutoReturn's variable fees are adjusted annually based on the lesser of three percent or the Consumer Price Index (CPI). Fees charged to vehicle owners are set by SFMTA.

SFMTA leases 556,055 square feet of space at a facility located at 2650 Bayshore Boulevard in Daly City. Under the contract, AutoReturn uses 330,771 square feet for storage and transfer of vehicles, public lien sale auctions, and office space. AutoReturn does not pay rent but pays all utilities, services, and security for the space. SFMTA also rents 450 7th Street for AutoReturn to use as its short-term storage facility.

According to Mr. Steven Lee, SFMTA Streets Division Manager, AutoReturn has been meeting or exceeding performance measures for the contract. The three key performance measures are timeliness of revenue deposits into SFMTA's account (within 24 hours), tow truck dispatch response times (35 minutes during peak commute hours and 25 minutes during non-peak hours), and customer service wait times (average of seven minutes). According to Mr. Lee, revenues have been deposited without any delays. Tow trucks have a 97 percent on-time rate, above the 90 percent contract requirement, and the average customer service wait time is two minutes.

## FISCAL IMPACT

The proposed third amendment would increase the not-to-exceed amount of the AutoReturn contract by $23,200,000, for a total not to exceed $88,600,000. According to Mr. Lee, actual expenditures through February 2021 total $63,251,753. Actual and projected expenditures are shown in Table 1 below.

**Table 1: Actual and Projected Contract Expenditures**

| Year | Management Fee | Variable Fee | Total Expenditures |
|---|---:|---:|---:|
| Year 1[2] | $8,704,272 | $4,413,678 | $13,117,950 |
| Year 2 | 8,203,839 | 4,776,759 | 12,980,598 |
| Year 3 | 8,449,856 | 5,441,590 | 13,891,446 |
| Year 4 | 8,703,444 | 5,198,730 | 13,902,174 |
| Year 5[3] | 8,928,568 | 2,094,654 | 11,023,222 |
| *Subtotal – Actual Expenditures* | $42,989,979 | $21,925,410 | $64,915,390 |
| Proposed Year 6 | $8,468,188 | $2,701,718 | $11,169,906 |
| Proposed Year 7 | 8,722,233 | 3,347,431 | 12,069,664 |
| *Subtotal – Proposed Expenditures* | $17,190,421 | $6,049,149 | $23,239,570 |
| **Total** | **$60,180,400** | **$27,974,559** | **$88,154,960** |

[2] The Management Fee in Year 1 includes $720,000 in rent payments for the 7th Street facility paid by AutoReturn and reimbursed by SFMTA because Caltrans, the landlord, was not compliant with Chapter 12B of the City's Administrative Code. AutoReturn, which had previously rented the facility directly from Caltrans, paid eight months of rent until the City Administrator's Office approved the Chapter 12B waiver, allowing SFMTA to assume the lease.

[3] Year 5 expenditures are a combination of actual expenditures through February 2021 ($63,251,753) and projected expenditures for March 2021 ($943,636).

Total actual and projected contract expenditures through March 2023 are approximately $88,154,960, or approximately $445,040 less than the not-to-exceed amount of $88,600,000 in the proposed third amendment. Therefore, the Budget and Legislative Analyst recommends amending the proposed resolution to reduce the not-to-exceed amount of the contract to $88,200,000, allowing sufficient funding authority for the contract.

According to Mr. Lee, SFMTA expects to have received $97,435,112 in revenues from the tow program through the initial five-year term of the contract.[4] Projected revenues for the next two years are approximately $26,444,713. According to Mr. Lee, the tow program is a cost-recovery program and funded by tow fee revenues and the SFMTA operating budget. SFMTA cannot make a profit from the tow program. Over the next two years, the projected net cost to SFMTA for the tow program, or costs minus revenues, is approximately $16,649,969. The total net cost through the seven years of the contract is projected to be approximately $41,891,662, as shown in Table 2 below.

**Table 2: Tow Program Costs and Revenues**

| Year | AutoReturn Contract | Rent | SFMTA Administrative Cost[5] | Total Program Cost | Tow Revenues | Net Program Cost |
|---|---|---|---|---|---|---|
| Year 1[6] | $13,117,950 | $1,995,469 | $9,247,156 | $24,360,575 | $20,769,426 | $3,591,149 |
| Year 2 | 12,980,598 | 2,789,312 | 9,475,761 | 25,245,671 | 21,968,176 | 3,277,495 |
| Year 3 | 13,891,446 | 2,939,229 | 10,166,840 | 26,997,515 | 23,768,474 | 3,229,041 |
| Year 4 | 13,902,174 | 3,039,396 | 10,545,264 | 27,486,834 | 23,083,883 | 4,402,951 |
| Year 5 | 11,023,222 | 3,134,545 | 4,442,398 | 18,600,165 | 7,845,153 | 10,755,012 |
| *Subtotal – Actuals* | *$64,915,390* | *$13,897,951* | *$43,877,419* | *$122,690,760* | *$97,435,112* | *$25,255,648* |
| Proposed Year 6 | $11,169,906 | $3,257,017 | 5,879,716 | $20,306,639 | $11,810,943 | $8,495,696 |
| Proposed Year 7 | 12,069,664 | 3,398,733 | 7,319,647 | 22,788,044 | 14,633,769 | 8,154,275 |
| *Subtotal – Proposed* | *$23,239,570* | *$6,655,749* | *$13,199,363* | *$43,094,682* | *$26,444,713* | *$16,649,969* |
| **Total** | **$88,154,960** | **$20,553,700** | **$57,076,782** | **$165,785,442** | **$123,879,825** | **$41,905,617** |

## Management Fee Costs

According to Mr. Lee, the Management Fee was bid out as a flat fee to maintain a consistent level of service, rather than a negotiated amount based on costs to AutoReturn. Estimated Management Fee costs for the Proposed Contract Year 6 (April 2021 through March 2022) are shown in Table 3 below.

[4] Actual expenditures through February 2021 total $96,795,494, and projected revenues in March 2021 are $639,618.

[5] Administrative costs include SFMTA staff time, overhead, work orders, and credit card processing charges.

[6] As described in Footnote 2 above, the AutoReturn contract amount in Year 1 includes $720,000 for eight months' rent paid by AutoReturn and reimbursed by SFMTA.

**Table 3: Estimated Management Fee Costs, Year 6**

| Item | Cost |
|---|---|
| Personnel (Including Overhead and Benefits) | $5,728,774 |
| Security Services and Professional Fees | 1,059,773 |
| Office and Network Infrastructure | 509,891 |
| Storage Lot Equipment, Repairs, and Capital Improvements | 499,893 |
| Other General and Administrative (Insurance, Utilities, Taxes, Damage Claims, etc.) | 419,910 |
| Profit | 249,947 |
| **Total Management Fee** | **$8,468,188** |

## POLICY CONSIDERATION

**Tow Volume Reduction**

Due to the COVID-19 pandemic, AutoReturn's tow volume has dropped from 45,210 tows for the period of March 2019 – February 2020 to 16,241 tows for the period of March 2020 – February 2021. The reduction in tows has reduced revenue to SFMTA, which has had to subsidize the tow program at an amount of approximately $10,755,012 for Contract Year 5 (April 2020 through March 2021). According to Mr. Lee, SFMTA management directed towing to be suspended for 72-hour violations, scofflaws (five or more unpaid citations), expired registration (extended tow threshold from six months to 12 months expired), booted vehicles, abandoned vehicles, commute lane violations, and yellow zone violations. A detailed list of tow volume by category for each year is shown in Attachment 1 to this report.

**Cost Containment**

SFMTA incurred a net program cost of $25.2 million over the initial five-year term of the tow program, which is funded through SFMTA revenues that would otherwise be available for transit operations and SFMTA projects. According to Mr. Lee, SFMTA has not increased tow fees to fully cover tow program costs because of Board of Supervisors policy direction to reduce fees. As an alternative to increasing tow fees, which tend to impact lower income residents more than other San Francisco residents, SFMTA should evaluate reduction in costs.

The Budget and Legislative Analyst noted in our report to the March 2, 2016 Budget and Finance Committee that the management fee paid to AutoReturn was based on an estimated 44,000 towed vehicles each year. According to our March 2, 2016 report, because the tow fees charged to owners of vehicles are based on the tow program costs and the number of towed vehicles, if the number of towed vehicles decreases, SFMTA will have to consider increasing tow fees to cover program costs, including the management fee. In response, SFMTA told the Budget and Legislative Analyst that SFMTA had included a clause in the contract stating that should tow volume increase or decrease significantly, the SFMTA and AutoReturn will renegotiate the fixed management fee to ensure that the cost per tow to the public is not impacted. According to Mr. Lee, the contract clause was not intended to address temporary reductions in tow volume, such as COVID-19, but sustained reductions in volume that would enable operations to be consolidated into a singular location where operating cost savings could be realized. The intent of the flat Management Fee and a Variable Fee was to ensure a stable operation to address fluctuations in tow volume. Due to COVID-19, SFMTA negotiated a five percent Management Fee reduction in FY 2021-22. According to Mr. Lee, AutoReturn operates on a slim margin and further reductions to the Management Fee would result in staff layoffs. Because of the increasing costs to operate the tow program, the Budget and Legislative Analyst recommends amending the resolution to request that SFMTA provides a comprehensive report on the tow program and cost containment strategies to the Board of Supervisors by March 31, 2023.

## RECOMMENDATIONS

1. Amend the proposed resolution to reduce the not-to-exceed amount of the contract by $400,000, for a total not to exceed $88,200,000.
2. Amend the proposed resolution to request that SFMTA provides a comprehensive report on the tow program and cost containment strategies by March 31, 2023.
3. Approve the resolution as amended.

## Attachment 1: Vehicle Tows by Category

| CATEGORY | March 2019 – February 2020 | % of Total | March 2020 – February 2021 | % of Total | % Change |
|---|---|---|---|---|---|
| ABANDONED | 1,942 | 4.30% | 740 | 4.56% | -62% |
| ACCIDENT | 901 | 1.99% | 740 | 4.56% | -18% |
| ARREST/INVESTIGATION/MOVING VIOLATION | 1,172 | 2.59% | 1,088 | 6.70% | -7% |
| CONSTRUCTION | 1,969 | 4.36% | 1,508 | 9.29% | -23% |
| COURTESY-DPT | 262 | 0.58% | 200 | 1.23% | -24% |
| COURTESY-SFFD | 2 | 0.00% | 4 | 0.02% | 100% |
| COURTESY-SFPD | 5 | 0.01% | 3 | 0.02% | -40% |
| DRIVEWAY | 6,352 | 14.05% | 3,908 | 24.06% | -38% |
| HAZARD | 921 | 2.04% | 679 | 4.18% | -26% |
| HIT & RUN | 352 | 0.78% | 366 | 2.25% | 4% |
| NON-TOW | 564 | 1.25% | 165 | 1.02% | -71% |
| OTHER | 32 | 0.07% | 44 | 0.27% | 38% |
| OTHER PARKING VIOLATIONS | 1,738 | 3.84% | 382 | 2.35% | -78% |
| OWNER REQUEST-SERVICE | 21 | 0.05% | 15 | 0.09% | -29% |
| OWNER REQUEST-TOW | 131 | 0.29% | 84 | 0.52% | -36% |
| RELOCATION | 187 | 0.41% | 106 | 0.65% | -43% |
| SCOFFLAW/CITATIONS | 2,001 | 4.43% | 58 | 0.36% | -97% |
| SCOFFLAW/CITATIONS/REGISTRATION | 738 | 1.63% | 20 | 0.12% | -97% |
| SCOFFLAW/NO VEHICLE ID | 35 | 0.08% | 33 | 0.20% | -6% |
| SCOFFLAW/REGISTRATION | 3,044 | 6.73% | 1,511 | 9.30% | -50% |
| SCOFFLAW/REGISTRATION/MOVING | 114 | 0.25% | 21 | 0.13% | -82% |
| SPECIAL EVENT | 1,907 | 4.22% | 876 | 5.39% | -54% |
| STOLEN RECOVERY | 1,939 | 4.29% | 2,713 | 16.70% | 40% |
| TOWAWAY - COMMUTE LANE | 15,489 | 34.26% | 616 | 3.79% | -96% |
| UNLICENSED/SUSPENDED LICENSE | 943 | 2.09% | 259 | 1.59% | -73% |
| YELLOW ZONE | 2,449 | 5.42% | 102 | 0.63% | -96% |
| **TOTAL** | **45,210** | | **16,241** | | **-64%** |