

# AIRPORT COMMISSION

CITY AND COUNTY OF SAN FRANCISCO

RESOLUTION NO. 21-0092

**APPROVAL OF THE FOURTH MODIFICATION TO CONTRACT NO. 50006, THE HOTEL MANAGEMENT AGREEMENT WITH HYATT CORPORATION, TO REDUCE THE BASE MANAGEMENT FEES PAYABLE IN 2021 AND 2022 AND TO ADJUST CERTAIN MANAGEMENT AGREEMENT TERMINATION EVENTS, TO EXTEND THE INITIAL 10-YEAR TERM BY AN ADDITIONAL TWO YEARS, AND TO PROVIDE FOR PAYMENT OF A NET ADDITIONAL AMOUNT OF \$3,896,462 OF MANAGEMENT FEES TO BE PAID FROM HOTEL REVENUE, AND RELATED ACTIONS**

- WHEREAS, on September 22, 2015, by Resolution No. 15-0178, the Airport Commission (Commission) awarded Contract No. 50006, the Hotel Management Agreement (HMA), to Hyatt Corporation (Hyatt), to manage the Grand Hyatt at SFO (Hotel) with a term of 10 years and one 5-year option to extend at the discretion of the Commission, and a not-to-exceed compensation amount of \$19,945,418, plus reimbursement of expenses; and
- WHEREAS, on December 1, 2015, by Resolution No. 434-15, the San Francisco Board of Supervisors (Board) approved the execution and delivery of the HMA under Section 9.118 of the San Francisco Charter; and
- WHEREAS, the HMA has been administratively modified to clarify certain matters by a First Modification, dated as of June 1, 2017, a Second Modification, dated as of August 1, 2017, and a Third Modification, dated as of May 9, 2018; and
- WHEREAS, the Hotel opened on October 4, 2019 and has been operating at a loss since the onset of the COVID-19 pandemic in March 2020 due to substantially reduced guest reservations and event facility bookings; and
- WHEREAS, the HMA provides for Hyatt to receive compensation in the form of a Management Fee for its services as Hotel manager, according to a fixed fee schedule, with a portion (the Base Management Fee) being paid from gross Hotel revenue, and a portion (the Subordinate Management Fee) being paid from net Hotel revenue after funding certain reserves and paying debt service on special facility bonds issued to finance the Hotel; and
- WHEREAS, Airport staff have negotiated a Fourth Modification to the HMA to (1) reduce the Base Management Fees by 60% for 2021 and by 30% for 2022, for a total fee reduction of \$1,158,535; (2) extend the commencement date for certain performance termination events that allow the Commission to terminate the HMA due to Hyatt's performance as manager; (3) extend the initial HMA term by two years, for a new initial term of 12 years while retaining one 5-year option to extend at the discretion of the Commission; (4) provide for payment of additional Management Fees of \$5,054,997 to compensate Hyatt for its management services during the additional two years of the initial HMA term; and (5) make changes necessary to preserve the tax-exempt status of interest on the related bonds, among other changes; and

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WHEREAS, on June 6, 2018, the Commission issued \$260,000,000 aggregate principal amount of bonds secured solely by Hotel revenues (the Hotel Special Facility Bonds), pursuant to a Trust Agreement with U.S. Bank National Association as trustee (the Hotel Bonds Trustee), to finance the Hotel; and

WHEREAS, on June 6, 2018, pursuant to Resolution No. 91-0210 as supplemented and amended, the Commission also issued \$276,340,000 aggregate principal amount of its San Francisco International Airport Second Series Revenue Bonds, Series 2018B and Series 2018C (the 1991 Resolution Bonds), to finance the construction of the Hotel and certain related projects; and

WHEREAS, using a portion of the proceeds of the 1991 Resolution Bonds, the Commission invested in the Hotel Special Facility Bonds by causing the Hotel Special Facility Bonds to be purchased by a separate trust entity created under Delaware law for the purpose of making such purchase, with the Commission as trust beneficiary; and

WHEREAS, as Hotel Special Facility Bonds investor and trust beneficiary, the Commission has authority to direct The Bank of New York Mellon Trust Company, N.A (BNY Mellon Trust), as trustee of the separate trust entity that is the bondholder of the Hotel Special Facility Bonds, to take actions and give directions to the Hotel Bonds Trustee on the Commission's behalf; and

WHEREAS, the HMA requires that the Hotel Bonds Trustee consent to any modification to the HMA; now, therefore, be it

RESOLVED, that this Commission finds that the above recitals are true and correct; and, be it further

RESOLVED, that this Commission approves the Fourth Modification to the HMA with Hyatt as described above and in the Airport Director's memorandum accompanying this Resolution, with a revised initial term of 12 years and one 5-year option to extend at the discretion of the Commission, and a net increase to the total compensation amount of \$3,896,462; and, be it further

RESOLVED, that the Airport Director is authorized to execute and deliver the Fourth Modification to the HMA in the form on file with the Commission Secretary; and, be it further

RESOLVED, that the Airport Director is authorized and directed, for and on behalf of and in the name of the Commission, as Hotel Special Facility Bonds investor and trust beneficiary, to direct and instruct BNY Mellon Trust, as trustee of the separate trust entity that is bondholder of the Hotel Special Facility Bonds, to consent to and approve the Fourth Modification to the HMA, and to execute and deliver any related consents, certificates or instructions; and, be it further

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RESOLVED, that the Commission Secretary, for and on behalf of and in the name of the Commission, is authorized and directed to seek approval of the Fourth Modification to the HMA from the Board under Section 9.118 of the San Francisco Charter; and, be it further

RESOLVED, that the actions of the officers, agents, and employees of the Commission taken prior to the adoption of this Resolution to carry out the purposes and intents of this Resolution are ratified, approved, and confirmed.

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*I hereby certify that the foregoing resolution was adopted by the Airport Commission*

*at its meeting of* \_\_\_\_\_ **APR - 6 2021** \_\_\_\_\_

  
\_\_\_\_\_  
*Secretary*



San Francisco International Airport

**MEMORANDUM**

April 6, 2021

TO: AIRPORT COMMISSION  
Hon. Larry Mazzola, President  
Hon. Eleanor Johns, Vice President  
Hon. Richard J. Guggenlime  
Hon. Everett A. Hewlett, Jr.  
Hon. Malcolm Yeung

21-0092

APR - 6 2021

FROM: Airport Director

SUBJECT: Approval of the Fourth Modification to the Hotel Management Agreement, Contract No. 50006, with Hyatt Corporation

DIRECTOR'S RECOMMENDATION: APPROVE THE FOURTH MODIFICATION TO CONTRACT NO. 50006, THE HOTEL MANAGEMENT AGREEMENT WITH HYATT CORPORATION, TO REDUCE THE BASE MANAGEMENT FEES PAYABLE IN 2021 AND 2022 AND TO ADJUST CERTAIN MANAGEMENT AGREEMENT TERMINATION EVENTS, TO EXTEND THE INITIAL 10-YEAR TERM BY AN ADDITIONAL TWO YEARS, AND TO PROVIDE FOR PAYMENT OF A NET ADDITIONAL AMOUNT OF \$3,896,462 OF MANAGEMENT FEES TO BE PAID FROM HOTEL REVENUE, AND RELATED ACTIONS.

**Executive Summary**

Staff recommends approval of the Fourth Modification to the Hotel Management Agreement (HMA) between Hyatt Corporation (Hyatt) and the Airport Commission (Commission). The Fourth Modification will provide savings of \$1,158,535 in calendar years 2021 and 2022 through the reduction of the Base Management Fee payable to Hyatt for the management and operation of the on-Airport Grand Hyatt at SFO (Hotel). These near-term fee reductions will help the Hotel weather the significant financial impacts triggered by the COVID-19 pandemic. In addition, the Fourth Modification will extend the start date for certain HMA-stipulated performance termination events by two years, providing more time for the Hotel to generate positive income levels as required under the HMA and will add two years to the existing 10-year initial term of the HMA, for a new initial term of 12 years, while retaining the existing five-year option to extend at the discretion of the Commission. The Fourth Modification provides for a net increase to the total compensation amount of \$3,896,462 to compensate Hyatt for its management services during the additional two years of the initial HMA term.

**Background**

The Commission is the owner of and sole investor in the Hotel, which is managed by Hyatt pursuant to a competitively-procured HMA between Hyatt and the Commission.

THIS PRINT COVERS CALENDAR ITEM NO. 2

AIRPORT COMMISSION CITY AND COUNTY OF SAN FRANCISCO

LONDON N. BREED MAYOR    LARRY MAZZOLA PRESIDENT    ELEANOR JOHNS VICE PRESIDENT    RICHARD J. GUGGENHIME    EVERETT A. HEWLETT, JR.    MALCOLM YEUNG    IVAR C. SATERO AIRPORT DIRECTOR

On September 22, 2015, by Resolution No. 15-0178, the Commission awarded Contract No. 50006, the HMA, to Hyatt, to manage the Hotel with an initial term of ten years plus one 5-year option to extend at the discretion of the Commission, and a not-to-exceed compensation amount of \$19,945,418 plus reimbursement of expenses. On December 1, 2015, by Resolution No. 434-15, the San Francisco Board of Supervisors (Board) approved the execution and delivery of the HMA under Section 9.118 of the San Francisco Charter. The HMA has been administratively modified to clarify certain matters by a First Modification, dated as of June 1, 2017; a Second Modification, dated as of August 1, 2017; and a Third Modification, dated as of May 9, 2018.

Following its opening in October 2019, the Hotel was ramping up its performance and penetrating the highly competitive lodging market. Since the COVID-19 health crisis began in March 2020, the Hotel has been experiencing a substantial reduction in income and limited operations, attributable to the pandemic and compliance with the related health orders. This significant reduction in income is expected to continue for at least the next two years. As such, the Hotel's initial two years of operation, which in normal conditions would have been a time of startup and stabilization, have been extremely volatile and challenging.

Staff initiated negotiations with Hyatt to reduce its fixed management fees under the HMA in the near term, to help reduce the cost burden to the Hotel, and the Fourth Modification to the HMA reflects the outcome of those negotiations.

The HMA provides for Hyatt to receive compensation in the form of a Management Fee for its services as Hotel manager, according to a fixed fee schedule, with a portion (the Base Management Fee) being paid from gross Hotel revenue, and a portion (the Subordinate Management Fee) being paid from net Hotel revenue (after funding certain reserves and paying debt service on special facility bonds issued to finance the Hotel).

Under the HMA, the Commission has the right to terminate Hyatt under specific circumstances (known as performance termination events), subject to Hyatt's right to cure and certain procedural requirements. Each of these requirements is described in Attachment A.

As the Airport is both the owner of the Hotel, the issuer of the Hotel Special Facility Bonds issued to finance the Hotel, and the ultimate investor in the Hotel Special Facility Bonds, Staff wants to ensure that the Hotel is a viable going concern to preserve the Airport's investment in the Hotel, which is a unique amenity unavailable at other Bay Area airports. Staff and Hyatt want to avoid facing a performance-based early termination scenario that would be premature given the ongoing and expected near-term challenges of operating during the COVID-19 pandemic. Over the last six months, Staff and Hyatt have been in discussions to minimize the risks of such scenarios, and the proposed amendment reflects this strong collaboration between the Airport and Hyatt.

### **Proposed Commission Action and Rationale**

Staff and Hyatt have negotiated a Fourth Modification to the HMA to (1) reduce the Base Management Fee by 60% for 2021 and by 30% for 2022, for a total fee reduction of \$1,158,535; (2) extend the commencement date for certain performance termination events that allow the Commission to terminate the HMA due to Hyatt's performance as manager; (3) extend the initial HMA term by two years, for a new initial term of 12 years, while retaining one 5-year option to

extend at the discretion of the Commission; (4) provide for payment of additional Management Fees of \$5,054,997 to compensate Hyatt for its management services during the additional two years of the initial HMA term; and (5) make changes necessary to preserve the tax-exempt status of interest on the related bonds, among other changes.

The Fourth Modification will result in a net increase of \$3,896,462 in Management Fees payable to Hyatt from Hotel revenue, as shown in the table below:

Additional Management Fees – Years 11 and 12	\$5,054,997
<u>Less: Reduction in Management Fees – 2021 and 2022</u>	<u>(\$1,158,535)</u>
Net Increase in Management Fees	\$3,896,462

The present value of the net increase in management fees is approximately \$2,400,000.

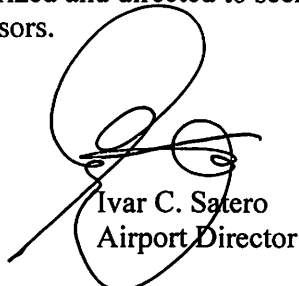
The proposed changes to the HMA performance termination events under the Fourth Modification are summarized in Attachment A. Avoiding these termination events benefits the Airport by continuing the consistent operation of the Hotel and helping to preserve the Airport's investment in the Hotel, while still holding Hyatt accountable once the Hotel has had an opportunity to stabilize. Both Staff and Hyatt intend for the existing relationship to endure for the length of the term, with mutual benefits resulting from the Hotel's continued operation.

Staff recommends that the Commission adopt the attached Resolution, which would approve the Fourth Modification and authorize the Airport Director to take two actions:

- (1) on behalf of the Commission (as Hotel owner), to execute the Fourth Modification; and
- (2) on behalf of the Commission (as investor in the Hotel Special Facility Bonds), to give instructions necessary to cause the Hotel Special Facility Bonds trustee to consent to and approve the Fourth Modification.

### **Recommendation**

I recommend the Commission adopt the attached Resolution approving the Fourth Modification to the HMA authorizing the Airport Director to execute and deliver the amended HMA, authorizing the Airport Director to instruct the Hotel Special Facility Bonds Trustee to consent to the Fourth Modification, and authorizing other related actions by Staff. If the attached Resolution is adopted, the Commission Secretary will be authorized and directed to seek approval of the Fourth Modification to the HMA from the Board of Supervisors.



Ivar C. Satero  
Airport Director

Prepared by: Kevin Bumen  
Chief Commercial Officer

**Attachment A**

**SUMMARY OF CHANGES TO PERFORMANCE TERMINATION EVENTS  
IN THE FOURTH MODIFICATION TO THE HOTEL MANAGEMENT AGREEMENT (HMA)**

The following table summarizes the negotiated amendments to the HMA's performance termination events. The specific amendments are underlined.

<b>Performance Termination Events</b>		
	<b>Current HMA</b>	<b>Amended HMA</b>
<b>ADR Requirement</b>	Commencing with the third (3rd) full Operating Year, if the Average Daily Rate (ADR) for the Hotel, as certified in writing by Manager's Chief Financial Officer, is less than 135% of the ADR for the Hyatt Regency in Burlingame in any two (2) Operating Years;	Commencing with the <u>fifth (5th)</u> full Operating Year, if the ADR for the Hotel, as certified in writing by Manager's Chief Financial Officer, is less than 135% of the ADR for the Hyatt Regency in Burlingame in any two (2) Operating Years;
<b>RevPAR Requirement</b>	Commencing with the fourth (4th) full Operating Year, if the Revenue Per Available Room (RevPAR) for the Hotel is less than 120% of the average RevPAR for the Competitive Set in any two (2) consecutive Operating Years; or	Commencing with the <u>sixth (6th)</u> full Operating Year, if the RevPAR for the Hotel is less than 120% of the average RevPAR for the Competitive Set in any two (2) consecutive Operating Years; or
<b>NOI Requirement</b>	Commencing with the fourth (4th) full Operating Year, if Net Operating Income (NOI) is less than ten million two hundred thousand dollars (\$10,200,000) (the Hurdle Amount), in any two (2) consecutive Operating Years. The Hurdle Amount shall be adjusted each Operating Year commencing with the fourth (4th) full Operating Year by the Bay Area Consumer Price Index (CPI) for the immediately preceding calendar year.	Commencing with the <u>sixth (6th)</u> full Operating Year, if NOI is less than ten million two hundred thousand dollars (\$10,200,000) (the Hurdle Amount), in any two (2) consecutive Operating Years. The Hurdle Amount shall be adjusted each Operating Year commencing with the <u>sixth (6th)</u> full Operating Year by the Bay Area CPI for the immediately preceding calendar year.

\*Each of the above requirements is independent of the others. A full Operating Year is an Operating Year consisting of twelve calendar months.