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Edward D. Reiskin, Director of Transportation

March 11, 2019

The Honorable Members of the Board of Supervisors  
City and County of San Francisco  
1 Dr. Carlton Goodlett Place, Room 244  
San Francisco, CA 94102

*Subject: Request for to enter into a Lease Agreement with Tad's, Inc. for  
SFMTA retail space at 44 Ellis Street, San Francisco*

Honorable Members of the Board of Supervisors:

The San Francisco Municipal Transportation Agency (SFMTA) requests that the San Francisco Board of Supervisors authorize the SFMTA to execute a Commercial Lease Agreement with Tad's Inc. for retail space, located at 44 Ellis Street in the Ellis-O'Farrell Garage, for a ten-year term that will result in \$5,317,064 in revenue and includes two five-year options to extend the lease.

### **Background**

The Ellis-O'Farrell Garage, located at 123 O'Farrell Street, is owned by the City and is under the jurisdiction of the SFMTA. It provides about 950 parking spaces and includes three commercial retail spaces totaling 11,000 square feet. The retail space associated with the lease is a 5,368 square foot space that operated as a restaurant at 44 Ellis Street.

On May 17, 2013, the SFMTA issued a Request for Proposal for the lease of the retail space at 44 Ellis Street and only received one response from the then-current tenant, Les Joulins. Les Joulins had been a tenant in the retail space since April 1997, and because of their long tenure, the SFMTA accepted their proposal.

The SFMTA entered into a lease agreement with Les Joulins on March 1, 2015. Two years later, on March 1, 2017, Tad's assumed the Lease. The Lease includes an initial term of ten years. Six years remain from the initial Lease term. The total amount of base rent for the first ten years of the Lease is \$5,127,000. The Lease includes \$250,000 in rent credits upon completion of certain pre-authorized improvements.

For over 20 years, the retail space at 44 Ellis Street has been occupied but has not undergone any major improvements. The Lease contemplates certain improvements to the premises and includes a list of pre-approved work such as hood ventilation replacement, and electrical, plumbing, ceiling, flooring and bathrooms upgrades. When Tad's assumed the Lease, Tad's agreed the list of pre-authorized work was necessary, and also determined the space needed a

new mechanical system and ductwork, a new fire protection system for sprinkler and hood, new lighting fixtures, and new exterior façade and canopy to meet building codes. The Lease allows tenant to apply up to \$250,000 as a rent credit against the base rent due, if tenant completes any of the improvement project from the pre-approved list. The rent credit is not an estimate of the total cost for the list of pre-authorized tenant improvement work. The SFMTA recognized the space needed work and the rent credit was intended to allow for some upgrades. None of the improvements that were the subject of the rent credit were completed while Les Joulins occupied the space. Due to the extent of the work needed to bring the space up to building code and safe operating standards, Tad's has not been able to open their business since assuming the Lease.

It is mutually beneficial to the SFMTA and Tad's to have the retail space at 44 Ellis Street completely renovated and to retain a local business. Tad's would like to terminate the existing Lease and enter into a new lease agreement that extends the term and includes rent abatement which would allow them to make the necessary capital investments. Considering that a major portion of the work constitutes a capital investment for the Ellis-O'Farrell Garage, the SFMTA would like to facilitate the completion of these improvements.

In November 2018, the SFMTA hired an independent appraiser, R. Blum, to appraise the market rent of the subject space. R. Blum used the direct comparison method and based on recent comparables, the range of rental rate is between \$82.50 and \$87.50 per square foot. With consideration of nine months of rent abatement, the market rent is adjusted upward to between \$87.50 and \$92.50 per square foot. R. Blum determined the market rent as of November 15, 2018, in as-is condition, is estimated to be \$87.56 per square foot per year. In December 2018, the SFMTA hired another independent appraiser, David Tattersall (Tattersall), to provide an appraisal review of the report by R. Blum. Tattersall concluded he is in agreement with the R. Blum report.

The proposed new lease agreement is for a ten-year term, and the initial nine months of rent abatement which will result in \$5,317,064 in revenue and includes two five-year options to extend the lease. The first five-year option to extend will be at 103 percent of the base rent from the lease year immediately prior. The second five-year option to extend is at the greater of 103 percent of the base rent from the lease year immediately prior or 95 percent of the market rent.

The rent for the proposed lease starts at \$82.50 per square foot per year, which is approximately \$5 per square foot below R. Blum's evaluation due to consideration of nine months of rent abatement. The rent abatement allows the tenant appropriate time to construct the space. Tad's intends to completely renovate the restaurant and make the necessary building improvements to bring the space up to code, at a reported cost of \$2,700,000. No additional rent credit for tenant improvement work is included. Even though

Tad's has not been able to open their business since assuming the Lease, Tad's has consistently met its obligation to pay the rent due under the Lease, totaling \$730,791 as of February 1, 2019. Comparing the current Lease with the proposed lease over a ten-year term, the result is a net revenue increase of \$190,154 to the SFMTA.

Tad's has been operating in the greater Union Square area for over 45 years. Tad's is considered a "legacy business" and retaining a local small business contributes to a proper public purpose. Tad's will be keeping the "Tad's Steaks" sign at the request of San Francisco Arts Commission, which is part of San Francisco's history. The current Lease is still in effect and the approval of the new lease agreement is subject to termination of the Lease.

### **Public Outreach**

Tad's has been fully engaged. No other additional public outreach was done for this Commercial Lease Agreement.

### **Alternatives Considered**

The SFMTA considered keeping the current Lease and leaving the space in its current condition, however, that approach does not facilitate a good business relationship with the tenant considering the substantial improvements that must be made by the tenant to bring the space up to current building codes. A second alternative considered was to amend the current Lease, however, the Lease would require significant changes and both parties agreed it is better to terminate the current Lease and enter a new lease agreement. The SFMTA wants to retain this local small business in the greater Union Square for the long term.

### **Funding Impact**

The proposed termination of the Lease and subsequent consideration of a new lease with Tad's will result in a net revenue increase to the SFMTA of \$190,024 between the two agreements when compared over a ten-year term. The current Lease generates \$5,127,000 in total base rent. The proposed terms of the new lease agreement will have a ten-year term, and the lease will generate \$5,317,024 in total base rent. The new lease structure will enable Tad's to make necessary building improvements thereby strengthening efforts for small business retention.

### **Environmental Review**

On January 23, 2019, the SFMTA, under authority delegated by the Planning Department, determined that the Commercial Lease Agreement is not defined as a "project" under the California Environmental Quality Act (CEQA) pursuant to Title 14 of the California Code of Regulations Sections 15060(c) and 15378(b).

A copy of the CEQA determination is on file with the Secretary to the SFMTA Board of Directors and is incorporated herein by reference.

**SFMTA Board Action**

On March 5, 2019, the SFMTA Board of Directors approved Resolution 190305-028 which authorized the Director of Transportation the SFMTA to execute a Commercial Lease Agreement with Tad's Inc. for retail space, located at 44 Ellis Street in the Ellis-O'Farrell Garage, for a ten-year term that will result in \$5,317,064 in revenue, and includes two five-year options to extend the lease.

**Recommendation**

The SFMTA requests that the San Francisco Board of Supervisors authorize the SFMTA to execute a Commercial Lease Agreement with Tad's Inc. for retail space, located at 44 Ellis Street in the Ellis-O'Farrell Garage, for a ten-year term that will result in \$5,317,064 in revenue, and includes two five-year options to extend the lease.

Thank you for your time and consideration of this proposed Lease agreement. Should you have any questions or require more information, please do not hesitate to contact me at any time.

Sincerely,



Edward D. Reiskin  
Director of Transportation