


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

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November 15, 2012

**TO:** Government Audit and Oversight Committee  
**FROM:** Budget and Legislative Analyst   
**SUBJECT:** November 19, 2012 Government Audit and Oversight Committee Meeting

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**Item 3**  
**File 12-0987**

**Department:**  
Recreation and Park Department (RPD)

## EXECUTIVE SUMMARY

### Legislative Objectives

- The proposed resolution would approve and authorize a new ten-year lease of the 1,170 square-foot Marina Degaussing Station at the Marina Green between the City on behalf of the Recreation and Park Department (RPD), as landlord, and Woodhouse Marina Green, LLC (Woodhouse Marina Green), as tenant, commencing on November 1, 2012 with two options to extend the lease by an additional five years each, resulting in a total 20-year lease term if both options are exercised. Under the proposed lease, Woodhouse Marina Green would operate a 25 seat café restaurant, with additional seating of up to 50 people on the restaurant's outdoor patio.

### Key Points

- Monthly Rent to be paid by Woodhouse Marina Green to RPD's Marina Yacht Harbor Fund would be equal to the greater of either (a) base rent of \$9,167 per month (\$110,000 annually), which is \$94 per square foot per year, or (b) percentage rent of 10 percent of gross receipts under \$2,000,000 and 12 percent of gross receipts of \$2,000,000 or more.
- Gross receipts are defined as all amounts received and receivable from all sales and business conducted in, from, or attributable to the premises. The term gross revenue, which appears on pages 2 and 16 in the proposed lease, is not defined. RPD advises that gross revenue is the same as gross receipts. Therefore, the lease should be amended on pages 2 and 16 to reflect the term gross receipts rather than gross revenue so all terms in which payments are dependent are consistent and fully defined. RPD concurs and advises they will make this correction in the lease.
- Woodhouse Marina Green would be required to make certain tenant improvements estimated to cost \$655,172 to rehabilitate and renovate the Marina Degaussing Station building to allow for the operation of a restaurant while retaining the envelope of the historic building.
- Rent payments would begin the day after the Woodhouse Marina Green receives the final permits required for the proposed tenant improvements, which is currently estimated to occur by March 1, 2013, or approximately four months after the lease commencement date of November 1, 2012.
- Once rent payments commence, RPD will provide Woodhouse Marina Green a rent credit of \$160,000. In addition, RPD is proposing to defer rent payments by Woodhouse Marina Green for approximately four months from November 1, 2012, or an additional \$36,668 in rent (4 times \$9,167), until all permits for the tenant improvements are secured. If additional unanticipated tenant improvements are required, RPD would provide Woodhouse Marina Green with additional rent credits of up to a maximum of \$50,000.
- Beginning in the sixth year of the lease, Woodhouse Marina Green is required to deposit an amount into a maintenance fund equal to the lesser of (a) one percent of the total gross revenue (receipts) for the prior lease year, or (b) \$20,000, which would be expended solely on capital improvements or major building repairs to the leased premises.

### **Fiscal Analysis**

- RPD would receive an estimated \$1,723,368 in percentage rent over the initial 10-year term of the proposed lease.
- Under the proposed lease, RPD would not receive an estimated \$196,668, including \$160,000 in negotiated rent credits for tenant improvements plus \$36,668 as a waiver of rent pending the obtaining of needed permits. If unanticipated tenant improvements, necessitate RPD to issue an additional \$50,000 in rent credits, RPD would not receive up to an estimated \$246,668 in rent under the proposed lease (\$196,668 plus \$50,000).
- Woodhouse Marina Green would be required to deposit an estimated \$99,053 into a maintenance fund between years 6 and 10, as required by the proposed lease.

### **Recommendations**

- The lease should be revised on page 2 and 16 to reflect the term gross receipts instead of gross revenue. RPD concurs and advises that this correction in the subject lease document will be made.
- Approve the proposed resolution contingent upon the lease correction noted above.

## **MANDATE STATEMENT / BACKGROUND**

### **Mandate Statement**

Charter Section 9.118(c) requires that any new lease, which extends for ten or more years or has anticipated revenue to the City and County of \$1,000,000 or more, must first be approved by resolution of the Board of Supervisors.

### **Background**

The Marina Degaussing Station<sup>1</sup>, originally built by the United States Navy in 1943, is a one-story 720 square foot building with a 450 square foot patio on the west side of the building, for a total of 1,170 square feet. The Marina Degaussing Station sits along the pedestrian walkway on the northern edge of the Marina Green on the Marina Green seawall. In the 1980s, the US Navy transferred ownership of the Marina Degaussing Station to the City, under the auspices of the Recreation and Park Department (RPD) and has sat vacant since the transfer.

Ms. Cassandra Costello, Property Manager for RPD, advises that, on April 22, 2011, RPD issued a Request for Proposal (RFP) seeking a qualified restaurateur to operate a café restaurant in the Marina Degaussing Station based on the criteria shown below in Table 1.<sup>2</sup>

<sup>1</sup> The Marina Degaussing Station was used during World War II to demagnetize a large boat's natural magnetic field, thus making it less likely to be detected by a nautical mine.

<sup>2</sup> According to Ms. Costello, the RFP was (a) posted on the RPD website, (b) sent to hundreds of restaurants and cafes in San Francisco, (c) sent to local restaurant groups, (d) was announced in articles in the Marina Times and Curbed SF, and (e) advertised through the Marina Merchants' Association. RPD also conducted additional outreach regarding the RFP to the surrounding community and neighborhood organizations.

**Table 1: Evaluation Criteria for Marina Degaussing Station RFP**

<b>Evaluation Criteria</b>	<b>Points</b>
Experience, Qualifications, and Financial Capability	35
Business and Marketing Plan	35
Proposed Financial Terms	30
<b>Total Points</b>	<b>100</b>

RPD convened a selection panel to review the proposals submitted. The three-member selection panel was composed of one member of the community, one RPD employee, and the Chief Financial Officer (CFO) of the Port. RPD received 2 proposals and selected Woodhouse Marina Green in December, 2011. Lease negotiations began shortly thereafter.

**DETAILS OF PROPOSED LEGISLATION**

The proposed resolution would approve and authorize a new ten-year lease of the 1,170 square-foot Marina Degaussing Station at the Marina Green between the City on behalf of the Recreation and Park Department (RPD), as landlord, and Woodhouse Marina Green, LLC (Woodhouse Marina Green), as tenant, commencing on November 1, 2012 and expiring on October 31, 2022 with two options to extend the lease by an additional five years each, resulting in a total 20-year lease term if both options are exercised.

Under the proposed lease, Woodhouse Marina Green would operate a 25 seat café restaurant, with additional seating of up to 50 people on the restaurant’s outdoor patio. The restaurant would be required to serve “affordably priced and fresh food featuring seasonal and sustainable ingredients using organic products when possible” with minimum hours of operation between 11 a.m. and 7 pm. Operations of the Woodhouse Marina Green’s restaurant would be monitored for the first six months and business hours would be subject to change by the General Manager of RPD based upon that monitoring.

Key provisions of the proposed lease include:

Monthly Rent would be equal to the greater of either (a) Base Rent of \$9,167 per month or \$110,000 annually, equal to approximately \$94 per square foot per year, or (b) Percentage Rent equal to a percentage of the following gross receipts<sup>3</sup>:

<u>Annual Gross Receipts</u>	<u>Percentage</u>
Under \$2,000,000	10%
\$2,000,000 or More	12%

- Every month, Woodhouse Marina Green would deliver a statement showing Sales Taxes paid and the gross receipts from the preceding calendar month along with the aggregate gross receipts for the current lease year in order to determine the percentage rent payable for that month.

<sup>3</sup> In the proposed lease, gross receipts are defined as all amounts received and receivable from all sales and business conducted in, from, or attributable to the premises.

- Base rent would increase on an annual basis by the Controller-certified Consumer Price Index (CPI).
- Woodhouse Marina Green would be required to make certain tenant improvements to rehabilitate and renovate the Marina Degaussing Station building to allow for the operation of a restaurant while retaining the envelope of the historic building. The tenant improvements would include (1) foundation upgrades, (2) upgrades to the electrical, heating, ventilation, and air conditioning (HVAC), and plumbing systems, (3) utility service upgrades, (4) roof improvements, and (5) the relocation of the Marina Degaussing Station Building away from the seawall to allow for the creation of a pedestrian walkway in line with the current path of travel along the Marina Green. Ms. Costello advises that the tenant improvements, subject to final approval by the Recreation and Park Commission once the lease has been executed, are currently estimated to cost a total of \$655,172. Under the proposed lease, these tenant improvements, currently estimated to take between 3 and 5 months, would be required to be completed within 8 months of the November 1, 2012 commencement date, or by June 30, 2013, and, if not completed, would constitute a breach of the lease terms. The restaurant's opening is currently estimated for the summer of 2013.
- Although the lease would commence on November 1, 2012, rent payments would not begin until the day after the Woodhouse Marina Green receives the final permits required for the proposed tenant improvements. Ms. Costello advises that the process of securing all final permits is currently estimated to be completed by March 1, 2013, approximately four months after the lease's commencement date of November 1, 2012. Therefore, RPD would waive approximately four months' rent from Woodhouse Marina Green, resulting in \$36,668 in waived rent payments to RPD (four times the monthly base rent of \$9,167).
- Once rent payments are due to commence, RPD would provide Woodhouse Marina Green with a rent credit of \$160,000, equal to approximately 17.5 months of current monthly Base Rent of \$9,167. The \$160,000 rent credit amount was negotiated based on the estimated total cost of \$655,172 in tenant improvements to be completed by Woodhouse Marina Green. If, during construction of the tenant improvements, Woodhouse Marina Green determines the need for additional unanticipated improvements<sup>4</sup>, including additional foundation work beyond the currently incorporated standard foundation work<sup>5</sup> that is estimated to cost over \$50,000, RPD would provide Woodhouse Marina Green with an additional rent credit in an amount by which the unanticipated improvements exceed \$50,000 with a maximum additional RPD rent credit of \$50,000 for unanticipated improvements of \$100,000 or more. Therefore, RPD could provide Woodhouse Marina Green with a maximum of \$210,000 (\$160,000 plus \$50,000) in rent credits should unanticipated improvements reach \$100,000. If the cost of unanticipated improvements exceeds \$100,000, Woodhouse Marina Green would also have the right to terminate the lease.

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<sup>4</sup> Unanticipated improvements do not include normal increases in the cost of materials or labor, cost overruns, or budgeting errors.

<sup>5</sup> The lease stipulates that standard foundation work is a 6 inch slab on grade with perimeter footing.

- Beginning in the sixth year of the lease, Woodhouse Marina Green would commence depositing a sum into a maintenance fund that is equal to the lesser of (a) one percent of the total gross revenue (receipts) for the prior lease year, or (b) \$20,000, which would be expended solely on capital improvements or major building repairs. Any expenditure from this maintenance fund would require approval by the General Manager of RPD.
- The term gross revenue, which appears on page 2 and 16 in the proposed lease, is not defined. However, Ms. Costello advises that gross revenue is the same as gross receipts, which is defined in the proposed lease as all amounts received and receivable from all sales and business conducted in, from, or attributable to the premises. Therefore, the lease should be amended on page 2 and 16 to reflect the term gross receipts rather than gross revenue so all terms in which payments are dependent are consistent and fully defined.
- Woodhouse Marina Green would be responsible for paying all utilities.
- Woodhouse Marina Green would be required to cooperate with RPD to prevent any interference by the restaurant with the America's Cup event and activities taking place in the summer/fall of 2013, with the understanding that areas adjacent to the property may be used for temporary structures, housing/hospitality services, general merchandise sales, food and beverage concessions, sponsor displays, first aid stations, or restrooms. Woodhouse Marina Green would also be prohibited from selling or promoting any product unduly seeking to capitalize on the America's Cup unless authorized by the America's Cup Event Authority<sup>6</sup>. All food, drink, and merchandise sold would be subject to review and approval by RPD in order to meet special operating requirements during the America's Cup events, which have yet to be determined.
- If Woodhouse Marina Green decides that it will not be able to profitably operate due to those yet-to-be-determined special operating requirements pertaining to the America's Cup, Woodhouse Marina Green may elect to close during the days that those special operating requirements are in effect and that month's rent will be prorated to reflect the restaurant's closure on those dates.

## FISCAL ANALYSIS

Table 2 below summarizes Woodhouse Marina Green's total estimated tenant improvement budget of \$655,172 to renovate and relocate the Marina Degaussing Station building.

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<sup>6</sup> The America's Cup Event Authority is responsible for the professional organization, management and financing of the 34<sup>th</sup> America's Cup, including any exhibition matches, the challenger series, and the final America's Cup match in San Francisco.

**Table 2: Estimate of Tenant Improvements**

Tenant Improvement	Cost
General Conditions (fencing, toilets, supervision)	\$28,700
Site Work (demolition, asphalt, landscape)	38,425
Concrete (foundation, curbs)	42,500
Carpentry	76,270
Thermal and Moisture (roof, insulation)	11,925
Doors and Windows	18,400
Finishes (paint, wall treatments, flooring)	33,660
Millwork and Specialty (cabinets, trim, awning)	43,010
Furnishings	8,050
Plumbing	47,150
Mechanical (HVAC system)	44,750
Electrical	25,800
Utilities	24,320
Equipment (Kitchen Cooking Equipment)	40,610
Contractor Overhead	101,602
Architecture, Engineering, Soils, and Miscellaneous	65,000
Replacement of Public Right of Way	5,000
<b>Total</b>	<b>\$655,172</b>

Ms. Costello advises that many of the \$655,172 in tenant improvements shown above in Table 2, which are required to be performed by Woodhouse Marina Green under the proposed lease, would typically be paid for by the landlord, in this case RPD, in order to make the property usable by a tenant. Ms. Costello notes that RPD will continue to own the subject property and \$650,172, or 99.2 percent, of the \$655,172 in tenant improvements to be paid for by Woodhouse Marina Green would remain the property of RPD upon expiration of the subject lease. The remaining \$5,000 (\$655,172 less \$650,172) in kitchen equipment and furniture would be considered Woodhouse Marina Green's property and be removed at the end of the proposed lease.

As noted above, because RPD does not have sufficient capital funds to perform the necessary tenant improvements to convert the subject vacant property into a cafe, according to Ms. Costello, RPD negotiated a rent credit of \$160,000 to be provided to Woodhouse Marina Green to partially offset the estimated cost of \$655,172 that Woodhouse Marina Green would incur for the tenant improvements. In addition, RPD is proposing to waive rent payments by Woodhouse Marina Green from November 1, 2012 until February 28, 2013, or approximately four months<sup>7</sup>, which is equal to an estimated additional \$36,668 in rent payments, until all needed permits for the tenant improvements are secured by Woodhouse Marina Green. This \$36,668 will also partially offset Woodhouse Marina Green's estimated cost of \$655,172 to make the needed tenant improvements.

<sup>7</sup> Approximately four months' base rent x \$9,167 per month during construction would be equal to \$36,668.

Therefore, RPD would not receive a total of approximately \$196,668 (\$160,000 plus \$36,668) of rent under the proposed lease. In addition, if unanticipated tenant improvements of \$100,000 are necessary by Woodhouse Marina Green, beyond the \$655,172 shown in Table 2 above, RPD would provide up to \$50,000 in additional rent credits to Woodhouse Marina Green. If the maximum additional \$50,000 of rent credits are provided by RPD, RPD would not receive a total of \$246,668 (\$160,000 plus \$36,668 plus \$50,000) in rent under the proposed lease.

Table 3 below summarizes the total \$1,723,368 in estimated rent which RPD’s Marina Yacht Harbor Fund would receive during the 10-year term of the proposed lease. As shown in Table 3 below, percentage rent is projected to be received in all years because gross receipts are estimated to exceed the amount of the base rent in all 10 years of the proposed lease.

**Table 3: Summary of \$1,723,368 in Estimated Rent Received by RPD Under the Proposed Lease**

Year of Lease	Estimate of Woodhouse Marina Green's Gross Receipts	Estimate of Base Rent	Base Rent Rate Per Square Foot	Estimate of Percentage Rent	Percentage Rent Rate Per Square Foot
1	\$1,425,000	\$0	\$0	\$0	\$0
2	1,567,500	63,300	54.10	139,250	119.02
3	1,645,875	65,199	55.73	164,588	140.67
4	1,728,169	67,155	57.40	172,817	147.71
5	1,814,577	69,170	59.12	181,458	155.09
6	1,905,306	71,245	60.89	190,531	162.85
7	2,000,571	73,382	62.72	200,069	171.00
8	2,100,600	75,584	64.60	212,072	181.26
9	2,205,630	77,851	66.54	224,676	192.03
10	2,315,911	80,187	\$68.54	237,909	\$203.34
<b>Total</b>	<b>\$18,709,139</b>	<b>\$643,071</b>		<b>\$1,723,368</b>	

Ms. Costello advises that the revenue received from the proposed lease would be deposited directly into RPD’s Marina Yacht Harbor Fund<sup>8</sup>, per State legal requirements which state that all revenues generated in the Marina by the City must be used exclusively to finance annual facilities maintenance projects and capital improvement projects in the Marina.

Table 4 below summarizes the current estimate of \$99,053 that Woodhouse Marina Green would be required to deposit into the maintenance fund from year six through 10 of the proposed lease.

<sup>8</sup> RPD’s Marina Yacht Harbor Fund is the repository for all revenue generated at the Marina and the Fund is required to be used to finance annual facilities maintenance projects and capital improvement projects in the Marina.



**Table 4: Estimate of Deposits in a Maintenance Fund**

<b>Year of Lease</b>	<b>Estimate of Woodhouse Marina Green's Gross Revenues (Receipts)</b>	<b>Estimate of Amount to Be Deposited into Maintenance Fund</b>
6	\$1,905,306	\$19,053
7	2,000,571	20,000
8	2,100,600	20,000
9	2,205,630	20,000
10	2,315,911	20,000
<b>Total</b>	<b>\$10,528,018</b>	<b>\$99,053</b>

As previously noted, the term gross revenue which appears on page 2 and 16 of the proposed lease is not defined but is equivalent to gross receipts, which is defined. Therefore, the proposed lease should be revised on page 2 and 16 and the term gross revenue should be removed and replaced with the term gross receipts. RPD concurs and advises that this correction will be made in the subject lease.

**RECOMMENDATIONS**

1. The lease should be revised on page 2 and 16 to reflect the term gross receipts rather than gross revenue. RPD concurs and advises that they will make this correction in the subject lease.
2. Approve the proposed resolution contingent upon the lease correction noted above.