

1 [Real Property Sublease - 1440 Harrison Street - Harrison Assets, LLC - Human Services
2 Agency - \$3,577,644 Total Rent in the First Year]

3 **Resolution authorizing a Sublease for the term of July 1, 2017, through**
4 **September 30, 2025, at 1440 Harrison Street, with Harrison Assets, LLC, a California**
5 **limited liability company, for approximately 56,788 square feet at \$298,137 monthly**
6 **for a total first year rent of \$3,577,644 which amount shall increase annually on each**
7 **July 1 beginning in 2018 by 3% and two five-year options to extend for use by the**
8 **Human Services Agency.**

9
10 WHEREAS, The City's Human Services Agency ("HSA") has occupied the entire
11 property commonly known and numbered 1440 Harrison Street for thirty (30) years; and

12 WHEREAS, 1440 Harrison Street consists of approximately 56,788 square feet, as
13 recently re-measured using BOMA standards, of office and public program space and
14 includes approximately 31 parking stalls; and

15 WHEREAS, HSA's Affordable Care Act and Medi-Cal Health Connections site at 1440
16 Harrison links San Franciscans from all age groups and ethnicities with the appropriate health
17 coverage services available to them; and

18 WHEREAS, HSA provides health coverage services to over 195,000 San
19 Franciscans, more than one fifth of the population; and

20 WHEREAS, Between October 2013 and October 2016, the number of Medi-Cal
21 enrollees rose by 93,367, a 92% increase. The Medi-Cal households (HHs) enrolled rose
22 by 85% (56,377) between Oct 2013 and Oct 2016, to 122,599 households; and

23 WHEREAS, The site also provides efficient one-stop access to Cal-Fresh (Food
24 Stamps) assistance for families, seniors, and persons with disabilities, and also houses two
25

1 CAAP programs, CALM and CAPI, which assist aged and disabled who are not eligible for
2 SSI; and

3 WHEREAS, Harrison Assets LLC, a California limited liability company, as
4 successor in interest, is Master Landlord under a lease with the San Francisco Unified
5 School District; and

6 WHEREAS, The City's current Sublease at 1440 Harrison Street is scheduled to expire
7 on June 30, 2017; and

8 WHEREAS, The Real Estate Division has negotiated a new Sublease (the
9 "Sublease") for an extension with the Harrison Assets LLC as Sublessor; and

10 WHEREAS, The proposed Base Rent under the Sublease was found to be less than
11 Fair Market Rent by an independent MAI appraisal; and

12 WHEREAS, An Appraisal Review by an independent MAI Appraiser has been
13 completed and recommended; and

14 WHEREAS, The proposed Sublease is subject to enactment of a resolution by the
15 Board of Supervisors and the Mayor, in their respective sole and absolute direction, approving
16 and authorizing such Agreement; now, therefore, be it

17 RESOLVED, In accordance with the recommendation of the Director of the Human
18 Services Agency and the Director of the Real Estate Division, that the Director of Property
19 is hereby authorized on behalf of the City and County of San Francisco as Sublessee, to
20 execute a Sublease, a copy of which is on file with the Clerk of the Board of Supervisors in
21 File No. 161363, for an additional period of approximately 8 years and 3 months on the
22 terms and conditions contain therein with Harrison Assets LLC, a California limited liability
23 company, as Sublessor; and, be it

24 FURTHER RESOLVED, The Agreement shall commence upon July 1, 2017, and
25 expire on September 30, 2025; and, be it

1 FURTHER RESOLVED, That the Base Rent will be \$289,137.00 per month which
2 shall increase annually by 3% on each July1 beginning July 1, 2018; and, be it

3 FURTHER RESOLVED, That the City shall continue to pay for its own utilities,
4 janitorial, maintenance, and security; and, be it

5 FURTHER RESOLVED, That City agrees to indemnify, defend and hold harmless
6 Landlord and its agents from and against any and all claims, costs and expenses,
7 including, without limitation, reasonable attorneys' fees, incurred as a result of (a) City's use
8 of the premises, (b) any default by City in the performance of any of its obligations under
9 this lease, or (c) any negligent acts or omissions of City or its agents, in, on or about the
10 premises or the property; provided, however, City shall not be obligated to indemnify
11 Landlord or its agents to the extent any claim arises out of the active negligence or willful
12 misconduct of Landlord or its agents; and, be it

13 FURTHER RESOLVED, That the Board of Supervisors authorizes the Director of
14 Property to enter into any amendments or modifications to the Sublease (including without
15 limitation, the exhibits) that the Director of Property determines, in consultation with the City
16 Attorney, are in the best interest of the City, do not increase the rent or otherwise materially
17 increase the obligations or liabilities of the City, are necessary or advisable to effectuate the
18 purposes of the License or this resolution, and are in compliance with all applicable laws,
19 including City's Charter; and, be it

20 FURTHER RESOLVED, City shall occupy said premises for the entire lease term
21 unless funds for rental payments are not appropriated in any subsequent fiscal year, at
22 which time City may terminate this lease with written notice to Landlord, pursuant to
23 Charter, Section 3.105, of the City and County of San Francisco; and, be it
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1 FURTHER RESOLVED, That within thirty (30) days of the Sublease being fully
2 executed by all parties, the Director of Real Estate shall provide a copy of the Sublease to the
3 Clerk of the Board for inclusion into the official file.

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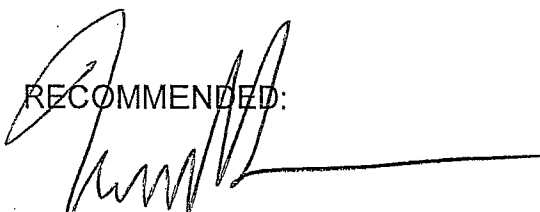
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\$3,577,644.00 Available
(Base Rent 7/1/17 to 6/30/18)

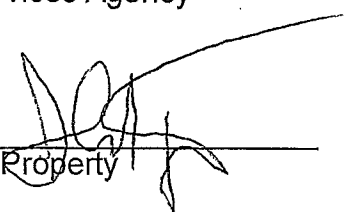
Index Code: 45ADOH
Sub Object: 03011


Controller
Subject to the enactment of the 2017/2018
Annual Appropriation Ordinance

RECOMMENDED:



Director
Human Services Agency



Director of Property

<p>Item 11 File 16-1363</p>	<p>Departments: Human Services Agency (HSA) and Real Estate Division (RED)</p>
<p>EXECUTIVE SUMMARY</p>	
<p style="text-align: center;">Legislative Objectives</p>	
<ul style="list-style-type: none"> • The proposed resolution would approve the exercise of an eight-year, three-month option to extend the sublease of office space at 1440 Harrison Street between the City, on behalf of the Human Services Agency (HSA) as the sublessee, and 1440 Harrison Street Development Group LLC, as sublessor, from July 1, 2017 through September 30, 2025. 	
<p style="text-align: center;">Key Points</p>	
<ul style="list-style-type: none"> • 1440 Harrison Street is owned by the San Francisco Unified School District (SFUSD) and leased to a master tenant, 1440 Harrison Street Development Group, LLC. The City has subleased 1440 Harrison Street since 1983 for HSA’s Medi-Cal and Food Stamps programs. • Under the current sublease agreement, which expires on June 30, 2017, HSA pays annual rent of \$1,215,216 or \$23.28 per square foot per year.¹ Under the proposed eight-year sublease extension, the City would pay annual rent of \$3,577,644 or \$63 per square foot per year for the first year, an increase of 194 percent. After the first year, monthly rent would increase by 3 percent per year. • The proposed sublease extension would have three additional five-year options to extend. Therefore, the proposed resolution should be amended to state that the existing sublease has three remaining extension options rather than two. 	
<p style="text-align: center;">Fiscal Impact</p>	
<ul style="list-style-type: none"> • Including the costs of utilities, janitorial services, and security services, over the eight-year term of the proposed sublease extension, the total estimated costs to HSA would be \$38,905,456, which would be funded from 18.5 percent in Federal funds, 18.5 percent in State funds, and 63 percent from the City’s General Fund. 	
<p style="text-align: center;">Policy Consideration</p>	
<ul style="list-style-type: none"> • The market value of office space could flatten over the next eight-year period, resulting in market rents for office space of less than the rent provided in the proposed sublease in the final year. The current sublease includes three five-year options and a final eight-year option to renew. Because the proposed sublease extension would commit the City to an eight-year, three-month term, rather than the five-year extension term provided in the existing sublease, the Budget Analyst considers approval of the proposed resolution to be a policy matter for the Board of Supervisors. 	
<p style="text-align: center;">Recommendations</p>	
<ul style="list-style-type: none"> • Amend the proposed resolution to state that the existing sublease has three remaining extension options rather than two. • Approval of the proposed resolution as amended is a policy matter for the Board of Supervisors. 	

¹ The current sublease is measured at 52,200 square feet; and was re-measured for the proposed sublease at 56,788 square feet.

MANDATE STATEMENT

City Administrative Code 23.27 states that any lease with a term of one year or longer or with rent of \$5,000 or more and where the City is the tenant is subject to Board of Supervisors approval.

BACKGROUND

Since 1983, the City has subleased an office building located at 1440 Harrison Street, between 10th and 11th Streets, from the 1440 Harrison Street Development Group, LLC, for the Human Services Agency's (HSA) Medi-Cal and Food Stamps programs.² The building is owned by the San Francisco Unified School District, which has leased the space to the 1440 Harrison Street Development Group, LLC under a long-term master lease.³

In 2005, the Board of Supervisors approved renewing the sublease agreement with 1440 Harrison Street Development Group, LLC for 52,200 square feet of office space at 1440 Harrison Street for HSA for seven years from August 12, 2005 through June 30, 2012 (File 05-1124), which had four additional options to extend the sublease by five years, totaling 20 years to August 2032, plus one final additional extension of 8 years, 3 months to October 2040. In 2012, the Board approved extending the existing sublease through June 30, 2017 by exercising the first five-year option (File 12-0585). The extended sublease expires June 30, 2017.

The 1440 Harrison Street building is one of two major sites for Medi-Cal and Cal-Fresh⁴ eligibility screenings and serves more than 330 clients per day. In addition to performing Medi-Cal and Cal-Fresh eligibility screenings, staff also assists clients with Cash Assistance Linked to Medi-Cal (CALM) applications and Covered California applications if they are not eligible for Medi-Cal.

According to Mr. Robert Walsh, Director of Facilities and Operations at HSA, HSA serves approximately 195,000 clients at the 1440 Harrison Street building, with 263 HSA employees. Since 2012, the number of clients served has increased by approximately 88,000 (82 percent) from 107,000 to 195,000 clients, and the number of employees has increased by 79 (43 percent) from 184 employees to 263 employees at the site due to implementation of the Affordable Care Act. After the sublease was extended in 2012, new cubicles were added, and the size of cubicles was reduced to accommodate the additional staff.

² HSA's housing and homeless services were previously located on this site but have since been relocated.

³ According to Mr. Charlie Dunn, Senior Real Property Officer in the Real Estate Division, the property was master leased in 1985 for a term of 55 years (30 years plus options to extend) to a developer with the expertise and capital to renovate the building. The master lease provides for reappraisal based on fair market rent and expires in 2040.

⁴ Federally known as the Supplemental Nutrition Assistance Program (SNAP), or food stamps.

DETAILS OF PROPOSED LEGISLATION

The proposed resolution would approve an eight-year, three-month extension of the existing sublease from July 1, 2017 through September 30, 2025 for 56,788 rentable square feet⁵ of office space at 1440 Harrison Street between the City, on behalf of HSA as the sublessee, and 1440 Harrison Street Development Group, LLC, as the sublessor. The proposed eight-year and three-month sublease provides for:

- Monthly rent of \$298,137 for the first year and an annual increase of 3 percent beginning July 1, 2018 over the term of the sublease
- Utilities, janitorial services, and security services to be paid by the City
- Two five-year options to extend the sublease at rent levels equal to 95 percent of the fair market value
- All other lease obligations in the sublease agreement remain the same as the current sublease provisions

The effective date of the sublease would be July 1, 2017, such that the rent for July 2017 would be at the new higher rental rate. Table 1 describes the current sublease and the proposed sublease.

⁵ The property was re-measured in 2016 using Building Owners and Managers Association (BOMA) standards. The change in BOMA standards allowed more common area space to be included in the building's rentable square footage, resulting in a higher square footage estimate. The previous estimate was 52,200 square feet.

Table 1: Current and Proposed Sublease Details

	Current Sublease	Proposed Sublease	Change
Premises	52,200 square feet plus 31 car parking	56,788 square feet* plus 31 car parking	Increase of 4,588 square feet
Base Rent (monthly)	\$101,268	\$298,137	Increase of \$196,868 (194%)
Operating Expenses (monthly)	\$54,275	\$54,275	No change
Base Rent Increase Date	N/A	Annually on July 1	
Base Rent Increase Amount	None	3% (annually)	
Term	June 30, 2017 (five years)	September 30, 2025 (eight years and three months)	
Options to Extend	Three (3) five-year options and one eight- year, 3 month, 15 day option at 95% FMR**	Two (2) five-year options at 95% FMR ⁶	

Source: Real Estate Division

* The property was re-measured in 2016 using Building Owners and Managers Association (BOMA) standards.

** Fair Market Rent

FISCAL IMPACT

The monthly rent for the proposed eight-year, three-month term would be \$298,137 per month or \$5.25 per square foot per month for the first year, which reflects an increase of \$196,869 per month or 194 percent. After the first year, monthly rent would increase by 3 percent on an annual basis.

The proposed monthly rent represents 95 percent of the current fair market rent⁷ established by an independent appraisal conducted by CBRE, Inc. and confirmed as recommended under an appraisal review by John Clifford Advisory. The 3 percent annual increase provision reflects typical lease agreements in the commercial real estate market. According to Mr. Charlie Dunn, Senior Real Property Officer in the Real Estate Division, the increase in sublease rent reflects increases in the commercial real estate market over the last five years due to a lack of new construction and high demand from tech, tech-related, and tech-serving businesses. Mr. Dunn states that the Real Estate Division considered the only three other available properties with square footage of at least 55,000, but none of these was open to renting to HSA.

⁶ There should be three five-year options remaining, rather than two. Therefore, the proposed resolution should be amended to correctly reflect the remaining extensions.

⁷ As of July 1, 2017, the fair market rent for the property was \$66.30 per square foot per year according to the appraisal.

In addition to the annual rent, HSA is responsible for paying annual utilities, janitorial services, and security services, at an estimated cost of \$651,300 as of November 2016. According to Mr. Dunn, such costs are estimated to increase by approximately 3 percent annually. The total estimated cost of the proposed eight-year and three-month sublease extension to the City would be \$38,905,456, as shown in Table 2 below.

Table 2: Total Costs by Year under Proposed Sublease Extension

Year	Annual Rent	Annual Operating Costs*	Total Cost
FY 2017-18	\$3,577,644	\$651,300	\$4,228,944
FY 2018-19	3,684,973	670,839	4,355,812
FY 2019-20	3,795,522	690,964	4,486,486
FY 2020-21	3,909,388	711,693	4,621,081
FY 2021-22	4,026,670	733,044	4,759,714
FY 2022-23	4,147,470	755,035	4,902,505
FY 2023-24	4,271,894	777,686	5,049,580
July 2024 - Sept 2025**	5,500,063	1,001,271	6,501,334
Total	\$32,913,624	\$5,991,832	\$38,905,456

Source: Addendum to Sublease Agreement, Budget and Legislative Analyst calculation

*Assumes annual increase of 3%

**Period of one year and three months

According to Mr. Walsh, the funding sources for the proposed sublease are comprised of approximately 18.5 percent from Federal funds, 18.5 percent from State funds, and 63 percent from the City’s General Fund, and would be included in HSA’s annual operating budgets.

POLICY CONSIDERATION

The City would pay rent of \$63 per square foot under the proposed sublease extension, increasing by 3 percent per year over the eight-year, three-month term of the sublease, resulting in rent per square foot in the final year of the sublease of approximately \$77.50. While the sublease rent of \$63 per square foot represents 95 percent of fair market value, based on an independent appraisal, the market value of office space could flatten over the next eight-year period, resulting in market rents for office space of less than \$77.50 per square foot in the final year, as provided by the proposed sublease.

According to the City’s Five Year Financial Plan for FY 2017-18 through FY 2021-22, “signs emerged in 2016 that [the City’s economic performance] may be reaching a plateau”, including a potential slow-down in the technology industry that is independent of the availability of office space. The report states, “Technology is a high-paying industry that has a greater capacity than other local industries to absorb high housing and labor costs, and high office rents. If it were only a matter of capacity constraints and high rents driving out employment, we would expect tech to withstand it better than other industries, yet the data suggests tech employment growth is slowing more than other industries.”

A recent Jones Lang LaSalle report⁸ showed a flattening in commercial rents in 2016 compared to prior years and categorized the real estate market for office space as “a peaking market”, rather than a “rising market.” The report also states that an additional 5.8 million square feet of office space will be completed in the next five years. A slow-down in the technology industry, combined with an increase in office space, could put downward pressure on commercial rents in future years.

The existing sublease between the City and 1440 Harrison Development Group provides for three five-year extension options and one final eight-year, three-month extension option. The City is choosing to exercise the eight-year, three-month extension option at this time, rather than the five-year option, based on negotiations between the City and 1440 Harrison Development Group.

According to Mr. John Updike, Director of Real Estate, the proposed rent of \$63 per square foot is based on an extension term of eight years and three months. Reducing the extension term to five years would require new negotiations and could result in a higher rent per square foot. In the event that the City and 1440 Harrison Development Group cannot agree on the rent per square foot, the existing sublease provides for additional appraisals to determine the fair market rent.⁹ Mr. Updike states that an alternative appraisal could show a greater fair market value, resulting in rent greater than the \$63 per square foot in the proposed sublease.

However, because the proposed sublease extension would commit the City to an eight-year, three-month term, rather than the five-year extension term provided in the existing sublease, the Budget Analyst considers approval of the proposed resolution to be a policy matter for the Board of Supervisors.

RECOMMENDATIONS

1. Amend the proposed resolution to state that the existing sublease has three remaining extension options rather than two.¹⁰
2. Approval of the proposed resolution as amended is a policy matter for the Board of Supervisors.

⁸ San Francisco Office Insight Report, fourth quarter 2016.

⁹ The City and 1440 Harrison Development Group can each submit an appraisal, and the fair market rent will be the average of the two appraisals if the appraisals are within 10 percent. If the appraisals differ by more than 10 percent, a third appraisal will determine which of the first two appraisals represents fair market rent.

¹⁰ The proposed resolution states that there are two remaining five-year extension options. The existing sublease provides for three five-year extension options and one final eight-year, three month extension option, totaling four extension options; exercise of an extension option would result in three remaining extension options.

**Addendum to Sublease Agreement for 1440 Harrison Street, San Francisco,
between Harrison Assets, LLC, Sublessor, and
City and County of San Francisco, a municipal corporation, Sublessee**

This Addendum to Sublease Agreement for 1440 Harrison Street, San Francisco, between Harrison Assets, LLC, Sublessor, and City and County of San Francisco, a municipal corporation, Sublessee, is dated for reference purposes November 14, 2016.

Recitals

A. On or about October 15, 1985, the San Francisco Unified School District, a political subdivision of the State of California (“Master Lessor”), and Sublessor’s predecessor in interest, 1440 Harrison Development Group, LLC, as the tenant, entered into a October 15, 1985 Master Lease (attached as Exhibit A) for that certain real property commonly known as 1440 Harrison Street in the City and County of San Francisco, California, being Lot 51 of Assessor’s Block 3520, a three story and basement brick building (the “Building”) containing approximately 56,788 rentable square feet and a paved and fenced outdoor area including 31 parking stalls (hereafter the “Subleased Premises”).

B. On August 3, 2005, 1440 Harrison Development Group, LLC, Sublessor Harrison Assets, LLC (“Sublessor”) predecessor in interest, and Sublessee City and County of San Francisco, a municipal corporation (“City”), entered into a Sublease Agreement attached hereto as Exhibit B, for the Subleased Premises.

C. On or about February 28, 2007, Sublessor’s predecessor in interest, 1440 Harrison Development Group, LLC, assigned to Sublessor all of its right, title and interest as a Tenant under the Master Lease (attached as Exhibit A) with the San Francisco Unified School District, a political subdivision of the State of California (“Master Lessor”), in a Consent and Assumption Agreement with Limited Release recorded as Document No. 2007, I348269-00, at Reel J341, Image 0206.

D. City timely provided notice of exercise of its option to extend the term of the Sublease for an additional five years from July 1, 2012 to June 30, 2017.

E. City and Sublessor want to enter into this Addendum to Sublease Agreement to extend the term of the Sublease commencing July 1, 2017, on the terms and conditions stated below.

F. City and Sublessee have measured the Subleased Premises, and the rentable square footage is 56,788. The Premises includes an adjacent parking lot consisting of 31 stalls. A plan of the Subleased Premises is attached as Exhibit C.

AGREEMENT

It is hereby agreed:

1. Recitals Incorporated as Contractual Terms. The Recitals stated above are incorporated into this Addendum, not as terms of recital, but as contractual terms.

2. Amendment to Sublease Agreement. The Sublease Agreement is amended as follows:

A. The above Recitals A through F inclusive shall replace the Recitals in the Sublease Agreement.

B. The "Basic Sublease Information" on pages 2, 3 and 4 of the Sublease Agreement are deleted and replaced by the following:

"Basic Sublease Information.

The following is a summary of basic sublease information (the "Basic Sublease Information" or the "Summary") in the Addendum to Sublease. Each item below shall be deemed to incorporate all of the terms in this Addendum to Sublease pertaining to such item. In the event of any conflict between the information in this Section and any more specific provision of this Addendum to Sublease, the more specific provision shall control. Capitalized terms not defined elsewhere shall have the meanings given below or in the Sublease, or in the Addendum to Sublease, as the case may be.

Sublease Reference Date:	November 14, 2016.
Sublessor:	Harrison Assets, LLC.
City: corporation.	City and County of San Francisco, a municipal
Building (Recital A):	1440 Harrison Street, San Francisco, California.
Subleased Premises (Recitals A & E):	The entire property consisting of approximately 56,788 rentable square feet of office space in the Building, and the Outdoor Area as shown on <u>Exhibit C</u> , attached hereto.
Initial Term: (Section 2(a)):	8 years, 3 months Commencing on July 1, 2017.
Extension Options: (Section 2(c)):	Two (2) additional terms of five (5) years each.
Commencement Date:	July 1, 2017.
Rent Commencement Date:	July 1, 2017

Base Rent: (Section 3(a)) \$298,137 per month industrial gross for Year 1, with 3% annual increases for Years 2 through 8.

Permitted Use (Section 4(a)): Cal-Win and other public programs, general office space and City administrative or business related purpose in accordance with the provisions of the Master Lease.

Tenant Improvements (Section 5): None.

Utilities and Services (Section 8): Provided and paid by City.

Address for Rent Payments: Harrison Assets, LLC
c/o Ronaldo Cianciarulo
827 DeHaro Street
San Francisco, CA 94107.

Notice Address of City (Section 23): Phil Arnold
Department of Human Services
170 Otis Street, 8th Floor
San Francisco, CA 94103

and copy to: Attn: Director of Property
Real Estate Division
25 Van Ness Avenue, Suite 400
San Francisco, CA 94102
Fax No.: (415) 552-9216

and copy to: Office of the City Attorney
City Hall, Room 234
1 Dr. Carlton B. Goodlett Place
San Francisco, CA 94102-4682
Attn: Eileen M. Malley
Deputy City Attorney.

Key Contact for City: Phil Arnold

Telephone No.: (415) 557-5641

Notice Address for Sublessor (Section 23): Harrison Assets, LLC
c/o Ronaldo Cianciarulo
827 DeHaro Street
San Francisco, CA 94107.

Key Contact for Sublessor: Ronaldo Cianciarulo

Telephone No.: (415) 793-3200

Alternate Contact for Sublessor:

Bill Cianciarulo

Telephone No.:

(415) 515-4922

C. Section 2(a) Term of Sublease is revised by deleting the first two sentences, and replacing it the following: “The term of the Sublease is eight years, three months, commencing on July 1, 2017 (the “Commencement Date”) and ending on September 30, 2025 (the “Expiration Date”). From and after the Commencement Date, the terms of this Addendum to Sublease Agreement supercede the corresponding terms of the Sublease Agreement.”

D. Section 2(b) Commencement Date Memorandum is deleted.

E. Section 2(c) Extension Options is revised by deleting the first sentence, and replacing it with the following: “City shall have the right to extend the Initial Term of this Sublease (the “Extension Option(s)”) for two additional terms of five (5) years each.” In the second sentence after “Section 3(b) of this Sublease”, the words “and (ii) Sublessor shall make the improvements described in Section 5(e) of this Sublease” are deleted.

F. Section 3(a) Initial Term is deleted and replaced by the following:

“(a) Initial Term. The monthly Base Rent for the Initial Term shall be as follows:

Year 1 - July 1, 2017 to June 30, 2018	\$298,137.00
Year 2 - July 1, 2018 to June 30, 2019	\$307,081.11
Year 3 - July 1, 2019 to June 30, 2020	\$316,293.54
Year 4 - July 1, 2020 to June 30, 2021	\$325,782.35
Year 5 - July 1, 2021 to June 30, 2022	\$335,555.82
Year 6 - July 1, 2022 to June 30, 2023	\$345,622.49
Year 7 - July 1, 2023 to June 30, 2024	\$355,991.17
Year 8 - July 1, 2024 to September 30, 2025	\$366,670.90

G. Section 3(b)(iii) is deleted and replaced by the following:

“(iii) If only one appraisal is submitted within the requisite time period, it shall be deemed to be the prevailing market rate. If both appraisals are submitted within such time period, and if the two appraisals so submitted differ by ten percent (10%) or less of the higher of the two, then the average of the two shall be the prevailing market rate. If the two appraisals differ by more than ten percent (10%) of the higher of the two, then the two appraisers shall immediately select a third appraiser. Within thirty (30) days after the appointment of the third appraiser, a majority of the appraisers shall determine the prevailing market rate which shall be the Base Rent for the first year of the Extended Term.

The Base Rent for years 2 through 5 of each Extended Term shall increase three percent (3%) over the rent for the immediate prior year.”

H. Section 3(b)(v) deleted and replaced by the following:

(v) All appraisers specified herein shall be members of the American Institute of Real Estate Appraisers (MAI) with not less than five (5) years' experience appraising leases of commercial properties similar to the Subleased Premises in the South of Market area of San Francisco. Sublessor and City shall pay the cost of the appraiser selected by such party and one-half of the cost of the third appraiser plus one-half of any other costs incurred in the arbitration. The third appraiser shall not have served as an appraiser, or have been otherwise employed, on behalf of or by either Sublessor or City.

I. Section 3(c) No Additional Rent or Additional Charges is deleted.

J. Sections 5 Tenant Improvements is deleted in its entirety.

K. Paragraph 7(a). Paragraph 7(a) is amended by deleting the words “including graffiti removal from the exterior of the Building and the fences”. Paragraph 7(a) is further amended by adding the words “the elevators” after the words “drainage systems”.

L. Paragraph 7(b) City's Repairs is amended to insert in the first sentence after “Subleased Premises” the following words: including graffiti removal from the exterior of the Building and the fences,”.

M. A new Paragraph 7(d) is added, as follows:

7(d). Increases in Taxes, Insurance Premiums, and Operating Expenses over Year 1. Sublessee shall pay the increases in Taxes, Insurance Premiums and Operating Expenses for the Subleased Premises over the Year 1 expenses.

(a) A. “

(b) Definitions

For purposes hereof, the following terms shall have the meanings hereinafter set forth:

- i) "Base Year" means the calendar year 2017
- ii) "City's Percentage Share" means the one hundred percent (100%).
- iii) "Expense Year" means each calendar year commencing January 1st of each year during the Term, including any partial year in which this Lease commences; provided that Landlord, upon advance written notice to City, may change the Expense Year to any other twelve (12) consecutive month period and, in the event of any such change, City's Percentage Share of Operating Costs shall be equitably adjusted for the Expense Years involved in any such change. Expense Year shall not include the Base Year.

- iv) "Operating Costs" means the total reasonable and prudent costs and expenses actually paid or incurred by Landlord in connection with the management, operation, maintenance and repair of the Building, including, but not limited to: (1) the cost of repairs and all labor and material costs related thereto, and the cost of general maintenance, cleaning and service contracts and the cost of all supplies, tools and equipment required in connection therewith, (2) the cost incurred by Landlord for the insurance required to be carried on the Building by this Sublease, (3) wages, salaries, payroll taxes and other labor costs and employee benefits relating to employees of Landlord or its agents engaged in the repair or maintenance of the Building, allocated in proportion to the percentage of such person's working time actually spent working in connection with the Building, (4) fees, charges and other costs of all independent contractors engaged by Landlord, allocated in proportion to the percentage of such person's working time actually spent working in connection with the Building, (5) the cost of capital improvements made to the Building as a labor-saving or energy saving device or to effect other economies in the operation or maintenance of the Building and which benefit the Premises, or made to the Building after the Effective Date of this Lease that are required under any governmental law or regulation that was not applicable to the Building on the Effective Date, unless caused by Landlord's deliberate or negligent violation of such law, rule or regulation, and (6) other expenses reasonably incurred in connection with the operation, maintenance or repair of the Building (other than Real Estate Taxes and any services for which Landlord is separately and directly reimbursed by City) which would, under generally accepted accounting principles, be considered an operating expense. The computation of Operating Costs shall be made in accordance with generally accepted accounting principles. With respect to the costs of items included in Operating Costs under (5), such costs shall be amortized over the useful life thereof, together with interest on the unamortized balance at a rate per annum equal to three (3) percentage points over the Treasury Rate charged at the time such item is constructed, but not more than the maximum rate permitted by law at the time such item is constructed.
- v) All Operating Costs shall be reasonable and if necessary, equitably adjusted. In no event shall Landlord recapture more than one hundred percent (100%) of the Operating Costs in any Expense Year.
- vi) Notwithstanding the foregoing, "Operating Costs" shall exclude the items described on the attached Addendum Exhibit A.
- vii) "Real Estate Taxes" means all taxes, assessments and charges levied upon or with respect to the portion of the Building owned by Landlord, or Landlord's interest in the Building. Real Estate Taxes shall include, without limitation, all general real property taxes and general and special assessments, charges, fees, or assessments for transit, housing, police, fire, or other governmental services thereof, service payments in lieu of taxes that are now or hereafter levied or assessed against Landlord by the United States of America, the State of California or any political subdivision thereof, public corporation, district, or any other political or public entity, and shall also include any other tax, fee or other excise, however described, that may be levied or assessed as a substitute for, or as an addition to, in whole or in part, any other Real Estate Taxes.
- viii) Notwithstanding the foregoing, Real Estate Taxes shall exclude (1) franchise, transfer, inheritance, gross receipts, or capital stock taxes or income taxes of Landlord from all sources unless, due to a change in the method of taxation, any of such taxes is levied or assessed against Landlord as a substitute for, or as an addition to, in whole or

in part, any other tax that would otherwise constitute a Real Estate Tax, (2) any penalties, fines, interest or charges attributable to the late payment of any taxes, except to the extent attributable to City's failure to pay its portion of Real Estate Taxes hereunder, (3) any personal property taxes payable by City hereunder or by any other tenant or occupant of the Building, or (4) any increase in Real Estate Taxes due to any reassessment upon a transfer of any of Landlord's interest in the Building or the real property on which the Building is located.

- ix) "Tax Year" means each calendar year during the Term, including any partial year during which this Lease may commence; provided that Landlord, upon notice to City, may change the Tax Year from time to time to any other twelve (12) consecutive month period and, in the event of any such change, City's Percentage Share of Real Estate Taxes shall be equitably adjusted for the Tax Year involved in any such change. Tax Year shall not include the Base Year.

(c) Payment of Percentage Share of Operating Costs

During the Term, commencing after the end of the Base Year, City shall pay to Landlord each month, as Additional Charges, one twelfth (1/12) of City's Percentage Share of the amount, if any, by which Operating Costs for each Expense Year exceed the Operating Costs for the Base Year. City shall make such payments, in advance, in an amount estimated by Landlord in reasonable detail in a writing delivered to City. Landlord may revise such estimates of Operating Costs from time to time and City shall thereafter make payments on the basis of such revised estimates, provided that no such revisions shall be retroactive and Landlord may not make any such revisions more than twice in any given Expense Year and no such revision may be made any earlier than four (4) months subsequent to the prior estimate for such Expense Year. With reasonable promptness not to exceed sixty (60) days after the expiration of each Expense Year, Landlord shall furnish City with a statement (herein called "Landlord's Expense Statement"), prepared by an independent certified public accountant, setting forth in reasonable detail the Operating Costs for such Expense Year and City's Percentage Share thereof. If City's Percentage Share of the actual Operating Costs for such Expense Year exceeds the estimated Operating Costs paid by City for such Expense Year, City shall pay to Landlord (whether or not this Lease has terminated) the difference between the amount of estimated Operating Costs paid by City and City's Percentage Share of the actual Operating Costs within thirty (30) days after the receipt of Landlord's Expense Statement. If the total amount paid by City for any such Percentage Share of Operating Costs exceeds City's Operating Costs Share of the actual Operating Costs for such Expense Year, such excess shall be credited against the next installments of Operating Costs due from City to Landlord hereunder, or refunded to City, at City's option.

(d) Payment of Percentage Share of Real Estate Taxes

During the Term, commencing after the end of the Base Year, City shall pay to Landlord each month, as Additional Charges, one twelfth (1/12) of City's Percentage Share of the amount, if any, by which Real Estate Taxes for each Tax Year exceed Real Estate Taxes for the Base Year. City shall make such payments, in advance, in an amount estimated by Landlord in reasonable detail in a writing delivered to City. With reasonable promptness not to exceed thirty (30) days after Landlord has received the tax bills for any Tax Year, Landlord shall furnish City with a statement ("Landlord's Tax Statement") setting forth the amount of Real Property Taxes for such Tax Year and City's Percentage Share thereof. If City's Percentage Share of the actual Real Estate Taxes for such Tax Year exceeds the estimated Real Estate Taxes paid by City for such Tax Year, City shall pay to Landlord (whether or not this Lease has terminated) City's Percentage Share of the actual Real Estate Taxes within thirty (30) days after the receipt of Landlord's Tax

Statement. If the total amount of estimated Real Estate Taxes paid by City for such Tax Year exceeds City's Percentage Share of the actual Real Estate Taxes for such Tax Year, such excess shall be credited against the next installments of Real Estate Taxes due from City hereunder, or at City's option, such excess shall be refunded to City.

(e) Proration

If the Commencement Date or Expiration Date shall occur on a date other than the first or last day of a Tax Year or Expense Year, City's Percentage Share of Real Estate Taxes or Operating Costs for the Tax Year or Expense Year in which the Commencement Date or Expiration Date occurs, shall be prorated based on a three hundred sixty-five (365)-day year.

(f) Audits

City shall have the right, upon not less than five (5) business days' notice to Landlord, to audit the books and records of the Building related to Operating Costs and Real Estate Taxes. If such audit discloses any discrepancies which would result in a reduction of City's Percentage Share of Operating Costs for any Expense Year, Landlord shall immediately refund to City the amount of any overpayment by City. City shall pay the cost of such audit, provided that if such audit discloses any discrepancies which result in a reduction of City's Percentage Share of Operating Costs of three percent (3%) or more for any Expense Year, then Landlord shall pay the costs of such audit.

(g) Records

Landlord shall maintain at its offices in San Francisco in a safe, complete and organized manner all of its records pertaining to this Lease and Real Estate Taxes, Operating Costs and any other charges paid by City pursuant hereto, for a period of not less than three (3) years following expiration of the Term. Landlord shall maintain such records on a current basis and in sufficient detail to facilitate adequate audit and review thereof. All such books and records shall be available for inspection, copying and audit by City and its representatives, at City's expense, subject to the provisions of subsection (e) above.]

N. Paragraph 8(d) Janitorial and Security is amended by adding after "janitorial services" the words "(and graffiti removal)", and deleting the second and third sentences.

O. . .

P. Paragraph 14(b) Sublessor's Default is changed as follows: In the first and second sentence, the word and number "ten (10)" are deleted and replaced with the word and number "thirty (30)". In addition, the word "substantially" is inserted before the word "interferes" in the third sentence from the end of this paragraph. In addition, the word "substantially" is inserted before the word "impairs" in the next to last sentence.

Q. Paragraph 22 Brokers is deleted and replaced by the following:

"22. Brokers. City agrees that it has not used any real estate broker in connection with the procuring, execution of delivery of this Addendum to Sublease Agreement. Sublessor is

represented by Mike McCarthy, Colliers International Group, Inc. Each party hereto agrees to indemnify and hold the other harmless against any claims by any broker for services rendered to the indemnifying party in connection to this Addendum to Sublease Agreement.”

R. In paragraph 23 Notices, the Sublessor’s address is deleted, and replaced by the following:

Sublessor: Harrison Assets, LLC
c/o Ronaldo Cianciarulo
827 DeHaro Street
San Francisco, CA 94107.

3. Exhibits Attached. All exhibits described herein are attached to this Agreement.

ADDENDUM EXHIBIT A - EXCLUSIONS FROM OPERATING COSTS

4. Other Sublease Agreement Terms Not Changed By This Addendum to Sublease Agreement Shall Remain in Effect. All other terms and conditions of the Sublease Agreement that were not changed by this Addendum to Sublease Agreement shall remain in full force and effect.

IN WITNESS WHEREOF, the parties have executed this Addendum to Sublease Agreement on the date first above written.

SUBLESSOR: HARRISON ASSETS, LLC,
a California limited liability company,
by Baker Hamilton Properties, Inc.,
Its sole member

By: _____
Ronaldo Cianciarulo
Its President

CITY: CITY AND COUNTY OF SAN FRANCISCO,
a municipal corporation

By: _____
John Updike
Director of Property

RECOMMENDED:

Director, Department of Human Services

APPROVED AS TO FORM:

DENNIS J. HERRERA, City Attorney

By: _____
Heidi Gewertz
Deputy City Attorney

ADDENDUM EXHIBIT A

EXCLUSIONS FROM OPERATING COSTS

1. Costs of capital repairs, capital improvements and equipment, except for those (i) required by laws enacted on or after the date of the Lease amortized over the useful life of the improvement and/or equipment, together with interest at the actual interest rate incurred by Landlord in connection with such capital improvements, or (ii) acquired to cause, in Landlord's good faith judgment, an immediate (i.e., commencing within the first year after completion of such repairs or improvements or installation of such equipment) reduction in other Operating Costs, amortized over the useful life of such improvements at an annual rate reasonably calculated to equal the amount of Operating Costs to be saved in each calendar year throughout the Term (as determined at the time Landlord elected to proceed with the capital improvement or acquisition of the capital equipment to reduce operating expenses), together with interest at the actual interest rate incurred by Landlord;
2. Rentals and other related expenses for items (except when needed in connection with normal repairs and maintenance of permanent systems) which if purchased rather than rented, would constitute a capital improvement which is specifically excluded in item 1 above (excluding, however, equipment not affixed to the Building which is used in providing janitorial or similar services);
3. Costs incurred by Landlord for the repair of damage to the Building, to the extent that Landlord is reimbursed by insurance proceeds (excluding any deductible) and costs occasioned by the exercise of the right of eminent domain;
4. Intentionally omitted;
5. Depreciation, amortization and interest payments, except to the extent provided herein pursuant to items 1(i) and 1(ii) above and except on materials, tools, supplies and vendor-type equipment purchased by Landlord to enable Landlord to supply services Landlord might otherwise contract for with a third party where such depreciation, amortization and interest payments would otherwise have been included in the charge for such third party's services, all as determined in accordance with generally accepted accounting principles, consistently applied (as applied to commercial real estate), and when depreciation or amortization is permitted or required, the item shall be amortized over its reasonably anticipated useful life (as reasonably determined by Landlord);
6. Leasing commissions, attorneys' and other professionals' fees, space planning costs and all other costs and expenses in connection with negotiations with prospective tenants or other occupants in the Building or any present or future ground lessors or holders of any mortgages or other encumbrances affecting any of the Building or the defense of Landlord's title to the Building or the real property on which it is located;
7. Intentionally deleted;
8. Costs incurred by Landlord due to violation by Landlord of applicable laws, rules or regulations, the terms and conditions of any lease, ground lease, mortgage or deed of trust, or other covenants, conditions or restrictions encumbering the Building or the real property on which it is located;

9. Overhead and profit increments paid to Landlord or to subsidiaries or affiliates of Landlord;
10. Any ground lease rental or rental under any other underlying leases;
11. Except as specifically permitted by items 1(i) and 1(ii) above, interest, principal, points and fees on debts or amortization on any mortgage, deed of trust or any other debt instrument encumbering any of the Building or the real property on which it is located;
12. Advertising or promotional expenditures, and the costs of acquiring and installing signs in or on any of the Building
13. Intentionally omitted;
14. Intentionally omitted;
15. Intentionally omitted;
16. Tax penalties incurred as a result of Landlord's negligence, inability or unwillingness to make payments when due;
17. Costs arising from the presence of Hazardous Material in or about the Building including, without limitation, groundwater or soil conditions, except if such Hazardous Material is brought onto the Premises or Property by City or its Agents;
18. Landlord's charitable or political contributions;
19. To the extent the following costs arise during any applicable warranty periods, costs as a result of repairs of latent defects in the Building core and shell or improvements installed by Landlord or in the Building Systems, and any costs incurred by Landlord in the event any portion of the Building is made untenantable by fire or other casualty required to be insured against pursuant to the terms of the Lease;
20. Capital costs for sculpture, paintings or other objects of art;
21. Costs (including, without limitation, all attorneys' fees and costs of settlement, judgments and payments in lieu thereof) arising from claims, disputes or potential disputes, including, without limitation, tax disputes, except to the extent that such dispute results in a cost savings with respect to Operating Costs;
22. All direct cost of refinancing, selling, exchanging or otherwise transferring ownership of the Building or the real property on which it is located or any interest therein or portion thereof, including broker commissions, attorney's fees and closing costs;
23. Reserves for bad debts, rent loss, capital items or further Operating Costs; and
24. Landlord's general corporate overhead and general and administrative.
25. Any other expense that under generally accepted accounting principles would not be considered a maintenance or operating expense.

Attachment #1
1440 Harrison Lease

	Current	Proposed
Premises	52,200 SF plus 31 car parking	56,788 SF** plus 31 car parking **The building was measured using BOMA standards
Base Rent	\$101,268 monthly	\$298,137 monthly
Operating Expenses	\$54,275 monthly	\$54,275 monthly
Base Rent Increase Date	NA	Annually on February 1
Base Rent Increase Amount	NA	3%
Term	June 30, 2017	September 30, 2025
Options to Extend	NA	Two (2) five year options at 95% FMR

The term of the proposed Sublease renewal will be for eight (8) years, three (3) months, commencing upon July 1, 2017 and expiring on September 30, 2025. Under the proposed Sublease the City has (2) 5 year options to renew the term (subject to further Board of Supervisors approval). Base Rent during the Option Terms are at 95% of the then fair market value considering all factors.

The Base Rent for the proposed Sublease shall be \$298,137 per month for Year 1 (approximately \$63.00 per square foot annually measured on the building area only), with 3% annual increases for Years 2 through 8. The City will continue to pay for repairs, utilities, janitorial services and security.

The proposed rental rate has been validated by a MAI appraisal by CBRE, Inc. and the CBRE appraisal has been approved using USPAP guidelines by Clifford & Associates.

The Human Services Agency reports that the funding source for 1440 Harrison Street is approximately 63% from the General Fund, 37% from State and Federal Funds.

We recommend approval of the proposed Sublease. If you have any questions regarding this matter, please contact Charlie Dunn of our office on 554-9861.

Respectfully,



John Updike
Director of Property

Attachments

cc: Trent Rhorer, Executive Director, HSA
Dan Kaplan, Deputy Director of Admin and Finance, HSA
Robert Walsh, Director of Facilities and Operations, HSA

FORM SFEC-126:
NOTIFICATION OF CONTRACT APPROVAL
(S.F. Campaign and Governmental Conduct Code § 1.126)

City Elective Officer Information <i>(Please print clearly.)</i>	
Name of City elective officer(s): Members, SF Board of Supervisors	City elective office(s) held: Members, SF Board of Supervisors

Contractor Information <i>(Please print clearly.)</i>	
Name of contractor: Harrison Assets LLC, a California limited liability company	
<i>Please list the names of (1) members of the contractor's board of directors; (2) the contractor's chief executive officer, chief financial officer and chief operating officer; (3) any person who has an ownership of 20 percent or more in the contractor; (4) any subcontractor listed in the bid or contract; and (5) any political committee sponsored or controlled by the contractor. Use additional pages as necessary.</i>	
(1) Ronaldo J Cianciarulo , Managing Member (2) Ronaldo J Cianciarulo , Managing Member (3) Ronaldo J Cianciarulo (4) None (5) None	
Contractor address: 827 DeHaro Street, San Francisco, CA 94107	
Date that contract was approved:	Amount of contract: \$32,913,625.26 over 99 months
Describe the nature of the contract that was approved: Lease at 1440 Harrison Street for the Human Services Agency	
Comments:	

This contract was approved by (check applicable):

- the City elective officer(s) identified on this form (Mayor, Edwin Lee)
- a board on which the City elective officer(s) serves San Francisco Board of Supervisors
Print Name of Board
- the board of a state agency (Health Authority, Housing Authority Commission, Industrial Development Authority Board, Parking Authority, Redevelopment Agency Commission, Relocation Appeals Board, Treasure Island Development Authority) on which an appointee of the City elective officer(s) identified on this form sits
Print Name of Board

Filer Information <i>(Please print clearly.)</i>	
Name of filer: Clerk of the Board, Angela Calvillo	Contact telephone number: 415-554-5184
Address: City Hall, Room 244 San Francisco, CA 94108	E-mail: board.of.supervisors@sfgov.org

Signature of City Elective Officer (if submitted by City elective officer)

Date Signed

Signature of Board Secretary or Clerk (if submitted by Board Secretary or Clerk)

Date Signed