

MEMORANDUM

March 7, 2017

TO: AIRPORT COMMISSION
Hon. Larry Mazzola, President
Hon. Linda S. Crayton, Vice President
Hon. Eleanor Johns
Hon. Richard J. Guggenhime
Hon. Peter A. Stern

FROM: Airport Director

SUBJECT: Adoption of Two Resolutions Relating to the On-Airport Hotel Project: (1) Amendment of the Fiscal Year 2016/2017 Five-Year and Ten-Year Capital Plans to Increase the Hotel Project Budget by \$30 Million; and (2) Twentieth Supplemental Bond Resolution, in Connection with the On-Airport Hotel, Increasing Airport Capital Plan Bond Authorization by \$35 Million from \$243 Million to \$278 Million in Principal Amount, and Increasing Hotel Special Facility Bond Authorization by \$35 Million from \$225 Million to \$260 Million in Principal Amount

DIRECTOR'S RECOMMENDATION: AMEND THE FISCAL YEAR 2016/2017 FIVE-YEAR AND TEN-YEAR CAPITAL PLANS TO INCREASE THE HOTEL PROJECT BUDGET BY \$30 MILLION; AND APPROVE ADDITIONAL BOND AUTHORIZATIONS FOR THE ON-AIRPORT HOTEL, INCREASING AIRPORT CAPITAL PLAN BONDS AUTHORIZATION BY \$35 MILLION, FROM \$243 MILLION TO \$278 MILLION IN PRINCIPAL AMOUNT, AND INCREASING HOTEL SPECIAL FACILITY BONDS AUTHORIZATION BY \$35 MILLION, FROM \$225 MILLION TO \$260 MILLION IN PRINCIPAL AMOUNT.

Executive Summary

Since the fall of 2015, the Bay Area has experienced a significant increase in construction costs, which has hampered the Airport's ability to deliver the On-Airport Hotel (the "Hotel") within the existing project budget without significantly reducing the number of guest rooms. This construction cost escalation, as well as increases in the amount of Hotel space dedicated to revenue-generating meeting facilities and food and beverage outlets, has led to a \$30 million increase in the project budget.

This increase in the project budget makes it possible to construct the Hotel with approximately 351 guest rooms. This will generate more revenue than if the existing budget were adhered to and a substantially smaller Hotel with 289 rooms were to be built. The original program with 351 rooms will generate total gross revenues of \$60 million annually. This is \$12 million higher by the third year of operation for the 351-room Hotel than for a smaller, 289-room Hotel. A smaller 289-room Hotel will generate only \$48 million annually. Further, the Hotel will be able to provide more rooms to accommodate the Airport's growing number of passengers. Updated revenue projections show that the Hotel remains financially viable, even with the higher budget.

This change in the project budget will require three actions: (1) amending the Fiscal Year ("FY") 2016/2017 Five-Year and Ten-Year Capital Plans Hotel Project Budget; (2) approving additional Airport capital plan bond authorization, and (3) approving additional hotel special facility bonds authorization.

THIS PRINT COVERS CALENDAR ITEM NO. _____

Background

On September 22, 2015, the Commission adopted Resolution No. 15-0182, the Eighteenth Supplemental Bond Resolution, which designated the Hotel as a “special facility” and authorized the issuance of up to \$243 million in principal amount of Airport Capital Plan Bonds and \$225 million principal amount of Hotel Special Facility Bonds, to finance the construction and development of the Hotel.

The Hotel’s cash-flow must be kept separate from that of the Airport, so that the Hotel operator can pay Hotel expenses directly from Hotel revenues. To establish this separate treatment of Hotel revenues, in 2015 the Airport Commission designated the Hotel as a “special facility” under the Airport’s 1991 Master Bond Resolution. To finance the Hotel at the lowest available cost while maintaining its special facility status, the Commission has approved the issuance of two types of bonds:

- Tax-exempt Airport Capital Plan Bonds (i.e., general airport revenue bonds), which would be sold to investors; and
- Tax-exempt Hotel Special Facility Bonds, which would be purchased by the Commission with Airport Capital Plan Bond proceeds.

On June 1, 2016, the Commission adopted Resolution No. 16-0166, which approved the FY 2016/2017 Five-Year and Ten-Year Capital Plans, including a Hotel project budget of \$225 million (\$210 million for the Hotel and \$15 million for the new Hotel AirTrain Station). Airport staff has engaged a Design-Build team and a hotel operator.

The increase in budget of \$30 million is due primarily to: 1) significant construction cost escalation, particularly in the areas of electrical, mechanical, glazing and interior finishes; and 2) increases in the amount of space allocated for revenue-generating facilities (e.g., meeting facilities and food and beverage outlets). This represents a 14.3 percent increase in the construction budget since the fall of 2015. In comparison, an independent cost management firm estimates that San Francisco construction costs have increased by 17.9 percent in the past year.¹

The Airport and its financial advisors have determined that the increase in the project budget would result in a \$35 million increase in the authorization required for both Airport Capital Plan Bonds and Hotel Special Facility Bonds to cover the increase in project cost and associated financing costs. The changes in the Airport’s proposed Hotel financing plan are summarized on the following page.

Costs Payable from Airport Capital Plan Bonds	October 2015	February 2017 Revision
Hotel AirTrain station construction costs:	\$ 15,000,000	\$ 15,000,000
Costs of issuance:	3,000,000	3,000,000
Purchase of Hotel Special Facility Bonds:	225,000,000	260,000,000
Project Costs Payable from Hotel Special Facility Bonds		
Hotel construction costs (including repayment of commercial paper principal and reimbursement of operating funds):	\$210,000,000	\$240,000,000
Capitalized Interest, Commercial Paper Interest:	20,000,000	25,000,000
Less contribution from Hotel operator:	<u>(5,000,000)</u>	<u>(5,000,000)</u>
<i>Total Hotel Special Facility Bonds:</i>	\$225,000,000	\$260,000,000
Total Airport Capital Plan Bonds:	\$243,000,000	\$278,000,000

Airport staff, in consultation with the Commission’s hospitality consultant and financial advisors, expects the Hotel to produce positive financial results at this new project budget, in part because the hospitality consultant’s updated projections show a higher average daily room rate for the Hotel compared to projections from 2015. By maintaining the original program with 351 guest rooms, the Airport expects to

¹ Rider Levett Bucknall, “USA Report, Quarterly Construction Cost Report,” December 2016.

derive higher “net profits” (i.e., total hotel revenues less total hotel operating expenses, required reserve deposits, and debt service costs) than a smaller 289-room Hotel that is within the existing project budget. Once occupancy has stabilized, total gross revenues are estimated to be approximately \$12 million per year higher for the 351-room Hotel than for the smaller, 289-room Hotel.

Therefore, Airport staff requests that the Commission adopt a resolution amending the FY 2016/2017 Five-Year and Ten-Year Capital Plans to increase the Hotel project budget by \$30 million, for a new total budget of \$255 million (\$240 million for the Hotel and \$15 million for the Hotel AirTrain Station). To generate \$30 million in additional Hotel project funds, and to cover associated financing costs, Airport staff also requests that this Commission adopt a resolution (the “Bond Resolution”) that would authorize:

- Up to \$35 million principal amount of additional Hotel special facility bonds, bringing the total approved amount to \$260 million, to finance Hotel and related costs or to refinance Commercial Paper issued for Hotel costs, and fund a capitalized interest account. As currently authorized, the Hotel special facility bonds will have a maturity of 40 years and bear interest at a fixed rate to be determined at the time of issuance; and
- Up to \$35 million principal amount of additional Airport Capital Plan Bonds, bringing the total approved amount to \$278 million, to finance the purchase of the Hotel special facility bonds by the Commission, along with financing for the Hotel AirTrain station and/or refinancing of Commercial Paper issued for the station, and associated costs of issuance. There is no change in the maximum bond maturity of 40 years, or in the interest rate limitations set forth in Resolution No. 50-11 of the Board of Supervisors. The Airport Capital Plan Bonds will be sold prior to June 30, 2020, and may be issued as Variable Rate Bonds.

Airport staff is also requesting approval of the supplemental appropriation of the additional Airport revenue bond proceeds and Hotel special facility bond proceeds, and \$60,000 in additional Airport operating funds that will support the City Services Auditor Division (“CSA”) pursuant to Section F1.113 of the City Charter. As required, 0.2 percent of the project cost is budgeted to support CSA services.

Request to the Board of Supervisors

If the Twentieth Supplemental Bond Resolution is adopted by this Commission, the Commission Secretary will request that the Board of Supervisors approve the increase in Airport Capital Plan Bonds and Hotel Special Facility Bonds. The Airport will also request the necessary increase in appropriations. Once final approval is obtained from the Board of Supervisors, I will return to the Commission for approval of one or more sale resolutions prior to selling and issuing the Airport Capital Plan Bonds and the Hotel Special Facility Bonds.

Recommendation

I recommend that this Commission adopt the two attached Resolutions: (1) amending the Fiscal Year 2016/2017 Five-Year and Ten-Year Capital Plans to increase the Hotel Project budget, and (2) approving additional bond authorization for the Hotel.

Ivar C. Satero
Airport Director

Prepared by: Leo Fermin
Chief Business and Finance Officer

AMENDMENT OF THE FISCAL YEAR 2016/2017 FIVE-YEAR AND TEN-YEAR CAPITAL PLANS, TO INCREASE THE HOTEL PROJECT BUDGET BY \$30 MILLION

- WHEREAS, the Airport Commission (the “Commission”) of the City and County of San Francisco, on June 1, 2016, adopted its Resolution No. 16-0166, approving the Airport’s \$5.7 billion Five-Year Capital Plan for Fiscal Years (“FY”) 2016/2017 to FY 2020/2021 and \$6.1 billion Ten-Year Capital Plan for FY 2016/2017 to FY 2025/2026 (collectively, the “FY 2016/2017 Five-Year and Ten-Year Capital Plans”); and
- WHEREAS, the total budget for the On-Airport Hotel project (including both the On-Airport Hotel and the Hotel AirTrain station) under the FY 2016/2017 Five-Year and Ten-Year Capital Plans was \$225 million; and
- WHEREAS, construction cost escalation, as well as increases in the amount of On-Airport Hotel space dedicated to revenue-generating meeting facilities and food and beverage outlets, has led to a \$30 million increase in projected project costs; and
- WHEREAS, updated revenue projections show that the Hotel remains financially viable, even with the higher budget; and
- WHEREAS, the Airport has identified the necessary capital funding sources to support a \$30 million increase to the On-Airport Hotel project budget under the FY 2016/2017 Five-Year and Ten-Year Capital Plans; now therefore be it
- RESOLVED, that this Commission approves a \$30 million increase in the On-Airport Hotel project budget under the FY 2016/2017 Five-Year and Ten-Year Capital Plans; and, be it further
- RESOLVED, that Resolution No. 16-0166, except as supplemented and amended by this Resolution, is hereby ratified, approved and confirmed and remains in full force and effect.

TWENTIETH SUPPLEMENTAL BOND RESOLUTION, IN CONNECTION WITH THE ON-AIRPORT HOTEL, INCREASING AIRPORT CAPITAL PLAN BONDS AUTHORIZATION BY \$35 MILLION FROM \$243 MILLION TO \$278 MILLION IN PRINCIPAL AMOUNT, AND INCREASING HOTEL SPECIAL FACILITY BONDS AUTHORIZATION BY \$35 MILLION FROM \$225 MILLION TO \$260 MILLION IN PRINCIPAL AMOUNT

WHEREAS, the Airport Commission (the “Commission”) of the City and County of San Francisco (the “City”), on December 3, 1991, adopted its Resolution No. 91-0210, providing for the issuance of San Francisco International Airport Second Series Revenue Bonds, which Resolution, as previously supplemented and amended, including as amended and supplemented by Resolution No. 03-0220, adopted on October 21, 2003, Resolution No. 08-0035, adopted on February 19, 2008, Resolution No. 10-0316, adopted on October 26, 2010, Resolution No. 12-0050, adopted on March 20, 2012, Resolution No. 14-0024, adopted on February 18, 2014, Resolution No. 15-0182, adopted on September 22, 2015 (the “Eighteenth Supplemental Resolution”), and Resolution No. 16-0274, adopted on November 1, 2016, is herein called the “1991 Resolution”; and

WHEREAS, the 1991 Resolution provides for the issuance by the Commission from time to time of revenue bonds (the “1991 Resolution Bonds”); and

WHEREAS, as part of implementation of the Airport Master Plan approved by the Commission in 1992, the Commission is undertaking the development of an on-Airport hotel to be owned by the Commission (the “Hotel”) on a portion of Plot 2 at the former Hilton Hotel site, along with a new AirTrain station to connect the Hotel with the AirTrain system (the “AirTrain Station” and collectively with the Hotel, the “Hotel Project”); and

WHEREAS, the Commission, pursuant to the 1991 Resolution, has previously authorized the issuance of up to \$7,791,725,000 aggregate principal amount of 1991 Resolution Bonds (the “Capital Plan Bonds”) for the purpose of financing and refinancing the development, acquisition, construction, and equipping of capital projects approved by the Commission and costs related thereto, of which an aggregate principal amount of \$5,502,605,000 remains unissued, including an aggregate principal amount of \$4,358,695,227 that remains subject to the approval of the Board of Supervisors; and

WHEREAS, pursuant to the Eighteenth Supplemental Resolution, the Commission: (a) authorized the issuance of not to exceed \$243,000,000 aggregate principal amount of Capital Plan Bonds (the “Airport Capital Plan Bonds”) to finance and refinance costs associated with the Hotel Project; and (b) authorized the issuance of special facility bonds in accordance with the terms of the 1991 Resolution in the aggregate principal amount of up to \$225,000,000 (the “Hotel Special Facility Bonds”) to finance and refinance costs associated with the Hotel; and

WHEREAS, to maintain the special facility status of the Hotel and finance it at the lowest available interest rates, the Commission determined to combine the desirable features of the Airport Capital Plan Bonds which are secured and payable from Airport net revenues and can therefore be sold to investors at the lowest available interest rates, and the Hotel Special Facility Bonds by selling the Airport Capital Plan Bonds to investors and purchasing the Hotel Special Facility Bonds with the proceeds of the Airport Capital Plan Bonds; and

- WHEREAS, the Airport Capital Plan Bonds and the Hotel Special Facility Bonds will be issued in accordance with the 1991 Resolution, applicable provisions of the Charter of the City, ordinances and resolutions of the Board of Supervisors, and the statutes of the State of California; and
- WHEREAS, the estimated costs of the Hotel have increased, thus requiring an increase in the authorized principal amount of both the Airport Capital Plan Bonds and the Hotel Special Facility Bonds of \$35,000,000 to pay the costs thereof; and
- WHEREAS, the Airport Master Plan was the subject of a Program Environmental Impact Report (“EIR”) certified by the San Francisco Planning Commission on May 28, 1992, by Motion No. 13356; and
- WHEREAS, the Environmental Planning Division of the San Francisco Planning Department reviewed the Hotel Project and issued an addendum to the EIR (“Addendum”) on February 5, 2014, determining that the Hotel Project is within the scope of the EIR and no additional environmental review is required under the California Environmental Quality Act (Public Resources Code Section 21000 et seq., “CEQA”); and
- WHEREAS, on May 19, 2014, the Commission, by Resolution No. 14-0095, adopted findings under CEQA related to the Hotel Project, determined to proceed with the Hotel Project, and authorized the Airport Director to proceed with implementation of the Hotel Project; and
- WHEREAS, the project files, including the EIR, Addendum and Commission Resolution No. 14-0095, have been made available for review by the Commission and the public, and those files are part of the record before the Commission; and
- WHEREAS, pursuant to Section 9.01(f) of the 1991 Resolution, the Commission, by Supplemental Resolution, may make any change or addition to the 1991 Resolution to provide for the issuance of, and to set the terms and conditions of, additional Series of Bonds under the 1991 Resolution; now, therefore, be it,
- RESOLVED, that this Commission has reviewed and considered the information in the EIR and Addendum, and hereby incorporates the CEQA findings contained in Resolution No. 14-0095, including findings of the Statement of Overriding Considerations, by this reference as though fully set forth in this Resolution; and be it further
- RESOLVED, that this Commission finds that since the EIR and Addendum were finalized, there have been no substantial project changes and no substantial changes in project circumstances that would require major revisions to the EIR due to the involvement of new significant environmental effects or an increase in the severity of previously identified significant impacts, and there is no new information of substantial importance that would change the conclusions set forth in the EIR and Addendum; and be it further
- RESOLVED, as follows:
- Section 1. Commission Findings. The Commission hereby finds and determines that the foregoing recitals are true and correct.
- Section 2. Defined Terms. Capitalized terms used but not otherwise defined in this Resolution shall have the meanings set forth in the 1991 Resolution.

- Section 3. Airport Capital Plan Bonds.
- (a) Increased Authorization of Capital Plan Bonds. In accordance with Section 9.01(f) of the 1991 Resolution, the Commission hereby authorizes the issuance of an additional aggregate principal amount of not to exceed \$35,000,000 of Airport Capital Plan Bonds for the Hotel Project.
- (b) Parameters of the Airport Capital Plan Bonds. The Airport Capital Plan Bonds shall be sold prior to June 30, 2020, and may be issued as Variable Rate Bonds.
- Section 4. Hotel Special Facility Bonds. The Commission hereby authorizes the issuance of an additional aggregate principal amount of not to exceed \$35,000,000 of Hotel Special Facility Bonds for the Hotel. The Hotel Special Facility Bonds shall be secured solely by, and payable solely from, the Hotel Revenues.
- Section 5. Ratification of Eighteenth Supplemental Resolution. The Eighteenth Supplemental Resolution, except as supplemented and amended by this Resolution, is hereby ratified, approved and confirmed and remains in full force and effect.
- Section 6. Delegation by Airport Director. The Airport Director is authorized to delegate the authority granted to him pursuant to this Resolution in writing to a member of Airport management upon consultation with the Office of the City Attorney.
- Section 7. Approval of Board of Supervisors. The Commission Secretary, for and on behalf of and in the name of the Commission, is authorized and directed to seek any approvals the Airport Director deems necessary or desirable from the Board of Supervisors of the City in order to carry out the intents and purposes of this Resolution, including approval of the additional Airport Capital Plan Bonds and Hotel Special Facility Bonds, and any necessary supplemental appropriations.
- Section 8. Ratification of Prior Acts. The actions of the officers, agents and employees of the Commission to carry out its intents and purposes taken prior to the adoption of this Resolution are ratified, approved and confirmed.
- Section 9. General Authorization. The Airport Director and the other officers, agents and employees of the Commission are authorized and directed to execute and deliver such documents, agreements and certificates and to take such other actions, upon consultation with the Office of the City Attorney, as may be necessary or desirable and in the best interests of the Commission to carry out the purposes and intents of this Resolution and the transactions contemplated hereby.
- Section 10. Effectiveness. This Resolution shall become effective on and as of the date of adoption hereof.
- Section 11. Severability. Should the application of any provision of this Resolution to any particular facts or circumstances be found by a court of competent jurisdiction to be invalid or unenforceable, then (a) the validity of other provisions of this Resolution shall not be affected or impaired thereby, and (b) such provision shall be enforced to the maximum extent possible so as to effect the purposes and intents of this Resolution.

ADOPTED by the Airport Commission of the City and County of San Francisco this 7th day of March, 2017,
by the following vote:

Ayes:

Noes:

Absent:

[SEAL]

Approved as to Form:

DENNIS J. HERRERA
City Attorney

By _____
Brooke D. Abola
Deputy City Attorney