

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

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TO: Budget and Finance Committee

FROM: Budget and Legislative Analyst



SUBJECT: February 8, 2018 Budget and Finance Committee Meeting

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Item 2 File 18-0070	Department: Department of Public Health (DPH) Real Estate Division (RED)
EXECUTIVE SUMMARY	
<p>Legislative Objectives</p> <ul style="list-style-type: none"> • The proposed resolution approves the fourth amendment to a lease agreement between BRCP 1390 Market, LLC as landlord, and Department of Public Health (DPH) as tenant, for approximately 27,826 square feet of office space at 1390 Market Street, increasing the annual rent from \$993,817 to \$1,801,120, with three percent annual increases thereafter, and extending the lease for three years, from December 1, 2018 through November 30, 2021, with two five-year options to extend. <p>Key Points</p> <ul style="list-style-type: none"> • In 1996, the Board of Supervisors approved a seven year lease for DPH to occupy 25,939 square feet of office space at 1390 Market Street for its Environmental Health Section (EHS). The Board of Supervisors approved three lease modifications to exercise five-year options to extend the lease in 2003, 2008, and 2013, and has authorized expansion of the leased premises to 27,826 square feet. DPH currently pays \$993,817 in annual rent, or \$35.72 per square foot. • The lease is scheduled to expire November 30, 2018 and DPH has an option to extend for another five years. However, EHS is scheduled to move into the new City office building at 49 South Van Ness in mid-2020, and the additional five years are not needed. The proposed fourth amendment to the lease extends the term for an additional three years, beginning December 1, 2018 and expiring November 30, 2021, but provides for the City the right to terminate the lease any time after November 30, 2019 with at least 270 days notice. DPH would have two five-year options to extend the lease through November 2031. <p>Fiscal Impact</p> <ul style="list-style-type: none"> • The initial annual rent of \$1,801,120 would be an increase of \$807,303 from the current rent of \$993,817. The annual rent of \$1,801,120 equals \$64.72 per square foot, which was determined to be fair market value based on a third party appraisal and appraisal review. • Over the three-year term of the lease extension, DPH would pay \$5,567,082 in total rent. <p>Recommendation</p> <ul style="list-style-type: none"> • Approve the proposed resolution. 	

MANDATE STATEMENT

City Administrative Code 23.27 states that any lease with a term of one year or longer or with monthly rent of \$5,000 or more and where the City is the tenant is subject to Board of Supervisors approval. If the base rent is more than \$45 per square foot, the Director of the City's Real Estate Division must obtain an independent appraisal; if the base rent is more than \$60 per square foot, the Director of the City's Real Estate Division must obtain an appraisal review.

BACKGROUND

In 1996, the Board of Supervisors approved a seven year lease for the Department of Public Health (DPH) to occupy 25,939 square feet of office space for its Environmental Health Section (EHS) at Fox Plaza, 1390 Market Street (Resolution 699-96). The Board of Supervisors has approved three lease modifications to exercise five-year options to extend in 2003 (File 03-0179, Resolution 159-03), 2008 (File 08-0121, Resolution 74-08), and 2013 (File 13-0295, Resolution 174-13). The 2013 amendment increased the leased premises to 27,826 square feet. DPH currently pays \$993,817 in annual rent, or \$35.72 per square foot.

The current lease is scheduled to expire November 30, 2018. The City has an option to extend the lease for an additional five years, through November 30, 2023. However, according to Mr. Charlie Dunn, Senior Real Property Officer, EHS is planning to move into the new City building at 49 South Van Ness in mid-2020, so DPH does not need to exercise the option.

DETAILS OF PROPOSED LEGISLATION

The proposed resolution would extend the lease between BRCP 1390 Market, LLC as landlord and DPH as tenant for a term of three years, beginning December 1, 2018 and expiring November 30, 2021. DPH would pay annual rent of \$1,801,120 for approximately 27,826 square feet, or \$64.72 per square foot annually. The rent would increase by 3 percent each year. The premises are comprised of 14,549 square feet in Suite 210, 3,247 square feet in Suite 410, 4,646 square feet in Suite 810, 4,971 square feet in Suite 910, and 413 square feet of storage space. DPH may terminate the lease after November 30, 2019 with no penalty as long as written notice is provided 270 days in advance. DPH has two five-year options to extend the lease through November 30, 2026 and November 30, 2031. The key provisions of the lease amendment are shown in Table 1 below.

Table 1: Key Provisions of Lease Amendment

Premises	27,826 square feet
Annual Rent	\$1,801,120 (\$64.20 per square foot)
Operating Expenses	Approximately \$0.60 per square foot per year for electricity on Suite 210 space. Janitorial services, maintenance, and operating costs paid by landlord.
Term	3 years from December 1, 2018 to November 30, 2021
Early Termination	City may terminate early with 9 months written notice after November 2019
Options to Extend	City has two five year options to extend through November 2026 and November 2031 at 95% of Fair Market Rent
Rent Adjustment	3% annually on December 1, starting in 2019

FISCAL IMPACT

In the first year of the lease extension, DPH will pay \$1,801,120 in rent. This is an increase of \$807,303, or approximately 81 percent, from the current annual rent of \$993,817. According to Mr. Dunn, the rental rate is derived from an appraisal conducted by Mateo Advisors and reviewed by Clifford & Associates showing \$66 per square foot for fully serviced office space and \$12 per square foot for storage space. The breakdown of the rent paid on each piece of the premises is shown in Table 2 below.

Table 2: Initial Rent Paid by Leased Area

Area	Square Feet	Annual Rent per Square Foot	Base Annual Rent
Suite 210	14,549	\$65.10	\$947,140
Suites 410, 810, 910	12,864	66.00	849,024
Storage Premises	413	12.00	4,956
Total	27,826	64.72	1,801,120

According to Mr. Dunn, the rent for Suite 210 is slightly lower than for the other suites because it has its own electricity meter and electricity is supplied through the San Francisco Public Utilities Commission's (SFPUC) Hetch Hetchy Power System. DPH pays approximately \$0.60 per square foot per year, or \$8,729, to SFPUC for electricity for this space and receives a \$0.90 per square foot per year, or \$13,094, reduction in rent for Suite 210. For the other suites, the landlord provides the electricity, which it builds into the rental rate.

Over the three year term of the lease extension, DPH would pay \$5,567,082 in rent. Should DPH decide to extend the lease for an additional five years, it would pay 95 percent of Fair Market Rent, based on rents of similar buildings in the Civic Center area. The breakdown of the rent paid by year is shown in Table 3 below.

Table 3: Annual Rent Paid by DPH over Extension Term

Year	Annual Rent
Year 1 (December 2018 – November 2019)	\$1,801,120
Year 2 (December 2019 – November 2020)	1,855,154
Year 3 (December 2020 – November 2021)	1,910,808
Total	\$5,567,082

RECOMMENDATION

Approve the proposed resolution.