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Edward D. Reiskin, Director of Transportation

March 11, 2019

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

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

Honorable Members of the Board of Supervisors:

The San Francisco Municipal Transportation Agency (SFMTA) request that the San Francisco Board of Supervisors authorize the SFMTA to terminate the lease agreement with Tad's Inc. for retail space located at 44 Ellis Street in the Ellis-O'Farrell Garage.

Background

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

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

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

For over 20 years, the retail space has been occupied with no major improvements. The Lease contemplates certain improvements to the premises and includes a list of pre-approved work such as hood ventilation replacement, and electrical, plumbing, ceiling, flooring and bathrooms upgrades. When Tad's assumed the Lease, Tad's agreed the list of pre-authorized work was necessary. Tad's also determined the space needed a new mechanical system and ductwork, a new fire protection system for sprinkler and hood, new lighting fixtures, and new exterior façade and canopy to meet building codes.

The Lease allows the tenant to apply up to \$250,000 as a rent credit against the base rent due, if tenant completes any of the improvement project from the pre-approved list. The rent credit is not an estimate of the total cost for the list of pre-authorized tenant improvement work. The SFMTA recognized the space needed work, and the rent credit was intended to allow for some upgrades. None of the improvements that were the subject of the rent credit were completed while Les Joulins occupied the space.

Due to the extent of the work needed to bring the space up to building code and safe operating standards, Tad's has not been able to open their business since assuming the Lease. Nevertheless, Tad's has consistently met its obligation to pay the rent due, totaling \$730,791 as of February 1, 2019. Tad's intends to completely renovate the restaurant and make the necessary building improvements to bring the space up to code, at a reported cost of \$2,700,000. This Lease did not contemplate the high capital investment cost.

It is mutually beneficial to the SFMTA and Tad's to have the retail space at 44 Ellis Street completely renovated, and to retain a local business that has been operating in the greater Union Square for over 45 years. Tad's would like to terminate the existing Lease and enter into a new lease agreement that extends the term and includes rent abatement which would allow them to make the necessary capital investments. Considering that a major portion of the work constitutes a capital investment for the Ellis-O'Farrell Garage, the SFMTA would like to facilitate the completion of these improvements.

The SFMTA and Tad's desire to terminate the existing Lease in order to enter into a new lease agreement. The new lease agreement will be restructured in the range of market rate with a steady four percentage annual increase in base rent and nine months of rent abatement in exchange for a longer lease term. In December 2019, the SFMTA and Tad's finalized the terms for the proposed new lease agreement. The proposed new lease will result in a small net positive revenue increase to the SFMTA over the current Lease.

Public Outreach

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

Alternatives Considered

The SFMTA considered keeping the current Lease and leaving the space in its current condition, however, that approach does not facilitate a good business relationship with the tenant considering the substantial improvements that must be made by the tenant to bring the space up to current building codes. A second alternative considered was to amend the current Lease, however, the Lease would require significant changes and both parties agreed

it is better to terminate the current Lease and enter a new lease agreement. The SFMTA wants to retain this local small business in the greater Union Square for the long term.

Funding Impact

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

Environmental Review

On January 3, 2019, the SFMTA, under authority delegated by the Planning Department, determined that the Lease Termination Agreement is not defined as a "project" under the California Environmental Quality Act (CEQA) pursuant to Title 14 of the California Code of Regulations Sections 15060(c) and 15378(b).

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

SFMTA Board Action

On March 5, 2019, the SFMTA Board of Directors approved Resolution 190305-027 which authorized the Director of Transportation the SFMTA to terminate the lease agreement with Tad's Inc. for retail space located at 44 Ellis Street in the Ellis-O'Farrell Garage.

Recommendation

The SFMTA requests that the San Francisco Board of Supervisors authorize the SFMTA to terminate the lease agreement with Tad's Inc. for retail space located at 44 Ellis Street in the Ellis-O'Farrell Garage.

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

Sincerely,



Edward D. Reiskin
Director of Transportation