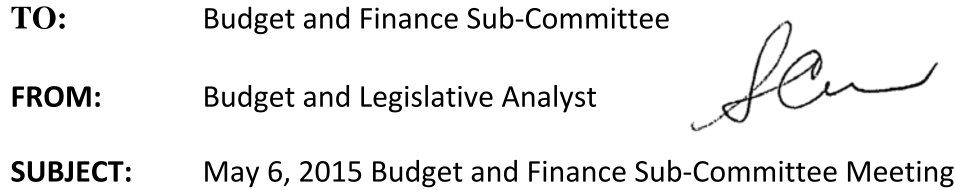
CITY AND COUNTY OF SAN FRANCISCO

BOARD OF SUPERVISORS

BUDGET AND LEGISLATIVE ANALYST

1390 Market Street, Suite 1150, San Francisco, CA 94102 (415) 552-9292
FAX (415) 252-0461

May 1, 2015



TO: Budget and Finance Sub-Committee

FROM: Budget and Legislative Analyst

SUBJECT: May 6, 2015 Budget and Finance Sub-Committee Meeting

TABLE OF CONTENTS

Item	File		Page
1	15-0210	Lease Agreement – Menzies Aviation (USA), Inc. – West Field Cargo Building 632 and Related Areas on Plot 9 - $6,434,187	1
2	15-0212	Lease Agreement Termination – Buth-na-Bodhaige, Inc., dba The Body Shop	6
3	15-0408	Purchase and Sale of Electricity and Related Products and Services – Public Utilities Commission	9
5	15-0342	Lease of Real Property – BRCP 1390 Market, LLC – 1390 Market Street - $479,031.70 in Initial Year	17
6	15-0312	Commercial Lease Agreement – Less Joulins, USA - 44 Ellis Street - $5,127,000	21

Item 1 **File 15-0210** *(Continued from April 29, 2015)*	**Department:** San Francisco International Airport (Airport)

EXECUTIVE SUMMARY

Legislative Objectives

The proposed resolution would approve a new three-year lease with three one-year options between Menzies Aviation (USA) Inc., (Menzies) and the Airport, for approximately 50,319 sf of exclusive use space in West Field Cargo Building 632 and related areas on Plot 9.

Key Points

- Menzies Aviation (USA), Inc. (Menzies) provides passenger, ramp, and cargo handling services to airlines operating at the Airport.
- Currently, Menzies leases 50,319 square feet (sf) of space from the Airport on a month-to-month basis. The Airport Commission approved a three-year lease with Menzies in October 2014 for 36,012 sf of exclusive use office and warehouse space in the West Field Cargo Building. The Airport Commission subsequently approved a lease with Menzies in February 2015 for 50,319 sf of West Field Cargo Building space based on Menzies' request to increase the space from 36,012 sf to 50,319 sf.
- Because the individual airlines operating at the Airport contract directly with Menzies for services, the contract and associated lease were not competitively bid by the Airport.

Fiscal Impact

- The Airport completed construction of the new 69,000 sf West Field Cargo Building in June 2014 to replace the existing cargo building at a cost of approximately $35 million. In order to ensure that the lease rates for the new West Field Cargo Building would not be significantly higher than rental rates for other Airport warehouse buildings, and remain affordable to Airport tenants, the Airport established a blended rental rate for space at all cargo buildings, which is $23.00 per sf in FY 2014-15 regardless of the age or location of the building.
- Under the proposed lease, Menzies would pay rent of $23.00 per square foot in FY 2014-15, increased annually by rates set by the Airport for warehouse space. Over the six-year term of the lease, including the initial three-year term and three one-year extensions, Menzies will pay an estimated $7,546,780 in rent to the Airport.

Recommendations

- Amend the proposed resolution to state the correct estimated minimum rent payable by Menzies to the Airport over the lease term ending April 30, 2021 to be $7,546,780, rather than $6,434,187, as stated in the proposed resolution.
- Approve the proposed resolution, as amended.

MANDATE STATEMENT / BACKGROUND

Mandate Statement

City Charter Section 9.118(c) states that leases, including options to renew, and modifications to leases, having anticipated revenue to the City of $1 million or more are subject to Board of Supervisors approval.

Background

Menzies Aviation (USA), Inc. (Menzies) provides passenger, ramp, and cargo handling services to airlines operating at San Francisco International Airport (Airport). Currently, Menzies leases 50,319 square feet (sf) of space from the Airport on a month-to-month basis under Permit No. 4096 pending approval of a long-term lease by the Airport Commission. The Airport Commission approved a three-year lease with Menzies in October 2014 for 36,012 sf of exclusive use office and warehouse space in the Airport's West Field Cargo Building and related areas on the Airport's Plot 9. Menzies subsequently requested in December 2014 that the Airport expand its exclusive use warehouse and office space in the West Field Cargo Building to 50,319 sf. The 50,319 sf is comprised of 42,620 sf of warehouse space and 7,699 sf of office space. Following this request, the Airport Commission approved the lease with Menzies for the 50,319 sf of space in February 2015.

Because the individual airlines operating at the Airport contract directly with Menzies for services, the contract and associated lease were not competitively bid by the Airport.

DETAILS OF PROPOSED LEGISLATION

The proposed resolution would approve a new three-year lease with three one-year options (Agreement No. 15-0033) between Menzies Aviation (USA) Inc., and the City, acting by and through its Airport Commission, for approximately 50,319 sf of exclusive use space in West Field Cargo Building 632 and related areas on Plot 9.

The proposed new three year lease would replace the existing lease which Menzies currently operates under a month-to-month permit at the Airport. The key lease provisions are shown in Table 1 below.

Table 1: Key Lease Provisions

Premises	50,319 sf of exclusive use warehouse and office space
Permitted Use	To conduct air cargo business for airlines operating at the Airport including receiving , delivering, dispatching, processing, handling and storage of air cargo and mail, and any other lawful purpose directly related to such activities
Term	Three years expected to commence May 1, 2015 for a total initial term through April 30, 2018
Options to Extend	3 one-year options through approximately April 30, 2021
Square Feet	42,620 sf warehouse space 7,699 sf of office space (3,853 sf 1st floor + 3,846 2nd floor) 50,319 sf total
First Year Rent to be Paid by Menzies to Airport	$23.00 per sf ($96,445 per month or $1,157,337 per year)
Rent Adjustments	Annual adjustments estimated to be 2.5 percent based on Airport's Rates and Charges for Cargo Facilities
Utilities	Tenant shall pay all utilities costs
Repairs	Airport shall pay the cost of repair to Airport Building infrastructure, systems, and equipment, which is deemed Airport Responsibility, in addition to routine maintenance and repair of the ramp and parking areas adjacent to said Premises. Airport shall provide janitorial services on all public areas, including public hallways, lobbies, elevators, stairwells, and bathrooms. Repair to all other systems or equipment is the responsibility of the Tenant.

FISCAL IMPACT

The proposed resolution would result in $7,546,780 in estimated rent to be paid by Menzies to the Airport for 50,319 sf of exclusive use space over the proposed lease term ending on April 30, 2021, as shown in Table 2 below.

Table 2: Total Estimated Rent to be Paid by Menzies to the Airport from May 1, 2015 through April 30, 2021

Initial Term	Rate/SF*	Square Feet	Rent
5/1/15 to 6/30/15 (2 months)	$23.00	50,319	$192,890
7/1/15 to 4/30/16 (10 months)	$23.58	50,319	$988,559
Year One Subtotal			**$1,181,448**
5/1/16 to 6/30/16 (2 months)	$23.58	50,319	$197,712
7/1/16 to 4/30/17 (10 months)	$24.16	50,319	$1,013,273
Year Two Subtotal			**$1,210,984**
5/1/17 to 6/30/17 (2 months)	$24.16	50,319	$202,655
7/1/17 to 4/30/18 (10 months)	$24.77	50,319	$1,038,604
Year Three Subtotal			**$1,241,259**
Initial Term Total Rent			**$3,633,692**
Option Terms			
5/1/18 - 6/30/18 (2 months)	$24.77	50,319	$207,721
7/1/18 - 4/30/19 (10 months)	$25.39	50,319	$1,064,570
Option Year One Subtotal			**$1,272,290**
5/1/19 - 6/30/19 (2 months)	$25.39	50,319	$212,914
7/1/19 - 4/30/20 (10 months)	$26.02	50,319	$1,091,184
Option Year Two Subtotal			**$1,304,098**
5/1/20 - 6/30/20 (2 months)	$26.02	50,319	$218,237
7/1/20 - 4/30/21 (10 months)	$26.67	50,319	$1,118,463
Option Year Three Subtotal			**$1,336,700**
Total Rent			**$7,546,780**

** Assumes an annual 2.5 percent increase*

The proposed resolution incorrectly states that the total estimated rent payable by Menzies to the Airport is $6,434,187 rather than the correct amount of $7,546,780.

The Airport completed construction of the new 69,000 sf West Field Cargo Building in June 2014 to replace the existing cargo building at a cost of approximately $35 million. According to Mr. Dan Ravina, Senior Property Manager, in order to ensure that the lease rates for the new West Field Cargo Building would not be significantly higher than rental rates for other Airport warehouse buildings, and remain affordable to Airport tenants, the Airport established a blended rental rate for space at all cargo buildings, which is $23.00 per sf in FY 2014-15 regardless of the age or location of the building. The Airport estimates an annual rental rate increase of 2.5 percent, equal to $23.58 per sf in FY 2015-16, based on a combination of rates and charges at the Airport, as well as the expected increase in inflation.

RECOMMENDATIONS

1. Amend the proposed resolution to state the correct estimated minimum rent payable by Menzies to the Airport over the lease term ending April 30, 2021 to be $7,546,780, rather than $6,434,187, as stated in the proposed resolution.

2. Approve the proposed resolution, as amended.

Item 2 **File 15-0212** *(Continued from April 29, 2015)*	**Department:** San Francisco International Airport (Airport)

EXECUTIVE SUMMARY

Legislative Objectives

- The proposed resolution would approve an early lease termination retroactively as of March 31, 2015 for The Body Shop, which currently occupies 2,500 square feet of Pharmacy, Health, and Beauty Store retail space in Terminal 3 Boarding Area F of the San Francisco International Airport.

Key Points

- On November 21, 2014, the Body Shop notified the Airport of its desire to terminate their lease agreement on March 31, 2015, more than one year prior to the April 7, 2016 lease expiration date due to the low volume of business in Boarding Area F. United Airlines, which is the only airline operating in Boarding Area F, shifted many of their flights from Boarding Area F to Boarding Area E in Terminal 3 after the completion of construction and the reopening of Boarding Area E in January 2014, resulting in a 23.8 percent decrease in passengers in Boarding Area F from 2013 to 2014.
- On January 20, 2015, the Airport Commission approved The Body Shop's request for an early lease termination date of March 31, 2015, provided that The Body Shop pay the Airport an early termination fee of $198,166, which is the equivalent of nine months of the MAG rent through December 31, 2015, prorated on a monthly basis.
- The Airport has identified the Hudson Group as a replacement tenant in Terminal 3 Boarding Area F. The Hudson Group's Fickle Bag product line, which specializes in handbags and accessories, is being displaced by the Airport due to construction at its current location in Terminal 3.

Fiscal Impact

- The loss in revenues to the Airport for the early termination of the lease with The Body Shop is $71,193, which is the difference between the MAG rent of $269,359 that The Body Shop would have paid from April 1, 2015 through April 7, 2016 less the early termination fee of $198,166. The Airport does not anticipate an overall loss in revenues since the estimated MAG paid by Hudson combined with rental of the storage areas will exceed the lost rent from The Body Shop.
- Under the Airport's residual rate-setting methodology (break-even policy), any reductions in non-airline revenues are automatically offset by increasing the total rent payable by the airlines operating at the Airport in accordance with the respective leases between the Airport and the airlines. The Airport's break-even policy requires that the total revenues paid to the Airport by all airlines in the fiscal year are sufficient to balance the Airport's budget.

Recommendation

- Approve the proposed resolution.

MANDATE STATEMENT

Mandate Statement

City Charter section 9.118(c) requires approval by the Board of Supervisors for the modification, amendment or termination of any lease that was entered into for a period of ten or more years, including options to renew, or had anticipated revenue to the City and County of one million dollars or more.

BACKGROUND

On October 2, 2008, the Board of Supervisors approved a lease agreement between Harmony Pharmacy and Health Center, Inc. (Harmony) and the Airport for the Boarding Area "F" Pharmacy, Health, and Beauty Store retail space in Terminal 3 of the San Francisco International Airport (File 08-1075). The lease agreement was for 2,500 square feet of retail space and an initial lease term of five years to November 2013, with one two-year option to extend through November 2015.

Under this lease, the annual rent payable by Harmony to the Airport was the greater of (a) the Minimum Annual Guarantee (MAG) or (b) percentage rent. Each year, Harmony paid the Airport MAG rent because their percentage rent based on gross revenues did not exceed the MAG. The MAG was adjusted annually to account for consumer price index (CPI) increases and adjustments to enplanements, representing the total number of passengers boarding the airline carrier.

In 2013, Harmony requested a transfer of their lease to another company because they were experiencing financial difficulties. On May 21, 2013, the Airport agreed to transfer the lease from Harmony to Butha-na-Bodhaige, Inc. (dba The Body Shop), and extend the lease term through April 7, 2016. While The Body Shop only used approximately 716 square feet of the total 2,500 square feet of available retail space, The Body Shop paid the required MAG rent based on the total 2,500 square feet of retail space.

DETAILS OF PROPOSED LEGISLATION

The proposed resolution would approve an early lease termination retroactively as of March 31, 2015 for The Body Shop, which currently leases 2,500 square feet of the Pharmacy, Health, and Beauty Store retail space in Terminal 3 Boarding Area F of the San Francisco International Airport.

On November 21, 2014, the Body Shop notified the Airport of its desire to terminate their lease agreement on March 31, 2015, more than one year prior to the April 7, 2016 lease expiration date, due to the low volume of business in Boarding Area F. According to Mr. Trevor Brumm, Airport Property Manager, United Airlines shifted many of their flights from Boarding Area F to Boarding Area E in Terminal 3 after the completion of construction and the reopening of Boarding Area E in January 2014. This caused a significant decline in enplanements in Boarding Area F. While United Airlines, the only airline operating in Boarding Area F since 2011, has since

reinstated their Express flights in Boarding Area F, annual enplanements declined by 23.8 percent from 2013 to 2014 in Boarding Area F.

Mr. Brumm advised that Airport approval of early lease terminations is rare for concession operators at the Airport, unless the Tenant can obtain another concession operator for the assignment of the lease to such other concession operator. However, with the lease termination date set at April 7, 2016, it was difficult for The Body Shop to find an alternate tenant to take over the lease for such a short period of time.

Based on negotiations with The Body Shop, on January 20, 2015, the Airport Commission approved The Body Shop's request for an early lease termination, provided that The Body Shop pay the Airport an early termination fee of $198,166, which is the equivalent of nine months at $22,018 per month of the MAG rent through December 31, 2015, prorated on a monthly basis.

New Tenant Already Identified to Lease Space

The Airport has identified the Boarding Area "F" Pharmacy, Health, and Beauty Store retail space as replacement space for the Hudson Group, whose Fickle Bag product line, which specializes in handbags and accessories, is being displaced by the Airport due to construction at its current location in Terminal 3. Under the lease amendment between the Airport and the Hudson Group for Fickle Bag, the Hudson Group is required to pay the Airport an estimated MAG rent of approximately $215.59 per square foot. The new Hudson store will occupy the 716 square feet of space vacated by The Body Shop, resulting in a first year MAG rent to the Airport of $154,362. The new lease with Fickle Bag will be subject to future approval of the Board of Supervisors.

The Airport will rent the remaining 1,784 square feet of space to other concession operators in the Airport for use as storage units on a month-to-month basis.

FISCAL IMPACT

The loss in revenues to the Airport for the early termination of the lease with The Body Shop is $71,193, which is the difference between the MAG rent of $269,359 that The Body Shop would have paid from April 1, 2015 through April 7, 2016 less the early termination fee of $198,166. According to Mr. Brumm, the Airport does not anticipate an overall loss in revenues since the estimated MAG paid by Hudson combined with rental of the storage areas will exceed the lost rent from The Body Shop.

Under the Airport's residual rate-setting methodology (break-even policy), any reductions in non-airline revenues are automatically offset by increasing the total rent payable by the airlines operating at the Airport in accordance with the respective leases between the Airport and the airlines. The Airport's break-even policy requires that the total revenues paid to the Airport by all airlines in the fiscal year are sufficient to balance the Airport's budget.

RECOMMENDATION

Approve the proposed resolution.

Item 3 **File 15-0408**	**Department:** Public Utilities Commission (PUC)

EXECUTIVE SUMMARY

Legislative Objectives

- The proposed ordinance authorizes SFPUC to use pro forma contracts to purchase and sell electricity and related products and services for electricity supplied by (1) Hetch Hetchy to municipal facilities, services and customers, and (2) the Community Choice Aggregation (CCA) program to supply electricity to City businesses and residents.

Key Points

- The goal of CCA is to provide San Francisco electricity customers with renewable energy service options at rates comparable to those currently being offered by PG&E. The program will be executed in phases. During the first phase, customers located within a select geographic region will be automatically enrolled in the program and will have four months to opt-out of participating. These customers will be offered a standard energy product that will consist of between 33 and 50 percent renewable energy. Customers citywide will also be able to opt into a premium product consisting of 100 percent renewable energy during this first phase.
- SFPUC staff will solicit offers from and enter into contracts with renewable energy providers for up to 25 years and $125 million. The proposed ordinance authorizes the SFPUC to use industry-standard pro forma contracts for purchases of electricity from renewable energy providers. Because these contracts do not contain many of the City's standard contracting requirements, the proposed ordinance waives these requirements.
- The proposed ordinance would allow SFPUC to enter into contracts with renewable energy providers for up to 25 years and $125 million without Board of Supervisors approval. According to SFPUC, these contracts need to be negotiated in a short time period to achieve competitive pricing under market conditions. The longer term contracts are necessary because suppliers of new renewable generation typically require a contract for the sale of the energy generation of the facility's output for 20-25 years in order to finance the construction of the facility.

Fiscal Impact

- SFPUC staff proposes setting initial CCA rates to be comparable to rates currently charged by PG&E for renewable energy products, which based on SFPUC's initial estimates will recover program costs. After being approved by the Commission, the Board of Supervisors will have a 30-day window to approve the rates.

Recommendations

- Amend the proposed ordinance to require that the annual reports submitted to the Board of Supervisors include program costs, the rates charged by SFPUC to CCA customers to recover costs, and the comparison of SFPUC rates to PG&E rates.
- Amend the proposed ordinance to state that the "SFPUC will issue competitive solicitations for the renewable energy supplies and related services."
- Approval of the proposed ordinance, as amended, is a policy matter for the Board of Supervisors.

MANDATE STATEMENT / BACKGROUND

Mandate Statement

Section 9.118(b) of the City's Charter requires approval by the Board of Supervisors for contracts with an expected term longer than ten years or requiring expenditures of 10 million dollars or more. The San Francisco municipal code contains numerous contracting requirements for the procurement of goods and services. In certain instances, the Board of Supervisors may exempt contracts from these requirements via ordinance.

Background

The San Francisco Public Utilities Commission (SFPUC) operates a power utility, which supplies clean, greenhouse-gas-free energy to San Francisco's municipal facilities, services and customers. The SFPUC may not sell Hetch Hetchy power to private entities who intend to resell the power under the Raker Act of 1913.

The City has adopted aggressive goals for greenhouse gas reduction and use of renewable energy. In Ordinance 81-08, the Board of Supervisors articulated the goal of having a greenhouse-gas-free electric system by 2030, and meeting all City electricity needs with renewable and greenhouse-gas-free sources.

State law allows cities and counties to develop Community Choice Aggregation (CCA) programs, through which local governments may choose to supply electricity to serve the needs of participating customers within their jurisdictions while the existing private utility (PG&E in San Francisco) continues to provide various services including billing, transmission and distribution.

San Francisco has already taken various steps towards implementing a CCA program. In 2012, the SFPUC negotiated a contract with Shell Energy North America to procure the necessary power for the CCA. Although the contract was approved by the Board of Supervisors, the contract was never executed because the SFPUC did not approve the CleanPowerSF program rates. Approval of program rates (which were also "not-to-exceed" rates) was a required step in the process.

In 2015, the Local Agency Formation Commission (LAFCo) retained EnerNex to produce a report describing the local build out of energy resources to support a CCA program. The report recommended that SFPUC staff obtain the necessary power on behalf of the CCA program on an on-going and as-needed basis. The report states that this will provide the benefits of cost-efficiency, while also mitigating the risks of contract failure and leveraging the in-house knowledge of SFPUC staff.

DETAILS OF PROPOSED LEGISLATION

The proposed ordinance authorizes SFPUC to use pro forma contracts to purchase and sell electricity and related products and services for electricity supplied by (1) Hetch Hetchy to municipal facilities, services and customers, and (2) the Community Choice Aggregation (CCA) program to supply electricity to City businesses and residents. Under the proposed ordinance,

- The pro forma contracts could deviate from certain City contracting requirements, as discussed below; and
- SFPUC could enter into future contracts without obtaining Board of Supervisors approval for the purchase of electricity generated by renewable and greenhouse-gas-free sources from facilities in California for up to 25 years and up to a total of $125 million, exceeding the City Charter requirement for Board of Supervisors approval for contracts over 10 years and $10 million, as required by City Charter Section 9.118(b).

SFPUC's Implementation of Community Choice Aggregation

The goal of Community Choice Aggregation is to provide San Francisco electricity customers with renewable energy service options from California generators at comparable rates to those currently being offered by PG&E.

SFPUC will execute the CCA program in phases. During the first phase, customers located within a select geographic region[1] will be automatically enrolled in the program and will have four months from their enrollment date to opt-out of participating in the program. These customers will be offered a standard energy product that will consist of between 33 and 50 percent renewable energy. Customers citywide will also be able to opt into a premium product consisting of 100 percent renewable energy during this first phase. Customers will submit payments to PG&E, as required under State law. SFPUC will pay PG&E a fee for billing and payment services.

According to Ms. Barbara Hale, SFPUC Assistant General, it is currently unknown which areas of the city will be selected to participate in the first phase. It is also uncertain how many customers will select the premium product in the San Francisco market. The second phase of the program will not be started until a sufficient number of customers participate in the program, and a competitive renewable energy rate is made available for purchasing electricity.

The City's Rate Fairness Board[2] approved proposed not-to-exceed rates on April 17, 2015, and SFPUC staff will present the proposed not-to-exceed rates for the standard and premium renewable energy to the SFPUC Commission on May 12, 2015. After being approved by the Commission, the Board of Supervisors will have a 30-day window to approve the rates. SFPUC staff recommends adopting not-to-exceed rates for the standard renewable energy product based on comparable current PG&E rates, less the Power Charge Indifference Adjustment (PCIA)[3]. The premium renewable energy product not-to-exceed rate is based on the projected PG&E Green Tariff[4] premium.

---

[1] The first phase will be 30 megawatts of customer load.

[2] The City's Rate Fairness Board was established by Proposition E, approved by San Francisco voters in November 2002, to advise the SFPUC on water, power and sewer rates. RFB members include the Director of Public Finance, two members appointed by the Mayor and two members appointed by the Board of Supervisors representing commercial and residential rate payers, one member appointed by the Controller, and one member appointed by the City Administrator.

[3] The Power Charge Indifference Adjustment (PCIA) is a charge assessed by PG&E to cover generation costs acquired prior to a customer's change in service provider. The rate charged by PG&E to residential customers who change providers in FY 2014-15 is $0.01101/kWh and the rate for businesses is $.01160/kWH.

[4] The PG&E Green Option is a clean energy program that offers customers a 100 percent renewable energy option.

Table 1 below illustrates the proposed Community Choice Aggregation Program not-to-exceed rates for the standard and premium renewable energy products that will be offered to residential and commercial customers.

Table 1: SFPUC Staff Recommendation to the SFPUC for the Proposed CCA Rates

Standard Product	**Rate**
Residential	$.086 / kWh
Small Commercial	$.092 / kWh
Premium Product	
Residential	$.107 / kWh
Small Commercial	$ .112 / kWh

Source: Public Utilities Commission

In the future, the rates for the CCA program will be set to recover program costs.[5]

Power Procurement

SFPUC anticipates that it will need to procure approximately 30 megawatts of renewable energy for the first phase of CCA service. To meet aggressive implementation targets and secure the best possible prices and terms, SFPUC staff will need to negotiate a mix of electricity contracts with existing multiple renewable energy providers. The SFPUC anticipates being able to execute such contracts with existing staff.

SFPUC expects to enter into contracts of varying term lengths (up to 25 years) with multiple providers for a variety of renewable energy sources including solar, wind and geothermal. The amount of renewable energy to be included in the standard product, between 33 and 50 percent, will depend on the price and availability of energy on the market. At the same time that the SFPUC is entering into contracts for this phase of the project, it will also begin the process of developing local renewable energy resources that would over time replace purchased renewable energy, if these projects can obtain the necessary environmental review.

Projects being considered for local build out include solar projects in Hunters Point, University Mound-North Basin, Sutro Reservoir, and at Port piers 90-94, as well as the Oceanside wind project. Potential regional projects include solar project sites at San Francisco International Airport parking lot, Pulgas Reservoir, Sunol Valley, Tesla Portal, the Geysers geothermal site, and wind projects at Sunol, Tesla Portal, Montezuma Hills, Altamonte Pass and Walnut Grove.

Authorization to Purchase Energy with Pro-Forma Contracts

The proposed ordinance authorizes SFPUC to utilize industry-standard pro forma contracts, as well as a city-specific contract to be developed by the SFPUC for purchases of electricity from distributed generation facilities, to ensure the availability of essential services in a timely and cost-effective manner. The industry-standard pro forma contracts, the Western System Power

[5] According to SFPUC staff, CCA program costs will be known once contracts with renewable electricity providers are signed. Based on SFPUC's preliminary estimates of renewable electricity pricing and administrative costs, the CCA program will recover costs based on rates comparable to PG&E's current rates.

Pool agreement, the Edison Electric Institute (EEI) agreement, and the Feed-in-Tariff Program, are described further below.

Western System Power Pool Agreement

The Western System Power Pool (WSPP) is a group of more than 300 publicly-owned and private utilities, including Alameda Municipal Power, the City of Palo Alto, the City of Roseville, the Sacramento Municipal Utility District, and Silicon Valley Power. The City of San Francisco is a member of the WSPP. The WSPP agreement form has been approved by the Federal Energy Regulatory Commission (FERC). The Board of Supervisors previously authorized the General Manager of the SFPUC to use the WSPP agreement for transactions lasting up to five years and waived for those transactions certain sections of the City's Environment and Administrative Codes.

Edison Electric Institute Master Agreement

The Edison Electric Institute (EEI), in collaboration with more than 80 member utilities, affiliated and independent power marketers, merchant power, and end-use representatives, developed an agreement form that sets forth standard terms and conditions for the purchase and sale of power and related products and services. The Board of Supervisors previously authorized the General Manager to enter into an agreement based on the EEI agreement with Shell Energy North America to provide services required to launch the CCA. However, that agreement was never executed.

Feed-in-Tariff (FIT) Program

A feed-in-tariff (FIT) program is a standard tariff for purchases of electricity from distributed generation facilities, such as roof-top solar photovoltaic systems. The FIT program establishes uniform rules for participation, standard-offer prices, and an agreement form. As the FIT contract typically lasts for 10-20 years, a FIT program creates an incentive for the development of local renewable resources by assuring project owners of a stable long-term revenue stream.

Authorization to Waive Standard Contract Provisions

The City requires that various contracts contain standard provisions to protect the City's interests and ensure accountability. The proposed ordinance authorizes SFPUC to award pro-forma contracts that may not contain the City's standard contract provisions; however, contract modifications, which in the judgment of the General Manager of the SFPUC and the City Attorney materially decrease the City's rights or materially increase the City's liabilities, are subject to Board of Supervisors approval.

The proposed ordinance specifically authorizes the waiver of the following standard City contract provisions, provided that the General Manager finds and documents in writing both that the transaction represents the best opportunity available to the City to obtain essential services and products or dispose of excess power in a manner that is beneficial to the City:

1) Review of the City's support of the MacBride Principles (Administrative Code 12F);
2) Increased participation by small and micro loan businesses in City contracts (Admin Code Chapter 14B);

3) The competitive bidding requirement (Admin. Code Section 21.1);
4) First source hiring requirements (Admin. Code Chapter 83);
5) The tropical hardwood and virgin redwood ban (Environ. Code Chapter 8);
6) Public access to meeting and records for non-profit organizations (Admin. Code Section 12L.2);
7) Sweatfree contracting (Admin. Code Section 12U.4); and
8) Food service waste reduction (Environ. Code Section 1605).

FISCAL IMPACT

The proposed ordinance authorizes the SFPUC General Manager to enter into pro forma contacts to purchase renewable energy with terms up to 25 years and amounts up $5 million per year or $125 million over the term of the contract without Board of Supervisors approval, as shown in Table 2 below. Under the proposed ordinance, the maximum aggregate amount of all such contracts is $500 million. SFPUC is required to report annually to the Board of Supervisors as to the duration, as products purchased and to cost of the contracts entered into.

Table 2: Proposed CCA Contracts Not Requiring Board of Supervisors Approval

Contract length	Not-to-exceed 25 years
Total expenditures	Not-to-exceed $5 million per year or $125 million over agreement term
Total allowable amendments	$500,000

Source: Proposed legislation

According to the proposed ordinance, "SFPUC anticipates issuing competitive solicitations for renewable energy supplies and related services". According to SFPUC staff, SFPUC will issue "Request for Offers" to renewable energy providers, which is expected to solicit more than one bid.[6]

SUMMARY

The proposed ordinance authorizes SFPUC to use pro forma contracts to purchase and sell electricity and related products and services for electricity supplied by (1) Hetch Hetchy to municipal buildings, and (2) the Community Choice Aggregation (CCA) program to supply electricity to City businesses and residents.

SFPUC plans to implement the CCA program to allow customers to choose between (1) purchase of electricity generated by 33 percent to 50 percent renewable energy resources, and

[6] According to SFPUC staff, SFPUC may also consider using the competitive solicitation process of other CCA programs to select and contract with renewable electricity providers, in accordance with Administrative Code Section 21.16.

(2) 100 percent renewable energy resources. The 33-50 percent option will be implemented in an undetermined geographic section of the City, with customers having the right to opt out within four months of being enrolled.

SFPUC plans to set rates for the 33-50 percent option at an amount equal to PG&E's current rates. The 100 percent option will be implemented Citywide, and customers can choose to opt in. SFPUC plans to set rates for the 100 percent option at an amount equal to PG&E's Green Tariff Premium.

SFPUC could enter into contracts for the purchase of electricity generated by renewable and greenhouse-gas-free sources up to 25 years and $125 million, exceeding the City Charter requirement for Board of Supervisors approval for contracts exceeding 10 years and $10 million.

The proposed ordinance specifically authorizes the waiver of the following contract provisions, provided that the General Manager finds and documents in writing both that the transaction represents the best opportunity available to the City to obtain essential services and products or dispose of excess power in a manner that is beneficial to the City:

1) Review of the City's support of the MacBride Principles (Administrative Code 12F);
2) Increased participation by small and micro loan businesses in City contracts (Admin Code Chapter 14B);
3) The competitive bidding requirement (Admin. Code Section 21.1);
4) First source hiring requirements (Admin. Code Chapter 83);
5) The tropical hardwood and virgin redwood ban (Environ. Code Chapter 8);
6) Public access to meeting and records for non-profit organizations (Admin. Code Section 12L.2);
7) Sweatfree contracting (Admin. Code Section 12U.4); and
8) Food service waste reduction (Environ. Code Section 1605).

According to Ms. Barbara Hale, SFPUC Assistant General Manager, waiving Board of Supervisors approval of contracts up to 25 years and $125 million to purchase electricity for CCA is necessary because suppliers of new renewable generation typically require a contract for the sale of the energy generation of the facility's output for 20-25 years in order to finance the construction of the facility. Using longer-term pro forma contracts will better position the SFPUC to compete for attractive, new renewable generation supply. Further, the SFPUC needs to develop a cost-effective supply portfolio with varying durations to ensure competitive program offerings and sustained program participation.

The proposed ordinance requires the SFPUC to annually report to the Board of Supervisors on the duration of energy power purchase contracts entered into by SFPUC, the type of product(s) purchased, and the costs of the contracts. The Budget and Legislative Analyst recommends

amending the ordinance to require an annual report on CCA program costs, the rates charged by SFPUC to CCA customers to recover costs, and the comparison of SFPUC rates to PG&E rates.

Although the proposed ordinance waives competitive bidding requirements under Administrative Code Section 21.1, the proposed ordinance also states that the "SFPUC anticipates issuing competitive solicitations for renewable energy supplies and related services." According to SFPUC staff and as noted above, SFPUC will issue "Request for Offers" to renewable energy providers, which is expected to solicit more than one bid. The Budget and Legislative Analyst recommends amending the proposed ordinance to state that the "SFPUC *will issue* competitive solicitations for the renewable energy supplies and related services."

The Budget and Legislative Analyst considers approval of the proposed ordinance to be a policy matter for the Board of Supervisors.

RECOMMENDATIONS

1. Amend the proposed ordinance to require that the annual reports submitted to the Board of Supervisors pertaining to the CCA program include program costs, the rates charged by SFPUC to CCA customers to recover costs, and the comparison of SFPUC rates to PG&E rates.
2. Amend the proposed ordinance to state that the "SFPUC will issue competitive solicitations for the renewable energy supplies and related services."
3. Approval of the proposed ordinance, as amended, is a policy matter for the Board of Supervisors.

Item 5 **File 15-0342**	**Department:** Department of Children, Youth and their Families (DCYF)

EXECUTIVE SUMMARY

Legislative Objectives

The proposed resolution would authorize (1) the second five-year option to extend the lease between the Department of Children, Youth and their Families (DCYF) and BRCP 1390 Market, LLC for Suites 900, 902, and 903, and (2) incorporate Suite 906 into the second five-year extension of the lease, in order to continue to provide office and program space for DCYF., for approximately 10,846 square feet of total leased space. Annual base rent is $574,838 ($53 per square foot), with the first two months of rent abated for total rent of $479,032 in the first year. The lease will commence on December 1, 2015 and expire on November 30, 2020.

Key Points

- DCYF has occupied Suites 900, 902 and 903 since 2005. The original lease was for five years with two five-year options to extend. Annual rent for the premises was $25.95 per square foot. In 2007, DCYF leased Suite 906 at 1390 Market Street to expand its program offerings at the site. The lease was signed on a month-to-month basis with annual rent of $36 per square foot.
- In 2010, the Board of Supervisors approved the first option to extend the lease of Suites 900, 902 and 903 for an additional five years, from December 1, 2010 to November 30, 2015. Annual rent during this period was reduced to $24.50 per square foot to reflect fair market value.
- DCYF is exercising the second five-year lease option for Suites 900, 902, and 903 from December 1, 2015 through November 30, 2020, and adding Suite 906. Total square footage is approximately 10,846.

Fiscal Impact

- Under the second extension, the for Suites 900, 902, 903 and 906 is $53 per square foot per year for the first year, reflecting market rates in the Civic Center. The proposed rental rate of $53 per square foot is 86 percent more than the current rental rate of $28.50 per square foot per year for Suites 900, 902, and 903; and 77 percent more than the current rental rate of $30 per square foot per year for Suite 906.
- The lease provides for a two-month rent, resulting in first year rent of $479,032 Total rent paid by DCYF over the five-year extension term is $2,886,844.

Recommendation

- Approve the proposed resolution.

MANDATE STATEMENT

Administrative Code Section 23.27 requires Board of Supervisors approval of all leases in which the City is a tenant, except as otherwise provided in Administrative Code Section 23.26.

BACKGROUND

In December 2005, the Board of Supervisors approved a lease at 1390 Market Street, Suites 900, 902 and 903, to provide office and program space for the Department of Children, Youth and Their Families (DCYF). Annual rent for the premises was $243,852 ($25.95 per square foot) for 9,397 square feet of space. The initial term of the lease was December 1, 2005 through November 30, 2010. The lease provided two options to extend the term for an additional five years each. Rent during the extension period was to be set at 95 percent of fair market value.

In 2007, DCYF leased Suite 906 at 1390 Market Street for 1,449 additional square feet to expand its program offerings at the site. The lease was signed on a month-to-month basis with annual rent of $52,164 ($36 per square foot). Mr. Leo Chyi, Director of Budget, Operations and Grant Support for DCYF, states that DCYF chose to lease Suite 906 on a month-to-month basis because DCYF wanted the ability to terminate the lease should their budget be reduced due to the economic recession. The lease of Suite 906 was not subject to approval by the Board of Supervisors[1]. In 2009, the Landlord agreed to reduce the annual rent to $43,470 ($30 per square foot) to reflect fair market value of comparable leases.

In 2010, the Board of Supervisors approved the first option to extend the lease of Suites 900, 902 and 903 for an additional five years, to commence on December 1, 2010 and expire on November 30, 2015. Annual rent was reduced to $230,227 ($24.50 per square foot), a decrease of $13,625 from the original rent of $243,852 to reflect fair market value, as specified by the lease. Annual rent was subject to increase by $1 per square foot per year. The current annual rental rate is $28.50 per square foot per year for Suites 900, 902, and 903. Table 1 below shows the total amount of rent to be paid by DCYF to the Landlord for Suites 900, 902, 903 and 906 from 2005 through 2015.

[1] Under Section 23.26 of the City's Administrative Code, the Director of Property has authority to enter into leases on a year-to-year or shorter basis where rent paid by the City is $5,000 per month or less.

Table 1: Rent Payments for Suites 900, 902, 903, and 906 at 1390 Market St.

Year	Rent Paid for Suite 900, 902, 903	Rent Paid for Suite 906	Total Rent Paid for All Suites	Annual % increase
FY 05-06	$243,852	N/A	$243,852	N/A
FY 06-07	243,852	N/A	243,852	0%
FY 07-08	243,852	$52,164	296,016	21%*
FY 08-09	243,852	52,164	296,016	0%
FY 09-10	243,852	43,470	287,322	-3%
FY 10-11	230,226	43,470	273,696	-5%
FY 11-12	239,624	43,470	283,094	3%
FY 12-13	249,021	43,470	292,491	3%
FY 13-14	258,417	43,470	301,887	3%
FY 14-15	267,815	43,470	311,285	3%
10-Year Total	**$2,464,363**	**$365,148**	**$2,829,512**	

* Reflects addition of Suite 906 to total leased space.

DETAILS OF PROPOSED LEGISLATION

The proposed resolution would authorize (1) the second five-year option to extend the lease between DCYF and API Fox Plaza for Suites 900, 902, and 903, and (2) incorporate Suite 906, which was previously on a month-to-month lease, into the second five-year option of the lease, in order to continue to provide office and program space for DCYF, for approximately 10,846 square feet of total leased space. Annual base rent is $574,838 ($53 per square foot), with the first two months of rent abated for total rent of $479,032 in the first year. The lease will commence on December 1, 2015 and expire on November 30, 2020. The key lease terms are shown in Table 2 below.

Table 2: Key Lease Terms

Premises	Suite 900 and 902 8,179 sq. ft. Suite 903 1,218 sq. ft. Suite 906 1,449 sq. ft. Total sq. ft. 10,846 sq. ft.
Permitted use	Offices and program space for DCYF
Term	Five years from 12/1/2015 – 11/30/2020
Extension Options	None
Annual Base Rent	Annually $574,838 ($53.00/sq. ft.) (first two months of rent are abated)
Rent Adjustments	Increase by $1 per square foot each year
Utilities & Services	Paid by the Landlord
Increases to Operating Expenses[2]	Paid by the Landlord

[2] Such increases to operating expenses may include increases to property taxes, insurance, security and other costs which may fluctuate during the term of the lease.

The existing lease provides that the rent for the second five-year extension option adjusts to 95 percent of fair market value for comparable properties in the Civic Center area. According to data from Jones Lang LaSalle[3] provided by the Real Estate Division, rental rates for comparable leases in the Civic Center area ranged from $55.22 to $78.54 per square foot per year, with an average price per square foot of $60.13 per year, as compared to the proposed rent of $53 per square foot per year.

According to Mr. Chyi, DCYF chose to include Suite 906 in the long-term lease with Suites 900, 902, and 903 to provide stability for the program uses in that suite[4], compared to being on a month-to-month lease which could have been terminated at any time by the Landlord.

FISCAL IMPACT

The rental rate for Suites 900, 902, and 903 at 1390 Market Street of $53 per square foot per year for the first year of the proposed lease is 86 percent more than the current rental rate of $28.50 per square foot per year for Suites 900, 902, and 903. The proposed rental rate of $53 per square foot per year is approximately 77 percent more than the current rental rate of $30 per square foot per year for Suite 906. As noted above, the Real Estate Division reports that the average rental rate for comparable leases in the Civic Center area is $60.13 per square foot per year compared to the rental rate of $53 per square foot per year in the proposed lease extension.

Annual rent costs will increase by $1 per square foot each year, as specified by the lease. Total rent to be paid by DCYF over the five-year extension term is $2,886,844, as shown in Table 3 below. According to Mr. Chyi, funds for the increased lease costs will be requested for appropriation in DCYF's FY 2015-16 budget.

Table 3: Five Year Rent Costs for DCYF at 1390 Market St.

Lease Year	$ per square foot	Total Rent Paid
Year 1	$53	$479,032
Year 2	$54	585,684
Year 3	$55	596,530
Year 4	$56	607,376
Year 5	$57	618,222
Total		**$2,886,844**

RECOMMENDATION

Approve the proposed resolution.

[3] Jones Lang LaSalle is a financial and professional services firm that specializes in commercial real estate services and investment management.

[4] Current program uses include older youth programs, grants management, and spaces for community-based organizations that partner with DCYF.

Item 6 **File 15-0312**	**Department:** San Francisco Municipal Transportation Agency (MTA)

EXECUTIVE SUMMARY

Legislative Objectives

- The proposed resolution would approve a new ten-year commercial lease agreement between MTA as landlord and the existing tenant Les Joulins, USA, Inc., and Osman Uner (Les Joulins) at 44 Ellis Street for use as a restaurant and nightclub.

Key Points

- Les Joulins currently leases 5,368 square feet of retail space in the Ellis O'Farrell Garage, located at 44 Ellis Street, managed by the MTA. The resolution would retroactively authorize a lease term of March 1, 2015 through February 28, 2025, with two five-year options to extend the lease through 2035.
- The RFP for the retail space invited prospective tenants to propose their own rent schedules, as long as the prospective tenant paid the MTA at least $4,980,000 over the initial ten-year lease term, which would be the equivalent of market rate rent for this property over ten years.
- MTA proposed a flexible rent schedule to allow the tenant to pay less rent during the first three years of the lease while making tenant improvements to the premises, which have significant deferred maintenance.

Fiscal Impact

- Les Joulins will pay MTA an annual rental rate of approximately $36 per square foot for the first two years with annual rent increases beginning in year three, paying the MTA a total of $5,127,000 over the ten-year lease period.
- Based on an inquiry by the Budget and Legislative Analyst's Office, the MTA renegotiated the lease terms to provide for a one-time rent adjustment applied at the beginning of the first five-year option, if the tenant exercises the option to extend. The rent adjustment would be equal to the higher of (1) the rent in year ten of the existing lease plus a 3 percent consume price index increase, or (2) 95 percent of fair market value.

Policy Consideration

- Les Joulins is eligible for rent credits of up to $250,000 from MTA as a partial reimbursement for tenant improvement project costs, after submitting a written request, including documentation with the total cost incurred and evidence of project completion.
- The lease provides for a 3 percent increase in the rent in effect at the beginning of each extension term, rather than adjusting the rent to fair market value.

Recommendations

- Amend the proposed resolution to specify a 3 percent per year rent increase in rent during the two five-year extension terms in the lease agreement.
- Approve the proposed resolution as amended.

MANDATE STATEMENT

Mandate Statement

City Charter Section 9.118(a) states that agreements entered into by a department, board or commission that will generate revenue in excess of $1 million or any modification of that contract are subject to Board of Supervisors approval.

BACKGROUND

The Ellis O'Farrell Garage (Garage), located on 123 O'Farrell Street, is owned by the City under the jurisdiction of the San Francisco Municipal Transportation Agency (MTA) and provides approximately 950 parking spaces and 11,000 square feet of retail space, leased to three tenants.

Property Management History

The City formed the non-profit Ellis O'Farrell Parking Corporation (Corporation) in 1963 to finance the construction and renovation of the Ellis O'Farrell Garage through the sale of Ellis-O'Farrell Parking Corporation bonds. MTA leased the Garage to the Corporation in 1965 to manage the day-to-day operations. MTA issued revenue bonds in 2012 to fully repay the outstanding Ellis O'Farrell Parking Corporation debt, and on February 19, 2013, the Board of Supervisors approved the retroactive termination of the lease between the MTA and the Ellis O'Farrell Parking Corporation, effective on January 31, 2013 (File 13-0057). The Garage is currently managed by the MTA.

44 Ellis Street Rental History

Les Joulins has operated a restaurant and nightclub at the 44 Ellis Street retail space for more than 30 years. Their first commercial lease with the non-profit Ellis O'Farrell Parking Corporation as landlord began on May 1, 1997, for an initial period of five years, with one five-year option to renew. On May 1, 2002, the Board of Supervisors approved a second amendment to the lease agreement, authorizing a five-year extension of the lease term through April 30, 2007. The lease still included the option to renew for an additional five years. Les Joulins subsequently exercised their option to renew the lease term through April 30, 2012. As of May 1, 2012, Les Joulins has been on a month-to-month lease (see Policy Considerations section below). The Les Joulins restaurant has 5,368 square feet of the total 11,000 square feet of the retail space in the Ellis O'Farrell Garage.

On May 17, 2013, the Real Estate Division issued a new Request for Proposals (RFP) for the 44 Ellis Street commercial lease currently occupied by Les Joulins, on behalf of the MTA, with a submission due date of June 21, 2013. Les Joulins was the only respondent to the RFP. The Real

Estate Division, in partnership with the MTA, reviewed the materials submitted by Les Joulins and engaged in negotiations to finalize a lease agreement

DETAILS OF PROPOSED LEGISLATION

The proposed resolution would approve a new ten-year commercial lease agreement between MTA as landlord and the existing tenant Les Joulins, USA, Inc., and Osman Uner (Les Joulins) of the 5,368 square foot retail space at 44 Ellis Street for use as a restaurant and nightclub. The resolution would retroactively authorize a lease term of March 1, 2015 through February 28, 2025, with two five-year options to extend the lease through 2035. Table 1 below outlines the key provisions in the commercial lease agreement. As shown in Table 2 below, the rent to be paid by Les Joulins to MTA over the initial ten-year lease term is $5,127,000.

Table 1. Key Points in the Commercial Lease Agreement

Lease term	March 1, 2015 – February 28, 2025
Size of property	5,368 square feet
Base rent paid by tenant in year one and two	$192,000 per year (approximately $36 per sq. ft.)
Annual rent adjustments year three through ten	Negotiated and includes cost of living increases.
Extension options	Two five-year options to renew through February 28, 2035.
Rent increase for the first five-year option	The higher of (1) the rent in year ten of the existing lease plus a 3 percent consumer price index increase, or (2) 95 percent of fair market value.
Rent credits	Up to $250,000; Tenant will be able to use these funds for MTA-approved tenant improvement projects.
Utilities and services	Tenant is responsible for the cost of all utilities and services provided to the premises.
Security Deposit	$50,000

Source: Commercial Lease between the City and County of San Francisco, acting by and through its Municipal Transportation Agency as "Tenant", and Les Joulins, USA, Inc., a California corporation as "Landlord".

FISCAL IMPACT

Under the proposed resolution, Les Joulins will pay MTA an annual rental rate of approximately $36 per square foot for the first two years with annual rent increases beginning in year three. As shown in Table 2 below, over the initial ten-year lease term, Les Joulins will pay the MTA $5,127,000 in rent. MTA will provide Les Joulins with rent credits of up to $250,000 for tenant improvement projects as approved by the MTA.

Table 2. 10-Year Rent Payable by Les Joulins to MTA

Lease Year	Annual Base Rent	Monthly Base Rent	Annual Square Foot Rental Rate
Year 1	$ 192,000	$ 16,000	$ 36
Year 2	192,000	16,000	36
Year 3	204,000	17,000	38
Year 4	574,681	47,890	107
Year 5	597,668	49,806	111
Year 6	621,575	51,798	116
Year 7	646,438	53,870	120
Year 8	672,296	56,025	125
Year 9	699,187	58,266	130
Year 10	727,155	60,596	135
Total	**$ 5,127,000**		

Source: Commercial Lease between the City and County of San Francisco, acting by and through its Municipal Transportation Agency as “Tenant”, and Les Joulins, USA, Inc., a California corporation as “Landlord”.

According to Mr. Rob Malone, MTA Acting Director of Parking, the Real Estate Division and the MTA evaluated the market value of the space prior to issuing the RFP. Following this analysis, the Real Estate Division recommended that the market-rate rent received over the ten-year lease term should be at least $4,980,000, which includes consumer price index increases. As noted in Table 2 above, the total rent to be paid of $5,127,000 exceeds the recommended rent of at least $4,980,000 by $147,000.

Tenant Improvements

The RFP for the 44 Ellis Street retail space invited prospective tenants to propose their own rent schedules, as long as the prospective tenant paid the MTA at least $4,980,000 over the ten-year lease period. According to Mr. Malone, MTA proposed a flexible rent payment schedule in order to allow the tenant to pay less rent during the first three years of the lease while making tenant improvements to the premises, which have significant deferred maintenance. The tenant is eligible for rent credits of up to $250,000 from MTA as a partial reimbursement for the cost of the tenant improvement projects listed below.

According to the lease, the tenant must request the rent credit in writing and include documentation evidencing the completion of the work and the amount paid for the work. According to Mr. Malone, the $250,000 in rent credits is projected to be only a small percentage of the total cost to complete all seven tenant improvement projects.

1. Installation of new ceilings
2. Installation of new flooring
3. Construction of two (2) new bathrooms
4. Replacement of kitchen hood ventilation system
5. Construct electrical upgrades
6. Update plumbing
7. Relocate/reconfigure non load-bearing interior walls

Rent Increase if the Option to Extend the Lease Term is Exercised

Under the proposed lease, the tenant has the option to extend the lease for two additional five-year terms through 2035. Based on an inquiry by the Budget and Legislative Analyst's Office, the MTA renegotiated the lease terms with Les Joulins to provide for a one-time rent adjustment applied at the beginning of the first five-year option, if the tenant exercises the option to extend. The rent adjustment would be equal to the higher of (1) the rent in year ten of the existing lease plus a 3 percent consumer price index increase, or (2) 95 percent of fair market value.

Also, the proposed lease does not specify annual rent adjustments during the two five-year optional extension terms, although Mr. Malone states that the intent is to increase the rent during the extension term by 3 percent per year. The proposed resolution should be revised to specify such 3 percent per year rent increases during the two five-year extension terms.

POLICY CONSIDERATION

MTA has extended the lease with Les Joulins on a month-to-month basis since May 2012, or almost three years, due to a lengthy lease negotiation process

Les Joulins continued to occupy the 44 Ellis Street retail space on a month-to-month lease after the lease with the nonprofit Ellis O-Farrell Parking Corporation expired on April 30, 2012. In 2012, when the Ellis-O'Farrell Garage was still managed by the Ellis-O'Farrell Parking Corporation, the Ellis-O'Farrell Corporation identified a new prospective tenant to occupy the space at 44 Ellis Street currently occupied by Les Joulins, and began negotiations with the new prospective tenant in May 2012. The Ellis-O'Farrell Corporation notified Les Joulins of their plans to enter into a new lease with the prospective tenant by July 1, 2012. However, MTA issued revenue bonds in 2012 to repay Ellis O-Farrell Parking Corporation's outstanding debt, and in January 2013, MTA terminated their lease with the Ellis O-Farrell Parking Corporation and began to directly manage the Ellis O-Farrell Parking Garage. Therefore, the potential new lease was never executed, and Les Joulins remained in the premises on a month-to-month basis.

As noted above, the Real Estate Division issued a new RFP to lease the retail space at 44 Ellis Street on May 17, 2013 with proposals to be submitted on June 21, 2013, a period of 35 days. Les Joulins was the only responder to the RFP. According to Mr. John Updike, City Director of Real Estate, the submission period was shorter than usual because the 5,368 square feet of retail space was advertised in 2012 for over a year. Given the prior market exposure, the Real Estate Division considered that a 35-day period to respond to the RFP was sufficient.

RECOMMENDATIONS

1. Amend the proposed resolution to specify a 3 percent per year rent increase in rent during the two five-year extension terms in the lease agreement.
2. Approve the proposed resolution as amended.