

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

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TO: Budget and Finance Sub-Committee

FROM: Budget and Legislative Analyst



SUBJECT: April 13, 2016 Budget and Finance Sub-Committee Meeting

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Item 4 File 16-0145	Department: San Francisco International Airport (Airport)
EXECUTIVE SUMMARY	
<p style="text-align: center;">Legislative Objectives</p> <ul style="list-style-type: none"> • The proposed resolution would approve Modification No. 1 to the 2011 Lease and Use Agreement between the San Francisco International Airport (Airport) and US Airways, Inc. (US Airways) granting the early termination of the lease with US Airways. Through the proposed modification, US Airways will relinquish its premises to the Airport and cease paying rent for the premises. <p style="text-align: center;">Key Points</p> <ul style="list-style-type: none"> • On November 5, 2010, the Board of Supervisors approved a new lease between US Airways, Inc. (US Airways) and the San Francisco International Airport (Airport) as part of the Airport's Lease and Use Agreement. On May 21, 2010, the Board of Supervisors approved a new lease between American Airlines (American) and the Airport as part of the Airport's Lease and Use Agreement. • In November 2011, American filed for bankruptcy. The resulting bankruptcy plan contemplated the merging of American and US Airways, under the parent company AMR Corporation. On October 1, 2015, US Airways co-located its passenger check-in functions with American in Terminal 2, and on October 17, 2015 ceased all flights nationwide under the US Airways brand. <p style="text-align: center;">Fiscal Impact</p> <ul style="list-style-type: none"> • Under the proposed modification to its lease, US Airways will relinquish its 20,347 square feet of Exclusive Use space to the Airport, thereby eliminating its current rent of \$2,706,206. American Airlines will add 8,586 square feet of Exclusive Use space to its premises, for a total of 56,095 square feet, and thereby increasing its rent paid in FY 2016-17 from \$8,491,040 to \$9,545,461, an increase of \$1,054,421. The result of these changes is a net reduction of \$1,651,785 in rent paid to the Airport. <p style="text-align: center;">Recommendation</p> <ul style="list-style-type: none"> • Approve the proposed resolution. 	

MANDATE STATEMENT

City Charter Section 9.118(c) states that any lease of real property for a period of ten or more years, including options to renew, and the amendments to such lease, are subject to Board of Supervisors approval.

BACKGROUND

On November 5, 2010, the Board of Supervisors approved a new lease between US Airways, Inc. (US Airways) and the San Francisco International Airport (Airport) as part of the Airport's Lease and Use Agreement, giving US Airways landing rights and rental of approximately 25,070 square feet of Exclusive Use space and 216 of Joint Use space in Terminal 1 Boarding Area B. The lease was for ten years from July 1, 2011 to June 30, 2021. Annual rent for the premises in FY 2015-16 is \$2,706,206.

On May 21, 2010, the Board of Supervisors approved a new lease between American Airlines (American) and the Airport as part of the Airport's Lease and Use Agreement, giving American landing rights and rental of approximately 47,509 square feet of Exclusive Use space and 78,747 of Joint Use space in Terminal 2 Boarding Area D. The lease was for ten years from July 1, 2011 to June 30, 2021. Annual rent for the premises in FY 2015-16 is \$8,491,040.

In November 2011, American filed for bankruptcy. The resulting bankruptcy plan contemplated the merging of American and US Airways, under the parent company AMR Corporation. In conjunction with the bankruptcy proceedings, the Airport and American negotiated an agreement which gave US Airways an option to co-locate with American in Terminal 2 Boarding Area D and eliminate US Airways' Exclusive Use Space in Terminal 1. In 2013, US Airways and American merged under the common control of American Airlines Group, Inc. On May 19, 2015 the Airport reduced US Airways' Exclusive Use space in Terminal 1 from 25,070 to 20,347 square feet. On October 1, 2015, US Airways co-located its passenger check-in functions with American in Terminal 2, and on October 17, 2015 ceased all flights nationwide under the US Airways brand.

DETAILS OF PROPOSED LEGISLATION

The proposed resolution would approve Modification No. 1 to the 2011 Lease and Use Agreement between the Airport and US Airways, granting the early termination of the lease with US Airways. Through the proposed modification, US Airways will relinquish its premises to the Airport and cease paying rent for the premises.

FISCAL IMPACT

Under the proposed modification to its lease, US Airways will relinquish its 20,347 square feet of Exclusive Use space to the Airport, thereby eliminating its current rent of \$2,706,206.

American Airlines will add 8,586 square feet¹ of Exclusive Use space to its premises, for a total of 56,095 square feet, and thereby increasing its rent paid in FY 2016-17 from \$8,491,040 to \$9,545,461, an increase of \$1,054,421. The result of these changes is a net reduction of \$1,651,785 in rent paid to the Airport, as shown in Table 1 below.

Table 1: Net Reduction of Rent Revenue to Airport

	Current Rent for FY 2015-16	Proposed Rent for FY 2016-17	Rent Increase (Decrease) in FY 2016-17
US Airways	\$2,706,206	\$0	(\$2,706,206)
American	8,491,040	9,545,461	1,054,421
Total	\$11,197,246	\$9,545,461	(\$1,651,785)

Table 2 below shows that the total increase in rent to be paid by American Airlines to the Airport for FY 2016-17 is \$1,054,421.

Table 2: Summary of Changes to American’s Premises

Cat	Rate/SF	Current Square Feet	Current Rent	Proposed Square Feet	Proposed Rent	Rent Variance
1	\$275.55	1,532	\$422,143	2,136	\$588,575	\$166,432
2	206.66	25,728	5,316,948	27,134	5,607,512	290,564
3	137.78	19,698	2,713,990	23,474	3,234,248	520,257
4	68.89	551	37,958	551	37,958	-
5	27.56	-	-	2,800	77,168	77,168
Total		47,509	\$8,491,040	56,095	\$9,545,461	\$1,054,421

The proposed Modification No. 1 will have no budgetary impact on the Airport’s budget because under the Airport’s break-even policy, the airlines operating at the Airport pay the Airport any difference between the Airport’s non-airline operating revenues and operating expenditures through the airlines’ annual terminal rentals and landing fees. The rates for these rental and landing fees are adjusted each year. Ms. Diane Artz, Senior Property Manager at the Airport, states that the Airport will not lease any of the remaining space formerly leased by US Airways because the Airport requires this space for its Terminal 1 renovation project.

RECOMMENDATION

Approve the proposed resolution.

¹ According to the City Attorney for the Airport the addition of 8,586 square feet is not subject to approval by the Board of Supervisors because any change in leased square space under 10 percent of the total square footage leased is considered to be a non-material change according to the 2011 Lease and Use Agreement.

Item 5 File 16-0146	Department: San Francisco International Airport (Airport)
EXECUTIVE SUMMARY	
<p style="text-align: center;">Legislative Objectives</p> <ul style="list-style-type: none"> • The proposed resolution would approve a lease of approximately five years and three months between the San Francisco International Airport (Airport) as Landlord and Qantas Airways, Limited (Qantas) as Tenant for Qantas to pay landing fees and rent space in the Airport's International Terminal. <p style="text-align: center;">Key Points</p> <ul style="list-style-type: none"> • In 2011, the Airport negotiated a new ten-year Lease and Use Agreement with its domestic and international airlines that operate at the Airport. This Agreement allows airlines to provide flight operations and rent terminal space at the Airport and provides a common set of lease provisions that are used for these airlines. • On November 10, 2015, the San Francisco Airport Commission approved a lease with Qantas to commence flight operations and rent terminal space at the Airport under provisions of the 2011 Lease and Use Agreement. Qantas began flight operations on December 18, 2015 under an Airline Operating and Space Permit. <p style="text-align: center;">Fiscal Impact</p> <ul style="list-style-type: none"> • The Airport estimates total rent for International Terminal Exclusive Space to be paid by Qantas to the Airport of \$749,411 over the five year and three month term of the proposed new lease. Annual rent increases are determined by Airport Finance Division, and are estimated to range from 6.4 percent to 7.3 percent per year. Ms. Diane Artz, Senior Property Manager at the Airport, states that because of the many variables related to Joint Use space rent and Landing Fee calculations, the Airport cannot project Joint Use space rent and Landing Fees for the fiscal years following FY 2015-16 at this time. <p style="text-align: center;">Recommendation</p> <ul style="list-style-type: none"> • Approve the proposed resolution. 	

MANDATE STATEMENT

City Charter Section 9.118(c) states that any lease of real property for a term of ten years or more, including options to extend, or that has anticipated revenues of \$1 million or more is subject to Board of Supervisors approval.

BACKGROUND

In 2011, the San Francisco International Airport (Airport) negotiated a new ten-year Lease and Use Agreement (Agreement) with its domestic and international airlines that operate at the Airport. This Agreement allows airlines to provide flight operations and rent terminal space at the Airport and provides a common set of lease provisions that are used for these airlines. Such provisions include rent and fees paid by the airlines to the Airport, permitted uses of the premises, use of common facilities, and numerous other provisions. The 2011 Lease and Use Agreement, as previously approved by the Board of Supervisors, began on July 1, 2011 and will expire on June 30, 2021.

On November 10, 2015, the San Francisco Airport Commission (Commission) approved a lease with Qantas Airways, Limited (Qantas) to commence flight operations and rent terminal space at the Airport under provisions of the 2011 Lease and Use Agreement. Qantas began flight operations on December 18, 2015 under an Airline Operating and Space Permit.

DETAILS OF PROPOSED LEGISLATION

The proposed resolution would approve a lease of approximately five years and three months between the Airport as Landlord and Qantas as Tenant for Qantas to pay landing fees and rent space in the Airport's International Terminal. Key provisions of the lease are shown in Table 1 below:

Table 1: Key Provisions of Lease between Airport and Qantas

Term	Lease commences upon approval by the Board of Supervisors and expires on June 30, 2021, approximately 5 years and 3 months
International Terminal Exclusive Use Space	566 square feet
International Terminal Joint Use Space	631,987 square feet
Exclusive Use Space Rent in Year One	\$206.66 per square foot
Rent Adjustment	Rent adjusted annually by Airport’s Rates and Charges ¹
Fees	Joint Use space rent is determined annually by formula. Landing Fees are determined by Airport Rates and Charges.
Utilities	Qantas to pay utilities, including electricity, telecommunications, and trash removal.
Deposit	Two months of terminal area rentals, landing fees, usage fees, per rates and charges.

Joint Use Space rent is determined through a formula based on multiple variables that change each year. The Airport determines the rent amounts annually based on data collected from the previous period.² Landing Fees are determined by the Airport’s Rates and Charges and are to be paid by Qantas based on its fleet mix and flight schedules. Ms. Diane Artz, Senior Property Manager at the Airport, states that because of the many variables related to Joint Use space rent and Landing Fee calculations, the Airport cannot project Joint Use space rent and Landing Fees for the fiscal years following FY 2015-16 at this time. For the two-week period from December 18, 2015 through December 31, 2015, Qantas paid a per passenger fee of \$11.15 in lieu of Joint Use Fees. Effective January 1, 2016, Qantas was added to the Joint Use Formula, pursuant to a mid-year adjustment, and is currently paying \$170,914.91 monthly in Joint Use space rent.

FISCAL IMPACT

As shown in Table 2 below, the Airport estimates total rent for International Terminal Exclusive Space to be paid by Qantas to the Airport of \$749,411 over the five year and three month term of the proposed new lease. Annual rent increases are determined by Airport Finance Division, and are estimated to range from 6.4 percent to 7.3 percent per year. As stated above, the Airport does not have an estimate at this time for Joint Use space rent and Landing Fees. Table

¹ Each year, the Airport’s Finance Department develops a forecast for revenue and expenses. The Airport then uses this forecast to adjust the rates for each category of rental space at the Airport.

² In the event there are several airlines that either commence or terminate flight operations in any given year, the Airport reserves the right to make mid-year adjustments.

2 below shows the estimated rent for Exclusive Use space to be paid by Qantas to the Airport through the approximate five year and three month lease term.

Table 2: Estimated Rent Paid by Qantas to Airport through Lease Term

Fiscal Year	Square Feet	Rent	Rent Percent Increase	Annual Rent*
FY 2015-16	566	\$206.66	N/A	\$29,242**
FY 2016-17	566	219.84	6.4%	124,429
FY 2017-18	566	235.95	7.3%	133,548
FY 2018-19	566	253.26	7.3%	143,345
FY 2019-20	566	271.75	7.3%	153,809
FY 2020-21	566	291.59	7.3%	165,037
Total				\$749,411

* Totals may vary due to rounding

** Includes rent for final three months of FY 2015-16

RECOMMENDATION

Approve the proposed resolution.

Item 6 File 16-0216	Department: San Francisco International Airport (Airport)
EXECUTIVE SUMMARY	
<p style="text-align: center;">Legislative Objectives</p> <ul style="list-style-type: none"> • The proposed resolution would approve an emergency public work contract between the San Francisco International Airport (Airport) and Pilot Construction Management, Inc. (Pilot) for the Superbay Hanger Emergency Fire Watch and Interim Foam Fire Suppression System Retrofit Project in an amount not-to-exceed \$4,366,164. <p style="text-align: center;">Key Points</p> <ul style="list-style-type: none"> • On December 18, 2015, Airport staff noticed a significant drop in water pressure within the Superbay Hangar fire suppression system. On January 14, 2016 the San Francisco Fire Department issued a notice to the Airport to correct fire hazards and to develop a plan to provide adequate fire protection at the Superbay Hangar or to close down the Hangar. • On February 5, 2016, the Airport declared the breakdown of the Superbay Hangar fire suppression system to be an emergency, in accordance with Administrative Code Section 6.60. The Airport entered into a contract with Pilot Construction Management, Inc. (Pilot) on February 5, 2016 for the Fire Watch and Interim Foam Fire Suppression System Retrofit Project and Pilot then began work on the Project. The Airport submitted the proposed resolution approving the emergency contract with Pilot on March 15, 2016. • The Airport did not solicit bids from other firms that could potentially perform this work, due to the emergency nature of the failure to the fire suppression system. According to Ms. Geri Rayca, Manager in the Airport’s Contract Management Unit, Pilot has already been working on several Superbay Hangar projects, including components of the fire suppressions system and bypass work at the Pump House. Because of their existing knowledge of the Superbay Hangar, Pilot would be able to perform its work with less delay, compared to finding an alternative contractor. <p style="text-align: center;">Fiscal Impact</p> <ul style="list-style-type: none"> • The total cost of the Superbay Hanger Emergency Fire Watch and Interim Foam Fire Suppression System Retrofit Project is \$4,366,164. According to Ms. Rayca, the Airport’s capital budget has sufficient funds to pay for the proposed emergency contract with Pilot. <p style="text-align: center;">Recommendation</p> <ul style="list-style-type: none"> • Approve the proposed resolution. 	

MANDATE STATEMENT

Administrative Code Section 6.60(b) states that the department head responsible for addressing an emergency may declare an emergency with immediate notice to the Board of Supervisors, the Mayor, the Controller, and the commission.

Administrative Code Section 6.60(d) states that emergency work of more than \$250,000 requires written approval of the commission overseeing the department. If the department is unable to obtain Board of Supervisors approval prior to performing emergency work of more than \$250,000, the department must submit a resolution to the Board of Supervisors approving the emergency determination within 60 days of the department head's emergency declaration.

BACKGROUND

The Superbay Hanger at the San Francisco International Airport was constructed in 1969 and is one of only four hangars in the United States that can house four 747 aircraft. The Superbay Hanger is currently occupied by American Airlines and United-Continental Airlines to perform necessary aircraft safety and maintenance checks.

On December 18, 2015, Airport staff noticed a significant drop in water pressure within the Superbay Hangar fire suppression system. Multiple leaks were identified within the 30" underground transit pipe which brings water from the external Pump House to the Superbay Hangar. As such, the Superbay Hanger does not have sufficient water pressure for fire suppression in the event of a fire. The Superbay Hangar is currently under temporary fire watch by the order of the Airport Fire Marshal. On January 14, 2016 the San Francisco Fire Department issued a notice to the Airport to correct fire hazards and to develop a plan to provide adequate fire protection at the Superbay Hangar or to close down the Superbay Hangar.

On February 5, 2016, the Airport declared the breakdown of the Superbay Hangar fire suppression system to be an emergency, in accordance with Administrative Code Section 6.60. The President of the Airport Commission subsequently gave written approval to perform emergency work to repair the Superbay Hangar fire suppression system.

The Airport entered into a contract with Pilot Construction Management, Inc. (Pilot) on February 5, 2016 for the Fire Watch and Interim Foam Fire Suppression System Retrofit Project, and Pilot then began work on the Project. The Airport submitted the proposed resolution approving the emergency contract with Pilot on March 15, 2016.

DETAILS OF PROPOSED LEGISLATION

The proposed resolution would approve an emergency public work contract between the Airport and Pilot Construction Management, Inc. (Pilot) to repair the Emergency Fire Watch and Interim Foam Fire Suppression System at the Airport's Superbay Hanger in an amount not-to-exceed \$4,366,164.

According to Ms. Geri Rayca, Manager in the Airport's Contract Management Unit, the Airport worked with the Airport Fire Marshal to develop a scope of work for repairs required to continue operations in the Superbay Hanger. These repairs must be completed in order to gain approval by the Airport Fire Marshal. The scope of work for the project includes:

- Perform fire main bypass to address leak outside the Pump House (to be completed by March 20, 2016);
- Provide 12 high-expansion high-trajectory foam hose reels (to be completed by May 20, 2016);
- Modify domestic water system for fire sprinklers on 1st, 2nd, and 4th floor offices, and aircraft parts storage (to be completed by May 20, 2016).
- Integration of Ultraviolet Infrared Detection system into existing foam system (to be complete by June 30, 2016);
- Modify pump control system at Pump House to respond to manual control system (to be completed by July 15, 2016);
- Fire watch for 24 hours-per-day, 7 days-per-week, as required by San Francisco Fire Department and Airport Fire Marshal (to be performed through January 31, 2017).

In accordance with Administrative Code section 6.60, the Airport was not required and did not solicit bids from other firms that could potentially perform this work, due to the emergency nature of the failure to the fire suppression system. According to Ms. Rayca, Pilot has already been working on several Superbay Hangar projects, including components of the fire suppressions system and bypass work at the Pump House. Because of their existing knowledge of the Superbay Hangar, Pilot would be able to perform its work with less delay, compared to finding an alternative contractor. Engineering staff at the Airport reviewed the scope of work and estimated the cost of these elements to be \$4,651,987. The proposed emergency contract with Pilot is for an amount not-to-exceed \$4,366,164, or \$285,823 less than the Airport engineering staff's estimate.

According to Ms. Rayca, the Airport plans to replace the current fire suppression system with a new permanent high-expansion foam fire suppression system. The Airport anticipates issuing a competitive Request for Proposals in June 2016 to award a contract to procure a design-build

contractor to install a new fire suppression system. The new system is expected to cost approximately \$20,000,000.

FISCAL IMPACT

The total estimated cost to repair the Superbay Hanger Emergency Fire Watch and Interim Foam Fire Suppression System is \$4,366,164, as shown in Table 1 below.

Table 1: Total Cost to Repair the Superbay Hanger Emergency Fire Watch and Interim Foam Fire Suppression System

	Fire Main Bypass	12 High-Expansion Foam Hose Reels	Modify Domestic Water System	Integration of Ultraviolet Infrared Detection	Modify Pump Control System	Fire Watch	Total
Labor	\$88,000	\$89,850	\$100,000	\$130,000	\$247,000	\$1,184,634	\$1,839,484
Equipment	217,000	760,000	359,000	471,000	252,000	-	\$2,059,000
Engineering	18,000	54,000	45,000	74,000	52,000	-	\$243,000
Contingency (5%)	24,820	68,000	38,190	51,330	42,340	-	\$224,680
Total	\$347,820	\$971,850	\$542,190	\$726,330	\$593,340	\$1,184,634	\$4,366,164

Ms. Rayca states the Airport's capital budget has sufficient funds to pay for the proposed emergency contract with Pilot. The capital budget was previously approved by the Board of Supervisors.

RECOMMENDATION

Approve the proposed resolution.