

PUBLIC UTILITIES COMMISSION

City and County of San Francisco

RESOLUTION NO. 17-0123

WHEREAS, The City and County of San Francisco (City) owns certain real property presently under the jurisdiction of the San Francisco Public Utilities Commission (SFPUC) consisting of approximately 199 acres of SFPUC Parcel 31 in the Peninsula Watershed in Burlingame, California (Premises); and

WHEREAS, In 1996, the SFPUC awarded a 20-year lease (Original Lease) to Crystal Springs Golf Partners, LP (Tenant) as the successful bidder in a competitive bidding process, for the operation of an 18-hole regulation length municipal golf course and driving range on the Premises; and

WHEREAS, The Original Lease expired on March 31, 2017, and Tenant desires to obtain a new lease to continue operating the municipal golf course and driving range at the Premises; and

WHEREAS, Since the Original Lease's inception in 1996, the golf course market has softened due to falling customer demand and an oversupply of new golf courses both nationally and in the Bay Area, and in 2003, in response to these conditions, the SFPUC amended the Original Lease to provide a rent reduction to Tenant; and

WHEREAS, In 2011, Tenant approached SFPUC staff with a request for an additional rent reduction and a lease term extension in response to a further softening of customer demand and worsening financial performance caused by the Great Recession; and

WHEREAS, The SFPUC did not act on Tenant's 2011 request at the time, but staff agreed to consider the request after consulting with experts in the golf course industry; and

WHEREAS, To inform the SFPUC's economic decisions regarding the Premises, SFPUC staff relied on the advice of consultants including Economic & Planning Systems, Inc. (EPS), an economic consulting firm, and Pro Forma Advisors LLC (Pro Forma Advisors), a firm which specializes in market analysis, financial feasibility, economic impact studies and appraisals for large-scale real estate developments, including golf courses; and

WHEREAS, The SFPUC's consultants found that after sharp declines in overall economic performance of golf courses over the past 10 to 15 years due to a 20% decline in the number of golfers, the Bay Area golf market has stabilized over the past three years. The SFPUC's consultants further found that the financial performance of Bay Area golf courses remains relatively flat, and the mid-to-long-term outlook for the regional golf market is highly uncertain; and

WHEREAS, The high fixed cost nature of the golf course business, coupled with the required capital investment and the high uncertainty of future demand for golf translates to very high risk for investors in the golf industry; and

WHEREAS, To minimize this risk, the SFPUC is seeking a lease rather than a fixed management fee arrangement with a golf course operator whereby the operator would retain all operating revenues and costs and pay a percentage of gross revenue to the SFPUC with a minimum base rent, requiring the operator to fund any operating shortfalls; and

WHEREAS, Golf course operators prefer a contract fee model, whereby property owners retain operating revenues and costs and pay the operator a fee, requiring the property owner to fund any operating shortfalls; and

WHEREAS, In 2014, SFPUC staff asked EPS to evaluate the likelihood of a successful request for proposals (RFP) process for a new golf course lease to replace the Original Lease upon expiration; and

WHEREAS, EPS's analysis of recent RFP releases confirm that golf course operators prefer a contract fee structure in order to reduce financial risk, suggesting that a RFP for a lease participation structure would not likely result in better deal terms for the SFPUC. Recent attempts by public agencies to lease courses have resulted in few or no bids, and proposed terms have included substantially reduced rent or rent credits for rapid recovery of any invested capital. For example, the County of Los Angeles received no bids on the Marshall Canyon golf course, the City of Portland received no qualified bids for the Heron Lake golf course, and the Los Angeles Department of Airports received only one bid for the Westchester golf course from its incumbent operator; and

WHEREAS, EPS concluded that given the ongoing soft economic conditions of the golf course industry, the continuing capital investment needs at the Golf Course, and the likelihood of low tenant interest in responding to an RFP by the SFPUC due to golf operators' preference for a management fee arrangement rather than a lease structure, especially a lease requiring tenant-funded capital investments, there is a substantial risk that the SFPUC's issuance of an RFP will yield disadvantageous rent terms to the SFPUC or a golf course tenant that does not suit the SFPUC's needs; and

WHEREAS, Based on the advice of the SFPUC's consultants, SFPUC staff concluded that it is impractical to competitively bid the new lease opportunity and instead negotiated with Tenant proposed terms and conditions of a new 20-year lease in the form attached to this Resolution as Exhibit A and incorporated herein (New Long-Term Lease); and

WHEREAS, The SFPUC and Tenant negotiated in good faith for over a year to finalize the terms and conditions of the proposed New Long-Term Lease, and although lease negotiations are completed, due to no fault of Tenant there was insufficient time to seek the necessary City approvals of the proposed New Long-Term Lease prior to the expiration of the Original Lease; and

WHEREAS, the SFPUC and Tenant entered into a new month-to-month lease so that Tenant can continue to operate the golf course while seeking City approval of the proposed New Long-Term Lease; and

WHEREAS, The New Long-Term Lease fair market rent structure was determined using a comprehensive financial model developed by SFPUC staff (SFPUC Model) that determined the percentage rent and base rent structure based on an expected internal rate of return (IRR) on Tenant's required investment; and

WHEREAS, The SFPUC consulted with leading industry experts to validate the proposed fair market rent structure throughout the negotiations with Tenant; and

WHEREAS, Under Professional Services Contract CS-287, Century Urban, a SFPUC sub-consultant specializing in economic and feasibility analysis and asset management, validated the SFPUC Model; and

WHEREAS, Pro Forma Advisors vetted the proposed fair market rent structure reflected in the SFPUC Model, and in its view, concluded that given the current and anticipated market conditions, and expected operating performance at Crystal Springs, the proposed rent structure is well within the range of current fair market rental terms; and

WHEREAS, Pro Forma Advisors cited the annual Financing and Investment Survey from the Society of Golf Course Appraisers, an organization dedicated to the advancement of the golf course consulting and valuation profession, that showed that the expected IRR for golf courses ranges from 10 percent to 22 percent, averaging 14 percent; and

WHEREAS, Given the above, SFPUC staff determined that the projected IRR of 13.95 percent under the SFPUC Model for Crystal Springs is consistent with current industry investment criteria; and

WHEREAS, SFPUC staff have consulted with the Director of Property, who concurs that the proposed rent structure reflects fair market rent; and given that such proposed rent is less than \$45 per square foot, and the rent structure has been validated by an independent, qualified golf course appraiser, Administrative Code Section 23.30 does not require a formal appraisal; and

WHEREAS, Any capital improvements proposed by Tenant will be subject to prior SFPUC approval, and the New Long-Term Lease expressly acknowledges that the SFPUC may not consider the proposed improvements before completion of all environmental review required by law, and

WHEREAS, the new lease would entail minor alterations to existing facilities, no new ground disturbance, and no vegetation removal with the exception of dead, previously-planted trees; and any subsequent capital improvements would be subject to subsequent approvals by SFPUC's Natural Resources Land Management Division (NRLMD) and to the provisions of the Peninsula Watershed Management Plan (SFPUC 1998), and contingent on future reviews by the Bureau of Environmental Management and the Planning Department, and the proposed lease is exempt from the California Environmental Quality Act (CEQA) under CEQA Guidelines Section 15301, Class 1(Existing Facilities); now, therefore, be it

RESOLVED, That this Commission hereby ratifies, approves and authorizes all actions heretofore taken by any City official in connection with the proposed New Long-Term Lease; and be it

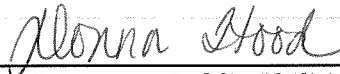
FURTHER RESOLVED, That based on the advice of the SFPUC's consultants, this Commission finds that it would be impractical to competitively bid the opportunity for a new golf course lease at the Premises; and be it

FURTHER RESOLVED, That this Commission hereby approves the terms and conditions of the New Long-Term Lease; and be it

FURTHER RESOLVED, That this Commission hereby authorizes the SFPUC General Manager and/or the City's Director of Property to seek approval by the Board of Supervisors and Mayor of the New Long-Term Lease under Charter section 9.118 and, upon such approval, to execute the New Long-Term Lease in substantially the form of attached Exhibit A; and be it

FURTHER RESOLVED, That, upon approval by the Board of Supervisors and Mayor, this Commission authorizes the SFPUC General Manager and the City's Director of Property to enter into any amendments or modifications to this New Long-Term Lease, including without limitation, the exhibits, they or the City Attorney believe are in the best interest of the City; do not materially increase the obligations or liabilities of the City or materially diminish the benefits to the City; are necessary or advisable to effectuate the purposes and intent of this resolution; and are in compliance with all applicable laws, including the City Charter.

I hereby certify that the foregoing resolution was adopted by the Public Utilities Commission at its meeting of May 23, 2017.



Secretary, Public Utilities Commission