



MEMORANDUM

August 6, 2021

TO: MEMBERS, PORT COMMISSION
Hon. Kimberly Brandon, President
Hon. Willie Adams, Vice President
Hon. John Burton
Hon. Gail Gilman
Hon. Doreen Woo Ho

FROM: Elaine Forbes
Executive Director 

SUBJECT: Request Approval of: (1) Increasing Phase 1 Budget from \$145 Million to \$184.2 Million and (2) Modified China Basin Park Construction Sequencing for the Mission Rock Project at Seawall Lot 337, bounded by China Basin Channel, Third Street, Mission Rock Street and San Francisco Bay

DIRECTOR'S RECOMMENDATION: Approve the Attached Resolution No. 21-33

Executive Summary

On September 24, 2019, by Resolution No. 19-39, the Port Commission approved the \$145 million Mission Rock Phase 1 budget. Subsequently, despite significant constraints due to the Covid-19 pandemic, the project team successfully obtained the project-wide Street Improvement Permit ("SIP"), Phase 1 Final Map, and Phase 1 Notice to Proceed. Construction of Phase 1 horizontal infrastructure commenced in late 2020 and is scheduled to be complete in late 2022.

The Project's development is governed by the Disposition and Development Agreement ("DDA") and related agreements between the Port and the Developer. Consistent with the requirements of the DDA, this past April, the Developer notified the Port of Phase 1 cost increases primarily attributable to 1.) higher than expected costs to approve the use of Lightweight Cellular Concrete ("LCC") in the project's streets; 2.) an enhanced design of the China Basin Park; 3.) rising construction materials costs; 4.) increased City agency costs due to additional staff time to review of unique project conditions; 5.) higher costs for electricity facilities to accommodate both PG&E and SFPUC onsite on a temporary basis; and 6.) impacts from Covid-19, among others.

The net result of these cost increases – after value engineering and delaying costs that can be sequenced – results in a Phase 1 budget of \$184.2 million. The DDA sets forth an approval process for increases to infrastructure costs based upon five criterion related to demonstrating sufficient sources of funding and the costs being reasonable to implement the DDA. Higher costs to implement the DDA will negatively impact the Port's net present value revenues from the project; however, on a nominal dollar basis the Port's revenues from the project remain strong.¹ Based upon Port staff's review of the cost increase request and DDA criteria – along with our real estate and engineering consultant's analyses, the cost increases appear reasonable and the Project does have sufficient sources to repay Phase 1 horizontal infrastructure costs. This conclusion is based on numerous assumptions about future development. Cost escalation and timing of phases are crucial assumptions. To narrow the likelihood of a delay in the next phase, Port staff and the Developer have agreed to a monetary penalty if Phase 2 is delayed, and staff have implemented other tools contemplated in the DDA for a Phase 1 cost increase.

Underlined sections of this memorandum indicate changes in text from the informational memorandum submitted for the July 13, 2021 Port Commission meeting. These underlined sections include additional information on the four topics:

1. Details on the public's experience in China Basin Park once the inland portion is built out and the in-water construction is occurring.
2. Clearer presentation of total and local business enterprise (LBE) contraction.
3. Details on the proposed December 31, 2022 deadline for submittal of the Phase 2 budget.
4. Explanation of the total Phase 1 contingency

The below staff report includes the following sections:

- I. Project Background and Status
- II. Phase 1 Budget Challenges
- III. Phase 1 Budget: Proposed Solutions
- IV. Recommendation

I. Project Background and Status

Project Overview

At full build out, the Mission Rock project will include approximately 1,200 units of new, rental housing, 1.4 million square feet of new commercial and office space, and rehabilitation of historic Pier 48, as well as space for small-scale manufacturing, retail and

¹ This is primarily because higher costs also affect vertical construction costs, upon which the model projects assessed value and taxes. The Port benefits from out-year taxes, thus the net present value revenue can go down while the total nominal (meaning, escalated) revenues to the Port over a 75 year period can (and have) gone up.

neighborhood services, a waterfront park, and public infrastructure.

Following Port Commission approval of the \$145 million Phase 1 budget in September 2019, the Project team has accomplished the following milestones:

1. Issuance of SFPW Director's Order authorizing use of lightweight cellular concrete (LCC) in the project's streets
2. Approval of project-wide Tentative Map and Phase 1 Final Map
3. Approval of China Basin Park Schematic Design
4. Issuance of Phase 1 Street Improvement Permit (SIP)
5. Issuance of Notice to Proceed with the installation of horizontal infrastructure
6. Secured Bond Financing for District Utilities
7. Closed on all four Phase 1 Parcel Leases
8. Approval of new street names honoring Dr. Maya Angelou and Toni Stone
9. Successful preparation, marketing, and sale of \$43.3 million CFD bonds
10. Awarded \$31.0 million in contracts and an additional \$62.6 million in LBE contract commitments (as of March 2021)
11. Commenced construction of Phase 1 horizontal infrastructure
12. Commenced construction of three of the four Phase 1 vertical buildings

Contracting

Mission Rock was one of the City's first development projects to commit to a Local Business Enterprise ("LBE") participation goal; the goal established in the DDA is that 20% of horizontal contracting and 20% of vertical contracting will be with LBEs. As of Q1 2021, the project team has awarded \$31.3M in contracts to local business enterprises. Local Business Enterprise awards make up 19% of overall horizontal awards and 4% of overall vertical awards.

The Developer notes that the project is trending toward the 20% overall LBE participation goal as its general contractors continue to execute subcontracts to advance the commitments in their respective contracts. Port's contracting staff have found that LBE participation in vertical contracting often starts on the lower end (as initial contracting is for capital-intensive pile driving and foundational work) and ends with higher participation. Table 1 below provides specific dollar values.

Mission Rock Partners continue to work proactively and collaboratively with Port Staff, the San Francisco Contract Monitoring Division, general contractors, RDJ Enterprises, Monica Wilson Consulting to implement strategies that help identify and increase participation of small local businesses each quarter. During 1Q21, four additional local business enterprises received their first formal contract with Mission Rock: BEI Steel (Steel Stairs and Rails), Harris Hoisting (Hoist Operations), KCA (Surveying), YADEJS, Inc. (Cleaning). To date, Mission Rock Partners has partnered with 91 LBEs of which 60% are minority and/or women-owned businesses.

Table 1. Summary of LBE Contracting through March 31, 2021 [1]

PROJECT \$	<u>Thru 4Q20 \$</u>	<u>1Q21 \$</u>	<u>Project to Date</u>
Horizontal	\$ 83,401,752	\$ 4,500,040	\$ 87,901,792
Vertical	\$ 145,099,266	\$ 256,733,708	\$ 401,832,974
	<u>\$ 228,501,017</u>	<u>\$ 261,233,748</u>	<u>\$ 489,734,765</u>

LBE \$	<u>Thru 4Q20 \$</u>	<u>1Q21 \$</u>	<u>Project to Date</u>
Horizontal LBE	\$ 14,408,781	\$ 2,109,282	\$ 16,518,063
Vertical LBE	\$ 10,463,397	\$ 4,380,554	\$ 14,843,951
	<u>\$ 24,872,178</u>	<u>\$ 6,489,836</u>	<u>\$ 31,362,014</u>

LBE %	<u>Thru 4Q20 %</u>	<u>1Q21 %</u>	<u>Project to Date</u>
Horizontal	17.28%	46.87%	18.79%
Vertical	7.21%	1.71%	3.69%
	<u>10.88%</u>	<u>2.48%</u>	<u>6.40%</u>

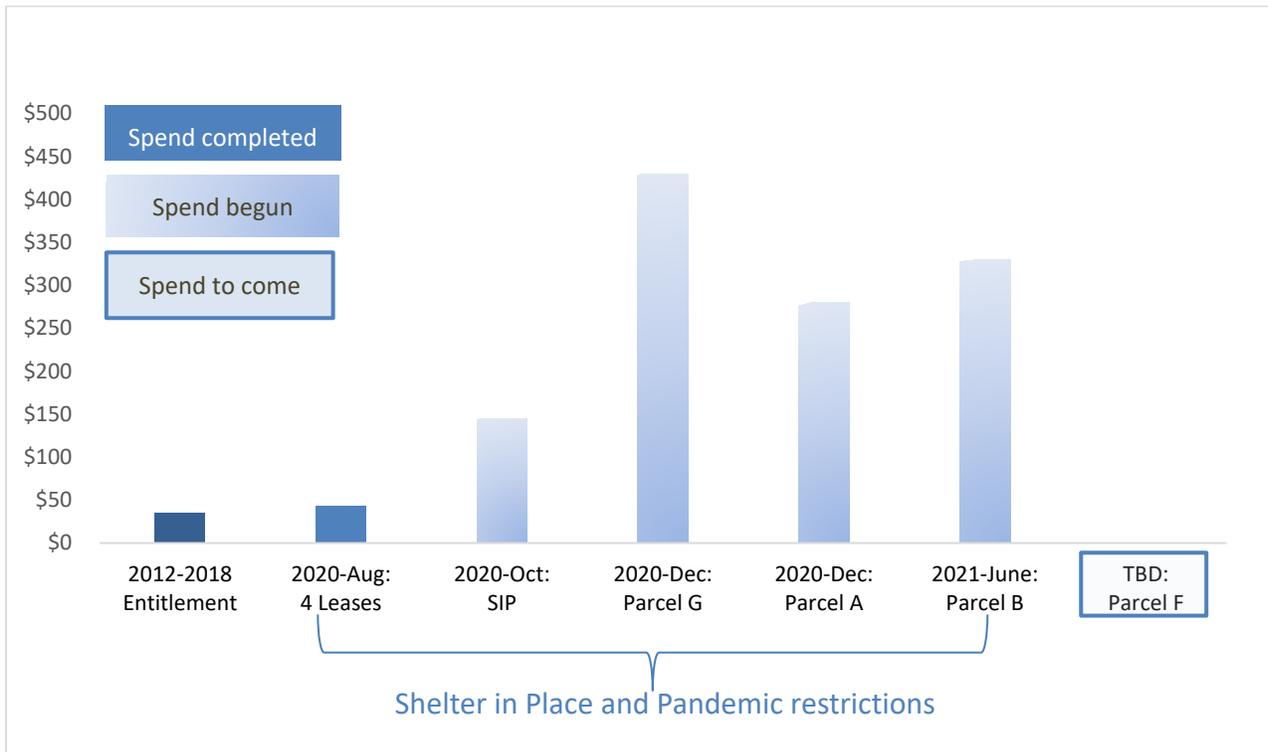
[1] Note that the dollars reported above are dollars under contract as of March 31, 2021. The Developer has also voluntarily reported to the Port that its contracts with the general contractors (GCs) at Mission Rock include contractual commitments that the GCs subcontract specific amounts of their work to LBEs. The Developer reports that an additional \$4.84M (resulting in a total of 24.3%) in horizontal contractual commitments and \$57.8M (resulting in a total of 18.1%) in vertical contractual commitments for LBEs are in place, through the end of Phase 1. These numbers will increase as the fourth building in Phase 1, Building F, gets under construction.

Partnership's Phase 1 Progress

Port staff are gratified to report that this public-private partnership has advanced without any major slowdown due to the pandemic. **Figure 1** below illustrates expenditures (completed, begun, or to come) and the month that the expenditure began. During the heart of the shelter in place, the Developer has commenced construction on over \$1 billion in horizontal and vertical projects, a strong showing of commitment to the success of Mission Rock during what continues to be an unsteady real estate market.

The vast majority of this spend is related to the vertical projects and this progress has allowed the Port to increase the 2021 bond amounts:

Figure 1. Investment in Project: Spend Start Dates (millions)



II. Phase 1 Budget Challenges

Phase 1 Cost Increases

The approved 2019 Phase 1 Budget included an overview of the expected cost and payment sources for the phase improvements in sufficient detail for the Port to determine consistency with the approved transaction documents. In Spring 2021, in accordance with requirements in the DDA, the Developer notified the Port of Phase 1 cost increases attributable to:

- higher than expected costs to approve the use of LCC in the project’s streets, and associated LCC warranty and monitoring costs
- an enhanced design of China Basin Park to include physical access to the shoreline and water
- rising construction material and labor costs
- continued design modifications at the request of city agencies
- unforeseen subsurface conditions and associated required design modifications
- unanticipated electrical utility modifications

- increased City agency review costs due to additional staff review of unique project conditions]
- Impact of Covid-19

Note that the Port Commission approved the Phase 1 budget nearly 2 years ago. As shown below, costs for Phase 1, including the more fully designed portions of China Basin Park that were in preliminary conceptual design form at the time of the Phase 1 budget approval, have increased \$57 million to a total of \$202 million.

Analysis of Phase 1 Cost Increases

Port staff and the Port’s consultants have conducted due diligence related to the revised Phase 1 costs and have concluded that the costs meet the DDA requirement for “reasonable projections”. Specifically, the Port retained Hollins Consulting to meet with the Developer and conduct a line-by-line analysis of the Developer’s revised Phase 1 horizontal hard costs. While the Port’s consultant raised questions on some line items, the review concluded the Developer’s estimate of horizontal development hard costs to be commercially reasonable and consistent with project requirements.

Description of Phase 1 Contingency

The Project’s phase 1 contingency has been resized to account for approximately 10% of all remaining costs to complete the Phase 1 scope of work. Below is a summary of each of the contingency amounts contained within the proposed Phase 1 budget:

- a) \$3,035,988 of contingency within the China Basin Park total of \$33,395,979
- b) \$4,214,106 of contingency within the Owner Costs total of \$5,292,826. This is intended to serve as a hard cost contingency on the remaining scope of work.
- c) \$1,984,086 of contingency of soft cost contingency.

The sum of items (a), (b) and (c) is \$9,234,190 in contingency within the proposed budget which is available for use. This amount is a contingency and will only be spent to the extent that the dollars are required to complete the improvements. All uses of contingency will be in accordance with the controls outlined in the DDA.

III. Phase 1 Budget: Proposed Solutions

Port staff and the Developer have worked together to analyze potential cost reductions and options for delivering Phase 1 and the remainder of the Mission Rock phases, with costs and revenues aligned such that both the Developer and the Port achieve their respective financial goals. Below is a summary of these efforts:

Reduce scope of improvements

- Reduced the interim improvements at Channel Street and south of Parcel F
 - Savings of approximately \$300-\$600k

Pursue lower-cost design alternatives

- Requested and got a State approved variance to allow LPW line to route below an existing NPW line rather than full reroute
 - Savings of approximately \$100k
- Developed a less expensive pavement design for the Toni Stone Crossing transition to Terry A. Francois Blvd.
 - \$75k was saved through utilizing an all-asphalt pavement section, in lieu of a standard DPW full PCC + AB section for the phase 1 temporary transition from Toni Stone to Terry A. Francois Blvd. Some savings in Phase 1, and some savings in future phase with less demo to remove and rebuild permanent grade transition.
- Bldg. B Sanitary Sewer system discharge to existing City sewer in 3rd street was originally planned to be gravity but was in conflict with PG&E existing high voltage electrical duct bank. Rather than incur a large rerouting cost, the project design team worked with SFPUC to generate a workable sewer force-main option and Mission Rock Utilities – the private district utility for Mission Rock – accepted ownership of improvements to make the lower-cost option acceptable to PUC and Port.
 - Overall cost savings was minimal, but rather than cause significant schedule delays, developer took on an extensive (~4 months) design iteration process with SFPUC and DPW to make the force main sewer option work, rather than moving forward with the ~\$500k reroute cost of the existing PG&E duct bank to allow for conventional gravity sewer. The Developer also took on future O&M responsibilities by deviating from SFPUC standard to save the project near term construction costs.
- Convert some paver/site concrete to landscaping
 - Approximate savings of \$30k
- Reduce structural soil extents while maintaining healthy growing conditions for trees –
 - \$100-200k
- Change streetscape finishes from unit pavers to decorative concrete
 - Savings of \$2.0M for converting pavers to cast in place concrete
 - Savings of \$1.0M for converting lifted grove wood decking to cast in place concrete
- Eliminate stone columns and use permeable LCC at China Basin Park to reduce ground improvement cost
 - Savings of \$2-3M for stone columns

- Savings of \$1-2 M for permeable LCC and related savings in earthwork excavation/disposal

Strategically procure materials/scopes of work

- Combine certain SIP & CBP scope packages to capture economy-of-scale savings
 - Included above but an estimated 5% of overall savings
- Utilizing CM/GC process managed by Webcor, reach an extensive bidder network and leverage relationships to secure competitive subcontractor pricing.
 - Estimate of 1% of procurement which is roughly \$600k

Efficiently manage site resources

- Working with City & Port to re-use asphalt grindings from existing parking lot demo as road base
 - Could generate an estimated \$200-300k but this has not yet been approved
- Developed onsite water treatment plant to treat ground water and use for onsite dust control rather than discharge to City sewer
 - Cost savings of approximately \$200k

Notably, presentations during project approvals and the project DDA contemplated Phase 1 costs potentially exceeding Phase 1 sources of funds. This is because Phase 1 is burdened with much more than its share of horizontal costs. Phase 1 includes 4 of the 12 vertical parcels, but nearly 40% of project's horizontal improvement areas, including the project's signature waterfront park. Phase 1 revenues also must support sitewide entitlement costs, a sitewide infrastructure basis of design, project-wide Tentative Map, approval of lightweight cellular concrete and significant precedential documentation. Below are the tools staff propose for re-aligning costs and funding sources.

Sequencing In-Water Park Work with Phase 2 Budget Sources

Port staff and the Developer propose sequencing the construction of China Basin Park into "inland" and "in-water" portions (as shown in **Figure 2**). Developing China Basin Park in this sequence means that costs are spent over time, allowing more revenue streams to come online to support expenditures.

Under this sequencing plan, the inland portion of the park would be delivered in mid-2023 along with the occupancy of Parcels A and G. Sequencing the construction in this manner is expected to move \$23 million in expenditures from the revised Phase 1 budget to the next phase budget.

Construction of the in-water portion of the park would commence once: (a) the Developer has obtained required regulatory permits from the Army Corp of Engineers, BCDC, and RWQCB, and (b) the Port Commission has approved the Phase 2 Budget. The Project schedule anticipates that the Developer will achieve all of these milestones by the end of

2022 and will be prepared to commence and complete the in-water construction during that year's in-water work window.

Port staff and Developer reviewed this sequencing concept with the Port's Southern Advisory Committee at its June 23, 2021 meeting. The committee understood that the sequencing would allow delivery of the entirety of China Basin Park, as required permits and revenue streams from Phase 2 are brought forward. Port staff explained that the current project schedule indicates this construction will proceed relatively seamlessly, from the green area (shown in **Figure 2** below) and then moving to the waterside of China Basin Park. Staff cautioned though, that permitting requirements and the timing of funding from Phase 2 may mean a delay wherein the green portions of the Park are delivered and open while the team works to achieve permits and secures Phase 2 revenue and then mobilizes on the waterside, while the green portions of the Park remain open.

Construction of the shoreline portion of the park will occur outboard of the Bay Trail. The Inland portion of the park to be completed in Phase 1, including the Bay Trail, will remain accessible to the public during construction of the shoreline portion. The Developer will work to keep the entirety of the inland portion of the Park accessible during shoreline construction. However, there may be construction circumstances that require partial, temporary closures of portions of the Park. The team will work to limit these instances. An attractive barrier will separate park users from the construction site to maintain safety. Views of the Bay will be maintained from elevated portions of the site.

Figure 2. Sequencing of Improvements

Current Phase

- Streets, Infrastructure (Red)
- Inland CBP (Green)
- Public Restrooms
- Buildings

Sequenced Phase

- CBP Shoreline (Orange)
- F&B Pavilion (Purple)

Future Phase (Grey)

- Buildings
- Pier 48
- Mission Rock Square
- Knuckle Wharf Improvements



Apply Reduced Return for First \$10 Million of Phase 1 Cost Overages

The Financing Plan provides that if the parties are unable to identify measures to eliminate the Phase 1 costs that exceed the originally approved phase budget (including contingency), or unable to agree on measures that could be taken, the Port in its sole discretion may require the first \$10 million in Phase 1 cost overruns will be subject to a significantly lower return for the Developer (equal to LIBOR plus 400 basis points, which would equal 4.10% as of June 30) as compared to the approved 18% return. The first \$10 million in Phase 1 cost overruns will be subject to such lower rate of return.

Charges for Phase 2 Delay

The above tools help to mitigate Port revenue losses due to the Phase 1 cost increase challenges. It is important to note though that the financial success of the project, for both the Developer and the Port, hinges on the development of Phases 2-4. Because Phase 1 supports a significant portion of sitewide costs, subsequent phases have more opportunities for revenue sharing than Phase 1.

Accordingly, Port staff and Developer propose that the Developer will submit a complete Phase 2 Phase Submittal and Phase Budget by December 31, 2022 or Developer will be subject to an unreimbursable charge of \$25,000 per quarter during a first year of delay, rising to \$30,000 per quarter, and \$40,000 per quarter if the delay continues for 2 and 3 years, respectively.

At the Informational Presentation of this item at the July 13, 2021 Port Commission meeting, the Port Commission directed staff to conduct additional due diligence with the Developer to determine the feasibility of advancing this submittal deadline to a date earlier than December 31, 2022.

The current outside date for the Phase 2 submittal is the earlier of 5 years after the completion of all vertical development in Phase 1, or 10 years from the effective date of the transaction documents (earlier date anticipated to be August 2028). The December 31, 2022, target date for the Phase 2 submittal is more than 5 years in advance of the current Outside Date as defined in the DDA.

Port Staff and Developer remain focused on progress towards key Phase 1 milestones for the remainder of 2021, including the following:

- Series 2021B Bond Issuance and Disbursement (target Q4 2021)
- Parcel F Predevelopment Efforts (target construction Q4 2021 / Q1 2022)
- China Basin Park Predevelopment Efforts (target construction Q4 2021 / Q1 2022)

Port staff and Developer believe that taking into account the required focus to maintain progress on Phase 1, December 2022 is the earliest reasonable date for a Phase 2 Submittal. The Phase 2 Submittal will require the engagement of the Phase 2 horizontal design team, development of a Phase 2 Basis of Design (potential LCC use acknowledgements from the City), contractor engagement and preliminary pricing, LIHTC analysis to support the housing plan requirements of the submittal, Garage Report preparation and submittal (required for a Garage Phase) and subsequent coordination

with the Director of City Planning and Director of MTA. In addition, the Developer anticipates potentially commencing the preconstruction activities for the Phase 2 Vertical Parcels including architect selection, concept design progress and general contractor preliminary engagement to support pricing estimates prior to the Phase 2 submittal, to better define the Phase 2 building program.

The Port Staff and Developer team estimate the following durations for key components of the Phase 2 Submittal.

Phase 2 Submittal Preparation - Illustrative Timeframes	
Engage Phase 2 Horizontal Design Team	1-2 months
Develop Phase 2 Infrastructure BOD (price design)	2-4 months
<i>Mission Rock Square Concept Design (for pricing)</i>	3-5 months
<i>City Acknowledgment of LCC for Phase 2</i>	TBD
Garage Report preparation	4-6 months
Garage Report Submittal (coordination with Planning and Transportation director)	TBD

Based on this significant workload and a strong desire to maintain focus on delivering Phase 1, Port staff and Developer believe December 2022 is the earliest reasonable date for a Phase 2 Submittal.

Other Solutions Considered But Not Proposed For Approval at this Time

Port staff and Developer considered other potential solutions that were ultimately not recommended for the reasons below.

1. **Port Capital.** Under the terms of the DDA, both the Developer and the Port may invest at-risk capital to fund project costs. While the Port may elect to make this investment, the Developer must fund horizontal costs with Developer equity if public financing or land proceeds are not available. Port staff considered using Port Capital to fund a portion of the Phase 1 cost increase which would provide the Port a 10% return on funds. However, the Port’s significantly constrained resources due to the Covid-19 economic downturn led staff to reject this possibility at this time.
2. **No Phase 1 Budget Increase.** Port staff and Developer considered no increase to the Phase 1 Budget. In this case, the Developer would invest up to the \$145M budget which would not deliver any portion of China Basin Park, until Phase 2 budget approval. Given the Port’s and Developer’s steadfast commitment to delivery of China Basin Park in Phase 1 of the project, the project team rejected this alternative as too far out of line with the Project’s commitments to China Basin Park delivered in Phase 1.
3. **Future Phases Shoreline Tax.** Port staff also considered committing future-phase Shoreline Taxes to the in-water portions of China Basin Park in Phase 1. As future phase costs and revenues are defined, this funding tool may be analyzed, in concert with changes to other revenue streams, to secure Mission Rock’s public parks and infrastructure. However, without more certainty on Phase 2 costs and

revenues, Port staff rejected devoting any other revenue streams to Phase 1, in advance of a Phase 2 approval.

Phase 1 Budget: Financial Analysis

With the application of the solutions proposed above, the Phase 1 Budget is proposed as follows:

September 2019 Approved Budget:	\$145.0 million
Proposed Increased Phase 1 Budget:	\$207.2 million
Move In-Water Work and Food & Bev Pavilion to Phase 2	(less) <u>(\$23.0 million)</u>
Proposed Phase 1 Budget for Approval:	\$184.1 million

Table 2. Phase 1 2019 Budget and Proposed Budget

Cost Item	2019 Port Approved Budget	Proposed Budget	Proposed Change
<u>Hard Costs</u>			
Hard Costs	52,659,913	69,385,516	16,725,603
Inland CBP	27,397,300	33,395,979	5,998,679
Owner Costs	9,688,437	5,292,826	(4,395,611)
Total Hard Costs*	89,745,650	108,074,321	18,328,671
<u>Soft Costs</u>			
General**	\$38,583,205	\$53,476,902	14,893,697
Developer Items	\$13,461,848	\$18,907,674	5,445,826
Open Space	\$1,652,500	\$1,652,500	-
Soft Cost Contingency	\$1,984,086	\$1,984,086	-
Total Soft Costs	\$55,681,639	\$76,021,162	20,339,523
Totals	145,427,289	184,095,483	38,668,194

*Includes \$4.59 m in hard cost contingencies. Adding this to the \$1.98 m in soft cost contingency sums to \$6.57 m or 3.6% of the total \$184.1 m proposed budget.

**Includes about \$4m in additional legal, accounting, and tax consultant costs; \$3.5m in architectural and engineering design costs associated with multiple submittals & reviews for City's infrastructure agencies; and \$2m additional costs in fees, permits, and bond surety costs.

In the table below, the impact of the proposed budget increase is shown on projected Port revenue from the whole project.² To isolate variables and scenarios, the table shows several results which build, on to the next, as described below. Note that model result #3 *Shoreline Tax* is a scenario that is subject to future negotiation and would require Port

² It is worth noting that these projections include several assumptions about future market conditions which will be reflected in future parcels' Fair Market Values, construction costs, financing, and timing of actions by the Developer, the Port, and the City. As such, actual results will vary and Port staff will continue to update the Port Commission on progress.

Commission approval. Port staff are not seeking consideration of dedicating more Shoreline Tax to the project at this time because both parties require more information – to be developed as part of Phase 2 – to inform any decision regarding those taxes.

- **2019 Model.** Reports projected results at the time of the Phase 1 budget approval in September 2019.
- **2021, #1 Time Updates.** Reports revenues based upon model updates over last two years since 2019, including actual timing of expenditures and revenues over that time period and updated market assumptions and phase costs for Phases 2-4.
- **2021, #2a Cost Increase.** Builds upon #1 model by including Phase 1 costs increasing to \$184 million and the full park Shoreline and other park enhancements in Phase 2.
- **2021, #2b Cost Increase.** Builds upon #1 model by including Phase 1 costs increasing to \$184 million, but excludes Shoreline and other park enhancements from project.
- **2021, #3 Shoreline Tax to Project.** Builds upon #2 model by dedicating more Shoreline Taxes to the project.
- **2021, #4 Market Upside.** Builds upon #2 model with a market upside by increasing commercial rents by 3%, and the resulting impact to implied parcel values.

As shown, the Port’s NPV revenue decreased between 2019 and 2021, largely due to bond revenues coming in later than planned 2019 and land values coming in lower in future phases due to increased vertical construction costs and lower rental rates (as have been reset by the pandemic). The Phase 1 cost increase significantly reduces Port revenues. These revenues can be brought back up though, should the Port choose to invest more Shoreline Taxes into the project (subject to future approvals) or should the market improve.

Table 3. Summary of Potential Port Revenue Results

REVENUE ITEM	2019 MODEL	2021 MODELING SCENARIOS (MILLIONS)				
		#1. Time Updates	#2a. +Cost Increase w/full park	#2b. Cost Increase w/less park	#3. +Shoreline Tax to Project	#4 2+Market Upside
		2019 Model + 2021 Timing + Market + other updates	Model #1 + \$184M Phase 1 Budget + \$23M for Phase 2 park enhancements	Model #1 + \$184M Phase 1 Budget, <u>exclude</u> \$23M park enhancements	Model #2 + Shoreline Tax to Phase 2	Model #2 + Market Upside
TOTAL PORT REVENUE (NOMINAL)	\$1,768	\$1,939	\$685	\$1,939	\$1,929	\$1,936

REVENUE ITEM	2019 MODEL	2021 MODELING SCENARIOS (MILLIONS)				
		TOTAL PORT REVENUE (NPV W/ 6% DISCOUNT)	\$190	\$179	\$67	\$181

With the Phase 1 budget increase, the Developer's projected returns for Phase 1 drop from 18% to 17.8%. In addition and as noted above, the Developer has put a tremendous amount of capital at risk during unprecedented and unsteady market conditions. The Developer closed on all 4 Phase 1 Parcel Leases, at values determined pre-pandemic. The Developer has commenced construction on three of the four parcels, within a year of signing the VDDA (which is over two years in advance of the VDDA required timing), allowing the Port to leverage the value created on the site for increased bond issuances at a period of time with favorable interest rates. In addition, the Developer has proceeded with a district-scale thermal energy plant and blackwater treatment plant, but has financed these improvements separately, allowing the improvements to be delivered in Phase 1, but without receiving the 18% Developer return on these improvements.

IV. Recommendation

Staff recommend approval of the revised phase 1 budget and the sequencing of improvements at China Basin Park.

Prepared by: Phil Williamson
Senior Project Manager

For: Rebecca Benassini, Deputy Director of
Real Estate and Development

EXHIBITS

1. DDA Excerpts including Phase Budget Approval Criteria and notes related to those criteria

**PORT COMMISSION
CITY AND COUNTY OF SAN FRANCISCO**

RESOLUTION NO. 21-33

- WHEREAS, In January 2018, by Resolution No. 18-03, the Port Commission approved the terms of a Disposition and Development Agreement (“DDA”) between the Port and the Seawall Lot 337 Associates, LLC, a Delaware limited liability company (“Developer”) , and related transaction documents that are incorporated into the DDA, including but not limited to, a Financing Plan, for the development of approximately 28-acres located along the Port’s Central Waterfront and commonly referred to as “Mission Rock” (the “Project”), comprised of (1) Seawall Lot 337, bounded by Third Street on the west, Mission Rock Street on the south, Pier 48 to the east, and China Basin Park on the north; (2) Pier 48; (3) China Basin Park; (4) the marginal wharf between Pier 48 and Pier 50; and (5) Parcel P20 (collectively, the “Site”); and
- WHEREAS, Developer is a limited liability company, which is wholly owned by TSCE 2007 Mission Rock, L.L.C. and Giants Development Services, LLC, the former is an affiliate of Tishman Speyer Properties, L.P., and the latter is an affiliate of San Francisco Baseball Associates, LLC, the Major League Baseball franchise holder of the San Francisco Giants; and
- WHEREAS, In February 2018, the Board of Supervisors approved the DDA by Resolution No. 42-18, and approved the Development Agreement for the Project by Resolution No. 33-18; and
- WHEREAS, On April 4, 2019, Developer submitted to the Port its “Phase Submittal” for “Phase 1” of the Project and in September 2019, by Resolution No. 19-39, the Port Commission approved the Phase 1 Budget of \$145 Million; and
- WHEREAS, In April 2021, pursuant to the requirements in the DDA, Developer notified Port of Phase 1 budget increases of \$38 Million (not including the “in-water” work being delayed to a later phase); and
- WHEREAS, Port staff and its consultant have reviewed the Developer’s Phase 1 Budget increase and determined that it meets the requirements for Port Commission approval under DDA Section 3.5(e), as further described in the memorandum accompanying this resolution, in that it: (1) is consistent with funding goals, the project requirements and satisfies the project’s budget guidelines; (2) is based on reasonable projections; (3) provides for sources sufficient to fund Phase 1; (4) would not adversely affect project payment sources available to satisfy the project payment obligation for any later phases and the Project as a whole; (5) would not impair the Port’s fiduciary obligations under applicable Port laws; and

- WHEREAS, Developer proposes to bifurcate the delivery of China Basin Park into an inland portion to be completed as part of Phase 1 and an in-water portion to be completed as part of Phase 2 and
- WHEREAS, Acknowledging the importance of future project phases to the Project's overall success, Developer and Port propose that Developer will submit a complete Phase 2 Submittal by December 31, 2022 or be subject to unreimbursable charges of \$25,000 per quarter during the first year of delay, rising to \$30,000 per quarter, and \$40,000 per quarter if the delay continues for 2 and 3 years, respectively; and
- WHEREAS, The Financing Plan provides that if the Parties are unable to identify measures to eliminate the Phase 1 costs that exceed the originally approved phase budget (including contingency), or to agree on measures that could be taken, the Port in its sole discretion may require the first \$10 million of the Phase 1 cost overruns will be subject to a lower return for the Developer as compared to the approved 18% return; and
- WHEREAS, The actions contemplated in this resolution are within the scope of the project for which the Port Commission (Resolution No. 18-06) and the Board of Supervisors (Resolution No. 33-18) adopted on January 30, 2018 and March 6, 2018, respectively, affirmed the Planning Commission's certification of the Final Environmental Impact Report for the Seawall Lot 337 and Pier 48 Mixed-Use Project (Planning Commission Motion No. 20018) (FEIR) and made findings in accordance with the California Environmental Quality Act (California Public Resources Code section 21000 et. seq.) and Administrative Code Chapter 31, which resolutions are incorporated herein by reference; and
- WHEREAS, On August 2, 2021, the Planning Department determined that the Phase 1 budget increase and delay of in-water work at China Basin Park do not require further environmental review; now, therefore be it
- RESOLVED, That the Port Commission approves the \$38 Million Phase 1 budget increase and finds in accordance with DDA Section 3.5(e) that it: (1) is consistent with the funding goals and project requirements and satisfies the budget guidelines; (2) is based on reasonable projections; (3) provides for sources sufficient to fund the Phase; (4) would not adversely affect project payment sources available to satisfy the project payment obligation for any later phases; (5) would not impair the Port's fiduciary obligations under applicable Port laws; and be it further
- RESOLVED, That the Port Commission approves the delay of in-water work at China Basin Park as described in the staff report attached to this Resolution; and be it further

- RESOLVED, That the Developer will submit a complete Phase 2 Submittal by December 31, 2022, or be subject to unreimbursable charges of \$25,000 per quarter during the first year of delay, rising to \$30,000 per quarter, and \$40,000 per quarter if the delay continues for 2 and 3 years, respectively; and be it further
- RESOLVED, That Developer will earn a lower return on the first \$10 million in Phase 1 cost overruns as compared to the approved 18% return in accordance with the Financing Plan; and be it further
- RESOLVED, This Commission finds that (1) because the Phase 1 budget increase and delay of in-water work at China Basin Park do not cause new significant impacts not identified in the FEIR, no new mitigation measures are necessary to reduce significant impacts; (2) no new information has become available and no changes in circumstances have occurred showing the Project would cause new significant environmental impacts or increase the severity of previously identified significant impacts; and (3) as a result, no additional environmental review is required beyond the environmental review previously conducted.

I hereby certify that the foregoing resolution was adopted by the San Francisco Port Commission at its meeting of August 10, 2021.

Secretary

Exhibit 1 – DDA Excerpts and Port Staff Analysis

The DDA sets forth the Port Commission’s criteria in reviewing the revised phase Budget as follows:

“Criteria for Approval. *The Port Commission will approve the Phase Budget or modification if it reasonably finds that the Phase Budget or modification:*

- (1)** *is consistent with the Funding Goals and Project Requirements and satisfies the Budget Guidelines;*
- (2)** *is based on reasonable projections;*
- (3)** *provides for sources sufficient to fund the Phase and any carryover from Prior Phases;*
- (4)** *would not adversely affect Project Payment Sources available to satisfy the Project Payment Obligation for any Later Phases and the Project as a whole; and*
- (5)** *would not impair the Port’s fiduciary obligations under Applicable Port Laws.*

Port staff, along with the team members mentioned elsewhere in this memorandum, have reviewed the revised Phase 1 budget submission and found the submission complies with the conditions prescribed by the DDA.

These criteria are addressed in order below:

- (i) Staff and the Port’s third-party consultant team have reviewed the revised Phase 1 budget and found it to be in compliance with the funding goals, requirements and budget guidelines as described by the DDA.
- (ii) Staff, the Port’s third-party economic consultant, and the Port’s cost estimate reviewing consultant have reviewed the revised Phase 1 budget project cost and return projections and have found them to be reasonable
- (iii) Staff and the Port’s third-party economic consultants have concluded that the revised Phase 1 budget provides for sources sufficient to fund the Phase. However, the viability of subsequent phases is subject to interest rate risk, market and development risk, and continued construction cost escalation. The revised Phase 1 budget shows significant cost escalation as compared to the approved Phase 1 budget. If cost escalation continues or if the cost of public debt goes up, it may require the use of project sources to balance costs in subsequent phases. This would adversely affect payment sources in those phases and the Port’s financial position. Those future phases though, are subject to Port Commission approval.
- (iv) Staff and the Port’s third-party economic consultant have determined that the proposed revised Phase 1 budget would not adversely affect Project Payment Sources available to satisfy the Project Payment Obligation for any

Later Phases and the Project as a whole based on the Developer's underwriting, subject to the caveats described in criteria (iii) above.

- (v) The proposed revised Phase 1 budget would not impair the Port's fiduciary obligations under Applicable Port Laws. No City General Funds or Port Harbor Funds are pledged or made liable under this Phase 1 Budget. If Project sources are insufficient to cover costs the remainder will carryover into the next phase submittal.

The DDA also sets forth the Port Commission's criteria in reviewing proposed changes to an approved phase work scope as follows:

Changes to the Phase 1 Scope (Shoreline Improvements to be captured in Phase 2 Scope / Budget) (DDA Section 3.7)

Note: The Shoreline Improvements were not included in the Phase 1 Port Commission Approval, but have been subsequently reviewed.

(a) Changed Conditions. The Parties agree that many factors, including general economic conditions, local housing, office, and retail markets, capital markets, general market acceptability, and local tax burdens will affect the rate at which various residential and commercial uses within the Project can be developed and absorbed.

(b) Developer Request. Developer may request changes to a Phase Approval or changes to the Phasing Plan and related changes to any applicable Outside Dates. Except when Subsection 2.5(a) (Garage Phasing) applies, the Port will grant or withhold its approval based on whether, in its reasonable judgment, the modified Phase Approval or Phasing Plan would be consistent with the Phasing Goals.

The sequencing of China Basin Park construction, wherein the inland portion of the park is constructed and opened initially, while the project team assembles in-water construction permits, prepares construction for the annual in-water work window, and assembles Phase 2 funding for the Shoreline portion of the park, meets the Phasing Goals. This sequencing allows the entire inland portion of the Park, including the important Bay Trail, to open along with the rest of Phase 1 infrastructure. The Shoreline portion of the Park will follow either immediately (as the project schedule shows today) or when permits and Phase 2 funding allow. All the while, the vast majority of the Park will be open to the public in Phase 1, consistent with Project commitments and good practices of construction sequencing.

Other Phase Cost Controls

The DDA provides specific cost control steps the Developer and Port must follow, including:

- Developer and Port agree on list of general contractors who may participate in the General Contractor (GC) selection process.

- Developer may use a guaranteed maximum price contract for each phase; Developer has used this contracting type for Phase 1.
- GC must competitively bid subcontracts, but may seek approval of sole source subcontracting if costs are commercially reasonable or subcontractor is only such service or materials provider in the Bay Area.
- Developer must notify Port of any change orders above \$250,000.