

MEMORANDUM

December 7, 2018

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

FROM: Elaine Forbes
Executive Director

SUBJECT: Request approval of amendments to the following three agreements with San Francisco Bay Railroad, Inc. ("SFBR") relating to rail operations to extend the term of each agreement until December 31, 2033 (with one five (5) year mutual option) and to make other changes: (1) a first amendment to Amended and Restated Lease No. L-14397 ("Lease") of the Intermodal Container Transfer Facility located at 100 Cargo Way to adjust rent including Port's participation in a sale; (2) an amended and restated equipment Lease No. 14502 of two locomotives including the Port's new grant-funded locomotive for monthly lease payments; and (3) an amendment and restatement of Rail Agreement No. 14503 to require SFBR to perform a baseline repair project at its cost (Resolution No. 18-65)

DIRECTOR'S RECOMMENDATION: Approve Attached Resolution

Executive Summary

Port staff requests approval of the following three agreements relating to rail operations with the current rail operator SFBR to include the following key terms as further described in this Memorandum:

(1) an amendment to the Lease of the Intermodal Container Transfer Facility (ICTF) to extend the term; establish a process for rent adjustments; establish a tiered structure for wharfage; and increase Port's sale participation from ten percent (10%) to fifteen percent (15%);

(2) an equipment lease No. L-16372 to lease two Port-owned locomotives, including the Port's new grant-funded low-emission locomotive; to increase the monthly lease payment; and to require decommissioning of Locomotive No. 25; and

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(3) an amendment to Rail Agreement No. L-14503 to extend the term; to require SFBR to perform agreed-upon repairs at its sole cost and expense and to otherwise clarify SFBR's maintenance and repair obligations.

All three agreements will expire on December 31, 2033.

Background

The Port of San Francisco has regular rail traffic through its railyard situated on Cargo Way in the Southern Waterfront. For more than a decade the Port has contracted with San Francisco Bay Railroad (SFBR) to provide short line freight railroad services and rail terminal operations through ICTF Lease No. L-14397 and the related Rail Agreement No. 14503 and Locomotive Lease No. 14502. The Rail Agreement gives SFBR exclusive rights to use Port track, including Port tracks within and outside of the ICTF railyard. The Locomotive agreement leases SFBR two Port owned "ALCO" locomotives designated as "No. 23" and "No. 25". The ICTF railyard property is where SFBR conducts the majority of its operations including the loading and unloading of railcars. SFBR uses the additional Port track outside the facility for train movement and storage of railcars. The rail agreements were set to expire on December 31, 2018.

Currently, SFBR's primary business is transporting contaminated soils from various San Francisco construction projects to a landfill in Utah. SFBR has transported debris from various large San Francisco construction projects such as Doyle Drive, Transbay Transit Terminal, Salesforce Tower, UCSF and Kaiser Hospitals - Mission Bay, The Exchange at Mission Bay, 801 Brannan Street (formerly Concourse Exhibition Hall), the SFMTA Third Street Light Rail project, and most recently the Golden State Warriors Chase Arena. SFBR's rail operation removes approximately 10,000 truck trips annually from Bay Area freeways.

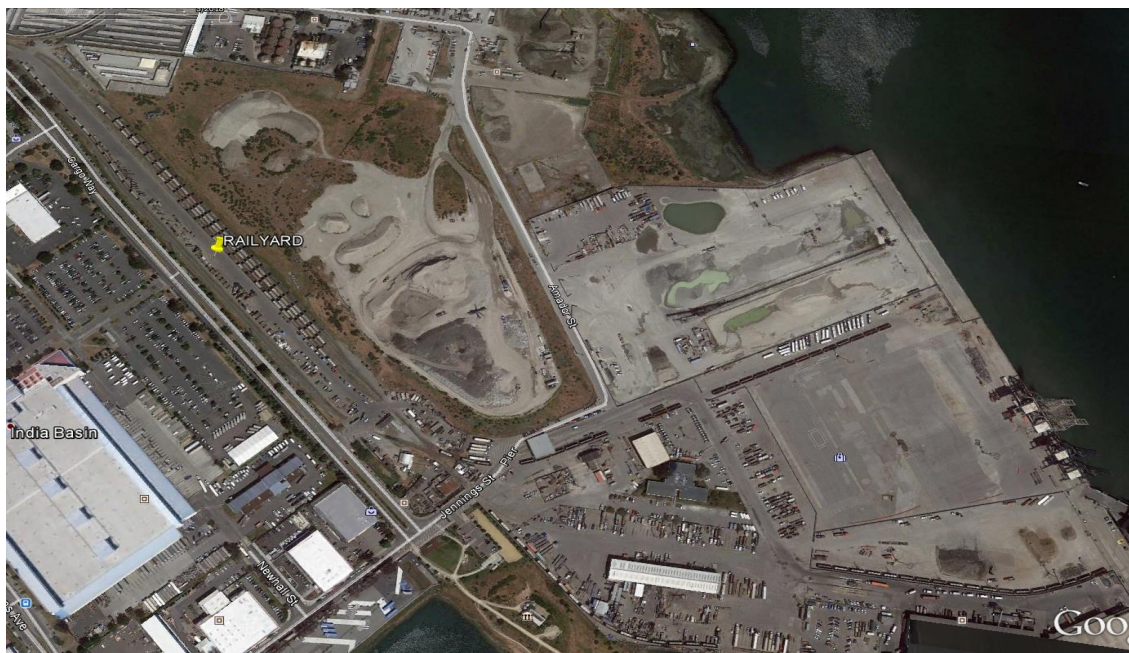
An active rail facility is a key component to the Port's maritime activity and potential future maritime cargo business lines. SFBR has performed rail service as needed for Port maritime tenants throughout its tenancy. The ICTF Lease includes a "Maritime Priority" provision that ensures current and future maritime cargo receives priority movement through the rail facility.

In early 2017, with steady volume growth over previous years and the upcoming Chase Arena project, SFBR approached the Port requesting an extension to its existing 2007 ICTF Lease and to partner with the Port in the construction of two additional rail tracks within the ICTF facility. SFBR had recently lost access to the tracks at Pier 80 due to the Pasha auto-terminal activation. With the projected high-volumes of the Chase Arena project, SFBR needed additional tracks to handle the increased volumes. The Port Commission approved a five-year extension on January 5, 2017 (Resolution 17-05) and the Port agreed to provide rent credits to SFBR for 50% of the \$1.2 million new track project for the mutual benefit of consolidating Port track within the ICTF railyard facility. SFBR successfully completed the project and all rent credits have been exhausted. Consolidating the tracks into the ICTF has increased efficiency and decreased the traffic impacts on the Southern Waterfront

community. The 2017 lease amendment and restatement also included the following terms: established a minimum annual guaranteed Wharfage payment (“MAG”) in an initial amount of Two Hundred Fifty Thousand Dollars (\$250,000); increased Wharfage rates under the Lease and the Rail Agreement from \$200 to \$250 per rail car and from \$40 to \$50 per bin/container payable to Port; increased all fees by 3% annually; slightly increased the acreage of the premises by about 24,000 square feet in order to accommodate the new track; and updated the lease form to be consistent with the current Port form lease and then-applicable City Requirements.

At the time of the ICTF Lease extension, both SFBR and the Port agreed to not extend the Rail Agreement or Locomotive Lease as they both had two more years of term and the Port was working towards a grant agreement which would bring a new “Tier-4” low-emission locomotive to the Port. When receiving approval for the 2017 ICTF lease amendment, staff informed the Port Commission that they would be returning before the end of 2018 to extend the Locomotive Lease and Rail Agreement so that all three agreements would be coterminous.

On February 14, 2017 through Resolution No. 17-08, the Port Commission authorized the Executive Director to seek Board of Supervisor’s approval to accept and expend grant funding from the Bay Area Air Quality Management District (BAAQMD) to purchase a “Tier-4” low emission locomotive. On July 11, 2017 through Resolution No. 278-17 the Board of Supervisors authorized the Port to accept and expend the grant funding and purchase the new locomotive. The new locomotive, “No. 30” is now ready for delivery.



SFBR has come to the Port requesting a 10-year extension of the ICTF Lease and a 15-year extension for both the Locomotive Lease and the Rail Agreement to make all three agreements coterminous expiring on December 31, 2033. The 15-year term

aligns with the BAAQMD grant requirement for the new locomotive to have a 15-year operating life.

Based in the Southern Waterfront within the Bayview-Hunters Point community, SFBR has strived to be a good steward of the neighborhood by maintaining a clean and environmentally-compliant operation, hiring its employees and subcontractors almost exclusively from the local community, and by seeking opportunities to improve the environment at the railyard and in the local neighborhood. SFBR is a tenant in good standing.

As described below, SFBR and the Port have negotiated a set of agreements that provides for a term extension which will allow SFBR to continue the ability to competitively market its services to major construction projects.

Business Terms

This section describes the material new business terms and material revisions to the existing agreements. The amendment to the Amended and Restated ICTF Lease will extend the lease term by ten years. The Lease will continue existing terms of a minimum annual guarantee (MAG) payment to the Port of \$257,500 and a railcar fee of \$257.50 per railcar. All fees are subject to an annual 3% increase.

New business terms to the ICTF Lease include: (i) a railcar fee increase of 20% for all railcars above 2,999 in any year; (ii) SFBR investment of an estimated of \$500,000 into rail infrastructure improvements bringing Port track to a baseline condition; (iii) an increase in Port's participation in sale proceeds from a sale of the lease from 10% to 15%; (iv) Port has the right to negotiate wharfage rates for any future rail loading/unloading services outside of the ICTF premises for potential Port maritime tenants or projects; and (v) Port has relinquished the unilateral right to terminate the lease in favor of another Port project given that the rail use is a trust consistent maritime use that the Port wishes to preserve.

The new Locomotive Lease will replace the existing Locomotive Lease. It will have a term of fifteen years. The Lease will include the addition of new Port owned low-emission Locomotive "No. 30". SFBR will pay the Port an increased lease payment of \$3,000 per month for the entirety of the term for locomotive No. 30 and will be responsible for the manufacturer recommended maintenance schedule and the grant requirements associated with operating the locomotive. SFBR will continue to lease locomotive No. 23 for \$1.00 annually. SFBR will be responsible for decommissioning of Locomotive No. 25 per the grant requirements up to a total cost of \$50,000.

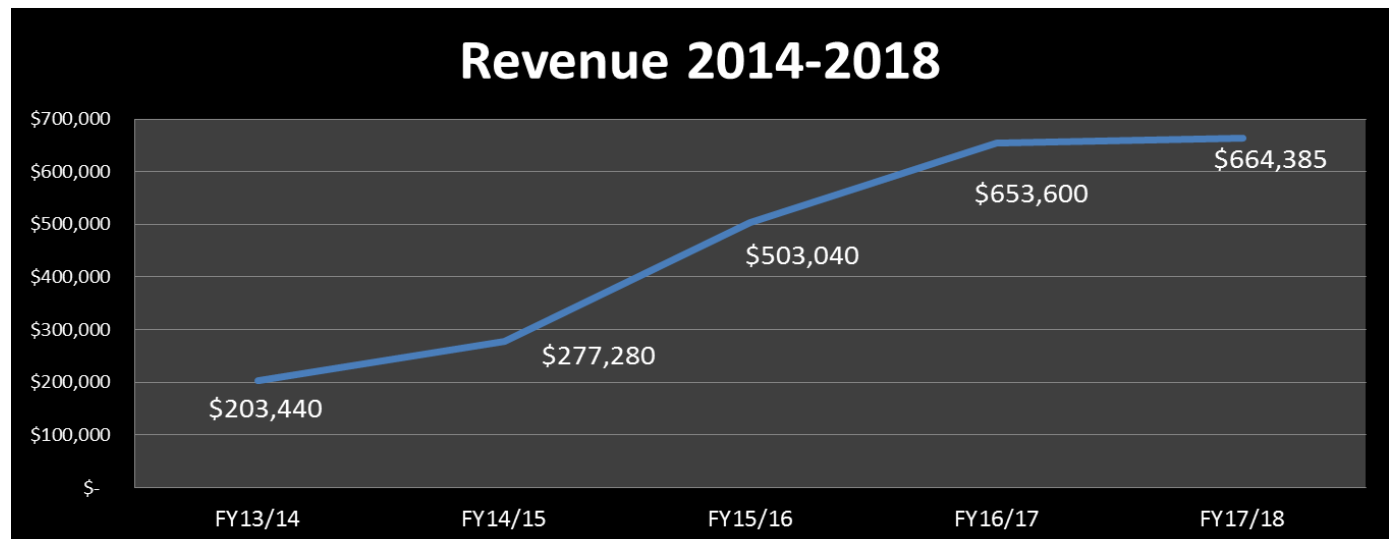
The amendment to the Rail Agreement will extend its term by fifteen years and require SFBR to perform track repairs and improvements on existing track by upgrading Port track to a baseline condition for an estimated cost of \$500,000 at its sole cost and expense. The Port and SFBR conducted independent surveys to identify and agree on needed areas of repair to bring the track to the baseline condition. These repairs will correct subsidence issues and upgrade high-traffic crossing areas of the track. The repairs will bring the track to a baseline standard to operate for the term of the

agreement. SFBR will be responsible for the inspection and repairs on all wear and tear of the Track throughout the term. As in the current agreement, Port reserves the right to alter Track provided that the alterations do not materially adversely affect the functional utilization of the Track for the permitted use. The amendment also continues SFBR’s eligibility for rent credits for major capital repairs or improvements with written approval from Port (after a \$20,000 per year “deductible” paid by SFBR). This could include replacing Track that Port wishes to take out of service with equivalent track. Any approved rent credits will be applied against (i) amounts in excess of 50% of the MAG. When considering whether to approve rent credits for major capital projects, Port has agreed to consider the following factors: safety concerns, Industry Standards, functionality of the Port Track, the rent credit amount sought, the cost of the proposed project and resulting benefits to Port, and the remaining lease term. Port has also agreed to a reasonableness standard for any single major capital project for which SFBR seeks rent credits of less than One Hundred Twenty-Five Thousand Dollars (\$125,000).

All three agreements will expire on December 31, 2033 and will include a mutual five year (5) extension option with the potential expiration date of December 31, 2038. The agreements are also being updated to be consistent with the Port’s current form agreements.

Projected Earnings

The chart below describes SFBR’s payments to the Port for the last five years. SFBR has had five consecutive years of strong revenue growth increasing from \$203,440 (FY2013-2014) to \$664,385 (FY 2017-2018). SFBR expects volumes to remain at the current level of approximately 2,500 railcars annually. The minimum annual guarantee of \$257,500 (increased annually by 3%) provides the Port security of guaranteed revenue if volumes experience a down period during the term.



Community Benefits

SFBR reports a wide range of community benefits as follows:

- SFBR employees 45 skilled and unskilled railroad, railyard and truck workers, paying a living wage to local employees.
- SFBR has partnered with the Bayview local truckers on an innovative short haul truck-to-rail system, which has sustained skilled work in the Southern Waterfront.
- SFBR have a good environmental regulatory record. According to SFBR, their rail operations saves approximately 1 million gallons of diesel fuel annually versus using long-haul trucking, moreover reducing the CO2 emissions by 22 million pounds annually, or 90% compared to long-haul trucking alternative. This in turn removes more than 10,000 one-way truck trips annually off Bay Area roads and bridges.
- SFBR operates the railyard with best practices ecologically with use of goats grazing instead of use of herbicides.
- SFBR will operate the Port's new grant funded low emission locomotive adding further environmental best practices to their operations.

Strategic Objective

This proposed Amended and Restated Lease is in line with the Port Strategic Plan as follows:

Engagement:

By proactively marketing Port maritime leasing opportunities through a robust multidimensional marketing campaign promoting the Port as a unique "brand".

Economic Vitality:

By "attracting and retaining maritime and non-maritime commerce in order to contribute to the economic vitality and long term viability of the Port and the City"; and

Stability:

By our Stability objective by "maximizing external investment capital for infrastructure funding

Recommendation

Port staff recommends that the Port Commission approve (1) the First Amendment to the Amended and Restated ICTF Lease (Lease No. L-14397); (2) the Second Amendment and Restatement of the Locomotive Lease (No. L-16372); and (3) the Amended and Restated Rail Agreement (No. L-14503) on the terms described above.

Prepared by: Brendan O'Meara
Maritime Marketing Manager

For: Peter Dailey
Deputy Director, Maritime

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

RESOLUTION NO. 18-65

- WHEREAS, Charter Section B3.581 empowers the Port Commission with the power and duty to use, conduct, operate, maintain, manage, regulate and control the Port area of the City and County of San Francisco; and
- WHEREAS, The Port’s railyard, also known as the Intermodal Container Transfer Facility (“ICTF”), is located at 100 Cargo Way in the City and County of San Francisco within the Port’s jurisdiction; and
- WHEREAS, An active rail facility is a key component to the Port’s maritime activity and cargo business lines; and
- WHEREAS, By Port Commission Resolution No. 07-46, in 2007, the Port Commission approved (i) Lease No. 14397 with LB Railco Inc. to operate the ICTF (“Lease”); (ii) Rail Agreement No. 14503 designating LB Railco Inc. as the Port’s dedicated short line rail operator (“Rail Agreement”); and (iii) Lease of Locomotive Nos. 25 and 23 leasing Port’s equipment to LB Railco Inc. (“Original Locomotives Lease”) effective January 1, 2008; All agreements were to expire on December 31, 2018; and
- WHEREAS, In March 2008, LB Railco Inc. changed its name to San Francisco Bay Railroad Inc. (“SFBR”); and
- WHEREAS, In 2009, by Port Commission Resolution Nos. 09-17 and 09-18, the Port Commission approved a First Amendment to the Original Locomotives Lease and a Second Amendment to the Lease; and
- WHEREAS, In order to take advantage of business opportunities, in January 2017, by Port Commission Resolution No. 17-05 the Port Commission approved an Amended and Restated ICTF Lease to extend the term of the Lease until December 31, 2023 and make other changes summarized in the Memorandum to the Port Commission dated December 7, 2018; the Rail Agreement and Original Locomotives Lease were not extended; and
- WHEREAS, In 2017, by Port Commission Resolution No. 17-08, the Port Commission authorized the Executive Director to seek Board of Supervisor’s approval to accept and expend grant funding from the Bay Area Air Quality Management District (BAAQMD) to purchase a “Tier-4” low emission locomotive and on July 11, 2017 through Resolution No. 278-17 the Board of Supervisors authorized the Port

to accept and expend the grant funding and purchase the new locomotive; and

WHEREAS, As described in the Memorandum to the Port Commission dated December 11, 2018; Port and SFBR have negotiated terms for: (1) an amendment to the Lease to extend the term; establish a process for rent adjustments; establish a tiered structure for wharfage; and increase Port's sale participation to fifteen percent (15%); (2) an equipment lease No. L-16372 to lease two Port-owned locomotives, including the Port's new grant-funded low-emission locomotive; to increase the monthly lease payment; and to require decommissioning of Locomotive No. 25; and (3) an amendment to Rail Agreement No. L-14503 to extend the term; to require SFBR to perform agreed-upon repairs at its sole cost and expense and to otherwise clarify SFBR's maintenance and repair obligations; all agreements will expire on December 31, 2033; and now, therefore be it

RESOLVED, The establishment, improvement, and conduct of railroad facilities are trust consistent uses of Port land under the Burton Act; and operation of the rail facilities is an important maritime function; and be it further

RESOLVED, The Port Commission approves (1) the First Amendment to the Amended and Restated ICTF Lease (Lease No. L-14397); (2) the Second Amendment and Restatement of the Locomotive Lease (No. L-16372); and (3) the Amended and Restated Rail Agreement (No. L-14503) on the terms described in the Memorandum to the Port Commission dated December 7, 2018; and be it further

RESOLVED, that the Port Commission authorizes the Executive Director or her designee, to enter into any additions, amendments or other modifications to the agreements, including exercising the extension option, that the Executive Director, in consultation with the City Attorney, determines when taken as a whole are in the best interest of the Port, do not materially increase the obligations or liabilities of the Port or materially decrease the public benefits accruing to the Port, and are necessary and advisable to complete the transaction and effectuate the purpose and intent of this Resolution, such determination to be conclusively evidenced by the execution and delivery by the Executive Director of any such documents.

I hereby certify that the foregoing resolution was adopted by the Port Commission at its meeting of December 11, 2018.

Secretary